The International Cyprus Funds Summit in May 2016

By Mr. Angelos M. Gregoriades, BSc, FCA
President of CIFA

Following the success of the Cyprus Funds Summit last October, CIFA is organizing a second Cyprus Forum to take place on 30 and 31 May, 2016 in Limassol, which aims this time to be an international event and attract participants from abroad.

The event is supported by the European Fund and Asset Management Association (EFAMA) and is under the auspices of the Ministry of Finance. The Minister of Finance will also honour us with his presence.

The Forum will address among others - the introduction of more stringent regulations, increasing compliance requirements and enhanced duties for key players, such as the asset manager and depositary and the importance of conforming to conformity – the EU initiatives in promoting alternative funding sources which will complement existing and traditional funding routes and the new cross-border fund vehicles and innovative forms of business financing, such as loan originating funds and ELTIFs – the main developments in key fund centres – how asset managers need to adapt their business and operations to investor demands and find new distribution channels.

This conference is an ideal meeting point in view of the location of Cyprus for asset managers, lawyers and other industry representatives from Europe and the EMEA region in particular, as attendance will constitute a prime opportunity to be updated on the recent developments in Europe and future challenges both from a market and regulatory perspective.

Attendees will benefit from the experience of speakers from the largest investment fund centres in Europe, who will be presenting the regulatory landscape and in particular the main developments in such fund centres.

Peter De Proft, the Director General of EFAMA, will be one of the key speakers and shall be introducing the current challenges for the asset management sector in the context of the Capital Markets Union and the retail financial services.

Evelyne Christiaens, Head of the Legal and Tax Department of the Association of the Luxembourg Fund Industry (ALFI), will present the recent regulatory developments in Luxembourg, including among others, available fund structures in Luxembourg; a new fund vehicle type, the Reserved Alternative Investment Fund and its
proposed main features and place in the alternative fund environment; the ELTIF (European Long Term Investment Funds) Regulation and its implementation in Luxembourg and other legislative developments (UCITS V implementation law, further initiatives of the Luxembourg legislator / regulator).

Ms. Sheila E. Nicoll, who has since June 2014 been heading the Public Policy at Schroders plc, one of Europe’s largest asset managers, and also served as a Director of conduct policy of the UK Financial Conduct Authority (formerly the Financial Services Authority) from October 2009 to April 2013, will be sharing her expertise in issues of public policy and regulation from a UK perspective.

The impact of MiFID II on investment funds and distribution: MiFID II and the PRIIP KID bring increased organisational and transparency requirements for fund distributors and managers. Managers will need to put in place a product governance process and specify the target market for each fund while current commission/retrocession practices will change. Further, managers will have to navigate an increasingly complex and evolving fund distribution landscape. Julie Patterson, Head of the Regulatory Centre of Excellence for Investment Management Regulation at KPMG UK, will share her experience and broad knowledge of the different fund and distribution structures around the EU, acquired through many years of working with EFAMA.

The importance of having robust compliance will be a theme addressed by Mr. Botopoulos, former Chairman of the Hellenic Capital Market Commission, Member of the European Securities and Markets Authority (ESMA) Board of Supervisors, Member of the ESMA Management Board, and Chairman of the ESMA Market Integrity Standing Committee dealing with cooperation, exchange of information and market surveillance. He was responsible for the capital markets legislative package during the Greek Presidency of the European Union (first semester 2014), and Chairman of the working group on the Benchmark Regulation.

Among other subjects that will be addressed are the key trends and new product opportunities in the fund industry; the role of the Depositary who has become a central figure in UCITS and AIF structures, following the recent EU developments that evolved the role and duties of the “custodian” and required Depositaries to re-assess their operational risk, pricing and interaction with other industry participants.

Representatives of the Big Four audit firms as well as reputable international law firms will also be present.

The role that Cyprus can play due to its proximity to other continents, while being a Member State of the EU will be emphasized. There will be an update on proposed changes to our legal and tax funds framework which will address in particular the proposed introduction of “unauthorized structures” following the initiatives of Luxembourg and Malta in this respect whose aim is to synchronise the fund regime with the new EU regulatory focus, which has moved from “product supervision” to “management supervision”, as well as the introduction of a new form of Limited Partnership with legal personality.

