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The topics addressed in this issue of Economic Research are the following: (i) *Measuring the Economy-wide Impact of the Tourism Industry in Cyprus*; (ii) *Financial literacy for financial resilience: Evidence from Cyprus during the pandemic period*; (iii) *Input Compensation, Inflation and Productivity Growth in Cyprus*; (iv) *Digital Competitiveness Ranking: Cyprus*.

“Measuring the Economy-wide Impact of the Tourism Industry in Cyprus”

Elias Giannakis, Neophyta Empora and Theofanis P. Mamuneas

An input-output (IO) model is combined with Tourism Satellite Account (TSA) statistics to estimate the direct and indirect contribution of the tourism industry to the Cypriot economy. Our analysis indicates that defining tourism as ‘Accommodation and Food’, in the absence of TSAs, underestimates the contribution of the sector to the main macroeconomic performance indicators of the country. The results of the IO multiplier analysis reveal that the ‘Accommodation and Food’ definition of tourism overestimates sector’s value added and employment multiplier effects, while underestimates sector’s gross output multiplier effects. Irrespective of the definition of tourism, the sector in general creates medium-to-high direct and indirect effects to the economy. Finally, our findings reveal the importance of establishing annual TSAs in the country in order to provide a comprehensive and holistic measurement of the sector’s contribution to economic growth.

“Financial literacy for financial resilience: Evidence from Cyprus during the pandemic period”

Panayiotis C. Andreou, Sofia Anyfantaki and Adele Atkinson

This study takes Cyprus as a case country to examine the role of financial literacy for financial resilience in the pandemic period. Responses to the survey questions to assess the level of financial literacy show that in 2021 less than 4 out of 10 respondents had a good financial knowledge proficiency level. The results also show that more than 1 out of 3 Cypriots are financial fragile, i.e., would not have been able to cover an unexpected financial need within a month without borrowing or asking for financial help. Moreover, about 6 out of 10 did not have a rainy-day fund to cover three months living expenses in case of losing their main source of income. The proportions are higher for young, not employed, low-income and larger households, indicating that these subgroups were the least resilient. These findings suggest that many Cypriot households were ill-prepared to face the economic consequences of the COVID-19 pandemic. Most importantly, the findings indicate that financial knowledge proficiency appears as a strong antecedent of one’s proclivity of being financially resilient. An important policy implication of the study’s conclusions is

that financial education could help households to improve their financial resilience and prepare for future shocks.

“Input Compensation, Inflation and Productivity Growth in Cyprus”

Neophyta Empora and Theofanis P. Mamuneas

This report examines the relationship between input compensation, productivity, and inflationary pressures in Cyprus, taking into account the implications of the Cost of Living Allowance (CoLA or ATA in Greek) mechanism. It employs fundamental economic theory to analyze patterns in labour and capital prices and their relationship with productivity growth in Cyprus. This is crucial since the relation between labour income and productivity is a key determinant of the standard of living of the employed population as well as of the distribution of income between labour and capital. Additionally, the report extends its analysis to investigate the relationship between labour income and productivity at the sectoral level. Data are from Eurostat covering the period from 1996 to 2022.

The report begins with the examination of the aggregate economy. The data indicate that the change in the compensation of the inputs fluctuates around the change in the value of their marginal product (nominal productivity). During the period between 2010 and 2016, characterized by financial crisis and substantial wage cuts, labour prices fell behind, and capital prices exceeded their nominal productivity growth. However, estimation results show that over the entire period, input compensation growth matches its nominal productivity growth.

Acknowledging that the overall economy conceals potential discrepancies between input compensation and productivity growth due to aggregation across sectors, a sector level analysis is presented. The sector-level analysis reveals significant heterogeneity, with some sectors experiencing lower labour income growth than productivity growth, while others exhibit the opposite trend. Notably, in sectors like Information & Communication (ICT) and Finance & Insurance wages do not follow the high increase in their labour productivity. Moreover, in the most recent period from 2017 to 2022, the gap between labour income and its nominal productivity growth widened for the ICT sector, and the Industry (except construction) sector's labour compensation growth fell below the change in its nominal labour productivity after 2017. This sector-level analysis underscores the necessity for tailored policies that take into account the unique dynamics within each sector. Attempting to adjust labour compensation at the aggregate level (CoLA) can exacerbate the income inequality across sectors.

The study proceeds by examining the relationship between input compensation, productivity, and inflation and emphasizes the need for caution when adjusting labour prices. The automatic link between wages and inflation has the potential to exacerbate inflationary trends. The CoLA mechanism, by ignoring changes in

productivity, restricts the economy's ability to adapt to economic shocks, thereby undermining its resilience and competitiveness.

Overall, the report underscores the importance of considering productivity growth in labour compensation adjustments and recommends sector-specific policies recognizing compensation and productivity growth variations. Collaboration among policymakers, social partners, and stakeholders is crucial to striking a balance that advances economic efficiency, living standards, and protects against inflation risks.

“Digital Competitiveness Ranking: Cyprus”

Nicoletta Pashourtidou

The ©IMD World Competitiveness Center has published the seventh 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 2023 Digital Competitiveness Ranking, Cyprus ranked 51st among 64 countries, moving down six places compared to 2022. The drop in Cyprus’s position resulted from the deterioration of the country’s performance in all factors under evaluation, namely knowledge, technology, and future readiness.