



Economic Analysis Division

Southeastern Europe & Mediterranean Emerging Market Economies



Bi-Weekly Report

18 - 31 October 2022

Countries in Focus in this Issue:
North Macedonia, Cyprus & Egypt

NORTH MACEDONIA 1

Bank profitability continued to improve in H1:22 on stronger operating income and reduced cost of risk

Against a challenging economic backdrop, bank profitability should come under pressure in the near-term, yet remain healthy

CYPRUS 2

Residential real estate prices continued to increase at a robust pace of 3.9% y-o-y in H1:22, mainly reflecting the pass-through of higher construction costs to buyers as demand remains resilient

The residential market should eventually cool-down in the medium-term, in line with weakening (real) disposable incomes and tightening (global) financing conditions

EGYPT 3

Egypt reaches USD 3bn IMF agreement after free floating its currency, containing the risk of a full-blown balance of payments crisis

APPENDIX:

DETAILED MACROECONOMIC DATA 4

REGIONAL SNAPSHOT: MACROECONOMIC INDICATORS . . . 7

FINANCIAL MARKETS 8

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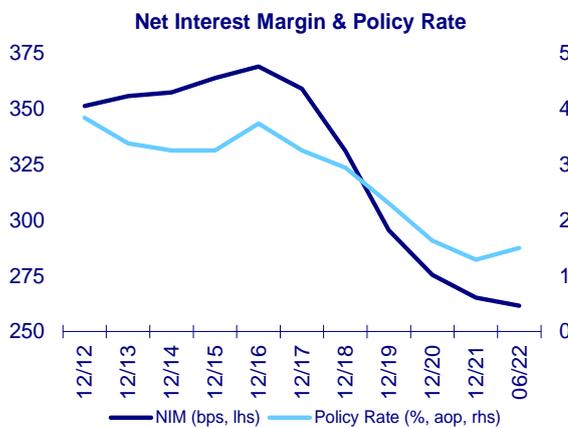
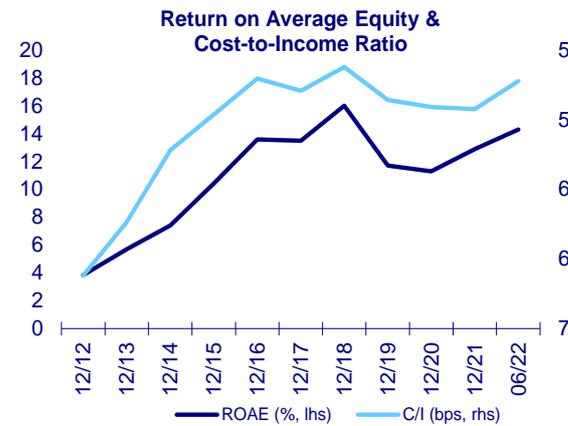
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North Macedonia

BB- / NR / BB+ (S&P / Moody's / Fitch)



Bank profitability continued to improve in H1:22 on stronger operating income and reduced cost of risk. In H1:22, banks' profits surged by 20.2% y-o-y to MKD 5.5bn (equivalent to 0.7% of GDP), with (annualised) ROAE and ROAA strengthening further to 14.3% and 1.7% -- among the highest in the region -- respectively, from 12.6% and 1.5% in H1:21.

Stronger operating income was the main contributor to banks' improved performance in H1:22. Specifically, net interest income (NII) rebounded in H1:22 (up 7.2% y-o-y), in line with faster credit expansion (up 9.8% y-o-y in June, a pace nearly double than that recorded a year ago). Note that, despite rising interest rates (with the NBRNM having raised its key rate by 75 bps in H1:22, to 2.0%), the (annualised) net interest margin (NIM) remained broadly flat at a low of c. 265 bps (still more than double that of EU banks). At the same time, net non-interest income (NNII) continued to grow at a robust pace (up 16.7% y-o-y), driven by net fees and commission income and FX gains.

Stronger top line revenue was partly offset by a broad-based increase in operating expenses, in line with growing inflationary pressures. That said, the annualised cost-to-income ratio improved to c. 52% in H1:22, below that of EU banks (c. 61%).

The further drop in provisioning charges (albeit from an already low base) also gave a small push to banks' profitability in H1:22. Indeed, despite lackluster economic growth and the significant challenges lying ahead (see below), the NPL ratio remained subdued (at 3.2% in June, broadly unchanged since end-2021, due, *inter alia*, to the impact of fast credit expansion), allowing banks to curtail their (annualized) cost of risk to just 23 bps in H1:22 from 32 bps in H1:21.

Against a challenging economic backdrop, bank profitability should come under pressure in the near-term, yet remain healthy.