It is expected that a significant level of expertise and experience will be gathered together both from the panel discussions and the audience. The message is the readiness to share knowledge and ideas which highly valuable and needed.

CIFA aims at establishing this Funds Summit as an annual event. Mark the date on your calendars and pass on the message; do encourage fund managers and other interested parties to support us in this event. We hope to see you all there!!

Mr. Angelos Gregoriades, BSc, FCA, is the Chairman and Head of Tax and Corporate Services of KPMG in Cyprus. He is also President of CIFA, and a Member of the Board of the Cyprus Investment Promotion Agency (CIPA). Mr. Gregoriades holds a degree in Accounting and Finance from the London School of Economics, and is a Fellow Member of the Institute of Chartered Accountants of England and Wales.
Cyprus: Exit from the Economic Adjustment Programme and current challenges

By Mr. Omiros Pissarides
Executive Director and Group General Manager, AXIA
Board Member of CIFA

Albeit recent, expressing in a few lines the intense agony that was widespread in Cyprus and the resulting pain that was experienced in March 2013 is rather difficult. At the time, the country suffered the first deposits’ impairment (bail-in) in the Eurozone and had a newly-elected Government in office that seemed overwhelmed by the intensity of the issues at hand. Quite rightfully so; with the country’s second biggest bank, Cyprus Popular Bank, shut overnight to be folded together with its Emergency Liquidity Assistance (ELA) standing at a massive 60% of the country’s GDP, into Bank of Cyprus, the strain was soaring. Add to that a GDP already in negative territory, a debt to GDP trajectory well beyond the original Maastricht Treaty criteria, continuous downgrades from credit rating agencies and an effective lockout from international bond markets due to unduly punitive interest rates and one could effortlessly refer to what has been described as the ‘perfect storm’. Indeed, the combination of the sovereign and banking crises working in parallel created such a negative economic spiral that simply proved too much for the island nation’s economy to handle.

Whether Cyprus’ allies in Europe could have done more to assist will probably remain an unanswered question in the foreseeable future. And while this question may be rather rhetoric, one clear fact can easily be deduced; countries that cannot be considered systemic should not expect to receive what may once have been considered their ‘rightful access’ to assistance as part of the wider Euro club. Whether Cyprus’ allies in Europe could have done more to assist will probably remain an unanswered question in the foreseeable future. And while this question may be rather rhetoric, one clear fact can easily be deduced; countries that cannot be considered systemic should not expect to receive what may once have been considered their ‘rightful access’ to assistance as part of the wider Euro club.

Fast forward to today and clearly the situation is vastly different. Indeed, comparing to 2013 one can easily determine that the economic realities appear completely diverse. Cyprus has just exited its three year Troika-led Economic Adjustment Programme (EAP) with very positive reviews and, in most respects, has proved to be a model bailout student; it has absorbed less than the original amount of funding allocated in the programme (about 75% of the EUR10bn), while ending the agreement with the IMF two months ahead of the original plan.

Moreover, the economy has returned to growth (figure 1), unemployment seems to be pursuing a downward trend from its 2014 high of 16%, the sovereign has already tapped the international bond markets a number of times (in October 2015 it achieved its lowest ever coupon for a 10-year sovereign bond), its debt levels against GDP are lower than originally expected (figure 1) and the current account is almost in balance. And with statements such as ‘the completion of the programme is not the end of the road but it is a new beginning’ by the highly praised Minister of Finance, Harris Georgiades, it is not difficult to comprehend the Eurogroup and IMF satisfaction on the conclusion of the Cyprus EAP. In separate statements, Eurogroup’s President, Jeroen Dijsselbloem, acknowledged that “the overall programme agreements have been essential to fiscal performance that has exceeded expectations”, while IMF Managing Director, Christine Lagarde,
congratulated Cyprus’ accomplishments under the EAP “which have delivered an impressive turnaround of the economy during the past three years”. At the same time, the global credit rating agencies have been responding positively to Cyprus’ achievements; their country credit ratings are indicating a return from the bottom scenario (figure 2), at a time when the sovereign’s cost of borrowing is declining, a far outcry from the double digit figures that peaked in 2013.

