



REPUBLIC OF CYPRUS

**ADDRESS  
BY THE MINISTER OF FINANCE  
BEFORE THE HOUSE OF REPRESENTATIVES  
ON THE OCCASION OF THE DEBATE  
ON THE BUDGETS FOR 1987**

by the  
Minister of Finance  
Mr. CHR. MAVRELLIS

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## CONTENTS

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	Page
IMPLEMENTATION OF THE FOURTH EMERGENCY ECONOMIC ACTION PLAN 1982—1986 . . . . .	3
ECONOMIC DEVELOPMENTS IN 1986 . . . . .	6
THE PRESENT STATE OF OUR ECONOMY . . . . .	8
THE FIFTH EMERGENCY ECONOMIC ACTION PLAN 1987—1991 . . . . .	9
THE OBJECTIVES OF THE FIFTH EMERGENCY ACTION PLAN . . . . .	10
THE DEVELOPMENT STRATEGY WITHIN THE FRAME- WORK OF THE FIFTH ACTION PLAN . . . . .	11
THE MAIN TARGETS OF THE FIFTH EMERGENCY ACTION PLAN . . . . .	13
ECONOMIC POLICY IN 1987 . . . . .	14
PROSPECTS FOR 1987 . . . . .	19

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**FEB 2012**

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MR. CHR. MAVRELLIS BEFORE  
THE HOUSE OF REPRESENTATIVES ON THE OCCASION  
OF THE DEBATE ON THE BUDGETS FOR 1987**

*Mr. President,*

*Members of the House,*

It is with feelings of honour and respect that I am addressing from the House floor the representatives of our people in order to analyse, on the occasion of the debate on the three budgets, the state of our economy and the short-term and long-term targets of the economic strategy and policy of the Government.

As 1986 was the last year covered by the Fourth Emergency Plan, while 1987 will be the first year of the implementation of the new Emergency Plan, I shall give particular emphasis to an evaluation of the results of the Fourth and the basic outlines of the Fifth Emergency Plan.

Since the provisions of the three budgets have already been analytically explained by the competent Ministers during consultations made at the Finance and Budget Committee of the House, I do not intend to make a special reference to them in my speech.

**IMPLEMENTATION OF THE FOURTH EMERGENCY ECONOMIC  
ACTION PLAN 1982—1986**

The basic aims of the Fourth Emergency Plan were the continuation of the upward trend of the Cyprus economy in conditions of external and internal stability while at the same time bringing about its gradual restructuring.

On the basis of provisional figures on developments until the end of 1986, it appears that the targets of the Fourth Emergency Plan have on the whole been attained. The economy has achieved a high rate of growth which surpassed the corresponding rate of the world economy and the target set, while at the same time overall internal and external stability was achieved and conditions of almost full employment were maintained. Also, the economy continued to invest a high percentage of the gross national income and the incomes and standard of living of the population improved further.

The surpassing of the economic growth target set was based to some extent on the fiscal policy which aimed at expanding production, which, however, coupled with the exceeding of the target for investments and the non-attainment of the target regarding savings, necessitated greater external borrowing than that envisaged, which, nevertheless, remained within manageable limits.

The average annual rate of growth of the gross domestic product at constant prices is estimated to have exceeded 5% which is considered to be high considering that the growth rate of the world economy was only around 2.7%. The rate of growth was also higher than the 4% target set.

The level of the investment activity of the economy should also be considered satisfactory, since investment is estimated to have shown an annual average rate of increase of 1.9%, as against the target of 1.5%. However, the composition of private investment by category of capital equipment and by sector of economic activity continued to diverge from its desired allocation.

Despite the fall in the purchasing power of our traditional markets, external demand continued to be the basic factor behind the growth of the Cyprus economy, because of the rapid growth of tourism and other export services. In contrast, domestic exports of goods lagged behind due to unfavourable developments in the last two years and to the specific problems faced by some of our main trading partners. The deviation from the target set regarding exports of goods was offset to some extent by domestic demand.

The relatively high rate of economic growth was associated with a high annual increase in employment. The rate of increase in employment surpassed the target of 1.6% rising to about 2%, which helped maintain conditions of almost full employment. However, the relatively higher increase in the supply of labour, coupled with the decrease of opportunities for temporary employment abroad, led to a marginal increase in unemployment.

The average annual rate of improvement in labour productivity also showed an increase higher than the target set. The increase was of the order of 3%, as against 2.4% envisaged in the Fourth Emergency Plan.