Under the burden of record-high inflation and rising interest rates, economic growth is set to remain weak in the period ahead. As a result, we see GDP growth moderating to 2.2% in FY:22 from 4.0% in FY:21, bringing the economy back to its pre-COVID-19 levels, albeit with a significant delay compared with its peers. Assuming some easing in inflationary pressures next year, we expect GDP growth to firm slightly to 2.4%.

Against this backdrop, we expect the private sector's repayment capacity to be tested, leading banks to build up provisions at a faster -- yet still controlled -- pace. Importantly, the relatively elevated NPL coverage ratio (standing at 66% in June, above the EU average of 44%) provides a buffer against a potential deterioration in asset quality.

Still, operating income should remain strong, providing a critical contribution to overall profitability. Although credit uptake cannot but be affected by slowing economic growth and tightening financing conditions, NII is unlikely to subside much from current record-high levels, benefitting from rising interest rates. Indeed, in view of banks' still strong liquidity position (with a loan-to-deposit ratio of slightly over 90%) and the large share of demand deposits in total customer deposits (c. 65%), NIM is set to increase in the period ahead, due to faster repricing of loans. Note that the NBRNM is seen raising its key by an additional 200 bps to 4.0% by early-2023.

On the other hand, operating expenses are set to continue rising, weighing on banks' profitability. Indeed, the jump in inflation, together with the continuing digital transformation of the banking system, should keep operating expenses on upward trend in the period ahead.

Importantly, the banking system's strong capitalisation remains strong, with the CAR standing at 17.3%, well above the minimum regulatory threshold of 8.0%, providing a line of defense against potential losses.

	31 Oct	3-M F	6-M F	12-M F
1-m SKIBOR (%)	2.0	2.5	2.8	3.3
MKD/EUR	61.6	61.6	61.6	61.6
Sov. Spread (2028. bps)	551	520	480	400

	31 Oct	1-W %	YTD %	2-Y %
MBI 100	5,655	3.5	-8.1	27.7

	2019	2020	2021	2022F	2023F
Real GDP Growth (%)	3.9	-6.1	4.0	2.2	2.4
Inflation (eop. %)	0.5	2.2	4.9	18.3	4.0
Cur. Acct. Bal. (% GDP)	-3.3	-3.4	-3.5	-6.8	-5.3
Fiscal Bal. (% GDP)	-2.0	-8.2	-5.4	-5.3	-4.6

Sources: Reuters, NBRNM & NBG estimates



Cyprus

BBB / Ba1 / BBB- (S&P / Moody's / Fitch)



Residential real estate prices continued to increase at a robust pace in H1:22, mainly reflecting the pass-through of higher construction costs to buyers as demand remains resilient. Growth in the CBC's Residential Property Price Index accelerated to 3.9% y-o-y in H1:22 from 1.3% on average in FY:21, in line with rapidly rising construction costs, in the aftermath of the jump in global commodity prices, which, nonetheless, have yet to affect demand. The latter appears to have remained strong, despite the unfavourable backdrop (see below) and the expiration of a mortgage subsidization scheme at end-2021, driven by both the domestic (accounting for c. 60% of total property sales) and foreign segments.

Although construction companies have so far absorbed a significant part of rapidly rising (underlying) costs, we believe that their pass-through to final prices has yet to be completed, meaning that residential prices should continue to increase at a solid pace in the short-term. Note that, according to the latest available data, construction costs were up c. 20% y-o-y in H1:22. The improvements in housing energy efficiency carried out under (an already running) state subsidy scheme should increase the value of the housing stock, adding to inflationary pressures. Strong demand from the Ukrainians (estimated at c. 15,000), who have fled to Cyprus, in the wake the Russia-Ukraine conflict, could also give a boost to the domestic market.

The residential market should eventually cool-down in the medium-term. Weakening (real) disposable incomes and tightening (global) financing conditions, together with poor economic sentiment, cannot but eventually take a heavy toll on demand for real estate, especially in view of the already very high household debt in Cyprus (currently standing at over 100% of GDP against a euro area average of slightly less than 60% of GDP). This demand effect should, in fact, outweigh the impact of the envisaged moderation in construction activity (note that building permits have already started to decline on annual basis), leading to a cool-down in the real estate market in the medium-term.

Still, the attractiveness of the sector as an asset class (with rental yields currently standing at c. 6.0-8.0%, above 10-year bond yields -- c. 4.0%), in combination with the liquidity amassed in the form of deposits during the COVID-19 crisis, should have some offsetting impact on the market. The broadening of the scope of the state-sponsored schemes aiming to attract foreign companies to Cyprus (should also help. Note that there has been growing interest recently from companies operating in Russia, Ukraine, and Belarus to relocate in Cyprus, so as to continue their business away from the risks related to Russia.