Figure 1: GDP Growth and Debt/GDP Evolution

Source: S&Ps, March 18, 2016

Complacency, however, is not a choice. Deep challenges remain. Cyprus has evidently been successful in terms of achieving sustainability of public finances but, when it comes to structural reforms, its record is more mixed. While commercialization of the Limassol Port seems to be well on track, an effective removal of the privatization of the Electricity Authority of Cyprus from the agenda has taken place and difficulties are experienced to vote through Parliament the first steps towards the privatization of the Cyprus Telecommunications Authority. As we approach the Parliamentary elections of May, in the absence of the EAP’s safety shield, pressures against much-warranted reforms will become more felt and will reverberate through the economy. At the same time, the waiver that Cyprus received as part of the EAP towards participating in the European Central Bank’s (ECB) Quantitative Easing (QE) programme has been terminated. Whether Cyprus will experience a rising cost of borrowing as a result of ECB’s inability to buy its bonds remains to be seen, taking into account that the sovereign has set aside sufficient funds and is faced with no outsize debt repayments over the next three years (figure 3).

Figure 2: Cyprus’ Sovereign Ratings evolution

Source: Moody’s, S&Ps

This point was also picked up by Fitch Ratings Agency which, in its March 16, 2016 statement, mentioned that Cyprus does not need QE support to tap the markets, potentially conveying a positive signal for a further upgrade of the economy in the medium-term.

Beyond local politics and a perceived risk of higher sovereign borrowing rates, there is a more immediate problem to tackle relating to the banks. While financial sector stabilization has been achieved to a significant extent, in large part due to the equity participation of international investors in Bank of Cyprus and Hellenic Bank and the sovereign’s participation in the Cooperative banks, the pervasive issue of the unduly high non-performing loans (NPLs) remains. Despite reaching a peak in deterioration of the banking sector’s asset quality, system NPLs are currently standing tall at around 57.5%. Whereas the banks’ reserve coverage has increased from 33% in 2014 to 38%, the remaining balance is covered by tangible collateral and enforcement and adoption of new legislation on foreclosures and insolvency.

Figure 3: Maturity of Cyprus General Government Debt

Source: Ministry of Finance, December 31, 2015
procedures will improve the capacity to manage NPLs, the process of cleansing the banks’ balance sheets will not be either an easy or a short one. What is certain is that, in the absence of more resolute measures, NPLs will continue to act as a drag on the capacity of the banks to fulfill one of their key tasks, that of financing the economy and fuelling its growth with a corresponding harmful impact on employment.

Overall, challenges remain and Cyprus is not out of the woods yet. However, Cyprus has achieved a lot over the past three years and is entitled to confront the future with optimism. Importantly, before the risk of economic collapse, Cyprus has reaffirmed, like never before, its ability to manage the most difficult of storms. And it has a lot going for it right now; a resilient business services sector, record tourism inflow and significant capital injections as a result of new investments in the pipeline (including an integrated casino resort and other large scale real estate developments). It also rides a positive wave, having successfully emerged from the programme amid strong relations with the IMF and the World Bank and experiencing political momentum towards a solution of the Cyprus problem. In addition, the potential development of its natural reserves may expand its geopolitical role and its capacity to exert higher regional influence over and above any direct revenue stream. But above all, Cyprus’ people seem to understand what is at stake. Assuming a different stance from other programme countries, which are either enduring ongoing economic and political setbacks or an inability to reach political consensus despite successful programme exits, Cypriots seem, for the most part, mature enough to reward their politicians that have taken painful but much-needed decisions.

In conclusion, when it comes to biting the bullet and achieving what was considered impossible just three years ago, Cyprus has come a long way. It has managed to regain much of its economic credibility and, armed with the wisdom of transforming past mistakes into future lessons, it now has the capacity and opportunity to achieve much more in the face of regional and global economic and political turmoil. It remains to be seen whether it has the will and the conviction to continue on the right path. The choice, as always, belongs to us.