Salary and wage earnings of employees in the period 1982—86 increased at an average annual rate of 10% in money terms and 5% in real terms. This rate, which exceeds the rate of increase in productivity, led to further improvement in the standard of living of working people, but also to the creation of problems concerning the competitiveness of our products both at home and abroad. The rate of inflation decelerated

considerably, falling from 11% in the 1979—81 period to 5% on average during the years 1982—86, while in 1986 it dropped to 1.2%.

During the Fourth Emergency Plan, developments in the balance of payments showed considerable deviations from the targets set, as a result mainly of the low growth of domestic exports of goods. At the same time, however, total imports of goods are estimated to have increased by an annual average rate of 7%, which was lower than the more adverse forecast of 13.5%, but higher than the rate of increase in exports of goods. Earnings from invisible sources are estimated to have increased by 14% annually while invisible payments rose by 11%. As a result, the surplus in invisible revenue is estimated to have more than doubled, reaching £360 m. in 1986, as against £165 m. in 1981. The overall balance of payments in 1986 ended in a surplus of about £25 m., compared with a £6 m. surplus envisaged in the plan, while foreign exchange reserves at the end of 1986 covered about 8.5 months of imports, compared with about 6 months in 1981.

In the fiscal sector the deficit was satisfactorily contained. As a percentage of the gross domestic product it was considerably lower in 1986, than that of 1981 (3.7% as against 6.6%).

The Government development expenditure realised by all sources is estimated to have reached about £400 m. which was the target of the Fourth Emergency Plan. If the votes of the Development Budget transferred to the Ordinary Budget are taken into consideration, then the target has been surpassed. During the Plan period the Nicosia-Limassol road, the major irrigation works in Paphos, the Larnaca and the Archbishop Makarios III hospitals, the Pitsilia Integrated Rural Development Scheme and the Paphos Airport were, inter alia, completed. Also the largest part of the Vassilikos-Pentaskinos irrigation project was completed and work commenced on the construction of the largest infrastructural work ever undertaken, that of the Southern Conveyor, and also on the Chrysochou valley water works and the Third Road Development Scheme. Many more minor development works were started. It is mentioned indicatively that in the water development field, as a result of the completion of works during this period, the capacity of our dams increased from 65 m. cubic metres to 176 m., while with the completion of the projects under construction, the capacity of our dams will increase to 297 m. cubic metres, a development that will solve the serious water problem of Cyprus.

The monetary/credit policy during the Fourth Emergency Plan was supportive of the overall development policy and was implemented with flexibility, adapted to the developments in the economy each year. Money

supply increased by an average annual rate of 12.5% i.e. a rate higher than the 11.2% target set, thus adequately financing development without, however, creating serious problems for the stability of the economy.

The overall development of the economy made possible the impressive improvement of social services provided by the state, such as new improvements in the social insurance scheme, which resulted in increasing benefits from the funds from £28 m. in 1981 to £74 m. in 1986, the introduction of free education throughout the entire public secondary education, the extension of compulsory education to gymnasia, the expansion and improvement of medical services as well as the continuation of the programme for tackling the problems of the persons displaced and affected as a result of the Turkish invasion. More specifically for the housing of displaced persons 16,045 housing units were constructed, increasing to 38,688 the total number of housing units constructed or improved within the framework of various projects for the displaced persons.

#### ECONOMIC DEVELOPMENTS IN 1986

The main feature of developments last year was the significant improvement of the internal and external stability of our economy, which was achieved without creating conditions of economic stagnation or recession. This improvement resulted from the positive effects of exogenous factors, but was due also to the flexibility and adaptability of Government economic policies.

The most positive development in 1986 was the sharp decrease in the external current account deficit of our economy. This deficit, the extent of which reflects the degree of economic stability of an economy, is provisionally estimated to have dropped from £100 m. in 1985 to about £15 m. in 1986. As a percentage of the gross domestic product, the deficit was reduced for the first time since 1968 to about 1%. It is noteworthy that the current account deficit during the last five years had ranged between 7% and 9% of the gross domestic product.

There has also been a marked decline in the rate of inflation, the level of which reflects the degree of internal stability of an economy. The average rate of inflation for the whole year fell from 5% in 1985 to 1.2%, the lowest in the last 20 years.

