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THE IMPACT OF CYPRUS–EUROPEAN UNION INTEGRATION ON THE FINANCING OF INVESTMENTS IN THE TOURISM SECTOR OF NORTHERN CYPRUS

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ABSTRACT

This paper examines the issue of tourism development and financing of investments in the tourism sector of Northern Cyprus. It discusses the current model for tourism financing in Northern Cyprus and analyzes possible implications on the efficiency of this model due to membership in the European Union. As such, the process of tourism financing in Northern Cyprus, its constraints, and its opportunities are better understood.

Introduction

The aim of this study is to examine the tourism financing facilities in the European Union (EU) and Northern Cyprus and to investigate how the tourism financing sources would be different in case of EU membership. Secondary sources such as Internet publications, codes of laws, guides for the related establishment, books, and brochures were used to prepare this paper. The paper is divided into the following sections:

- Importance and development of tourism in the EU
- The financing of tourism investments in the EU
- Importance and development of tourism in the Turkish Republic of Northern Cyprus (T.R.N.C.)
- The financing of tourism investments in the T.R.N.C.
- Cyprus-EU relationships
- The impacts of Cyprus-EU integration on the tourism sector of Northern Cyprus
- Conclusion

Importance and Development of Tourism in the EU

Before concentrating on tourism financing, we must examine the importance and development of tourism in the EU. In Europe, there are several groups of people with different languages, cultures, and traditions. In such variety, the changing creative and adaptive abilities of people are important. In the field of EU's tourism, different cultures have to be understood. Tourism makes the identity of Europe strong and helps to defend and introduce European values on the international stage.

With the social and cultural support of tourism, the variety of the traditions and cultures in Europe makes the EU the biggest tourist area in the world with 53% in the world

marketing. Tourism accounts for 5.5% of the EU GDP. Nine million persons are employed in tourism-related jobs. This number represents 6% of total employees of the EU. Therefore, tourism is an important source of occupation in the developing countries and villages.

Although there is not yet any collective tourism policy in the EU, community support in the tourism sector is being shown as an important factor.

Development of Tourism in the EU

The benefits of the government that are the members of the EU make differences while Northern Governments send tourists, Southern governments accept tourists. Therefore, the Tourism Information Counsel Committee was established in 1986 for the members of EU. The aim of the committee, originated from the representatives of 18 European Economic Area Countries, is to be informed, to consult, and to facilitate cooperation in the tourism area. The year 1990 was declared as "European Tourism Year" just for impressing the integrative function of tourism and also pointing out its social and economical importance. 7.74 million Euros was spent from the community budget.

With the frame of 1993-1995 Tourism Support Activity Plan, Europe was introduced as a tourism area. The first step of the cooperation with the countries, which are not the member of EU, was taken. Investigations on rural, cultural, educational, and environment tourism and pilot projects were financed with total 21.7 million euro.

The commission's acceptance of a Green Book titled *The Function of Cooperation in Tourism* (European Commission, 2002a) also show the importance given to tourism.

The Financing of Tourism Investments in the EU

The single largest source of European Union funding for tourism, in particular in the less prosperous regions, are the Structural Funds: the European Agricultural Guidance and Guarantee Fund (EAGGF), the European Regional Development Fund (ERDF), and the European Social Fund (ESF). It is widely recognized that tourism is contributing to regional development and job creation. The total community contribution on tourism projects over the period 1994-1999 through the structural funds was approximately 7.3 billion ECU.

Many local activities can benefit also from financial rapport through other community programs in diverse fields such as research and technology development, environmental protection, improving of the competitiveness of small and medium-sized enterprises (SMEs), restoration of cultural heritage, etc. (European Commission, 2002b).

The most important instruments for funding tourism investments for member and accession candidate counties in the EU can be given under the following headings.

Structural Funds

In the framework of Agenda 2000, the objectives and regulations of the Structural Funds underwent changes. Now there are 3 priority objectives, two of which are geographical in application and one of which now applies across the whole territory of the Union:

- Objective 1: Promoting the development and structural adjustment of regions whose development is lagging behind
- Objective 2: Economic and social conversion of areas facing structural difficulties (industrial, agricultural, fishing and urban areas)
- Objective 3: Adapting and modernizing systems of education, training and employment (Karluk, 2002:405-412)

European Agricultural Guidance And Guarantee Fund (EAGGF). The EAGGF is divided into two sections: the Guarantee Section finances price support measures to guarantee farmers stable prices, while the Guidance Section grants subsidies for rationalization schemes, modernization, and structural improvements in farming as well as measures of rural development.

