

The Deloitte logo is positioned in the top left corner of the page. It consists of the word "Deloitte" in a bold, blue, sans-serif font, followed by a period. The background of the entire page is a photograph of a modern building's interior, featuring large glass windows and pillars that offer a view of a city skyline with a prominent skyscraper. The lighting is bright, suggesting a sunny day, and the overall color palette is dominated by blues and greens.

Cyprus Real Estate Market Outlook

Real Estate Advisory Services
June 2016

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Executive Summary

Cyprus has officially exited its €10 billion Economic Adjustment Programme on 31 March 2016 having made considerable progress in improving its public finances and reforming the banking sector. Despite initial projections, the local economy returned to positive economic growth in 2015 with an overall improvement in most economic indicators. Private consumption has been encouraged by the negative inflation rate and the decrease in interest rates, while tourism and professional services remain the strongest sectors of the economy. At the same time, the emerging energy sector appears to provide promising prospects for Cyprus.

As emphasised by the European Commission, while Cyprus has taken advantage of the intensive supervision and reform programme in order to exit the economic recession, a number of challenges still need to be addressed. These include the reform of the public administration, the implementation of the privatisation plan and the reduction of unemployment which still remains at high levels, especially within younger groups.

The financial system of Cyprus has undergone a very deep transformation since the beginning of the economic adjustment programme. Following the bail-in in March 2013 and the rapid downsize of the banking sector, the three systemic banks of Cyprus have been successfully recapitalised and the Country was able to return to the international capital markets in late 2014. Nonetheless, another fundamental challenge for the Cyprus economy is the reduction of non-performing loans to healthy levels in order to maintain the viability of the financial system. As highlighted by the Eurogroup in its recent statement, this will be largely based on the rigorous implementation of the insolvency framework and foreclosures law adopted in 2015 and other non-performing loan management tools.

The real estate market has been very negatively affected as a result of the financial crisis with severe impact on construction activity and rapid fall in demand and property values. The recent indicators do however suggest that recovery may be underway for the sector as transaction activity is picking up compared to the past two years (Department of Lands and Surveys) and the rate of decrease in property prices is decelerating across all sectors (RICS). The construction sector is expected to remain weak in the short-term however building permits have recorded an increase during 2015 while confidence in the sector also appears to have improved (Eurostat).

In addition, the Cyprus property market seems to be regaining foreign investor interest in line with the Cyprus Citizenship and Permanent Residency Schemes promoted by the government and the new business opportunities that are emerging mainly in the energy, tourism and professional services sectors. Sales to overseas investors have increased during 2015 according to the Department of Lands and Surveys, while demand has shifted towards exclusive residential projects and prime investment assets. Investor appetite

The economic outlook for 2016 for Cyprus is positive, however challenges still remain particularly in the area of non-performing loans. The previous year has concluded with signs of stability in the real estate market in line with the increasing interest from foreign investors.

for larger projects such as marinas, casino resorts and infrastructure projects is also growing.

Other factors that are expected to encourage the recovery of the local real estate market include several tax reforms introduced by the Cyprus government in relation to transfer fees, VAT and capital gains tax, as well as the amendment of the legal framework regarding the issuance of title deeds. The latter is expected to improve the credibility of the local property market and encourage demand.

The outlook for the economy and the real estate market of Cyprus is therefore more positive now than three years ago with several growth opportunities emerging as a result of

the financial crisis. It is nonetheless vital for Cyprus to remain committed to the reform process in order to address remaining vulnerabilities and engage in more strategic planning in order to create and sustain new business opportunities. The property market is expected to benefit from the projected economic growth nonetheless its recovery is largely based on two main factors; liquidity and confidence. While there is still quite some road to cover in relation to the former due to the large volume of non-performing loans that are real estate related, confidence appears to be slowly returning to the market.



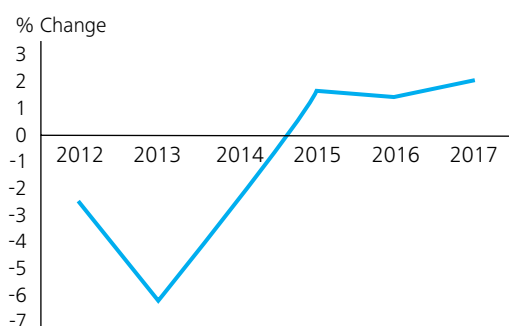
Economic Outlook

Cyprus has already completed the 'Economic Adjustment Programme' which was agreed on the 2nd of April 2013 between the local government and the European Commission (EC), the European Central Bank (ECB) and the International Monetary Fund (IMF). The main aim of the programme was to address short and medium term financial, fiscal and structural challenges that Cyprus is facing. The local economy has made significant progress since the beginning of the programme, returning to growth in 2015 and outperforming initial projections. The positive trend is expected to continue in 2016, mainly driven by domestic demand. The Cyprus Economic Sentiment Indicator is improving (113,3 in 2016M4 according to Eurostat) and investor confidence is building up.

Gross Domestic Product

According to the Cyprus Country Report 2016 published by the EC, Cyprus real GDP annual growth reached 1,6% by the end of 2015. Forecasted annual growth is expected to reach 1,5% in 2016 and climb up to 2,0% by 2017. Based on the same report, growth is driven by both domestic and external demand with additional support from the low inflation and depreciation of the euro. Growth has also been supported by the reduced public spending while investment momentum has shown mild signs of recovery. The main risks highlighted are the high levels of non-performing loans and the weakening of productivity-enhancing investment.

Figure 1: Gross Domestic Product Annual Projections



Source: Eurostat

Professional Services

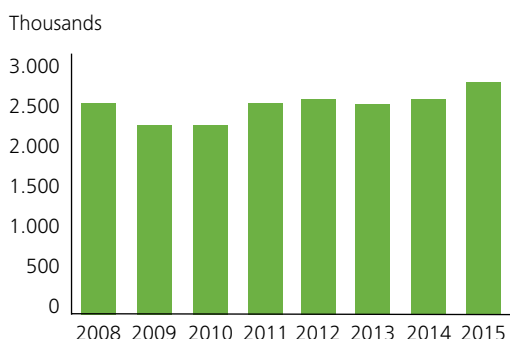
Professional services has been among the strongest sectors of the economy during 2015 (Cyprus Statistical Authority), favoured by an improved trend in foreign investment activity and new company registrations. According to the Economist Intelligence Unit (Country Report, April 2016), the sector is expected to continue driving economic growth in the short-

term alongside tourism. Overall, professional services have retained their credibility throughout the economic recession, enhancing the position of Cyprus as an international financial centre of excellence and creating new job opportunities.

Tourism

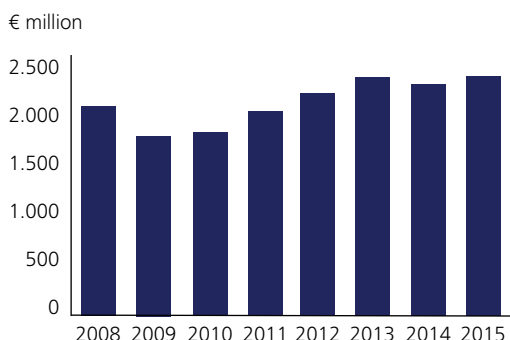
The tourism sector has also recorded solid growth during the past year and remains one of the key driving forces of the economy. According to Cyprus Statistical Authority (CyStat), tourist arrivals increased by 8,9% between 2014 and 2015 while revenue from tourism increased by 4,4%. This increase is attributed to a large extent to the strong sterling which pushed arrivals from the United Kingdom up by 19,5%. At the same time there has been an increase in visitors from Greece, Germany, Israel and the Arab States. Arrivals from Russia on the other hand decreased by 17,6% as predicted, due to the economic and political instability and the sanctions imposed to Russia by the European Union.