The rate of growth of the economy last year is provisionally estimated at about 3%, which is considered satisfactory, and exceeded once more that of the world economy. As in 1985, apart from the further increase in domestic demand, a positive contribution to the achievement of a relatively satisfactory rate of growth was also made by the very good

performance of the sector of tourism and other export services. Particularly remarkable was the approximately 11% increase in the number of foreign tourists who visited our country in 1986. Thus, thanks to the intensive efforts of the Cyprus Tourism Organisation, the Cyprus Airways and the other bodies concerned with tourism, the number of tourists exceeded for the first time 900,000. In contrast to the good performance of export services, exports of goods declined by 13%, which had negative effects on the level of economic activity, particularly in the manufacturing sector.

The fall in the exports of goods and the relative decline in the level of activity of the manufacturing sector was the main cause for the marginal increase in the unemployment rate, from 3.3% in 1985 to levels around 3.5%. It also had a negative effect on the level of productive investment by the private sector, which continued to be comparatively sluggish, despite the generous tax and other incentives and facilities provided by the Government.

During 1986 our foreign exchange reserves are estimated to have increased by 10% and reached £435 m. at the end of the year, which cover about 8.5 months of imports, compared with 6.8 months at the end of 1985, an extremely high percentage, by international standards. The external debt of the country as a percentage of the gross domestic product was stabilized at about 37% while in absolute figures it showed a slight increase compared with 1985, reaching £570 m. approximately. It should be stressed, however, that the servicing of the external debt showed a decrease to the equivalent of about 13% of the exports of goods and services, compared with 13.7% in 1985. This percentage is much lower than the average percentage of non-oil producing developing countries, which is about 23.5%.

Both the favourable and to some extent the unfavourable developments in 1986, reflected mainly the effects on our economy of the sharp fall in the price of crude oil. Thus, on the one hand, this fall led to a reduction in our imports and helped bring inflation down, while on the other it led to a decrease in our exports to Arab markets due to the fall in the incomes of these countries caused by it. The specific problems which some of our traditional trading partners are facing also had a negative effect on our exports.

Apart from the purely exogenous factors, the improvement of public finances and the significant increase in the propensity to save in the private sector of the economy also contributed to the strengthening of economic stability. Thus the fiscal deficit was limited to £57 m. as against £58 m. in 1985 while as a percentage of the gross domestic product it was reduced to levels round 3.7%, as against 4.1% in 1985. At the same time

savings by the public sector more than doubled, while savings by the private sector increased by £45 m., reaching £395 m. As a percentage of the private disposable income these savings amounted to 30% compared with 28% in 1985.

Among the negative developments in 1986 was a decline in the competitiveness of our production mainly in foreign markets as a result partly of the continuing increase in labour costs at a rate much faster than the increase in productivity and much higher than that of our competitors in foreign markets.

### THE PRESENT STATE OF OUR ECONOMY

An assessment of all the data clearly shows that the overall state of our economy can be described from the short-term point of view as very satisfactory, particularly if compared with the international economic situation.

The improvement in the stability of our economy in 1986, which was mainly achieved as a result of the fall in the price of oil, fully confirms the view I expressed last year from this floor, that one of the main causes of the destabilising tendencies in the last decade was, besides the devastating consequences of the Turkish invasion, the unduly high prices of crude oil in the world market. Despite the fact that the fall in the prices of crude oil helped the other non-oil producing countries to improve the stability of their economy, very few of them achieved the spectacular results of Cyprus.

The strengthening of the stability of our economy would have been even more impressive if all the Bills and other measures proposed by the Government last year, within the framework of a short-term programme for the strengthening of the stability of our economy, had been adopted. If these measures had been adopted, the fiscal deficit, about which there is so much discussion, would have completely disappeared, with immediate beneficial effects on the stability of our economy. Adoption of the Government proposal regarding the manner of the distribution of the economic benefits from the fall in the price of crude oil would have had particularly beneficial effects on our economy. On the basis of the revised proposal tabled before the House in the form of a Bill, half of the benefit would have gone to the public sector for the reduction of the fiscal deficit and the balance would have been used for the strengthening of the competitiveness of various productive sectors of the economy, particularly those which are export oriented. With the arrangement finally adopted, despite my appeal from this floor in my speech last year, the major part of the benefit was transferred to the private sector of the economy, and this

involves the danger of reinforcing in future the propensity to consume, with corresponding negative effects on the balance of payments of the country and the stability of our economy in general.