Importantly, given the significant undervaluation gap in the Cypriot residential real estate market, we expect the envisaged correction in prices to be manageable and not pose any threat to financial stability. According to the latest available data (EC, 2021), the domestic market appears to be undervalued by c. 10% with respect to economic fundamentals (including population, income, interest rates and the housing stock) compared with an (average, unweighted) overvaluation gap of over 10% in the euro area. The same conclusion was reached when assessing deviations of the price-to-income and price-to-rent ratios from their long-term averages.

Importantly, the successful implementation of the planned rent-to-mortgage scheme (still pending approval by the EC, involving primary residences and business premises with a market value below EUR 250,000) for vulnerable borrowers under the state-owned asset management company (KEDIPEs) should limit the risk of excess supply of housing inventory heading to the market. Note that the aforementioned scheme could tackle up to EUR 1.5 bn, or almost 40% of the banking system's NPEs.

	31 Oct.	3-M F	6-M F	12-M F
1-m EURIBOR (%)	1.25	1.65	2.40	2.45
EUR/USD	0.99	1.01	1.01	1.03
Sov. Spread (2025. bps)	192	180	170	140

	31 Oct.	1-W %	YTD %	2-Y %
CSE Index	76.6	1.1	11.6	79.1

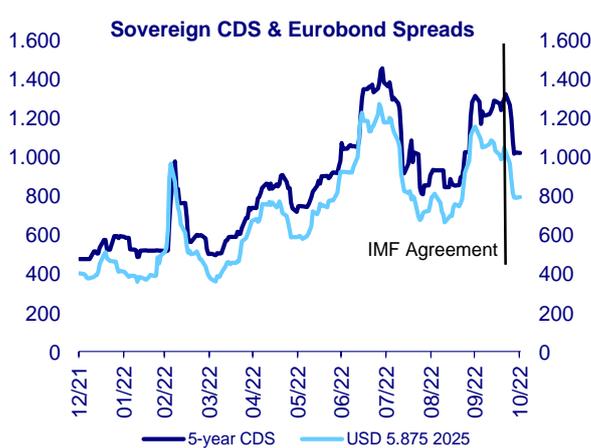
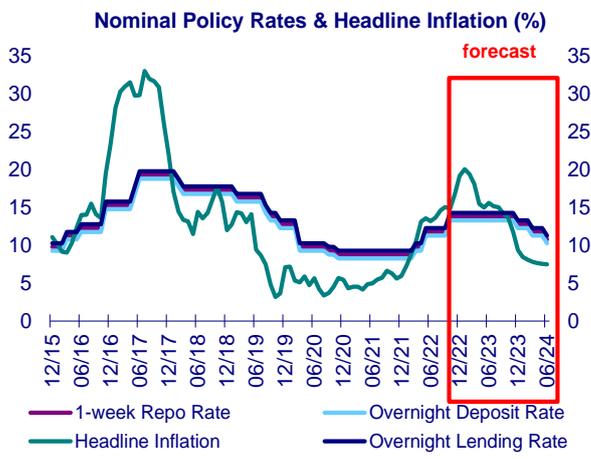
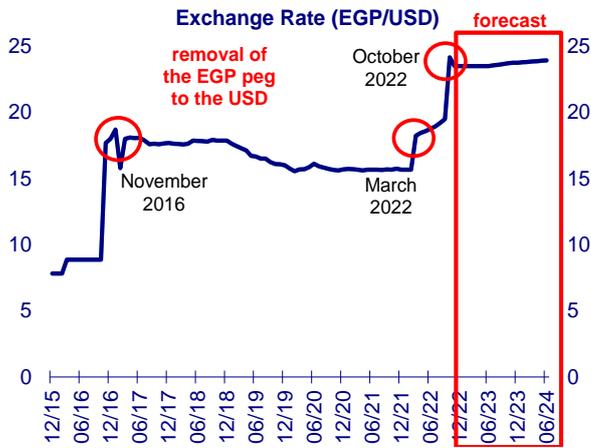
	2019	2020	2021	2022F	2023F
Real GDP Growth (%)	5.5	-4.4	6.6	4.4	1.8
Inflation (eop. %)	0.7	-1.1	4.8	8.5	2.8
Cur. Acct. Bal. (% GDP)	-5.6	-10.1	-6.8	-8.7	-7.1
Fiscal Bal. (% GDP)	1.3	-5.5	-1.7	0.5	0.8

Sources: Reuters, CBE & NBG estimates



Egypt

B / B2 / B+ (S&P / Moody's / Fitch)



Egypt reaches USD 3bn IMF agreement after free floating its currency, containing the risk of a full-blown balance of payments crisis. As expected (see our previous week's [Special Issue](#)), IMF and the Egyptian authorities reached a staff-level agreement on a 46-month USD 3bn Extended Fund Facility Arrangement (EFF) on October 27th -- pending IMF Board approval, expected in December.