Figure 2: Total Tourist Arrivals (2008-2015)



Source: Cyprus Statistical Authority

Figure 3: Total Revenue from Tourism (2008-2015)



Source: Cyprus Statistical Authority

According to the Cyprus Country Report (April 2016) issued by the Economist Intelligence Unit, the outlook for tourism is expected to remain positive throughout 2016. The Cyprus Tourism Organisation is focusing on reinforcing its key advantages while simultaneously diversifying into alternative tourism products such as agrotourism, conference, health, wellbeing and sports tourism. These niche areas alongside golf tourism which has also emerged in the recent years and the recently approved casino resort project, can create substantial potential for foreign investment with positive spillover effects to the real estate market. At the same time, Cyprus should focus on improving its tourism product by upgrading its hotel and other related infrastructure in order to become more competitive.

Energy Sector

The energy sector has arisen as a new growth area in Cyprus, following the discovery of natural gas reserves in its exclusive economic zone (EEZ). The government is placing important emphasis on the potential of transforming the island into a regional energy hub, while several strong coalitions have already been formed with key players in the sector. Following the successful discoveries of Noble Energy International in block 12 of the EEZ in 2011, gas exploitation licenses have been granted to the French Total and the Italian-Korean consortium Eni-Kogas in 2012. In November 2015 BG Group, world leader in natural gas, has announced a 35% equity in block 12, which adds to the encouraging developments in the promising energy sector.

Fiscal Performance

According to the EC's European Economic Forecast (Winter 2016), the government primary balance was forecasted to have achieved a surplus of 2,2% of GDP in 2015 which is expected to increase to 2,6% in 2016 and remain constant in 2017. Debt-to-GDP ratio is projected to decrease to 95,0% in 2017 from 108,4% in 2015.

As suggested by the EC, structural reforms are expected to play a key role in improving public finance figures and the competitiveness of the economy. These include the privatisation plan of state-owned entities (SOEs) which has been approved by the council of ministers in December 2013, in line with the Memorandum of Understanding. The relevant action plan targets to raise at least €1 billion by the end of the programme and a further €400 million by the end of 2018 through the privatization of SOEs and real estate assets as well as other sources of income such as casino licensing.

Inflation

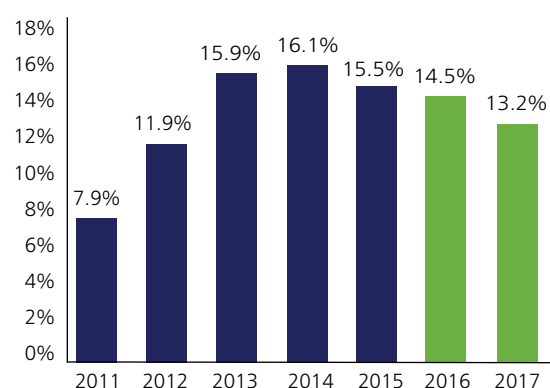
The harmonized index of consumer prices has recorded an annual decrease of 1,6% in 2015 compared to 2014, with deflation encouraging private consumption. The recent forecast issued by the EC indicates a projected inflation rate of 0,2% in 2016 and 1,3% in 2017 in line with the anticipated economic growth.

Labour Market

The high level of unemployment remains an important obstacle to the economic recovery of Cyprus. While the unemployment rate decreased to 15,5% in 2015 from 16,1% in 2014 (Cyprus Country Report 2016), it still remains substantially higher than the EU average (9,4%) and the pre-recession rate of 7,9% (2011). Nonetheless, the forecasted economic growth is expected to generate improvements in the local labour market with the EC's economic forecast indicating that unemployment is expected to decrease to 13,2% by 2017.

Furthermore, developments in the labour market are expected to play an important role in the recovery of the Cyprus real estate market. In the recent years of the economic recession, the high levels of unemployment have affected demand for property negatively as many people found themselves in a weak financial position to afford a property. The forecasted decrease in the unemployment rate is therefore expected to increase consumer confidence which will be in turn reflected in the demand for real estate and particularly residential properties. This is expected to give a boost to the market to enter into a recovery path.

Figure 4: Unemployment Rate Projections

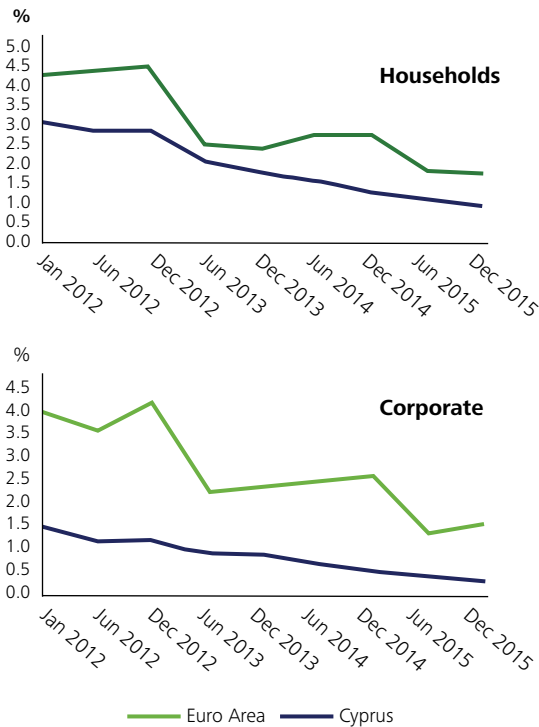


Source: Eurostat

Interest Rates

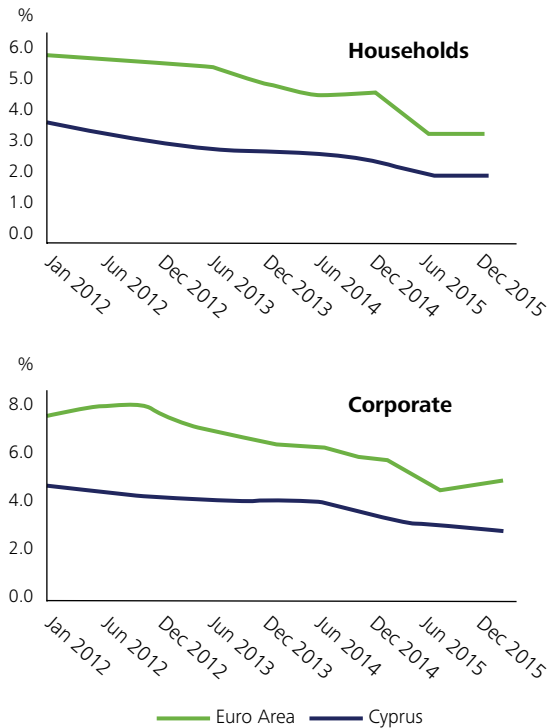
Both loan and deposit interest rates continued on a downward trend in 2015 following the decision of the Central Bank of Cyprus (CBC) to reduce the maximum deposit rate by one percentage point in February. Despite the reduction, interest rates in Cyprus remain amongst the highest in the Euro area. According to the ECB, household deposit rates were the second highest in the Eurozone in December 2015 (1,54%) while interest rates on deposits from non-financial corporations reached 1,49%, which was the highest rate in the Euro area for the specific period. For the same period, lending rates for house purchase reached 3,28% as opposed to 1,99% in the Eurozone and corporate loan rates for amounts of less than €1 million stood at 4,68% compared to the Euro area average of 2,63%. The drop in interest rates is expected to encourage private consumption, giving a further boost to the economic recovery of Cyprus.

Figures 5 & 6: Interest Rates on Deposits (with agreed maturity up to 1 year)



Source: European Central Bank

Figures 7 & 8: Interest Rates on Loans (floating rate and up to 1 year initial rate fixation)



Source: European Central Bank

Banking Sector

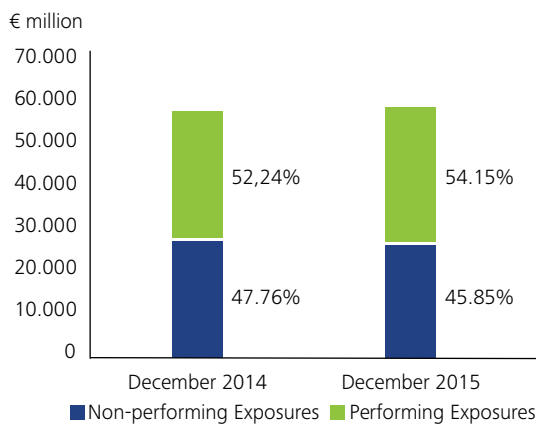
The Cyprus Banking Sector has undoubtedly made significant progress in restructuring its business model following the bail-in of the two major Banks in March 2013 and the strict capital controls which were imposed. As a result of the rapid downsizing and intensive supervision in line with the Economic Adjustment Programme, the sector has been successfully recapitalised. Furthermore, the successful issue of debt in international capital markets and the consecutive upgrades by international rating agencies have restored the credibility of the local banking industry. Liquidity and solvency have also improved while capital controls were lifted completely in May 2015.