Projects supported in the past concerned, for example, the development of a tourism product around mountain hiking or the adaptation of canals for water sports or farm tourism. Other measures eligible for financing under the EAGGF Guidance section may make an indirect contribution to the development of rural tourism, e.g., the renovation and development of villages, the protection and conservation of the rural heritage, measures to protect the natural environment of rural areas, the community-wide dissemination of knowledge, experience and results of work done for rural development as well as the processing and marketing of agricultural products.

European Regional Development Fund (ERDF). Under the ERDF financial assistance for disadvantaged regions is targeted mainly at:

- Supporting small and medium-sized enterprises
- Promoting productive investment
- Improving infrastructure
- Furthering local development.

Within community programs, the ERDF is a major source for funding of tourism development. Many of the Structural Funds programs include special measures for tourism development. Some examples from the range of projects assisted in the period 1994–1999 under the ERDF include improvements of hotels, development of tourism infrastructure (golf courses, conference centers), restoration of cultural heritage, promotion of rural tourism, and support for both setting up and upgrading tourism Sees (from 1994–1999 a total of £4.4 billion has been disbursed for tourism-related projects) (Şafaklı, 1998: 81).

European Social Fund (ESF). The ESF provides financial assistance for vocational training, work experience and placement schemes, training of teachers, trainers and public officials, employment counselling and job search assistance, employment aids and child-care facilities, schemes for developing or improving in-company training systems and structures, as well as research projects which anticipate and help plan for future work-force needs. These actions are targeted particularly at unemployed youth, the long-term unemployed, socially disadvantaged groups, and women. Programs are planned by member states together with the European Commission and then implemented through a wide range of provider organizations in both the public and the private sectors.

ESF-funded projects can support tourism development in regions eligible for Structural Fund assistance. The ESF provides funding for developing human resources, for retraining and re-qualification of the labor force, and aid for employment in the tourism sector, among others.

Financial Instrument For Fisheries (FIFG). The FIFG is applied in coastal regions, its main tasks being to increase the competitiveness of the structures in the fisheries sector and to develop viable business enterprises in the fishing industry, while at the same time striving to maintain the balance between fishing capacities and available resources. Other measures, such as the promotion and identification of new markets and as other initiatives undertaken by the industry, could also benefit from support.

Since the FIFG also contributes to revitalizing areas dependent on fisheries and aquaculture, it supports "socio-economic measures" and "the establishment of networks for... areas dependent on fisheries and aquaculture"; tourism projects might be eligible, provided they meet the relevant criteria (European Commission, 2002c; Lök, 1995:81–82).

European Development Fund (EDF)

National and regional indicative aid programs are agreed between the Commission and the beneficiary ACP states that establish the broad parameters and priorities of the Community's financial and technical cooperation financed by the EDF. Individual programs are similarly agreed within this framework, which take account of the development objectives and priorities of each country and region as well as those of the EU.

Many ACP states and regions are dependent on the tourism sector as part of overall economic development. The Commission's overall approach is defined in its co-operation strategy for tourism development (*Communication from the Commission to the Council and European Parliament on a EU strategy to support the development of sustainable tourism in the developing countries*, COM [1998] 563, 14.10.1998). Article 24 (Tourism) of the Cotonou Agreement between the ACP and the EU sets out the aims and strategies of the Parties to the Agreement for the tourism sector (Eur-Lex, 2002).

European Investment Fund (EIF)

The EIF is a European institution with specific remit to support the creation, growth and development of SMEs. The EIF is a public-private partnership. Its tripartite

shareholding includes the European Investment Bank (60.75%), the European Union represented by the European Commission (30%), and a number of European banks and financial institutions (9.25%). The EIF acts independently and commercially under market conditions, targeting appropriate returns for its shareholders. It conducts its activities in the member states of the European Union and in countries that have applied to become members and in respect of which the accession process has commenced. With regard to SMEs, the Fund's objective is to promote their development by facilitating access to financial resources. This is achieved through venture capital and guarantee instruments, either drawn from its own funds or within the framework of mandates entrusted to it by the European Investment Bank or the European Union. Note that the EIF does not work directly with SMEs. Instead, all the EIF's activities are conducted through intermediaries such as specialized venture capital funds (for its venture capital activity) and banks, leasing companies, guarantee institutions, mutual guarantee funds, etc. (for its guarantee activity).

