

Newsletter Issue 41, October 2020

The topics addressed in this issue of Economic Research are the following: (i) *Economic aspects of COVID-19, numerical illustrations, and policy implications* (ii) *Trends and Disparities in Economic Inequality in Cyprus and the EU*, (iii) *Public Debt Thresholds: An Analysis for Cyprus*, (iv) *Ideas for a Green Economic Recovery of Cyprus*, (v) *Digital Competitiveness Ranking: Cyprus*.

Economic Aspects of COVID-19, Numerical Illustrations, and Policy Implications

The new virus SARS-Cov-2 has caught many governments unprepared. The associated disease COVID-19 has typically given rise to ‘lockdown’ and isolation policies which aim to limit the spread of the virus and safeguard the capacity of medical systems to deal with this new illness. Relevant economic questions, including but not limited to the likely impact of these responses on GDP, arise.

Because the initial confinement of labour and consequent loss of production in the ‘non-essential’ sectors constitute a supply shock, a reasonable first step to understand relevant economic implications and have a stab at ‘forecasting’ the impact on GDP is a production function approach. One such approach is fleshed out and illustrated using details from the Republic of Cyprus. The estimated effects depend on the assumed severity and length of the disease and its impact on the all-important tourist industry. An optimistic scenario is that the impact on GDP for 2020 will be of the order of -9.3%, while a more realistic scenario suggests an impact of -16.8% with a more deleterious effect on government finances. Various associated economic issues are also examined, including how to ‘pay’ for this adverse exogenous shock.

Trends and Disparities in Economic Inequality in Cyprus and the EU

The goal of this paper is to examine the recent trends and disparities in economic inequalities for Cyprus and draw comparisons with the other EU countries for the period 1995-2016. We provide new estimates of intergenerational mobility of education, study the relationship between mobility and income inequality, and investigate trends and inequalities in a range of macro-level and micro-level indicators.

Our findings show that Cyprus is characterized by a relatively high degree of educational intergenerational persistence and moderate levels of income inequality. Recent trends in income inequality show a spike in top income inequality due to the recent economic crisis. We also find that Cyprus follows similar patterns as the EU average but generally lags behind the Nordic countries, especially for social protection benefits and educational outcomes. Finally, our findings show that the relative female labor force participation in Cyprus is similar to the EU average with small negative deviations from the average value for men’s returns to skills and moderate positive deviations for assortative mating. Notably, Cyprus enjoys the second smallest percentage of single-headed households in the EU.

Public Debt Thresholds: An Analysis for Cyprus

In this work, we examine whether a threshold exists in the debt-to-GDP and output growth relationship. Such a threshold exists, however, we find that prior to the threshold level, i.e.

when debt is lower, government spending has a negative impact on the economy, while after it the impact turns positive. When the unemployment rate is used as the threshold variable, we find that government spending has no impact until unemployment reaches 10%, after which a strong positive impact on GDP growth is registered. Overall, the results suggest that while additional government spending can crowd out the private sector when the economy is booming, it can still have a strong positive impact on GDP when unemployment is high. As such, the results highlight the fact that what matters is the timing and not the debt-to-GDP level per se.

Ideas for a Green Economic Recovery of Cyprus

The economic recovery of Cyprus will need substantial financing from national and EU funds and offers a great opportunity for economic policies to drive the transition to a low-carbon and resource-efficient society, by encouraging the development of innovative products and services that will reduce the environmental footprint of the economy and create green jobs for people of diverse skills and education levels. These policies should include generous public investments in electricity grids and sustainable mobility, as well as targeted support – through direct grants and enhanced state guarantees – to private investments which are aligned with the requirements of a circular and zero-carbon economy. In this way the Cypriot economy will get prepared for the transition to a strongly digitalised and environmentally challenging era, with multiple benefits for the living standards of the population.

Digital Competitiveness Ranking: Cyprus

The ©IMD World Competitiveness Center (www.imd.org/wcc) has published the fourth edition of the IMD World Digital Competitiveness Ranking. The Economics Research Centre and the Cyprus Employers and Industrialists Federation act as Partner Institutes of the IMD World Competitiveness Center for this edition by contributing to the collection of the necessary data for Cyprus. In the 2020 Digital Competitiveness Ranking, Cyprus ranked 40th among 63 countries, moving up 14 places compared to 2019. Cyprus registered the largest improvement in the ranking among the 63 countries under evaluation in 2020. Cyprus's position has improved in all three categories that make up the overall digital competitiveness ranking (i.e. knowledge, technology and future readiness), most notably in the categories of knowledge and future readiness.