Prior to the financial crisis, the organisational business model of banks was predominantly retail-oriented, whereas the new realities demand the targeted utilization of technology for e-banking solutions while services are of a more advisory nature. These developments might enforce banking institutions to take further downsizing actions.

Non-performing Loans

Nevertheless, a fundamental risk that remains to be addressed is the high level of non-performing loans (NPLs) which could dampen the recovery of both the financial sector and the economy as a whole. According to the Central Bank of Cyprus (CBC), on 31 December 2015 non-performing facilities (NPFs) stood at €26.685 million which represent approximately 45,85% of total facilities. In the respective period of 2014, NPFs stood at €27.328 million (47,76% of total facilities). Household loans constitute approximately 47,56% of total exposures while 49,71% of total NPFs relate to non-financial corporations.

Figure 9: Performing & Non-Performing Exposures



The Cyprus government passed the new legal framework on insolvency and foreclosures in spring 2015, in an attempt to assist banking institutions in dealing with the risk area of NPLs. The new framework aims to shorten the time required for

lenders to take possession of real estate collateral when the mortgagor defaults. Nonetheless, industry experts remain quite sceptical in relation to the implementation and efficiency of the specific law.

Many banking institutions are focusing their efforts on out of court settlement through viable loan restructurings with cooperative borrowers. According to the latest CBC statistics, on 31 December 2015 restructured facilities represented approximately 53,04% of total NPFs (€14.154 million) as opposed to 47,06% on 31 December 2014 (€12.860 million). Approximately €10.713 million of the total restructured facilities remain classified as non-performing in line with the new definition laid down by the European Banking Authority, according to which restructured facilities remain classified as NPFs for a minimum period of 12 months before being reclassified as performing. At the same time, banks are preparing for foreclosure auctions which are expected to commence within 2016. As publicly announced, the procedure will target mainly uncooperative and larger debtors while the aim is to protect primary residences and vulnerable groups.

Notwithstanding the efforts described above, experts from key international financial institutions are suggesting that more innovative solutions are required to speed up the reduction of NPLs. These include the introduction of external advisors who have the expertise to deal with this area, outsourcing of loan servicing to improve cash collections and development of a distressed debt market to attract overseas investors. Ongoing supervision is also encouraged to manage the existing volume of NPFs and prevent the creation of new ones. For this to be achieved, banks will have to refocus on a more risk-based approach to lending that is focused on cashflow rather than solely on collateral.

Figure 10: Tools for Resolving Non-Performing Loans



New Loans & Deposits

Despite the recent turmoil in the local banking sector and the initial predictions, total deposits are recording a gradual growth. Based on the Monetary and Financial Statistics issued by the CBC in May 2016, the annual growth rate of deposits stood at 2,4% in April 2016 compared to 2,0% in March 2016. Specifically, total deposits in April 2016 recorded a net increase of €144,9 million compared to a net decrease of €95,5 million in March 2016. Total loans decreased by €86,7 million as opposed to a net decrease of €613,1 million in March 2016, which represents an annual decrease of 7,3% and 7,5% respectively.

Furthermore, according to the Bank Lending Survey which is issued quarterly by the CBC, demand for corporate loans has remained constant during the last quarter of 2015 and no further changes are expected in 2016. On the other hand, demand for residential mortgage loans from households has picked up during 2015Q4 and is expected to increase further in the current year. According to the survey, lending criteria have remained unchanged despite the lower risk tolerance of the banks, due to competitive forces. This trend is not expected to change during 2016.

Currently, the limited access of households to credit facilities is holding back demand for real estate and therefore the ability of banking institutions to grant new loans is considered to be key for the recovery of the real estate market.



Real Estate Market Outlook

Looking Back

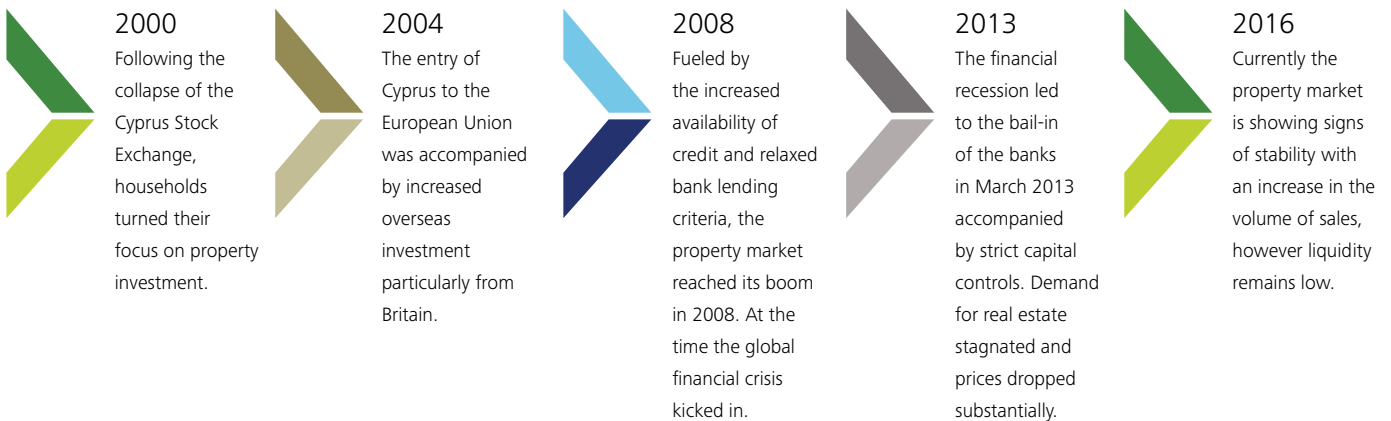
Prior to the financial crisis that continues to affect Cyprus, the local real estate market had been enjoying steady growth for many years, with the perception amongst local investors that property never loses value. This notion has however been completely turned-around, as the property market is currently experiencing its deepest recession ever. Nonetheless, the first signs of stability have been observed in the market during 2015 with sales recording an increase compared to the past two years and price drops slowing down.

The local property market and construction sector reached its peak in 2008 following a collective turn of investors to property once the Cyprus Stock Exchange collapsed in 2000. The accession of Cyprus to the European Union in 2004 brought more investment from abroad and particularly from British investors looking for a 'second home in the sun'. The banking sector contributed to the rally of the real estate market by increasing the granting of new loans to households and property developers.

At the same time that the local property market reached its peak, international markets went into recession thus affecting overseas investment. Cyprus started experiencing the first signs of the financial recession in 2010 which was reflected in the performance of the property market. The overexposure of the banking sector to Greek government bonds and the subsequent debt haircut of Greece were detrimental for Cyprus economy. In March 2013, Cyprus entered into a €10 billion bail-out agreement with the EC, ECB and IMF which caught worldwide attention due to the decision to impose a bail-in of the deposits of the two main banks of the island. The property sector was harshly affected with demand dropping at very low levels and severe price corrections.

Almost three years after the financial turmoil, the property market appears to be gradually stabilising with 2015 having recorded an increase in sales for the second consecutive year (Department of Lands and Surveys). According to the relevant indices issued by the CBC and RICS, the rate of decrease of property prices is slowing down while investor interest for specific property categories appears to be picking up. The government is making efforts to stimulate the recovery of the sector through several incentive schemes and tax reliefs. Construction activity remains weak mainly due to the lack of liquidity and current oversupply, however confidence appears to be slightly improving in the sector.