Funds are not only available for SMEs involved in high technology and knowledge-based industries. The financial intermediaries are open to all sectors, and tourism projects are eligible where they fulfill the related conditions. The financial intermediaries can, for example, finance environment-related tourism undertakings as well as fast-growing tourism businesses with a priority given to SMEs with fewer than 100 employees (European Investment Fund, 2002).

European Investment Bank (EIB)

The task of the European Investment Bank, the European Union's financing institution, is to contribute to the integration, balanced development, and economic and social cohesion of the member countries. To this end, it raises on the markets substantial volumes of funds, which it directs on the most favorable terms toward financing capital projects in accordance with the objectives of the Union. Outside the EU, the EIB implements the financial components of agreements concluded under European development aid and cooperation policies (European Investment Bank, 2002).

According to its functioning, EIB funding for tourism investments can be divided into that for the EU and that for accession candidate countries.

European Investment Bank for EU Countries. Unlike other banks and financial institutions, the EIB does not command resources drawn from deposit or current accounts. The Bank raises its resources on the world's capital markets where, by virtue of its active presence and its issuing techniques, it can mobilize significant volumes of funds on the finest terms available at the time ("AAA"). As it operates on a non-profit basis, the Bank passes on to its borrowers the benefits of its excellent credit rating, so furthering the objectives of the EU. A committed player in building the Europe of tomorrow, the EIB provides financing mainly for projects located inside the EU. It is therefore not surprising that the bulk of the resources it raises are in the currencies of the member states. Nevertheless, while it leaves its borrowers free to choose the currencies of their loans, the EIB is also active on the main non-EU currency markets, where the majority of its bond issues

are in U.S. dollars, Swiss francs, or Japanese yen. Active on capital markets, specializing in long-term financing, the EIB seeks to tailor its borrowings as closely as possible to its customers' needs (Kahraman, 1997: 63–64).

Loans given to EU countries can be categorized as *global* and *individual loans*. Global loans are credit lines made available to banks or financial institutions, which on lend the proceeds for small or medium-scale investment projects meeting the Bank's criteria. To complement EIB financing, the intermediary also advances funds in support of the projects concerned. These credits are given in the amount of 50% of the investment costs with the maturities between 5 and 12 years or 15years in exceptional cases.

With individual loans, promoters in both the public and private sectors, including banks, can borrow these credits for the amount to be agreed directly with the EIB if capital investment project exceeds EUR 25 million and up to 50% of the investment costs. The maturities in the industrial sector are up to 12 years, and for infrastructure projects 20 years, or more in exceptional cases.

European Investment Bank for Accession Countries to the EU. The EU integration of up to ten countries in Central Europe will create a single market of nearly 500 million customers and increase the EU's economic and political weight in the world. EU enlargement offers companies and corporations investing in the accession countries unprecedented growth opportunities based on free access to a larger market, the availability of well-trained workers earning competitive wages, economies of scale, and transfers of technological and organizational skills. By working closely with the accession countries' governments, utilities, and business communities for more than a decade, the EIB has acquired considerable knowledge and established useful contacts which make it an ideal partner for companies from the EU and elsewhere who intend to launch or expand activities in the accession countries. Since 1990, the EIB has financed directly or indirectly more than 1,000 small, medium- and large-scale investments in the accession countries, providing a total of EUR 15 billion. It has committed more long-term funds than any other bank to the transformation and EU integration of the Accession Countries. But this was only the beginning. EIB is in the accession countries to stay. In the present EU, about three quarters of EIB lending is going to projects in the regional development areas, mainly in Greece, Portugal, Spain, Southern Italy, and Eastern Germany.

Loans for up to 50% of the total investment project costs may also include technical/ price contingency provisions, permanent working capital needs and interest paid during construction.

Joint European Venture Initiative (JEV)

The objective of joint ventures is to create new economic activities, involving investment and employment creation within the Community. The Community contribution is intended to cover some of the expenses incurred in setting up a joint venture. In January 1998, the Commission proposed to allocate a larger appropriation to JEV, thereby permitting to finance 1,500–2,000 projects.

This program is open to all sectors, and tourism projects are eligible where they fulfill the related conditions. Tourism projects could include joint ventures developing and improving hotel infrastructures or the establishment of holiday villages, camping sites, and joint ventures between tour operators.

European Venture Capital

The Commission works closely with the European Venture Capital Association (EVCA). The EVCA aims to act as a catalyst for the development of capital markets for entrepreneurial managed European companies, and specifically to:

- Promote opportunities in the capital markets for entrepreneurial companies and encourage the active involvement of institutional investors, investment banks, securities dealers, investment funds, regulators, policy-markets and others.
- Facilitate the development of contacts and exchange of information among these market participants.
- Assess the need for, and viability of, a permanent association.
- Develop a framework for exploiting the opportunities offered by capital markets for entrepreneurial companies.
- Help specify priority actions for both policy-makers and market participants.