The agreement with the IMF came just after the central bank (CBE) announced its shift to a “durable” flexible exchange rate regime. In this context, the EGP lost a massive 13.8% of its value against the USD intraday. Pressures on the EGP have yet to ease, with the EGP currently trading at 24.2 against the USD, widening the y-t-d losses to 35.3% (recall that authorities had devalued the currency by 15.0% in March).

At the same time, the CBE hiked its overnight deposit, 1-week repo, and overnight lending rates by 200 bps to 13.25%, 13.75%, and 14.25%, respectively, aligning with the need to reduce external imbalances and tame inflation expectations. The CBE also committed to: i) gradually phase out import restrictions by end-2022 (recall that the latter were imposed in March to rein in import growth, leading, however, to significant raw material & consumer product shortages); and ii) set-up a derivatives market to deepen FX market liquidity.

According to the IMF, the new EFF is expected to unblock additional financing, including USD 5bn by mid-2023 from international and regional partners (mainly Gulf countries). The Egyptian authorities have also requested financing under the newly created Resilience and Sustainability Facility (RSF) that could unlock up to a further USD 1bn.

The available financing should help the country plug its sizeable external financing gap (estimated at c. USD 10.0bn in FY:22/23). The latter reflects not only the widening current account deficit, following the jump in imported food prices (note that Egypt is the largest global wheat importer), but also a sharp drop in FX financing (involving heavy portfolio withdrawals), due to increased risk aversion worldwide and Fed's tightening.

Besides sticking to a flexible exchange rate regime and continuing with inflation targeting, authorities have also reportedly agreed under the new EFF to carry out a series of reforms aiming at:

i) fiscal consolidation and the reduction of general government debt. In this context, authorities' efforts are expected to focus on improving the efficiency of the tax system (recall that tax revenue currently amounts to a mere 13% of GDP) and streamlining social protection schemes (in a country where 1/3rd of population lives below the official poverty line). Note that, in a bid to mitigate the impact of EGP devaluation, the government has recently announced a temporary 6-month extension of food subsidies, pension increases and a cap in electricity prices until June.

ii) the reduction of the public sector's “footprint” on the economy (with the state accounting for c. 30% of GDP, while employing almost 2 times more workers than the official private sector).

All said, although the weaker EGP should entail some short-term economic pain, it will help reduce external imbalances, securing macroeconomic stability in the long-term, while unlocking the economy's large growth potential. In this context, we see GDP growth almost halving this year (to 3.6% from 6.6% in FY:21/22) with inflation jumping at the same time (to a 5-year high of 16.4% on average this year from 8.4% in FY:21/22). Assuming some easing in price pressures next year, economic growth should rebound (to 5.5%, above the economy's long-term potential of c. 4.5%) and the current account start narrowing to more sustainable levels.

	31 Oct.	3-M F	6-M F	12-M F
O/N Interbank Rate (%)	13.4	13.4	13.4	12.4
EGP/USD	24.15	23.90	23.65	23.70
Sov. Spread (2029, bps)	1,036	900	800	500

	31 Oct.	1-W %	YTD %	2-Y %
HERMES 100	1,259	7.4	-1.6	18.7

	19/20	20/21	21/22E	22/23F	23/24F
Real GDP Growth (%)	3.6	3.3	6.6	3.6	5.5
Inflation (eop. %)	5.6	4.9	13.2	15.6	7.5
Cur. Acct. Bal. (% GDP)	-3.1	-4.6	-3.7	-3.6	-2.8
Fiscal Bal. (% GDP)	-7.9	-7.4	-7.2	-6.8	-6.2