Figure 11: Cyprus Real Estate Market – Timeline of Main Events



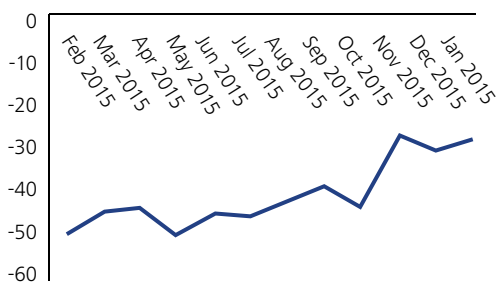
Construction Sector

The construction sector is unquestionably one of the worst affected sectors of the local economy as a result of the recession. Construction activity in Cyprus has contracted severely in the recent years. During the first three quarters of 2015 the contribution of the industry to the economy was limited to 2% as opposed to nearly 11% during 2008. The severe drop in demand which is in many cases accompanied by high levels of supply, as well as the restricted bank lending, are all acting as barriers to the recovery of the sector.

Nonetheless the most recent statistics issued by Cyprus Statistical Authority portray a more positive outlook, indicating an increase of 4,5% in 'Production in Construction' between 2015 and the previous year. The confidence in the sector also appears to be improving according to the 'Construction Confidence Indicator' issued by Eurostat, as shown on Figure 12 below.

The number of building permits issued during 2015 has increased marginally compared to 2014, however in terms of value and area, building permits have increased by 25% and 12% respectively. Nonetheless, all categories remain at very low levels compared to the peak years of 2008-2009, as shown on Figure 13. This indicates that construction activity will remain weak in the short-term, as the current oversupply needs to be absorbed by the market.

Figure 12: Cyprus Construction Confidence Indicator



Source: Eurostat

Figure 13A: Total Number of Building Permits Issued (2008-2015)

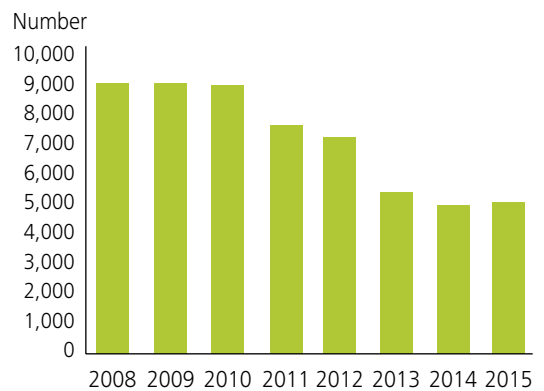


Figure 13B: Total Area of Building Permits Issued (2008-2015)

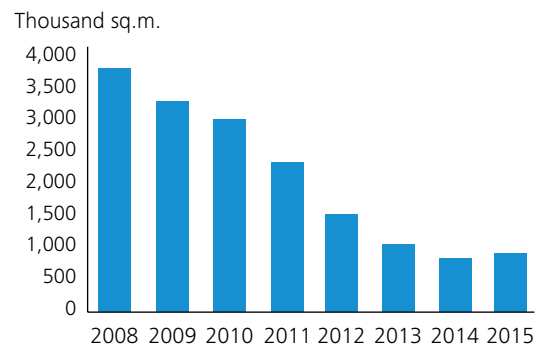
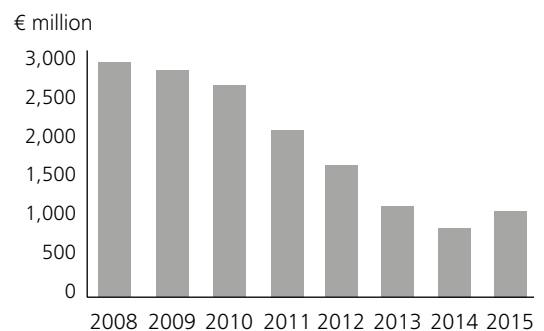


Figure 13C: Total Value of Building Permits Issued (2008-2015)



Source: Cyprus Statistical Authority

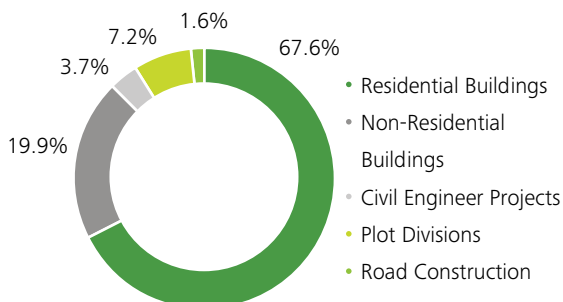
The majority of building permits issued in the past year relate to residential buildings (67,6%) followed by non-residential buildings (19,9%) and plot divisions (7,2%). In terms of residential units, 3197 new permissions have been granted in 2015, which is almost five times lower than 2008. The vast majority of permits related to smaller projects, nonetheless the number of permits issued for larger projects increased from 198 in 2014 to 229 in 2015.

Looking at regional distribution, Nicosia represented 37,7% of total building permits issued during 2015, followed by Limassol (25,2%), Paphos (17,9%), Larnaca (13,9%) and Famagusta (5,3%).

Highlight

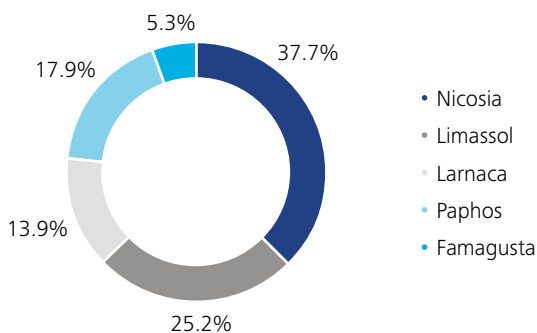
Even though the attractiveness of Cyprus as a foreign investment destination appears to be improving, the real estate market continues to be mainly driven by local demand (73% of the total property sales in 2015 were attributed to Cypriot buyers). The recovery of the property sector is therefore largely based on the ability of local purchasers to obtain mortgages to finance property investments. This in turn will be largely based on the effectiveness of financial institutions in dealing with the issue of NPLs in order to be in the position to grant new loans.

Figure 14: Building Permits per Type (2015)



Source: Cyprus Statistical Authority

Figure 15: Building Permits per Region (2015)



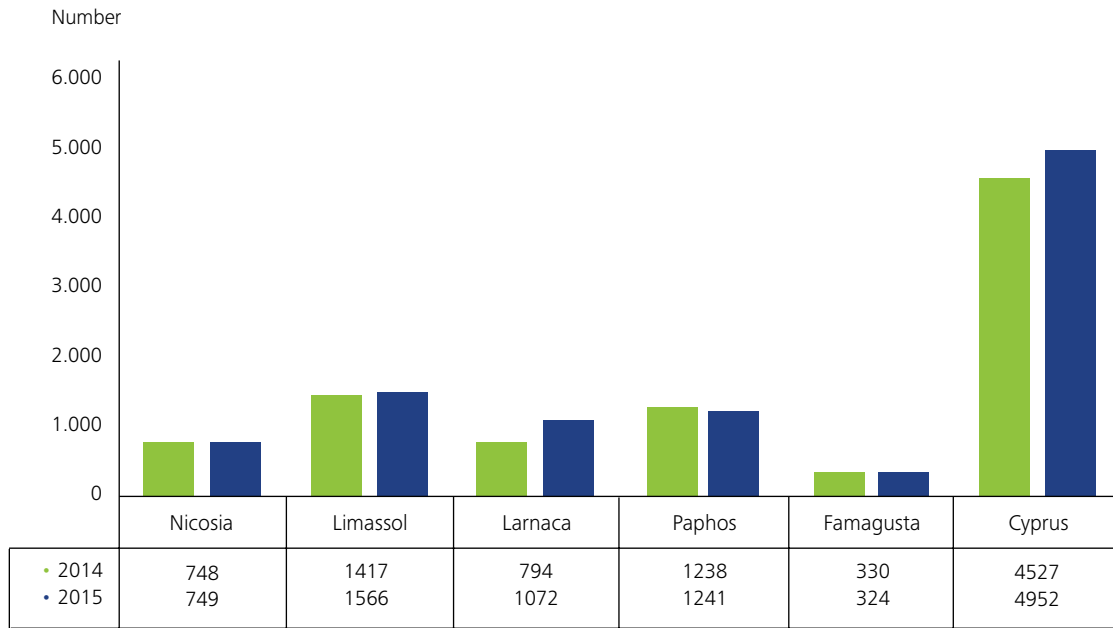
Source: Cyprus Statistical Authority

Transactions

The outlook for demand appears to be more encouraging, with property sales in Cyprus recording growth for the second consecutive year, while foreign investment in real estate is also picking up in all regions. According to the recent figures published by the Department of Lands and Surveys (Figure 16), the number of registered contracts of sale nationally has increased by approximately 9,4% between 2014 and 2015. This increase was led by Larnaca and Limassol Districts where sales rose by 35% and 10,5% respectively. Nicosia and Paphos experienced marginal increase while Famagusta sales decreased by 1,8%. As shown on Figure 17, the majority of sales occurred in Limassol (31,6%) followed by Paphos (25,1%) and Larnaca (21,6%).