Venture capital funds invest in all sectors, and tourism projects may be eligible where they fulfill the related conditions. Venture capital funds also give management and financial support to SMEs in their creation phase prior to embarking on the development and innovation phases. In addition to seed capital, venture capital funds provide business support services such as financial planning, advice on further sources of finance, market analysis, and business strategy development.

Mutual Guarantee Companies

The mutual guarantee company (MGC), whereby several enterprises club together in order to provide mutual guarantees for finance, is seen as a possible solution to problems in the access to credits. It permits the reappraisal of risk by companies with direct experience in the relevant sector, spreads the risk among more parties, reinforces the negotiating power of the members, and favors an effective allocation of public subsidies.

In order to encourage the promotion, development, and expansion of MGCs in the EU, the Commission works closely with the European Mutual Guarantee Association (EMGA) whose main areas of activity are:

- Supporting the setting-up of MGCs in countries where they do not yet exist;
- Improving the weighting of risks and the qualification for guarantee offered by MGCs under European banking law;
- Organizing mutual guarantee orientation seminars; and

- Assessing existing mutual guarantee systems in the new member states as well as extending their contacts in the countries of Central and Eastern Europe.

The Commission finances 50% of the feasibility studies over a maximum period of one year and 50% of the running costs for the creation of MGCs over a maximum period of three years.

The EMGA has also established contacts with the European Investment Fund that should take on several projects relating to the reinsurance of national mutual guarantee systems.

In contrast to other types of scheme, mutual guarantee schemes involve private groupings of companies, often linked to sector-specific interest groups, to provide loan insurance to banks. The philosophy behind this system is that closer links between the interest groups in SME-dominated industries, such as tourism, can help improve banks' knowledge of a company's standing and of the markets in which it operates. This in turn allows a better *ex ante* evaluation of the project by the lender and allows credit risk to be considerably reduced. The fact that the mutual guarantee organizations trust the enterprises and their projects, and express this trust by offering the lending bank a partial guarantee, makes it easier for the latter to grants loans.

SAPARD (Special Accession Program for Agriculture and Rural Development)

The SAPARD program enables the Community to provide financial and technical assistance for agriculture and rural development in candidate countries as they prepare for EU accession. Since tourism is a potential source of additional income in rural areas and needs an intact environment as a basic resource, certain measures that contribute to the development of rural tourism are eligible under the program. Many national SAPARD plans include the development of rural tourism (European Commission, 2002c).

Importance and Development of Tourism in the T.R.N.C.

The following two sections will explain the importance and development of tourism in the T.R.N.C.

Importance of Tourism in the T.R.N.C.

The T.R.N.C. tourism sector, which covers the area of 3355 square km of Cyprus island, is identified as the prior sector of the economy by the state policy, and it is given the duty of locomotive in progress, because of its geographical state and its proper weather conditions, natural beauties, rich archaeological remains, historical possessions, wide and clean beaches, and structure away from environmental problems (DPÖ, 1993:2).

Though the prior structure of tourism sector in the country, there are significant problems in getting the sector better, developing it, and increasing the demand for

tourism. These problems are as follows: transportation, since the country is not known; physical plan is not prepared which covers tourism planning and master plan is not applied; basic problems of water and electricity are not solved; an effective and an autonomous tourism organization is not established for the management and the control of tourism; there is lack of coordination with the other sectors, mainly with transportation and education; and there isn't enough finance for tourism investments (Şafaklı, 1999:14–24). Although the tourism sector has great problems, it is very important for the economy of the T.R.N.C.

Tourism in Northern Cyprus has priority for development because of its effect on foreign currency and its contributions to the balance of payments; income increases and creation of employment; and its help for the development of sectors like constructions, trade, agriculture and industry. These economic effects of tourism are explained below (Şafaklı & Erkut, 2002).

Contribution of Tourism Sector to GDP. In 1995, the tourism sector realized value added with 1977 fixed prices as 243.6 million USD; because bigger at the ratio of 3.7% when compared to 1994. Tourism sector value added reached 249.5 million USD in the year 1998. The sector's share at GDP on the basis of fixed prices became 3.0% in the year 1998 and in the year 2000 it became 3.2%.