Sources: Reuters, IMF, CBE & NBG estimates



DETAILED MACROECONOMIC DATA

NORTH MACEDONIA					
	2019	2020	2021	2022f	2023f
Real Sector					
Nominal GDP (EUR million)	11,274	10,657	11,754	13,678	15,309
GDP per capita (EUR)	6,074	5,772	6,399	7,477	8,402
GDP growth (real, %)	3.9	-6.1	4.0	2.2	2.4
Unemployment rate (% aop)	17.3	16.4	15.7	14.5	14.5
Prices and Banking					
Inflation (% eop)	0.5	2.2	4.9	18.3	4.0
Inflation (% aop)	0.8	1.2	3.2	13.9	9.3
Loans to the Private Sector (% change, eop)	6.1	4.7	8.0		
Customer Deposits (% change, eop)	9.8	6.2	8.5		
Loans to the Private Sector (% of GDP)	48.9	54.1	53.0		
Retail Loans (% of GDP)	24.9	28.4	27.7		
Corporate Loans (% of GDP)	24.0	25.7	25.2		
Customer Deposits (% of GDP)	55.5	62.3	61.2		
Loans to Private Sector (% of Deposits)	88.1	86.8	86.5		
Foreign Currency Loans (% of Total Loans)	41.5	41.6	40.7		
External Accounts					
Merchandise exports (EUR million)	5,347	4,817	5,996	6,518	6,965
Merchandise imports (EUR million)	7,296	6,622	8,371	9,630	10,165
Trade balance (EUR million)	-1,949	-1,805	-2,375	-3,112	-3,201
Trade balance (% of GDP)	-17.3	-16.9	-20.2	-22.8	-20.9
Current account balance (EUR million)	-0,368	-0,366	-0,416	-0,937	-0,814
Current account balance (% of GDP)	-3.3	-3.4	-3.5	-6.8	-5.3
Net FDI (EUR million)	0,363	0,155	0,435	0,522	0,588
Net FDI (% of GDP)	3.2	1.5	3.7	3.8	3.8
International reserves (EUR million)	3,263	3,360	3,665	3,515	3,615
International reserves (Months ^a)	4.6	5.3	4.6	3.8	3.7
Public Finance					
Primary balance (% of GDP)	-0.8	-7.0	-4.1	-4.0	-3.3
Fiscal balance (% of GDP)	-2.0	-8.2	-5.4	-5.3	-4.6
Gross public debt ^b (% of GDP)	48.8	60.5	60.3	61.7	61.5
External Debt					
Gross external debt (EUR million)	8,154	8,536	9,547	10,669	11,329
Gross external debt (% of GDP)	72.3	80.1	81.2	78.0	74.0
External debt service (EUR million)	2,468	3,300	3,550	3,300	3,700
External debt service (% of reserves)	75.6	98.2	96.9	93.9	102.4
External debt service (% of exports)	35.4	52.7	45.9	38.7	40.4
Financial Markets					
28-d CB bill rate (% eop)	2.3	1.5	1.3	3.8	4.0
28-d CB bill rate (% aop)	2.3	1.6	1.3	2.3	4.0
1-Y T-bill rate ^c (% eop)	0.6	0.4	0.5	2.8	3.2
Exchange rate: EUR (eop)	61.4	61.6	61.6	61.6	61.6
Exchange rate: EUR (aop)	61.4	61.6	61.5	61.6	61.6

f: NBG forecasts; a: months of imports of GNFS; b: incl. guaranteed debt; c: primary market



CYPRUS					
	2019	2020	2021	2022f	2023f
Real Sector					
Nominal GDP (EUR million)	23,176	21,895	24,019	27,193	28,798
GDP per capita (EUR)	26.278	24.546	26.677	29.874	31.293
GDP growth (real, %)	5.5	-4.4	6.6	4.4	1.8
Unemployment rate (% aop)	7.1	7.6	7.5	6.6	6.5
Prices and Banking					
Inflation (% eop)	0.7	-1.1	4.8	8.5	2.8
Inflation (% aop)	0.3	-0.6	2.4	8.4	4.1
Loans to the Private Sector (% change, eop)	-7.4	-5.6	-5.0		
Customer Deposits (% change, eop)	0.0	-0.6	5.4		
Loans to the Private Sector (% of GDP)	132.1	132.0	114.3		
Retail Loans (% of GDP)	60.9	61.2	50.9		
Corporate Loans (% of GDP)	71.2	70.8	63.5		
Customer Deposits (% of GDP)	178.7	188.0	180.7		
Loans to Private Sector (% of Deposits)	73.9	70.2	63.3		
Foreign Currency Loans (% of Total Loans)	---	---	---		
External Accounts					
Merchandise exports (EUR million)	3,080	2,969	3,590	4,041	4,011
Merchandise imports (EUR million)	7,711	7,180	7,907	9,267	9,227
Trade balance (EUR million)	-4,631	-4,211	-4,318	-5,226	-5,216
Trade balance (% of GDP)	-20.0	-19.2	-18.0	-19.2	-18.1
Current account balance (EUR million)	-1,288	-2,202	-1,638	-2,357	-2,041
Current account balance (% of GDP)	-5.6	-10.1	-6.8	-8.7	-7.1
Net FDI (EUR million)	817.0	7,454	4,369	4,369	5,571
Net FDI (% of GDP)	3.5	34.0	18.2	16.1	19.3
International reserves (EUR million)	---	---	---	---	---
International reserves (Months ^a)	---	---	---	---	---
Public Finance					
Primary balance ^b (% of GDP)	3.5	-3.4	0.1	2.3	2.5
Fiscal balance ^b (% of GDP)	1.3	-5.5	-1.7	0.5	0.8
Gross public debt (% of GDP)	90.4	113.5	101.0	88.0	83.0
External Debt					
Gross external debt (EUR million)	194,036	190,427	192,715	188,500	186,500
Gross external debt (% of GDP)	837.2	869.7	802.3	693.2	647.6
External debt service (EUR million)	---	---	---	---	---
External debt service (% of reserves)	---	---	---	---	---
External debt service (% of exports)	---	---	---	---	---
Financial Markets					
Policy rate (ECB refinancing rate, % eop)	0.0	0.0	0.0	2.5	2.8
Policy rate (ECB refinancing rate, % aop)	0.0	0.0	0.0	0.7	2.7
3-Y T-bill rate (% eop)	-0.1	-0.1	-0.2	2.6	3.0
Exchange rate: USD (eop)	1.121	1.221	1.137	1.010	1.030
Exchange rate: USD (aop)	1.119	1.142	1.183	1.050	1.020