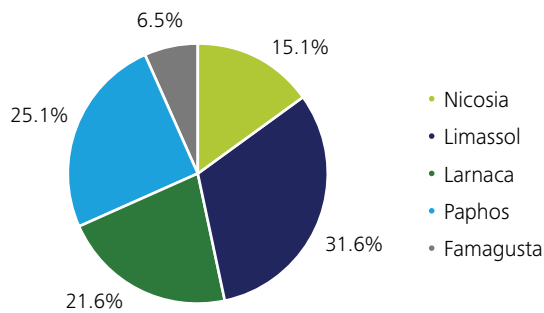
The percentage of sales to overseas markets has increased marginally compared to 2014. In 2015, approximately 27% of total sales deposited at the local Land Registry offices were in favour of overseas buyers (Figure 18). Paphos District in particular outperformed other regions in terms of overseas investment with 481 sales to overseas buyers in 2015, representing approximately 39% of the region's total sales for the year.

Figure 16: Total Contracts of Sale (2014-2015)



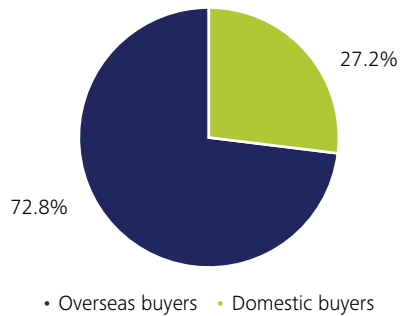
Source: Department of Lands and Surveys

Figure 17: Contracts of Sale per Region (2015)



Source: Department of Lands and Surveys

Figure 18: Contracts of Sale to Domestic & Overseas Buyers (2015)



Source: Department of Lands and Surveys

Market Performance

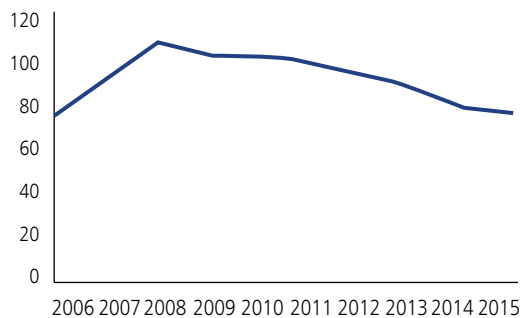
The prolonged recession in the local economy could not leave the real estate market of Cyprus unaffected. Both capital and rental values have been on a negative track since 2009 in line with the negative economic indicators and decline in demand. Nonetheless, the first signs of market stabilisation appeared in 2015 with continuing deceleration of the rate of decrease of property prices as demonstrated by the relevant property price indicators.

As stated by the Central Bank of Cyprus: “The recovery of the economy, the improvement in financial conditions, the lower lending rates and the improved framework for more efficient issuance of title deeds are expected to have a positive effect on the demand for properties and their prices” (RPPI).

Residential Property Price Index

The residential property sector has been experiencing decline in prices since the peak of mid-2008. The most recent figures published by the CBC (2015Q4) do however indicate a path of stabilisation in prices which is expected to continue in 2016. More specifically, according to the RPPI, on annual basis residential property prices decreased by 4,4% in 2015 as opposed to 8,7% decrease in the previous year. On a quarterly basis, the index remained unchanged while house prices experienced a marginal increase of 0,53% for the first time since 2009Q4.

Figure 19: Residential Property Price Index (2006-2015)



Source: Central Bank of Cyprus

In terms of price changes per region, on an annual basis the largest decline was recorded in Nicosia District (3,3%) and the smallest in Paphos District (1,2%). House prices in particular decreased annually by 2,5% in Nicosia and Limassol while the smallest decrease was recorded in Famagusta and Larnaca recorded marginal increase. The largest annual drop in apartment prices was recorded in Nicosia (5,3%) while Famagusta and Limassol apartment prices recorded an increase of 6,5% and 1,2% respectively.

As per the CBC, demand for residential properties is supported by various favourable financial developments, including the decrease in the lending interest rate and the increase in the demand for housing loans from households (CBC’s Bank Lending Survey). Reference is also made to the index of intention to build or purchase a home in the next 12 months issued by the European Commission (Business and Consumer Surveys) which remains negative but has improved compared to the period 2012-2014.

RICS Capital and Rental Prices

The Cyprus Property Price Index which is issued on a quarterly basis by the Royal Institution of Chartered Surveyors (RICS) Cyprus, provides an insight on market capital and rental values and appraisal based initial yields for the four main property sectors (residential, offices, retail and industrial) across the urban centres of Cyprus. The most recent publication for prices as at 31/12/2015, recorded signs of stability in line with the improvement of the economy. Capital prices decreased, nonetheless at a slower rate than previous years while for some sectors rental values recorded marginal increase on a quarterly basis. Yields remained relatively stable and at lower levels compared to overseas yields indicating that there is room for further capital re-adjustment.

Residential

Figure 20: RICS Property Price Index – Residential (2015Q4)

Houses (Three bedroom with garden, semi-detached, 250 sq. m., medium quality)						
	Nicosia	Limassol	Larnaca	Paphos	Famagusta	Cyprus
Capital Value (€ per sqm)	1.491	1.216	1.109	1.416	1.284	1.303
Rental Value (€ per sqm)	2,40	2,52	1,92	2,16	1,78	2,15
Initial Yield	1,9%	2,5%	2,1%	1,8%	1,7%	2,0%
Apartments (Two bedroom, 85 sq. m., medium quality)						
	Nicosia	Limassol	Larnaca	Paphos	Famagusta	Cyprus
Capital Value (€ per sqm)	1.238	1.243	1.318	1.136	945	1.176
Rental Value (€ per sqm)	4,44	4,39	3,92	3,22	3,19	3,83
Initial Yield	4,3%	4,2%	3,6%	3,4%	4,1%	3,9%

Source: RICS Cyprus

Average house prices in Cyprus decreased by a total of 18% between 2012Q1 and 2015Q4 while apartment prices dropped by nearly 24%. Nonetheless, as shown on Figure 21, the price corrections in all districts have been milder as of 2014Q1 for both houses and apartments, indicating that the effect of the recession is gradually starting to fade.

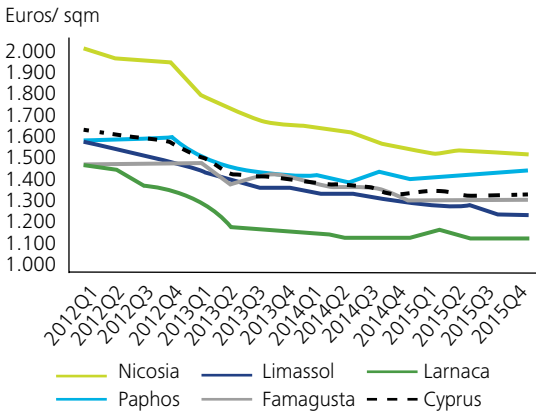
House price corrections have been more severe in Nicosia, nevertheless the capital continues to record the highest capital values for houses (€1.491 per sq.m.). Larnaca house prices are the lowest nationally as they experienced corrections very early in the recession (€1.109 per sq.m.). What is also noteworthy is the fact that house prices in Paphos District have recorded an increase for the fourth consecutive quarter in 2015Q4 which can be associated to the high percentage of foreign investment in the region.