Contribution of Tourism to the Balance of Payments. The T.R.N.C. has an island economy with few resources, limited production possibilities, a narrow internal market, and limited labor. Tourism is put on the agenda by bringing out the characteristic of utility economy like the economies of other small countries and being the biggest effect which is the helper for closing the balance of foreign trade that give deficit for years. In 1990, 71.1% of 316 million USD foreign trade deficit is received by net tourism incomes. This rate became 55.8% in 1992, 55.2% in 1998, and 53.0% in 2000. As it could be understood by these results, net tourism incomes played the greatest role in closing foreign trade deficit.

Contribution of Tourism to Employment. The tourism sector is a very important area of employment because it requires too much work. It affects the general level of employment in a positive way because of its contributions to GNP. The number of possibilities of employment created by the enterprises which directly present tourist goods and services, such as lodging, travel agencies and transportation, increases parallel with the increasing number of tourists. Therefore, both direct and indirect capacity of employment is created. In 1977, the total employment created was 1,302 people; this number increased to 1,435 in 1982, to 2,121 in 1987, and to 4,089 in 1992. It reached 6,042 in 1999 with a stabilized increase (Şafaklı & Erkut, 2001).

Development of Tourism in the T.R.N.C.

Even though the tourism sector has been selected as the locomotive sector of the Northern Cyprus economy, its contribution to the economy has not been satisfactory, especially when compared with the same indicators of Southern Cyprus. The contribution of tourism to Southern Cyprus's GDP, employment, bed capacity, and tourist

arrivals (thousand) are 19%, 9.7%, 86,151, and 2,222.7 respectively (www.stockwatch.com.cy; Dept. of Statistics and Research 1999:19; www.kypros.org). The 1998 figures for the T.R.N.C. are 3%, 3.8%, 8,972, and 393 respectively (DPÖ 2002:70–71; T.R.N.C. Ministry of Tourism and Environment, 2002:15, 58).

Authorities decided to take urgent actions to eliminate the obstacles to achieving economic contributions expected from tourism sector. In this perspective, the following basic policies and targets will be pursued according to Tourism Master Plan and Transition Programs in order to attain sustainable tourism development:

- Tourism investments suitable to incentive law (numbered as 47/2000) will be encouraged. Moreover, best efforts will be made to attract foreign investments.
- Environmental protection and development will be given necessary importance.
- An autonomous tourism organization will be established to manage and plan tourism activities in Northern Cyprus (DPÖ, 2001:211–212).
- Tourism development depending on regional differences will be adopted.
- In addition to mass tourism, special interest tourism will be adopted.
- Private enterprises, non-governmental organizations (NGOs), local administrations, and universities will be coordinated to restructure tourism.
- Social, economic, and physical capacities of the country will be taken into account in order to select a model for tourism development.
- Tourism targets for bed capacity, occupancy rate, and net tourism revenues (million US$) at the end of 2010 will be 16,738, 60%, and 557.6 respectively (KKTC Devlet Bakanlığı ve Başbakan Yardımcılığı, 2000).
- Increasing the number of foreign tourists and the length of stays, extending tourism season by solving seasonal problems, and encouraging group tourism and local tourism will be among the major objectives (Boğaziçi Üniversity, 1998).

The Financing of Tourism Investments in the T.R.N.C.

Tourism projects usually carry characteristics of fixed capital intensive, labor intensive, high fixed expenditures, and inseparable connection between infrastructure and establishment (Kahraman,1995:16–21). Because of these characteristics, tourism investments are accepted as long-term investments and should be financed by long-term sources of finance (Özen & Kuru, 1998). However, tourism investors of Northern Cyprus are facing serious difficulties in financing their projects with long-term credits. Even though the Development Bank was established in 1993, its available funds are not sufficient to meet all the applications of investors. Moreover, private banks prefer to give self-liquidating credits like financing exports and imports rather than financing tourism projects carrying high risk potential. On the other hand, the Central Bank and State Planning Organization take active role in providing tourism investors with credits and incentives.

The most important institutions for financing tourism investments in Northern Cyprus are given below.

Development Bank

Tourism investors should get their projects approved by the related authorities before requesting credit from the Development Bank.

In addition to new projects, projects that aim to renew, or to reform and to eliminate the deficiencies of, the existing foundations are also eligible for credit application. These projects also aim to complete the half-finished foundations. The total financing need of the project for investment, which will be given credit by the Development Bank, will definitely be financed with 50% local sources and 50% foreign sources. Credits given by the Development Bank are categorized as investment credits and business credits.