The Government services concerned have estimated that, despite the existing upward trend in the price of crude oil, as a result of the recent OPEC agreement to limit production, the degree of stability of our economy is not going to be disturbed to the point of causing serious concern, provided that the excessive claims of productive groups, even prosperous groups, for improvement of their standard of living would be confined within reasonable levels and to the potential of the state and the economy in general.

### THE FIFTH EMERGENCY ECONOMIC ACTION PLAN 1987—1991

*Mr. President,*

During the period of the implementation of the Emergency Plans following the Turkish invasion, the economy grew rapidly, unemployment fell sharply, the investment activity was intensive, the rate of growth of productivity was high and the expansion of social services impressive. The fiscal policy was, rightly, expansionary but deficits were unavoidably created, which were financed by external and internal loans.

At the same time, labour-intensive units which were justifiably encouraged with a view to rapidly reducing unemployment, have, as expected, created a structural problem. Despite the very good performance of tourism and exports, the dependence of Cyprus on imports and the successive price increases of oil created a problem of imbalance in the current account. This imbalance, which also reflected the fast rate of reactivation after the invasion and the insufficiency of domestic savings with regard to the deliberately very high level of investment, created the need to resort to external borrowing.

The present economic conditions are such as to allow us to shift the emphasis of our economic policy and strategy, within the framework of the implementation of the Fifth Emergency Action Plan, to the structural and modernisation problems we are facing.

Given the importance of external demand for achieving a high rate of growth of the Cyprus economy and the forthcoming agreement on the customs union of Cyprus with the EEC, the assessment of the medium-term development prospects is closely connected with prospects regarding the world economy in general and the European Economic Community in particular.

The medium-term prospects for the international economy appear to be relatively favourable. Provided the price of oil will remain at comparatively low levels, the forecasts by international organisations and other independent financial institutions are that the recovery of the international economy will continue, possibly at a slower rate, with positive results on the volume of world trade in general and the EEC in particular. In view of these prospects, Cyprus is called upon to exploit the opportunities that will present themselves, by implementing the appropriate policies which will make the Cyprus products competitive in international markets and to restructure the economy, by laying the foundations for the successful meeting of the challenge presented today by the forthcoming customs union agreement with the EEC.

#### THE OBJECTIVES OF THE FIFTH EMERGENCY ACTION PLAN

The guidelines and the aims of the Fifth Emergency Plan have been determined against the background of the existing data and of the trends and prospects of the world and the domestic economy.

Within this framework, in the course of the implementation of the Fifth Action Plan, the efforts to correct the imbalances and structural weaknesses of the economy will be intensified with a view to further strengthening our economy which is fundamental to the political struggle of Cyprus for survival.

More specifically, the medium-term objectives of the Fifth Action Plan can be summarised as follows:—

- Promoting the necessary structural changes and the technological upgrading of domestic production in various fields and adjusting the economy to the new conditions expected to be created by the customs union with the EEC.
- Achieving the highest possible rate of economic growth without disturbing the stability of the economy and by maintaining conditions of full employment.
- Consolidating conditions of stability regarding inflation, public finances, the balance of payments and financing of development.
- Constantly improving the organisation and performance of the public service for the purpose of maximizing its contribution to economic and social development.
- Saving energy and reducing the dependence of Cyprus on oil.
- More equitable distribution of the national income.

- Utilising, maintaining and preserving the natural environment and our historic and cultural heritage and promotion of cultural development through the widest possible participation of the people.

#### THE DEVELOPMENT STRATEGY WITHIN THE FRAMEWORK OF THE FIFTH ACTION PLAN

The development strategy of the Fifth Action Plan, for attaining the objectives to which I have referred, will be based on the technological, organisational and operational restructuring and upgrading of the economy. A basic element of this strategy is the creation of new large production units, rationally organised and with possibilities of success in the world trade, because only such units can undertake capital-intensive and high technology investments and manufacture new export-oriented products. In parallel, existing units should be modernised to be able to face the growing competition, both in the domestic and the external market. This becomes necessary also because of the present state of the Cyprus' economy, and also because of the forthcoming commencement of the transitional period of the customs union between Cyprus and the EEC.

Within this framework, existing incentives will be revised with the object of encouraging the restructuring of investment in favour of investment in machinery and other productive equipment. At the same time, the creation of the necessary institutional framework will be completed.

An essential element of the development policy in the next few years is the improvement of productivity, which will ease inflationary pressures and contribute substantially to the strengthening of the competitiveness of the economy. This improvement should come from technology-intensive productive investment, the upgrading of production units and the appropriate training and retraining.