Larnaca is leading the way in terms of apartment prices and has even recorded a marginal increase in the last quarter of 2015. Nicosia apartment prices have experienced the largest decrease since the beginning of 2012 (32%) while Famagusta remains the cheapest area in terms of apartment prices (€945 per sq.m.).

Similar to capital values, the rate of decrease of rental values has also decelerated during 2015 with marginal increases in certain cases. Limassol recorded the highest rents for houses (€2,52 per sq.m.) while Nicosia recorded the highest rents for apartments (€4,44 per sq.m.). Famagusta District recorded the lowest rental values for both apartments and houses. House rents in Paphos increased by nearly 14% between 2014Q4 and 2015Q4 while both Nicosia and Limassol experienced marginal increase in apartment rents.

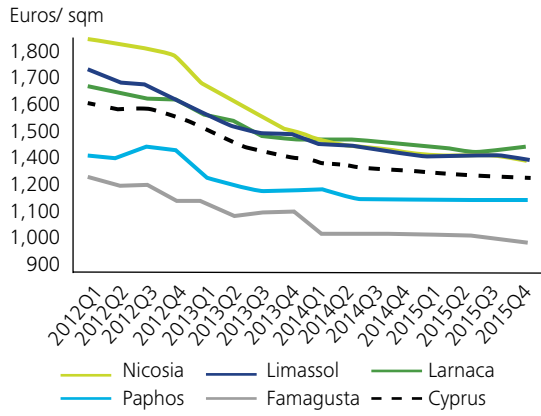
Residential properties in Cyprus have traditionally not been associated with the property investment market due to the high percentage of owner-occupation. Investors in residential property are generally focused on capital appreciation rather than the long-term income producing ability of the property. Residential yields (i.e. return on investment) therefore remain at low levels compared to traditional investment properties and are characterized by inconsistencies between different types of residential property. Appraisal based initial yields stood at 2,0% for houses and 3,9% for apartments in 2015Q4 with a very small differentiation compared to the previous year.

Figure 21A: RICS Property Price Index - Residential Capital Values (Houses)



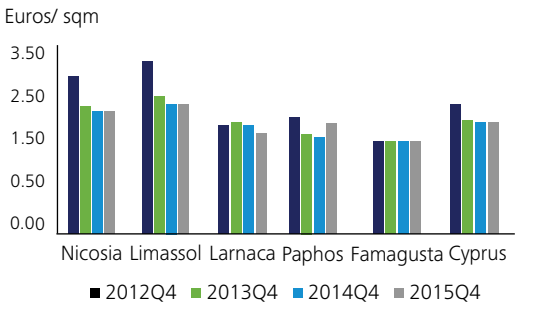
Source: RICS Cyprus

Figure 21B: RICS Property Price Index - Residential Capital Values (Apartments)



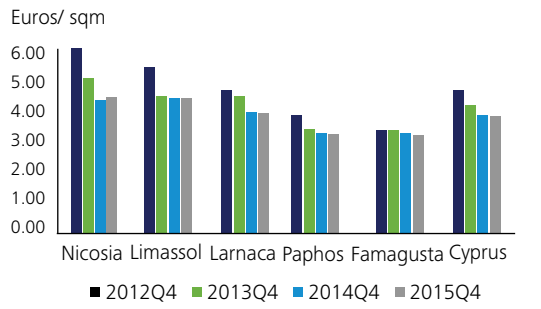
Source: RICS Cyprus

Figure 22A: RICS Property Price Index - Residential Rents (Houses)



Source: RICS Cyprus

Figure 22B: RICS Property Price Index - Residential Rents (Apartments)



Source: RICS Cyprus

Office

Figure 23: RICS Property Price Index – Offices (2015Q4)

Offices (Grade A, city centre, 200 sq.m.)						
	Nicosia	Limassol	Larnaca	Paphos	Famagusta	Cyprus
Capital Value (€ per sqm)	2.552	1.859	1.542	1.614	1.049	1.723
Rental Value (€ per sqm)	10,62	7,65	5,49	4,98	3,34	6,41
Initial Yield	5,0%	4,9%	4,3%	3,7%	3,8%	4,5%

Source: RICS Cyprus

Office prices in Cyprus decreased by nearly 25% between 2012Q1 and 2015Q4 as a result of the impact of the economic recession on business activity. The recent years saw numerous companies downsizing or even going out of business, causing the demand for office space and subsequently prices and rents to drop significantly particularly in Nicosia where the property boom was more pronounced.

As shown on Figure 23, the office sector of Nicosia remains stronger in terms of capital values (€2.552 per sq.m.) followed by Limassol (€1.859 per sq.m.) where business activity is picking up due to foreign investment. Famagusta has the lowest office prices (€1.049 per sq.m.) indicating that business activity in the area is limited. During 2015 office capital values decreased at a much slower rate compared to previous years (less than 1% between 2014Q4 and 2015Q4), while Nicosia even recorded a small quarterly increase in 2015Q4.

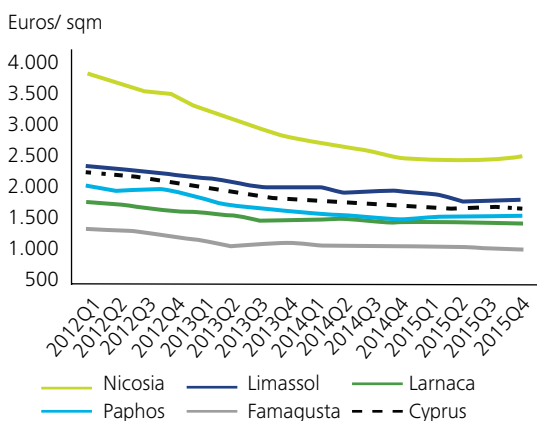
The trend is more or less the same for rental values, with Nicosia recording the highest rents and Famagusta recording the lowest rents nationally in 2015Q4. Nicosia has been subject to the highest rent reductions between 2012 and 2015 as rents decreased from nearly €13,5 per sq.m. to €10,6 per sq.m. Nicosia and Limassol experienced an increase in rental values between 2014 and 2015 and this can be partly attributed to the improvement of the quality of new prime office space and the set-up of new businesses by foreign investors.

Average office yields in Cyprus reached 4,5% in 2015Q4 which is only marginally higher than the respective quarter of 2014. The parallel reductions in capital and rental prices has kept yields relatively stable despite the recession. The highest yields were recorded in Nicosia (5,0%) and Limassol (4,9%) and the lowest in Paphos (3,7%) and Famagusta (3,8%).

Highlight

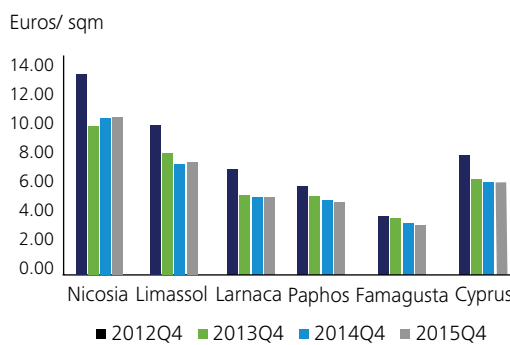
Despite the financial crisis, we have seen demand for high-tech self-contained office buildings in prime locations picking up in the past two years, particularly in Nicosia and Limassol. The two main drivers for this trend have been office relocations of large corporate occupiers who seek to upgrade their image by moving to new business premises as well as new international entrants setting up new businesses in Cyprus. At the same time, income-producing office buildings rented to AAA tenants are viewed very favourably by investors.