Mr. Omiros Pissarides joined AXIA in September 2010 and holds the positions of Executive Director, Group General Manager and Head of the Company’s Headquarters in Cyprus. With presence in five countries (Cyprus, Greece, Portugal, UK and USA) and plans for further expansion, AXIA is one of the region’s most dynamic and renowned investment banks. Mr. Pissarides possesses more than 15 years experience in Cyprus and abroad, having served as Regional Channel Manager for Middle East, Africa and Pakistan of Nasdaq-quoted Intermec Technologies and General Manager of Logicom for the GCC countries and Pakistan. Omiros has also worked for Arthur Andersen. He holds a Bachelor Degree in Economics and Accounting from Hull University and an MBA from Imperial College. Mr. Pissarides also sits on the Board of CIFA and the Cyprus Institute of Neurology and Genetics.

New investment opportunities in Iran

By Mr. Costas Markides
Board Member, International Tax, KPMG Limited

The impact of sanctions on Iran’s economy

A historic diplomatic agreement reached on July 14, 2015 between Iran and the permanent members of the UN Security Council to tightly regulate Iran’s nuclear development program in exchange for sanctions relief, came into force on January 16, 2016. The door for the much needed inbound foreign investment in an ailing economy and an energy industry that is in need of infrastructure modernization, technical knowhow and technology, has been slowly but steadily opening to the world.

This article aims to provide a general overview of the Iranian economy prior to and after the lifting of the international sanctions. In doing so, we will assess the opportunities that may arise by the lifting of the sanctions, since foreign direct investment, which had declined by billions of dollars following the tightening of sanctions in 2012, is expected to pick up.
The Iranian economy has been stagnated by years of sanctions. As a result of the sanctions, foreign investors have been hesitant to invest in a secluded Iranian economy with a financial system that misallocated and mispriced capital. Iran’s banks were unable to operate without government direction and with no suitable regulatory oversight to promote sound risk management.

Lifting sanctions related to Iran’s nuclear program will have a significant impact on the world oil market, the Iranian economy and Iran’s trading partners. Iran’s total return to the global markets is expected to add a million barrels of oil per day thus lowering oil prices by an estimate of USD 10 per barrel in 2016, according to the World Bank, which also expects economic growth in the country to surge to approximately 5% in comparison to 3% in 2015. The end of Iran’s near economic collapse as a result of international isolation is expected to allow the country to stand on its feet in the short term and regain financial stability in the long term.

**Iranian sanction relief implications**

The international sanctions have cost Iran more than USD 160 billion in oil revenue in the last few years alone. Once they are fully lifted, the country will be able to resume selling oil on international markets and using the global financial system for trade. Iran has the fourth largest oil reserves in the world and the energy industry is braced for lower prices. The lifting of energy sanctions means Iran could increase its revenue from oil exports to USD 10 billion (GBP 6.9 billion) by 2017. With the lifting of sanctions, Iran will be able to export as much crude oil to the world as it can, or as much as it can find demand for.

In addition, there are estimates that Iran holds approximately USD 100 billion worth of frozen assets overseas, of which an estimated USD 29 billion will be released immediately.

**Foreign investment opportunities**

Iran is the second-largest economy in the Middle East at USD 400 billion. Iran’s economy which suffered its greatest blow in the years following 2012, especially after the foreign direct investments in the country reached zero, is now dynamically returning to the global markets.

Following the lifting of the Iranian sanctions declaration, an increased interest from investors from all over the world, looking into expanding their trading activities in the Iranian market, has been observed, while Iranian businessmen have expressed interest in getting into the European market. After many years of isolation, Iran is in desperate need for new investment, technological aid and an upgraded and active economy. There is great excitement about its investment potential, particularly in the energy sector, at least for those undeterred by the deeply disturbing regional tensions and the precipitate fall in the oil price.

Foreign investment will therefore be crucial for Iran’s economy in its effort to integrate into the global economy. Without a doubt, Iran is ripe for economic transformation including a diversified economy, a trade surplus and a well-educated urban population. Foreign investment will allow Iran to capitalize on these strengths.