The sectors on which the growth of the economy will be based are not expected to be substantially different from those of the Fourth Action Plan. Thus, efforts will be intensified for the further development of agriculture, particularly by promoting new, more remunerative, irrigable varieties and early crops and by intensifying at the same time the effort to secure new markets, while emphasis will be given to the development of the manufacturing sector. As regards tourism, the new Plan's strategy will continue to aim at a better utilisation of the hotel infrastructure and at a balanced development, with the object of maintaining the natural environment and promoting the supplementary tourist services for enrich-



ment of the tourist product. Also efforts will be continued to promote services with export orientation and prospects which will utilise the advantageous geographical position of Cyprus and gradually turn the island into an international economic, trade and cultural centre in the broad Middle East area.

An assessment of the development potentials shows that only with successful exports of goods and services will it be possible to achieve a high rate of economic growth. These exports, however, should be diversified to developments in the international field, both from the point of view of the nature of products and services and from the point of view of markets. Success in the export drive necessarily presupposes improvement of the marketing of products, an activity in which the average Cypriot entrepreneur lags behind. Thus it is necessary to strengthen organisational arrangements to promote exports by setting up the new exports promotion body. As regards the destination of exports, the extent of the dependence of the export industry on certain countries should be gradually changed. Consequently, our basic export interest should concentrate, in the long run, on Europe, without this meaning that we shall not pursue a multidimensional foreign trade policy, particularly in the direction of countries absorbing products encountering difficulties.

Preliminary indications regarding the labour market show that the increase in the supply of labour will be relatively high compared with the increase in employment, while at the same time the imbalances observed in the supply of and demand for particular skills of labour are expected to continue. For this reason the strategy to be applied in the next few years will aim at the highest possible increase in employment with parallel improvement in productivity through proper training, retraining, industrial training and encouragement of mobility, both geographically and by sector of production and by profession.

Another element of this strategy is the slowing down of the rate of expansion of the total consumption demand, both public and private, given that the further restraining of the rate of growth of investment is not desirable, since the intensification of investment activity, particularly in the productive sectors, is an indispensable element for the continuation of the growth of our economy.

Within the framework of the implementation of the new Plan, the Government will complete the preparations for the establishment of a Stock Exchange, which is expected to contribute to the creation of a climate of confidence on the part of the public in public companies, and also other necessary institutional changes. In addition, other ways for encouraging savings will be explored and so will measures to improve our

financial system so that our restructural and more general development options may be more effectively promoted.

We believe that the need for fixed capital formation, the introduction of modern technology and the solution of our international marketing problems, all require, the participation of foreign investments in the productive process. For this reason the whole development strategy will aim at attracting more investments in Cyprus.

#### **THE MAIN TARGETS OF THE FIFTH EMERGENCY ACTION PLAN**

One of the specific targets, is the attainment of an approximately 4% average annual rate of growth of the gross domestic product, which will contribute to the further increase of incomes and improvement of the people's standard of living. In order to achieve this development target it is planned to increase investment at a rate of more than 1% per year. More specifically in the period 1987-91 investments of the order of 2 billion 460 million pounds at current prices, are planned to be made by all sources (including the private sector), while the state overall development expenditure in the same period is estimated provisionally at £530 m. As development should emanate basically from increased foreign demand, exports of goods should thus be increasing at current prices at an annual rate of 6% and those of services at 10%. These rates will help keep the current account deficit within tolerable limits. In parallel, it is planned to further contain the rate of growth of domestic demand within the framework of the expansion of domestic production with a view to improving the possibilities to save and reducing dependence on financing from abroad. In this context it is expected that the fiscal deficit will gradually be reduced.

The target of an annual increase in the gross domestic product of about 4% will, it is estimated, be achieved through an increase in the gainfully employed population by 1.5—2% and in productivity by approximately 2% annually, thus contributing to the maintenance of conditions of almost full employment. Unemployment as a percentage of the economically active population will remain at about 3.5%, while the average annual rate of inflation for the next five years is expected to show some increase mainly due to influences from exogenous factors. I must stress that an indispensable prerequisite for achieving the targets, as regards both the rate of unemployment and the rate of inflation, is to limit increases in all forms of incomes within the framework of the increase of productivity.