f: NBG forecasts; a: months of imports of GNFS; b: cash basis



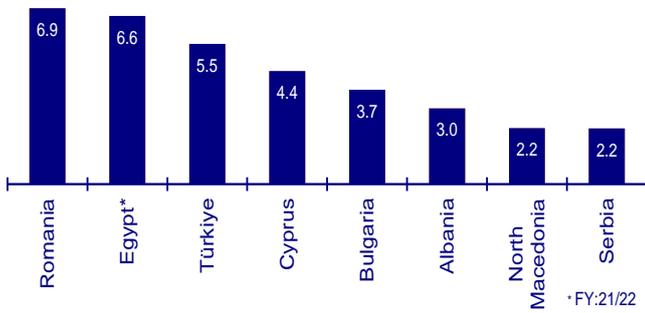
EGYPT					
	2019/20*	2020/21*	2021/22e*	2022/23f*	2023/24f*
Nominal GDP (USD million)	364,957	403,994	445,569	396,500	433,825
GDP per capita (USD)	3.628	3.926	4.245	3.704	3.973
GDP growth (real, %)	3.6	3.3	6.6	3.6	5.5
Unemployment rate (% aop)	8.3	7.3	7.3	7.2	7.1
Prices and Banking					
Inflation (% eop)	5.6	4.9	13.2	15.6	7.5
Inflation (% aop)	5.7	4.5	8.4	16.4	10.5
Loans to the Private Sector (% change, eop)	19.5	21.2	23.6		
Customer Deposits (% change, eop)	16.5	19.2	24.7		
Loans to the Private Sector (% of GDP)	24.8	27.8	29.7		
Retail Loans (% of GDP)	7.6	8.9	9.5		
Corporate Loans (% of GDP)	17.2	18.9	20.2		
Customer Deposits (% of GDP)	67.6	74.4	80.2		
Loans to Private Sector (% of Deposits)	36.8	37.4	37.1		
Foreign Currency Loans (% of Total Loans)	15.9	12.7	11.3		
External Accounts					
Merchandise exports (USD million)	26,376	28,677	43,906	50,785	58,078
Merchandise imports (USD million)	62,841	70,736	83,082	95,524	105,868
Trade balance (USD million)	-36,465	-42,060	-43,396	-44,739	-47,790
Trade balance (% of GDP)	-10.0	-10.4	-9.7	-11.3	-11.0
Current account balance (USD million)	-11,167	-18,436	-16,551	-14,437	-12,280
Current account balance (% of GDP)	-3.1	-4.6	-3.7	-3.6	-2.8
Net FDI (USD million)	7,102	4,835	8,591	10,309	11,856
Net FDI (% of GDP)	1.9	1.2	1.9	2.6	2.7
International reserves (USD million)	38,202	40,584	33,376	35,376	37,876
International reserves (Months ^a)	6.7	6.5	4.2	4.1	3.9
Public Finance					
Primary balance (% of GDP)	1.8	1.5	0.7	0.3	0.3
Fiscal balance (% of GDP)	-7.9	-7.4	-7.2	-6.8	-6.2
Gross public debt (% of GDP)	87.2	91.8	91.7	98.0	99.2
External Debt					
Gross external debt (USD million)	123,491	137,860	160,000	175,000	188,000
Gross external debt (% of GDP)	33.8	34.1	35.9	44.1	43.3
External debt service ^b (USD million)	16,100	18,500	22,600	26,300	33,100
External debt service ^b (% of reserves)	42.1	45.6	67.7	74.3	87.4
External debt service (% of exports ^c)	36.5	45.0	35.1	36.0	40.1
Financial Markets					
Policy rate (O/N deposit rate, %, eop)	9.3	8.3	11.3	13.3	10.3
Policy rate (O/N deposit rate, %, aop)	11.9	8.5	8.9	12.4	11.8
3-M T-bill rate (% eop)	13.3	13.2	15.4	17.0	14.5
Exchange rate: USD (eop)	16.11	15.66	18.76	23.50	24.00
Exchange rate: USD (aop)	16.04	15.70	16.45	22.30	23.75