**Favourable conditions for investments between Cyprus and Iran**

The lifting of sanctions as well as the industries that are fundamental for Iran’s economy, create important prospects of economic development between Iran and Cyprus. Cyprus has been at the forefront of these historic developments by concluding a double tax treaty agreement.

The Cyprus-Iran double tax treaty was signed on August 4, 2015. It is based on the OECD Model and is expected to enter into force on the 1st of January of the year, following the ratification process by both Cyprus and Iran. The ratification is still pending but it is expected to take place during 2016.

**Cyprus Funds investing in Iran**

As per the above structure, the tax benefits of using a Cyprus Fund to invest in Iran, are as follows:
1. Dividends paid from Iran to the Cyprus Fund will be exempt from withholding tax in Iran;
2. Incoming dividends are exempt from taxation in Cyprus (subject to relaxed conditions);
3. No Cyprus dividend withholding tax upon repatriation of profits to the shareholders;
4. No capital gains tax upon disposal of the Iranian investments.

Conclusion

Walter Wriston, the legendary former CEO and Chairman of Citicorp famously said, “Capital investment goes where it’s welcome and stays where it’s well treated.” If Iran genuinely seeks to attract foreign investment, it should proceed to implement a broad spectrum of reforms, including strengthening property rights, transferring state-owned assets to the private sector, and granting independence to its central bank. Ultimately, only then can Iran reap the full economic benefits of the nuclear deal and become a premium investment destination. A strong grasp of the legal parameters on the investors side that will apply going forward and their impact on transactions, matched with scrupulous due diligence will be the key in aligning opportunity with risk.

Mr. Costas Markides holds a Master’s degree in Accountancy with special concentration in International Taxation. He is a Certified Public Accountant (CPA) in the United States and a member of the Institute of Certified Public Accountants of Cyprus (ICPAC).

Since 2002 Mr. Markides has been working for KPMG in Cyprus and is currently a member of the Board of Directors. He is also a member of the Tax Committee of CIFA.

The role of the Fund Administrator in today’s market

By Mr. Vassos Kyprianou
Founder and Managing Director, Dimacos Capital Ltd
Chief Investment Officer, Dimacos Fund Ltd

The investing environment

The capital markets and investment environment have never been so complex and challenging as nowadays. Investment products constantly reach new forms on ingenuity in their endless effort to capture positive performance. New structures emerge every couple of years, sometimes adding value to the industry and sometimes destroying a big part of it.

The world, only eight years ago experienced a near-depression financial crisis that brought the global financial system to its knees. Most countries are still trying to recover and in their desperation resort to sub-par measures such as ZIRP (zero interest rate policies) and QEs (quantitative easing or endless money printing for the average person). After a number of major scandals and collapses in the industry (see Bernard Madoff, Peregrine Financial Group, MF Global, Stanford Financial Group, among others), regulators worldwide implemented new extensive regulatory measures sometimes really effective, sometimes just for the sake of added regulation, and sometimes bringing back old legislation that should never have been abolished (e.g. the separation of investment banking from commercial banking).

The role of the Fund Administrator

So, in such a dramatically changed investing environment, what is the role of the fund administrator and how should an administrator cope with such a different investment landscape? To answer this question we need to define the role of the fund administrator as an investment intermediary and how this service provider adds value to the investment business value chain.
Diagram 1: Fund Administrator Workflow

The fund administrator is in effect the independent service provider that stands between the investment manager and the investor. Before investors decide to invest, as part of their due diligence they need to address a number of issues including: (a) whether the investment is expected to have good performance for the risk they take; (b) if the measurement of such performance will be reliable and robust; and (c) will the custody of their holding be in good hands. The investment manager cannot undertake all three roles as there is a major conflict between these three functions. So the fund administrator steps in as a service provider independent from the investment manager to undertake the calculation of performance that the manager generates, as well as take custody of the register of investor holdings. Trust is an essential ingredient in the investment process and only when the investment structure becomes trustworthy will investors be induced to make their investment allocations.