Before concluding my reference to the new Plan, I would like to express my appreciation for the work done so far by the Advisory

Committees and reiterate the importance attached by the Government to this democratic process of planning economic and social development. I would also like to stress that the Government attaches particular importance to cooperation with the private sector given that, as a result of the nature of the socio-economic system, which we have adopted and in which we absolutely believe, the main responsibility in the productive process is shouldered by the private sector. It is in this framework that the Economic Advisory Committee will meet in a few days with an open agenda to hear the views of the representative bodies of the private sector on additional measures which could be adopted to strengthen our development potential and solve specific problems we are facing.

### ECONOMIC POLICY IN 1987

It goes without saying that our economic policy this year will be placed within the general framework of the objectives and targets of the Fifth Emergency Plan.

In our short-term policies special emphasis will be given to achieving greater economic stability and eliminating the various arrangements which create rigidities in our economic system, leave the door open for the possible creation of destabilisation problems in the future and constitute a factor impeding our further development drive.

In the fiscal sector our efforts will be focussed on the one hand on tackling the structural causes for the existence of a high fiscal deficit and on the other on modernising the operation of the public service so that to contribute more actively to the growth and technological upgrading of our economy. These two targets are to a great extent interlinked and supplementary to each other.

The measures we shall promote this year in the field of public expenditure will aim both at reducing the rate of growth of consumption expenditure and at the medium-term improvement of the structure of the overall public expenditure, by increasing the percentage of expenditure for economic and social infrastructure.

The various measures taken in 1986 to cut down expenditure for the operation of the public service, which have already started yielding results, will continue to be in force. Particular emphasis will be given to the continuation of the work of the Special Technical Committee which has undertaken to study in detail the whole spectrum of each Ministry's expenditure. On the basis of the suggestions of this Committee savings have already been made in various votes of the State Budgets.

In addition to these measures, the nature of which is such that the results cannot be spectacular, intensive and continuous negotiations, in cooperation with the civil service employees' organisation, are going on for the introduction of measures which will help reverse the existing structural trend, which is that the state employees' salaries increase in real terms at a rate faster than the growth of national productivity, and also for the modernisation of the civil service. Such measures are the decrease of salary scales for newcomers in the civil service and generally the harmonisation of the structure of salaries in the public service with that in force in the private sector of the economy, the implementation of interchangeability and readjustment of working hours, the constant improvement of the functioning of the public service and the creation of greater mobility between services, so that understaffing in one sector may be covered by available staff in other sectors. Also, additional measures will be taken to increase efficiency and speed up and simplify procedures, so that the public may be served better and more effectively, while at the same time the effort launched last year for more extensive use of modern technology and computers will be continued. Finally, the Government will continue taking all necessary measures to tackle decisively and radically the cases of breaches of the law, exploitation of post and negligent execution of duty, which, though applying to a small minority of civil servants, create, wrongly of course, negative impressions about civil servants as a whole. For the greater rationalisation of public expenditures, the Government will continue to study measures to harmonise the various subsidies, grants and financing and other schemes in accordance with the priorities set by the new Action Plan.

There is no intention to introduce new tax laws this year or to increase existing tax rates with a view to increasing the tax revenue of the state except that concerning the strengthening of the Defence Fund. All possible measures will, however, be taken for a more effective implementation of tax laws, particularly by combatting tax evasion and by the speed and more effective collection of taxes due. I hope that the House will soon enact into laws the two relevant bills pending before it so that the Inland Revenue Department may be given the necessary powers. In parallel, a series of administrative and procedural measures are being taken with a view to improving the performance of the Inland Revenue and Customs Departments.

The Government will continue its efforts to persuade the House to pass measures for the increase of the revenue of the Defence Fund. You are all aware of the tremendous needs in this vital field, which is directly linked to the prospects for survival on this land watered by the sweat and blood of our ancestors for thousands of years, and for this reason I

confine myself to merely expressing the warm request that all parties in the House approach this matter with the necessary sense of responsibility and to stressing once again that it is impossible to meet these needs by savings in other fields without affecting considerably either the developmental or the social role of the state. I wish to underline that the present economic reality is such that it makes it possible for us to reinforce our defence without lowering our truly enviable standard of living.

The Government intends in 1987 to introduce to the House a bill enabling Municipalities to raise the necessary funds to meet their expenditure as an essential consequence of the implementation in practice of the democratic principle of local government as this is implemented in politically and economically advanced countries.