*: fiscal year starting in July and ending in June; f: NBG forecasts; a: months of imports of GNFS

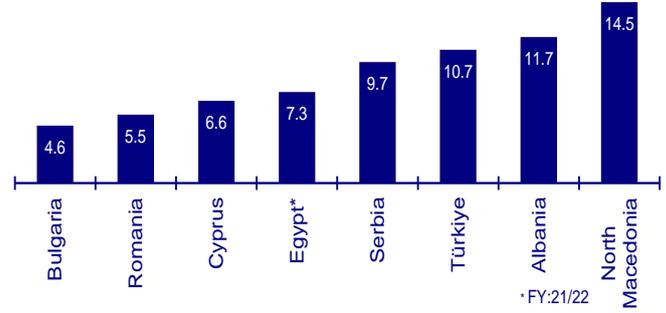


REGIONAL SNAPSHOT: MACROECONOMIC INDICATORS

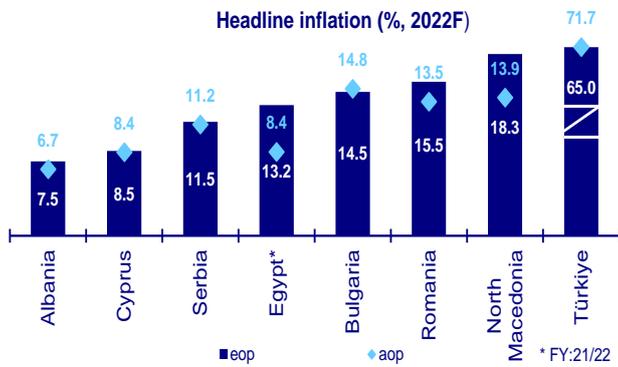
Real GDP Growth (% , 2022F)



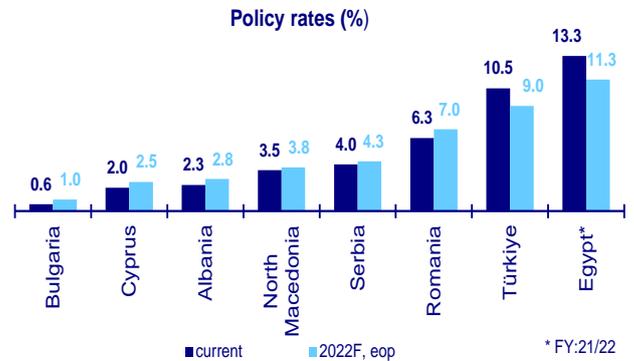
Unemployment (% , 2022F, aop)



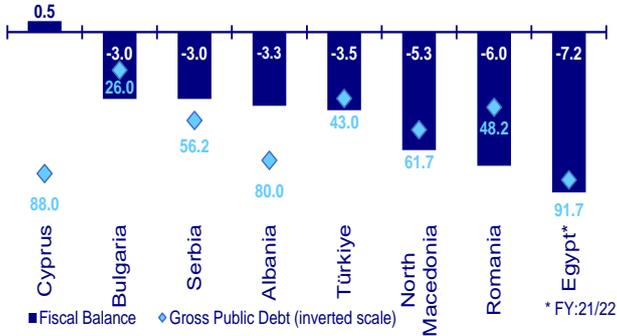
Headline inflation (% , 2022F)



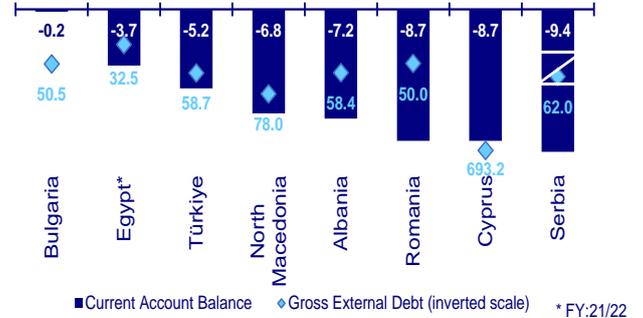
Policy rates (%)



Public Finance (% of GDP, 2022F)



External Accounts (% of GDP, 2022F)