Functions of the Fund Administrator

Some of the main functions of a fund administrator include:

- Fund accounting and calculation of Net Asset Values and maintenance of official books and records of the Fund;
- Acting as transfer agent and maintaining the share register;
- Processing of subscriptions, redemptions, transfers and switches;
- Issuing investor statements and other investor reporting requirements;
- Regulatory and tax compliance on behalf of the funds and the investment manager;
- Assisting in the preparation of statutory financial statements and liaison with auditors;
- Processing of dividend and other distributions;
- Providing middle office services (e.g. portfolio reporting);
- Fund structuring, set up and investment manager consulting;
- Processing of income collections and settlement oversight;
Ad hoc consulting on exceptional events such as: fund voluntary liquidations, valuation of hard-to-value portfolios, side pockets administration, fund restructuring, Fund re-domiciliation, etc.

Qualities of the Fund Administrator

In this context and as a result of the developments in the investing landscape noted above, the investment industry has become quite self-regulated in recent years. Investors themselves demand the separation of portfolio management from fund administration otherwise they will not even look at the proposed investment. Investors go deeper though, as part of their due diligence, and demand that a credible, well-established and structured fund administrator undertakes the administration for the investment funds. The fund administrator needs to demonstrate both to the investment manager as well as the investors that the following five objectives are consistently met:

- it acts in a totally independent manner to the investment manager;
- all information received from the investment manager is externally verified;
- it has a very strong internal control environment;
- there is clear segregation of duties; and
- there are formal processes consistently applied.

Of course this is not an exhaustive list. In practice, the role of the fund administrator is significantly more challenging. Taking into account the functions it performs, in effect the administrator is rendered as one of the most strategic advisors to the investment manager. Still it has to remain impartial and independent in servicing the fund administration mandates, and establish a credible environment between the investment manager and its investors.

Fund administrators that have successfully managed this delicate balance, have created significant brand value around their name in the fund administration business and recognition among investors which in turn attracts business from investment managers worldwide.

Implications for Cyprus

The additional regulation and compliance costs introduced worldwide during the last couple of years as well as investor demands for the use of reliable and reputable fund administrators have rendered fund administration and compliance an important part in the funds’ cost base. The problem is more intense with small funds and emerging investment managers where fee minimums take away a serious percentage of the asset base. At the same time the scarcity of good yields, have created additional investor pressure for better investment returns. This adds a further push to investment managers to seek for low-cost, reliable, fund administrators.

This is a once-in-a-lifetime opportunity for Cyprus to bridge this gap. A country with abundance in accountants and relevant professional advisors can offer, in time, reliable fund administration at a fraction of the cost provided in incumbent fund administration centres such as Ireland and Luxembourg. With a carefully designed regulatory framework for fund administrators, a gradually crisis-free economy coupled with a robust infrastructure, high quality human capital and above all relevant professional development, training and support, Cyprus can and should play a significant role in the worldwide fund administration industry.

Mr. Vassos Kyprianou is the Founder and Managing Director of Dimacos Capital Ltd, a research-based organisation that develops systematic absolute return investment strategies, and also provides strategic consulting and advisory services to investment industry intermediaries such as fund administrators and investment firms. Mr. Kyprianou is also the Chief Investment Officer of Dimacos Fund Ltd, an open-ended AIF that trades systematic absolute return investment strategies. Between 2005 and 2013, he held senior positions in the hedge funds sector including chief accountant, operations manager, chief operating officer and executive member of the board of directors of IKOS CIF Ltd. He is a Fellow member of the Institute of Chartered Accountants in England and Wales, a member of the Institute of Certified Public Accountants Cyprus, as well as a member of the Legal and Regulatory Committee of CIFA.
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For information, please contact:

Mr. Marios Tannousis
Member of the Board, Secretary
E-mail: mtannousis@investcyprus.org.cy
Severis Bldg. 9 Makarios III Ave., 4th Floor
Lefkosia 1065, Cyprus
PO Box 27032, Lefkosia 1641, Cyprus
Tel: +357 22 44 11 33
Fax: +357 22 44 11 34
E-mail: info@cifacyprus.org

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