During the year under review, the Government services concerned will go ahead with a study and codification of our whole tax system for the purpose of proposing reforms that would make it simpler, fairer and more up to date and more in line with our development requirements. The revision of the structure and philosophy of our tax system becomes necessary also as a result of the process for customs union with the EEC and the need that will arise for the introduction of a new tax on consumption, such as the value added tax, to offset losses in tax revenue that would result from the gradual abolition of import duties. The introduction of the value added tax will be combined with the reduction and/or abolition of other taxes so that low income groups will not be burdened as a result of changes in the system.

In the incomes policy field efforts will be stepped up to implement the principle that the increase of incomes of all kinds should be confined within the limits of the increase in productivity, a principle that unfortunately has not yet been implemented despite the unanimous, at least theoretical, support by all productive groups. Implementation of this principle is an indispensable precondition not only for the maintenance of economic stability but also for the revival of productive investment and exports and more generally for the upgrading of the economy and the continuation of its unimpeded growth.

In the field of monetary/credit policy the strengthening of economic stability makes it possible for the monetary authorities, despite the excessive increase in the overall liquidity observed in recent years, to adopt a monetary/credit programme that would ensure the financing of the anticipated increase in domestic production. At the same time, various measures to bring up to date the monetary/credit system will start to be promoted in 1987, in accordance with the conclusions and priorities to be adopted within the framework of the new Plan, with special emphasis on

assisting the financing of the activities of the most productive sectors of the economy, investment and export industries and services. Finally, the policy for the maintenance of a stable parity of the Cyprus pound with the weighted average of a basket of currencies will be continued.

Our basic aim in the development field during 1987 is the revival of productive investment with the parallel target of helping boost exports. A basic role in the whole effort will be played by various efforts and measures to attract foreign investment, particularly in advanced technology fields. The Council of Ministers has already made a reassessment of our foreign investment policy. The relevant Council of Ministers' decision clearly defines the fields where foreign capital may invest without the cooperation of local capital, these basically being the fields of advanced technology and the clearly export oriented enterprises in the Larnaca Free Industrial Zone. At the same time, it identifies the saturated fields where only in exceptional cases will permission be granted for participation of foreigners with a share of up to 24% and defines the criteria on the basis of which permission will be given for participation of foreigners with a share of up to 49% in the remaining fields, with the possibility for permission to be granted for higher participation in exceptional cases only. Furthermore, the cabinet decision simplifies and accelerates to a great extent the administrative procedures with special provisions in the case of overseas Cypriots and provides for the setting up of a Foreign Investment Advisory Committee to coordinate the whole policy. I would like to point out that the suggestions adopted were formulated with the cooperation of the organisations of the business community.

With the adoption of our new foreign investments policy and the recent extension in the validity of various incentives, especially the ten-year tax exemption incentive for the manufacturing of new products, which has been extended until April 1990, our institutional framework for encouraging productive investment both by foreign investors and by Cypriots entrepreneurs is significantly improved. The intension of the Government in 1987 is to launch, in full cooperation with the private sector, an intensive campaign to inform business circles abroad of the advantages and incentives provided by Cyprus for the establishment of foreign industries, especially in advanced technology fields. We hope that our campaign will be successful with corresponding positive effects on our economy, particularly in the exports field and the creation of employment opportunities for tertiary education graduates and other skilled labour.

Simultaneously, to encourage productive investment the Government will keep in force in 1987 many other tax and related incentives, such as the immediate depreciation of investment allowance in the manufacturing and agricultural sectors recently extended for one more year, the various

allowances for investments, the carry forward of tax losses practically without any time limit, the incentives for the merging of businesses and for self-financing of investments, tax deductions and exemptions for encouraging the establishment of public companies, the incentives for investments in the Free Industrial Zone, import duty exemptions and refunds, the various state guarantee schemes, etc. The provision of tax incentives and the implementation of the special schemes introduced by the Government for the enrichment of our tourist product will also be continued. The Council of Ministers has furthermore extended until 1997 the validity of tax incentives for offshore companies which would expire in 1987, while other incentives conducive to the development of other export services, such as consultative, legal, accounting and information services, computer programming and educational services, will continue to remain in force.

The current year is expected to see the completion of the study assigned to the Industrial Development Department of the U.K. Commonwealth Technical Cooperation Fund, in cooperation with the Development Bank, for the purpose of indentifying new industrial projects for investment in Cyprus and the preparation of comprehensive feasibility studies. During 1987 an evaluation will be made of the studies prepared by foreign experts for the establishment of an organisation or service to develop technology and promote new investment schemes. At the same time, the Government has asked a group of experts to prepare a study for the restructuring, on a long-term basis, of industrial branches expected to be affected by Cyprus' customs union with the EEC.