Investment Credits. The interest rate, terms, and the payment applied to investments credits are shown as follows:

TL	STG	USD	EURO	VALIDITY
40%	5%	4%	4%	2–9 Year

The realization and the collection of the interest and the installment of the main money are twice a year; one is on 31 August and the other is on 31 December.

Business Credits. The interest rates applied to business credits are shown as follows;

TL	STG	USD	EURO
50%	6%	5%	5%

The term of the business credits is one year. At the end of the year they are collected together with their interests. On the other hand, the term could be extended if the interest is paid and so is approved by the authorities at the end of one year.

According to data obtained by the Development Bank, the following credits were given to tourism investors between 1993 and 2002.

Investment credits	:	24,474,477 USD
Business credits	:	555,891 USD
Transfer*	:	7,641,806 USD
Total	:	32,672,174 USD

* Transfers include the debts that are taken over by the Development Bank from the private banks.

State Planning Organization

The applications made by real and legal investors who want to benefit from incentive precautions will be taken into consideration by the State Planning Organization with the opinion of the related ministry. The project approved by the State Planning Organization, will be given an "Incentives Certificate." Incentives that can be given to tourism investors, regardless of whether an investor is local or foreign may include investment

allowance, exemption from custom duties and funds, zero rate value added tax (VAT), government owned land and building lease, fund credits and exemption from construction license fee (SPO, 2002:16–18).

Economic and Financial Cooperation Protocol Between Turkey and Northern Cyprus

The Development Bank, with its procedure and principles, makes allocation, collection, and usability of the credits given by funds as a result of Economic and Financial Cooperation Protocol Between Turkey and Northern Cyprus. These credits are given as Turkish Liras. The total credits allocated for the project cannot be more than 60% of the total investment. The annual interest rate of the investment credit is 10% for the developing areas. The credit should turn back with nine equal payments will take seven years for the tourism sector, with the first three years being unpaid.

The interest rate of the business credit is 15% for the developing areas but for the other areas it is 20%. The total term for the business credit is three years. The first year is unpaid and the other period is divided into five equal payment periods. Because the fund is new, for the application made up to now, an incentives certificate has been given to the investors, but they have not been allowed to use any credits. On 24 September 2001, an agreement was made between the Turkish Republic and the T.R.N.C. with the frame of Economic and Financial Cooperation. US$160,000,000 was deposited for the private sector. US$140,000,000 of this amount will be allowed to be used by the T.R.N.C. Development Bank and US$20,000,000 will be allowed to be used by the Turkish Development Bank in five years.

Tourism projects having incentives certificates will be given credit by the T.R.N.C. Development Bank if they cost less than five trillion Turkish Liras. If they cost more than five trillion TL, the Turkish Development Bank will support them.

Central Bank

With the condition of nine months to be left to the end of the terms at the Central Bank, the commercial documents of the Judicial and the real persons related with tourism will be accepted as discounts. The Central Bank can also make an advance for the documents that could be discounted at the following rates:

	EURO	USD	STG
Rates of Interest:	9%	9%	10%

The term of the credit limit, for the business credit, is nine months, and it is given with the evaluation of amount demanded. On the other hand, the term of the credit limit for the investment credit is 36 months, and its credit limit is 100 billion. (The decision of the council of management of the Central Bank in TRNC / /8/2002 No: 478.)

Private Banks

Tourism investors primarily used the credits of private banks in order to finance their investments until 1993, when the Development Bank was established. However,

even after this year, tourism investors had to take private bank credits due to insufficient Development Bank credits. Therefore, these credits with very high interest rates increased the cost of investments and also made the repayment of these credits very difficult for investors.

Cyprus-EU Relationships

The relations of Cyprus with the European Economic Community, and subsequently with the European Union, have evolved gradually from an Association Agreement in 1972 to a Customs Union Protocol in 1987, followed by the application for full membership in 1990, the positive Opinion of the EU Commission on Cyprus' application in 1993, and the initiation of accession negotiations in March 1998. The evolution toward ever-closer relations with the EU has proceeded steadily, and it is remarkable that there have been few technical or commercial problems with the implementation of the agreements. One feature of all the agreements with the EU has been the mutual desire that they should benefit all the people of Cyprus, and despite the constraints, there have been such benefits in trade and in bi-communal projects such as the Nicosia sewerage scheme, the Nicosia Master Plan, the electricity project, and the water project, all of which have been funded from the financial protocols concluded within the EC-Cyprus association framework. The very close relations with the EU developed on the basis of the Association Agreement and, more particularly, the completion of the first phase of the EC-Cyprus Customs Union on 1 January 1998. These relations are being enhanced by the wealthy and healthy economy of Cyprus, which today is the leading country among the candidates, and it is expected to have a smooth ride during the change (Cyprus & European Accession Negotiations, 2002a).