Figure 24: RICS Property Price Index – Office Capital Values



Source: RICS Cyprus

Figure 25: RICS Property Price Index - Office Rents



Source: RICS Cyprus

Retail

Figure 26: RICS Property Price Index – Retail (2015Q4)

Retail (High-street, 100 sq.m. ground floor and 50 sq.m. mezzanine)						
	Nicosia	Limassol	Larnaca	Paphos	Famagusta	Cyprus
Capital Value (€ per sqm)	4.332	3.819	2.605	2.307	1.822	2.977
Rental Value (€ per sqm)	18,28	18,17	12,56	9,47	5,85	12,86
Initial Yield	5,1%	5,7%	5,8%	4,9%	3,8%	5,2%

* It is noted that for the purposes of estimation of the capital value of retail units per sq.m., the value of the mezzanine has been accounted at 33% of the value of the ground floor.

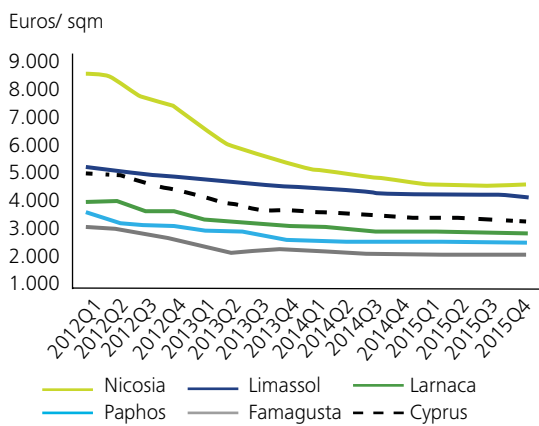
Source: RICS Cyprus

The performance of the retail property sector is directly related to household spending which is in turn affected by the state of the economy. It is therefore not surprising that the impact of the economic recession has been greater on retail properties compared to other properties. The large number of vacant shops and showrooms is representative, particularly in secondary locations.

Retail property values decreased by approximately 37% nationally between 2012Q1 and 2015Q4, with Nicosia recording the largest fall (almost 50%). Nonetheless prices of retail properties in the capital remain the highest nationally (€4.332 per sq.m.) followed by Limassol (€3,819 per sq.m.). As evident from Figure 27, capital values in the retail sector appear to be stabilizing in all regions with small increases recorded in Nicosia and Paphos in the last quarter of 2015.

Rental values for retail properties in Cyprus declined by 3,8% between 2015Q4 and the respective quarter of 2014. Once more Nicosia has experienced the largest rent reduction but remains the most expensive region in terms of retail rents (€18,28 per sq.m.), closely followed by Limassol (€18,17 per sq.m.). Famagusta recorded the lowest rental values for retail units (€5,85 per sq.m.), nearly 55% lower than the Cyprus average.

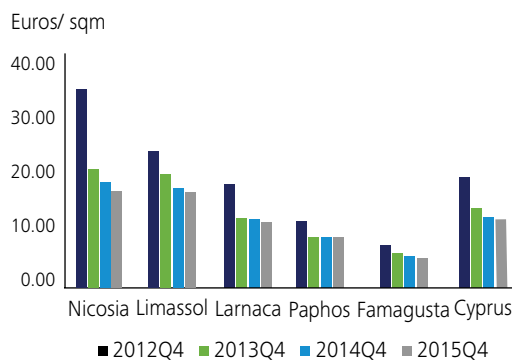
Figure 27: RICS Property Price Index - Retail Capital Prices



Source: RICS Cyprus

The average retail property yield for Cyprus stood at 5,2% in 2015Q4 compared to 5,3% in 2014Q4. The highest yields were evidenced in Larnaca (5,8%) and Limassol (5,7%). It must be noted that average yields for retail properties are higher compared to office yields, reflecting the greater perceived risk associated with the retail property sector of Cyprus.

Figure 28: RICS Property Price Index - Retail Rents



Source: RICS Cyprus



Other Market Influences

Issuance of Title Deeds

The amendment in the legal framework regarding the issuance of Title Deeds is expected to improve the credibility of the local property market and encourage demand, by protecting the property rights of 'trapped' buyers who could not proceed with the transfer of their properties due to outstanding taxes or mortgages of the developer.

The Amended Transfer & Mortgage of Properties Law No. 139(I)/2015 which came into effect on 4 September 2015, now gives the opportunity to 'trapped' purchasers of real estate to apply for the transfer of property in their name. Applications may be submitted to the relevant Land District Office by purchasers, vendors or mortgagees. The provisions of the Law apply where a contract of sale has been submitted to the Land Registry until 31 December 2014. The three main conditions for the transfer of the property in the name of the purchaser are the following:

- Full settlement of the purchase price
- The subject property holds a separate Title Deed
- The purchaser has fulfilled his tax obligations with regards to immovable property tax, town/ community and sewage rates.



Cyprus Citizenship and Permanent Residency Schemes

Cyprus remains an attractive destination for the purchase of an overseas home, with foreign investors seeking to benefit from the favourable tax regime and the sunny climate. The incentives which were introduced by the Cypriot government in 2013 in relation to the citizenship and permanent residency programme, continue to play an important role in attracting foreign direct investment from non-EU residents and they are expected to further reinforce the recovery of the local real estate market.

The acquisition of Cyprus Citizenship by Exception provides full EU citizenship to an investor and his / her dependents and the right of travelling with no restrictions within the EU member countries. According to the amended criteria, non-Cypriot citizens will be eligible to obtain Cypriot citizenship provided that one of the following is met:

- Purchase of state bonds of the Republic of Cyprus amounting to at least €5 million.
- Investment in financial assets of Cypriot companies or organisations (e.g. bonds / securities / debentures registered and issued in the Republic of Cyprus) amounting to at least €5 million.
- Investment of at least €5 million for the purchase or construction of buildings or for the construction of other land development projects (residential or commercial developments, developments in the tourism sector or other infrastructure related projects).
- Purchase, creation or participation in businesses or companies that are based and operating in the Republic of Cyprus, amounting to at least €5 million (It must be proved that the businesses and companies have physical presence in Cyprus and that they employ at least five Cypriot citizens).
- Personal fixed term deposits for three years in Cypriot banks or deposits of privately owned companies or trusts in the Republic of Cyprus amounting to at least €5 million.
- Combination of the above criteria amounting to at least €5 million.
- Collective investments of at least €12,5 million in either of the first four criteria mentioned above, where the amount that needs to be invested is €2,5 million for each investor participating in a special collective investment scheme.

An additional requirement for the obtainment of Cypriot Citizenship by Exception is the purchase of a residential property of a minimum market value of €500.000 (plus VAT).

The Permanent Residency Permit – regulation 6 (2) refers to individuals who have fully and freely at their disposal a secured annual income, high enough to allow a decent living in Cyprus, without having to engage in any business, trade or profession. Applicants have to fulfil the below criteria:

- Evidence of a steady income from abroad of at least €30.000, from sources other than employment in Cyprus (certificates of dividends, certificates of fixed deposits, pension statements, rents or salary advice).
- Deposits of a minimum capital of €30.000 in a Cypriot Bank from sources other than employment in Cyprus. The capital should be transferred from an International Bank to a local Cypriot Bank and it should be pledged for at least a period of three years.
- Purchase of a residential property of a minimum market value of €300.000 (plus VAT).



Tax Incentives

TAXES APPLICABLE ON IMMOVABLE PROPERTY OWNERS

Immovable property owners are subject to immovable property tax. In addition, immovable property owners are subject to property tax and sewage tax levied by the local municipalities.

Immovable Property Tax

Immovable property tax is imposed on an annual basis on the market value (MV) as at 1 January 1980, of the immovable property situated in Cyprus owned by each person as at 1 January of each year at the following rates:

MV (€) as at 1/1/1980	Rate
1- 40.000*	0,6%
40.001-120.000	0,8%
120.001-170.000	0,9%
170.001-300.000	1,1%
300.001-500.000	1,3%
500.001-800.000	1,5%
800.001-3.000.000	1,7%
3.000.001 and over	1,9%

* Owners of property, the total MV (as at 1 January 1980) of which does not exceed €12.500, are exempt from immovable property tax.

We understand that it is the short-term intention of the government to consolidate the immovable property taxes and the sewage tax into one property tax.