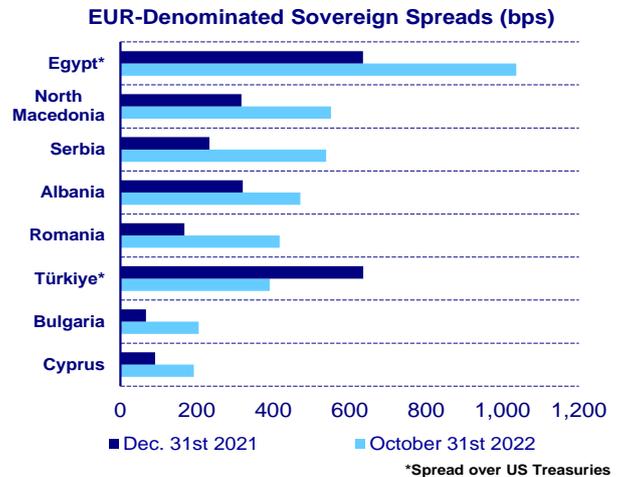
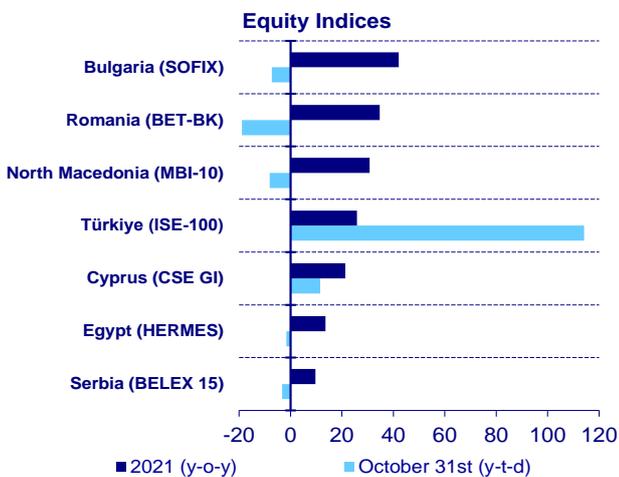
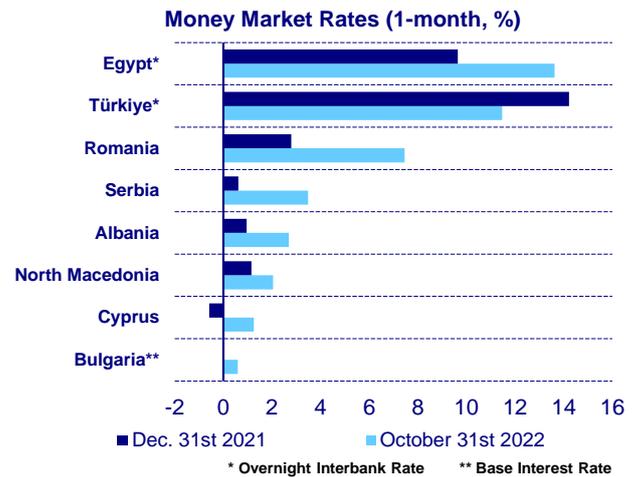
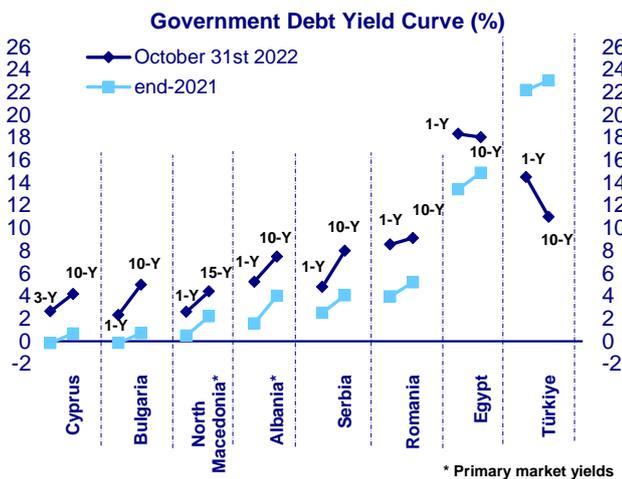
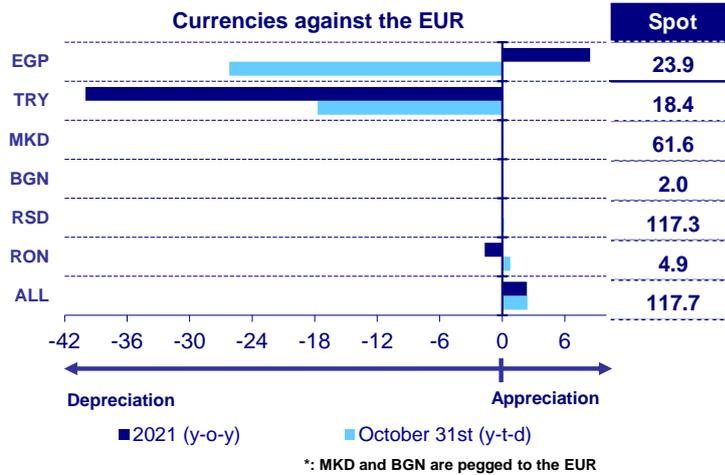


FX Reserves (Months of Imports, 2022F)





REGIONAL SNAPSHOT: FINANCIAL MARKETS



Sources: Reuters & NBS estimates



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