Latest Development

The European Commission has facilitated the accession negotiations, organizing the *acquis communautaire* into 31 chapters, of which 29 involve several EU policies that are under negotiation. For practical reasons, the Commission has decided to address issues in the remaining two chapters (Institutions and Others) at a later stage, when the accession negotiations are at a more advanced level. Cyprus began its accession negotiations with the EU in March 1998 and up until March 2002, it had provisionally closed 24 out of the 29 chapters under negotiations.

In the 16th Meeting of the Intergovernmental Conference for Cyprus Accession to the EU (19 April 2002), Cyprus became the first country to open the negotiations on the Chapter of Institutions, which deals with the participation of the country in the Institutions of the Union. Following the provisional closure of another four chapters (Institutions, Competition Policy, Taxation, and Regional Policy/Structural Instruments) during the Spanish Presidency, Cyprus has provisionally closed the 28 out of the 30 chapters now under negotiation.

The chapters still under negotiation are Agriculture and Budgetary and other Financial Provisions. Upon completion of the negotiations on these two chapters and their pro-

visional closure in the next few months, the remaining chapter (Other) will be negotiated and will include whatever could not be incorporated under all the other chapters (Cyprus & European Accession Negotiations, 2002b).

Assistance Provided by the EU

The EU supports various projects in Cyprus. Cyprus now participates in a series of programs as follows:

- 5th Framework Program for Research and Development
- Leonardo da Vinci II (Training)
- Socrates II (Education)
    - Ministry of Education and Culture
- Youth
- Media II - Media-Plus (Audiovisual)
- Multi-annual Program for SMEs

Cyprus is expected to participate soon in other EU programs like:

- Fiscalis (Taxation)
- Culture 2000 (Culture)
- Customs 2000 (Customs)
- SAVE II (Energy)
- Public Health Programs (Public Health)

Pre-Accession Financial Regulation of the EU (2000–2004). The EU will provide financial assistance to the implementation of Cyprus's harmonization program in the context of the new Financial Regulation for the Implementation of the Pre-Accession Strategy of Cyprus and Malta (2000–2004), which was approved by the relevant Council of Ministers of the EU in March 2000.

The basic aim of the new regulation, which has succeeded the Financial Protocols, is the application of pre-accession assistance (grants) in the two countries for the preparation needed for the application and implementation of the *acquis communautaire.* With regard to Cyprus, however, the promotion of cooperation between the two Communities is referred to as an additional basic aim.

The overall sum to be given to Cyprus for the period 2000–2004 is expected to reach 57 million EURO. The sum of financial assistance to Cyprus in the year 2000 was set to reach nine million EURO, out of which three million EURO were to be used for "bi-communal actions."

Cyprus (like Malta), due to the EU institutions' positions, was not able to participate in PHARE because this program was formed to comply with the specific needs of the

countries of Central and Eastern Europe. For this reason, a separate financial regulation had been formed for Cyprus and Malta.

Despite the intensive efforts by the government of the Republic, Cyprus has not until now been included in the ISPA and SAPARD group of countries that can receive Community financial assistance. The efforts made until today have been numerous at all levels. It is mentioned that the Minister of Foreign Affairs in a letter dated 18 February 1998 to the then relevant Commissioner, Mr. Hans Van den Broek, had officially submitted this issue. The most recent effort has been made on 15 December 2000 when the government of the Republic of Cyprus raised the issue again in front of the Association Committee between Cyprus and the EU, which was summoned in Nicosia. The French Presidency, the European Commission, and all member states were represented at this meeting.

In the meantime, the Chief Negotiator of the Harmonization Process and relevant letters made by the Minister of Foreign Affairs, the Minister of Finance, and continuous efforts and documents were submitted to the EU as related data supporting the request.

The reason the European Commission was initially against financing Cyprus through ISPA and SAPARD is that the rate of economic growth in Cyprus in relation to the other candidate states is high enough not to include Cyprus in the related economic sectors, which are financed by the afore-mentioned financial assistance programs.

Moreover, according to the relevant officials of the European Commission, it is very difficult to include Cyprus, at present, in the countries that receive assistance through ISPA and SAPARD because the sum of financial assistance has been set to be dispersed to the 10 candidate states of Central and Eastern Europe following the decision of the Berlin European Council in June 1999 (Cyprus & European Accession Negotiations, 2002c).