TAXES APPLICABLE ON IMMOVABLE PROPERTY TRANSACTIONS

Transactions involving immovable property may be subject to the following taxes:

- Capital gains tax
- VAT
- Transfer fees
- Stamp duty

Capital Gains Tax

Gains from the disposal of immovable property are subject to 20% capital gains tax subject to certain exemptions. In estimating the capital gain, the value of the immovable property as at 1 January 1980 (or cost if the date of acquisition is later), the cost of any additions, any expenditure incurred for the production of the gain and the indexation allowance, are deducted from the sale proceeds.

Key Exemptions:

- Land and/ or land with buildings acquired during the period 16 July 2015 – 31 December 2016 are exempt from capital gains tax upon future disposal. In order to qualify for this exemption, the immovable property must be acquired through a purchase agreement at market value, from a non-related party. The exemption does not apply to disposals of immovable property that have been acquired through an exchange, donation or under foreclosure procedures.
- The disposal of one's principal residence is exempt from capital gains tax provided that the sales consideration does not exceed the amount of €350.000 and the disposal is made before 31 December 2017, under certain approved arrangements.
- Transfers under a qualifying loan restructuring are also exempt from capital gains tax. A qualifying loan restructuring refers to the direct or indirect sale and transfer of immovable property and transfer of rights under a contract deposited with the Department of Lands and Surveys, between a borrower and/or debtor and/or guarantor regarding the same credit facility or grant or debt and a lender, made up to 31 December 2017, which aims to reduce or repay credit facilities or loans or debts granted to a borrower from a lender.
- Transfer of ownership in the event of company reorganisation.
- Exchange provided the gain is used for the acquisition of new property. The gain derived from the exchange reduces the cost of the new property and the tax is paid when the latter is disposed.
- Gifts between spouses, parents, children and third degree relatives.
- Transfer on death.

Value Added Tax

New Buildings:

The acquisition of immovable property (i.e. houses, flats, shops etc.) in Cyprus is subject to the standard VAT rate of 19%.

The standard VAT rate of 19% is reduced to 5% for the acquisition and/or construction of residences (houses and flats) for use as the primary and permanent place of residence by certain eligible persons. The reduced VAT rate applies for the first 200 square meters (sq.m.) of residences of a total covered area of up to 275 sq.m. provided that all conditions are met. The buyer or the client of the constructor/developer shall obtain the relevant certificate for the application of the reduced rate from the VAT authorities after the submission of his/her application.

Renovations & Repairs:

As of 4 December 2015, the reduced VAT rate of 5% applies for expenses incurred for the renovation and repair of all residential properties. The reduced rate applies to residential properties of more than 3 years old. However, in case the value of the materials exceeds the total value of the supply by more than 50%, the value of the materials is subject to the standard rate of VAT.

Plots of Land:

The purchase of a plot of land alone, is exempt from VAT in Cyprus. This applies for all categories of land i.e. for residential purposes and agricultural purposes.

Transfer Fees

Transfer fees are payable by the purchaser, upon a transfer of immovable property. Transfer fees are calculated on the MV of the property as estimated by the Department of Lands and Surveys at the following rates:

Market Value (€)	Rate
0- 85.000	3%
85.000-170.000	5%
170.000 and over	8%

In the case of free transfers of property between the following parties, the transfer fees are calculated on the value of the property as at 1 January 2013 at the following special rates: from parents to children 0%, between spouses 0,1% and between third degree relatives 0,1%.

Exemptions:

The following transfers are exempt from transfer fees:

- under a qualifying reorganisation
- under a qualifying loan restructuring
- in the context of bankruptcy, liquidation, disposal of mortgaged immovable property by the lender

Furthermore, for the period 2 December 2011 – 31 December 2016, transactions which are subject to VAT are exempt from transfer fees. During this period, a 50% exemption is also available for property transfers that are not subject to VAT and the property is either sold for the first time from the date of issue of the relevant building permit or the contract is submitted for the first time to the local District Land Registry office.

Stamp duty

A contractual agreement relating to the acquisition of a property situated in Cyprus is subject to stamp duty at the following rates:

Consideration (€)	Rate
0- 5.000	0%
5.000-170.000	0.15%
170.000 and over	0.2%

(subject to a maximum of €20,000 per contract)

Exemptions:

Contracts relating to transactions that take place in the context of a loan restructuring or a company reorganisation are exempt from stamp duty.



Large Investment Projects

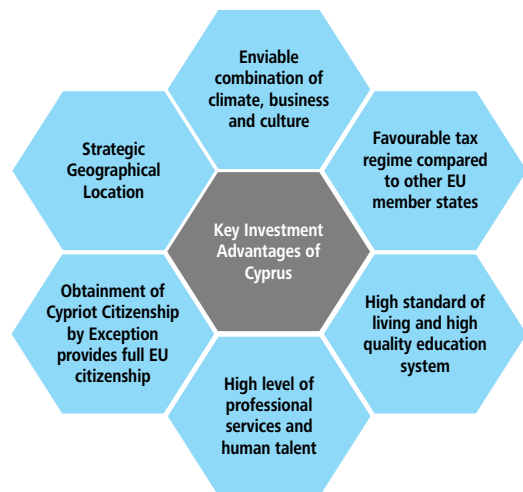
Despite the challenges currently faced by the real estate sector of Cyprus, in the recent years we have experienced new opportunities arising in the field of large investment projects which continue to attract strong interest from overseas investors. The market has shifted away from the mass provision of holiday homes mainly targeted to British buyers, to more innovative, high-end large scale developments including golf resorts, marinas and tourist development projects.

The Cyprus Investment Promotion Agency (CIPA) has been established by the local government in 2008 in an attempt to promote the country as an attractive international investment centre and provide support to investors. The agency is currently presenting 27 major projects to potential investors from around the world including shopping malls, commercial buildings, medical resorts, luxurious sea-front projects, infrastructure projects and golf resorts. At the same time, the Cyprus Naturalization Scheme is providing a very strong incentive for foreign direct investment and purchase of residential properties.

The success of the Limassol Marina, the new projects currently underway as well as the recent successful completion of Limassol Port Commercialisation are all positive indicators that investor interest for larger-scale projects is strong. In a recent development, the government has short-listed the three bidders

who will proceed to the final stage of the casino licensing process. The creation of an integrated casino resort, the first in Europe, is expected to give a boost to the tourism sector and the economy as a whole. In addition, the emerging energy sector of Cyprus is creating significant investment opportunities that are expected to benefit not only the economy but also the real estate market as key energy players are establishing their presence in Cyprus.

Figure 29: Key Investment Advantages of Cyprus



Looking Forward

The real estate market of Cyprus remains depressed for the sixth consecutive year in line with the economic recession affecting the island. Nonetheless, 2015 closed with several positive indicators that the market is slowly entering a recovery path in line with the forecasted economic growth.

While prices continue to fall, the rate of decrease has slowed down and the market appears to be stabilising. At the same time, the outlook for demand appears to be more positive with a recorded increase in the volume of contracts of sale deposited in the Department of Lands and Surveys during the previous year. On the supply side, recovery of the construction sector remains moderate.

Despite the first signs of possible stabilisation in the property market, the challenges still remain particularly in relation to the performance of the banking sector. Even though demand for new loans has increased during 2015, liquidity is still a restrictive factor. For new projects to be financed, financial institutions are required to first resolve the problem of non-performing loans which remain at very high levels. Banking institutions are currently increasingly involved in voluntary

asset-to-debt swaps. This raises the concern of possible market oversupply and subsequent fall in prices in the banks' attempt to liquidate repossessed properties, given the timeframe of three years currently permitted by the Central Bank. The implementation of the legal framework regarding foreclosures and the ability of banking institutions to effectively manage repossessed properties will therefore be crucial.

The economic recession can be characterised as a transition period for the Cyprus property market. The severe contraction of the construction sector and rapid fall in values and demand have led to a re-focus of the sector to a more innovative strategy while creating attractive investment opportunities. Foreign direct investment is expected to improve further in line with the citizenship and permanent residency schemes promoted by the Cypriot government. Investors interest is anticipated to focus mainly on prime investment assets and exclusive residential properties on seafront projects and integrated resorts. Larger investments in the fields of energy, tourism and marinas are also gaining momentum however their success will strongly depend on the ability of the government to draft a long-term strategy that will establish Cyprus as a regional energy hub and key business centre.

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