The establishment of a Stock Exchange is also expected to help encourage investment and the upgrading of industrial units. In the first quarter of 1987 the Government intends to introduce to the House a bill for the establishment of a Stock Exchange as a public corporation with its own board of directors which will consist by majority of representatives of the private sector and which will be directly supervised by the Government. The Stock Exchange will deal exclusively with stock exchange transactions.

Besides the various measures for the encouragement of investments in new export fields, the appropriate Government services will make every effort to boost exports of goods we are already manufacturing. This effort is expected to be significantly strengthened by the autonomous Export Promotion Organisation which is expected to go into operation this year and which, I wish to reiterate, the Government is determined to set up and have to play a significant role in the export promotion drive. At the same time, the extension for one more year of the increased incentive of

deducting 6% of export earnings from the chargeable income of the exporter will also be helpful.

The Government's investment expenditures will continue to be carried out with the same intensity during 1987 with clearly specified economic and social targets. The South Conveyor and the Chrysochou Valley Irrigation Projects will be further implemented. The execution of the Third Road Development Scheme will also be continued and the implementation of the Fourth Road Development Scheme will commence. A basic element of the latter will be the new Nicosia-Larnaca motorway. Preparations for the construction of the new Limassol and Paphos Hospitals will also be continued. Furthermore, other minor irrigation projects will be continued and various rural development projects, town and village water supply-projects, hospitals upgrading projects, etc, will also be promoted. The various housing and relief projects for the refugees and other afflicted persons will also be continued and criteria for eligibility will be modified so that medium income groups may also be covered.

On this occasion, I should like to express once more our appreciation and thanks to the Government and the people of Greece for their valuable assistance and support not only in the political but also in the economic field. I should also like to thank the United States for the assistance it has been providing to Cyprus through the U.N. High Commissioner for Refugees.

#### PROSPECTS FOR 1987

The prospects for 1987 are encouraging. Despite the upward trend in the price of crude oil, the stability of our economy is expected to remain at satisfactory levels. Thus, the rate of inflation, although expected to show a small increase, is anticipated to continue to be low. Also, the current account deficit is expected to continue to be at low levels, which can be financed by autonomous capital inflows.

The rate of growth of the economy is expected to remain at last years levels. Exports of services, including tourism, are expected to continue their upward trend, contributing to higher rate of growth while exports of goods, after the decline of the last two years, are expected to increase slightly.

It is anticipated that in 1987 conditions of almost full employment will continue to prevail, while it is hoped that productive investments will pick up, as a result of the extension of tax incentives and the intensification of government efforts to attract foreign capital and also the expected reduction in real interest rates that will result from the slight

increase of the rate of inflation. A slight increase is also expected in the production of the manufacturing sector of the economy.

The fiscal deficit is anticipated to remain at about the same level as in 1986, while the country's foreign debt is expected to be reduced in absolute terms.

*Mr. President,*

*Members of the House,*

Apart from the specific problems that emerge from time to time, and this is natural, our economy remains basically sound. Our standard of living is continuously improving at a rate much higher than the average rate of the world economy and this makes the standard of living of our people comparatively better.

If we are to protect and extend these economic achievements there is need for hard work, self-restraint in the claims of the productive groups of the population, as well as cooperation and understanding at all levels. It is also necessary, as I mentioned on other occasions, to eliminate trends such as xenomania, mimicking, consumerism, and short-run profit speculation, which in the last years have become endemic and which not only create problems to our economy but also affect adversely our efforts for survival and for bringing about a just solution to our national problem.

As I also stressed last year from this floor and as shown by the experience of the past, the economic policy of President Kyprianou's Government is not based on rigid ideological doctrines or theoretical approaches. Its basic characteristics are flexibility and adaptability to changing conditions, an above-party approach, constant exchange of views with the productive groups aiming at the finding of the most rational and, if possible, commonly accepted solutions, and serving the general interest of our country. In these difficult times, the joining and the common struggle of all groups and political forces, not only in the national issue but also in the economic sector, are essential prerequisites for the successful outcome of our struggle. Let us not allow political conflicts and party confrontations, particularly this year, to affect negatively our positions and attitudes towards the various economic problems, but let us be guided in our approach to them by the general interest of the country and the people as a whole.

Concluding with these thoughts, I ask for the support and help of all political parties for the success of our efforts in the economic field, and for your positive vote for the three budgets.