Financial Cooperation

In the past, four financial protocols on financial cooperation were signed between the EU and the Republic of Cyprus, covering a period of 22 years (1978 till 1999). During this time, € 210 million were made available under the form of loans (152 M€), grants (51 M€), and risk capital (7 M€). The main target sectors were small and medium enterprises, environment, energy, and transport. Since 2000, pre-accession aid has been available to Cyprus for an amount of 57 M€ to be programmed over five years (2000–2004). The new financial regulation on the "implementation of the pre-accession strategy" for Cyprus (and Malta) will ensure, like for all Candidate Countries of Central and Eastern Europe, that assistance is targeted toward pre-accession investment priorities, institution-building priorities, and support in economic and social cohesion. Additionally, the regulation foresees supporting "any operations to contribute to the reconciliation of the two Cypriot communities." For all harmonization operations, co-financing is being sought, be it national (compulsory) or with other donors (member states, international financing institutions).

In 2000, the € 9 million available for Cyprus were broken down for harmonization projects (5 M€), for bi-communal projects (3 M€), for co-financing Cyprus participation in

three education and training community programs (1 M€). In 2001, the EU was expected to provide € 11.5 million to support projects for institution building, adoption of the *acquis*, and bi-communal activities, and to help meet the costs of Cyprus's participation in EC programs and agencies. Cyprus also participates in, and benefits from, MEDA-funded multi-country and horizontal programs, and from the TAIEX instrument. The year 2001 was also the year of decentralization of EU assistance to Cyprus, along the lines applied to Central and Eastern European Countries (CEECs). Furthermore, an additional step is in the process of being tested, allowing Cyprus to assume a larger responsibility over the implementation of EU pre-accession assistance, in line with the orientations of the future Structural Funds (European Commission, 2002d).

The Impacts of Cyprus-EU Integration on the Tourism Sector of Northern Cyprus

According to accession negotiations between Cyprus and the EU, Cyprus most probably will be the member of EU till the end of 2004. As a result of this development, potential membership gate open to EU exists for Northern Cyprus if a possible agreement is reached for Cyprus issue.

In case of a solution to the Cyprus issue and a membership to the EU, the following developments related to tourism sector of the T.R.N.C. are expected to take place:

- Political constraints (isolation) on North Cyprus will be removed. Embargoes will be removed.
- The image of North Cyprus will change. It will no longer be perceived as underdeveloped, risky, or dangerous (Bıçak & Altınay, 1998).
- Infrastructure will be improved. Water, electricity, roads and public transportation will be improved and in the future will approach EU standards.
- There will be direct transportation and other company airways will have flights. A competitive situation and so good quality and cheap transportation will be possible. Of course, because of these, there will be an increase in the number of tourists.
- The difficulties in marketing and presentation will disappear.
- Employment will increase due to the increasing tourist establishments because of the increasing number of coming tourists. Therefore, there will be a reduction in the rate of unemployment and so hopefully the citizens who went to the other countries to work will come back to their home countries.
- Investments will increase. With the availability of soft loans and foreign initiatives, both private and public will increase.
- Northern Cyprus will be more attractive for foreign investors since the county risk will be lessened due to economic and political stability.
- Northern Cyprus will get the chance to finance her tourism projects at favorable terms by applying to various EU funds, such as the Structural Funds and the others explained above in detail.

Conclusion

This paper focused on the various ways that Northern Cyprus will be affected from a possible membership of EU with the special emphasis on the financing of tourism projects. In this respect, details of EU funding for tourist enterprises and destinations have been explained. It is concluded that EU funding will be a very important source of finance for tourism projects in Northern Cyprus since capital accumulation in the country is insufficient and the profits from tourism are not remarkable due to the inadequate number of incoming tourists.

The duration for Cyprus to be the member of the EU is still continuing and for this, the finance is provided for the approved projects, but this financing support is mostly given to South Cyprus. It will be possible to serve many more tourists if the whole of Cyprus becomes the member of the EU. If this becomes true, besides the financial support of EU for the all investments in Cyprus, there will be facilities for transportation because Northern Cyprus will be a recognized member of the EU.

As a result of the above assumptions, Northern Cyprus will get the chance to play the assigned role as the locomotive sector of the economy, and tourism revenues and the volume of tourists will be expected to reach the targets proposed in Tourism Master Plan put forward by Tourism Planning Office.

Moreover, the economy of the country will develop with the help of tourism because tourism has the capacity to affect all the other sectors and the gap between the per capita income of Northern and Southern Cyprus will disappear in coming years.

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