13. MALTA

The COVID-19 pandemic is having an acute impact on critical sectors of Malta's economy including tourism and external trade, leading to a temporary and limited increase in the unemployment rate. A modest recovery is forecast in 2021 and 2022 but considerable uncertainty surrounds the evolution of the pandemic and the impact of the change to less beneficial trading relations between the UK and the EU. After a major crisis-induced plunge in 2020, the general government balance is set to gradually improve, while public debt is expected to peak at 60% of GDP in 2021.

Tough toll of the pandemic on tourism-reliant sectors

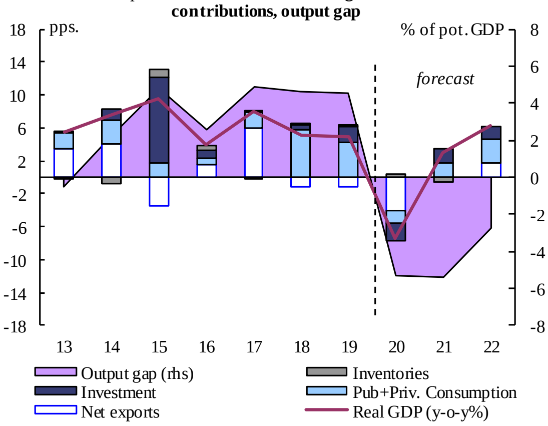
Until recently, Malta has recorded one of the highest real GDP growth rates in the EU. The impact of the COVID-19 pandemic, however, has shaken the foundations of that growth model, which is strongly reliant on tourism and immigration. Malta's GDP contracted significantly in the first half of 2020 as household consumption and construction activity fell sharply due to safety measures established by the authorities, and restricted air traffic interrupted international tourist arrivals to the island.

A temporary shift from a buoyant growth trend

While the pandemic is depressing economic activity in Malta, the government's stimulus package is expected to somewhat offset its toll on the economy. A voucher system to residents combined with wage supplements to affected employees should support consumption in the retail sector this year, offsetting some of the hit inflicted during the lockdown. Combined with these stimulus measures, high household savings have already shown the potential to unlock further consumption and residential property investment. In parallel, some large-scale investment projects are expected to maintain government expenditure. However, all GDP components apart from government consumption are likely to collapse this year, particularly net exports, resulting in a GDP contraction around 7¼%.

A recovery driven by domestic demand is expected to accelerate from slow GDP growth of 3.0% in 2021 to some 6¼% in 2022, reapproaching its 2019 level. Two factors weigh on the pace of the rebound in Malta: the evolution of the pandemic and the economic effects of the change to less beneficial EU-UK trading relations. The first will likely dictate how quickly the tourism sector may pull through the current crisis, while the latter has a considerable negative impact on the trade balance between the UK and Malta. The new trade relations are expected to have the strongest impact on growth in 2021 and to a lesser extent also in 2022. Consequently, the current account surplus is projected to continue to subside in 2021 before rising again in 2022.

Graph II.13.1: **Malta - Real GDP growth and contributions, output gap**



Nonetheless, Malta's economic outlook is closely tied to the economic performance of its main trading partners and their recovery. The uncertainty around the evolution of the pandemic may pose additional downside risks to Malta's trade balance with the rest of the world, affecting its ability to bounce back from the crisis.

A limited impact on the labour market

Prior to the outbreak of the pandemic, Malta's labour market was tight and the unemployment rate reached a historical low of 3.6% in 2019. National safety measures to contain the virus affected employment only to a limited extent, such that the unemployment rate is expected to reach 5.1% in 2020, decreasing to 4.1% in 2022, in line with an accelerating economic growth.

Inflation expected to ease amid recession

The contraction in private consumption, especially in the tourism-reliant retail sector, declines in demand for housing services and lower international energy prices are set to moderate headline inflation from 1.5% in 2019 to 0.8% in 2020. As the economic recovery unfolds next year, inflation is expected to pick up with a rise in the prices of services, reaching 1.3% in 2021 and 1.6% in 2022.

Public finances set to improve after a negative shock

The COVID-19 pandemic will have a major negative impact on public finances in 2020, with the government balance plummeting into a deficit of some 9½% of GDP, after a small surplus in 2019. The fall in household consumption will hit receipts from indirect taxes while lockdown measures will translate into corporate losses and subsequently, falling income tax revenues. Lower revenues are also expected from Malta's citizenship scheme for foreigners. A relatively good performance of the labour market will prevent a large dent in personal income tax revenues and social contributions. The measures to mitigate the negative impacts of the COVID-19 pandemic, including the wage support and voucher schemes, healthcare-related outlays and utility and rent subsidies for businesses, amounting to some 5¾% of GDP, will lead to a major increase in government spending in 2020.

In 2021, an improving economic environment is expected to support revenues and to contribute to a decline of the deficit to some 6¼% of GDP. Proceeds from the citizenship scheme are expected to stabilise at previous year's level. Several pandemic-related fiscal measures will still affect public finances including a temporary reduction of real estate transaction taxes, an extended wage supplement scheme, and a new round of the voucher scheme. Assuming no changes in policies, the deficit is forecast to decline further in 2022 to just below 4% of GDP. This forecast does not include any measures funded by Recovery and Resilience Facility grants, which also pose an upside risk to economic growth.

The government debt-to-GDP ratio is set to surge to 55¼% in 2020 and further to 60% in 2021 before declining to some 59¼% in 2022 mainly on account of a swift growth of nominal GDP.

Table II.13.1:

Main features of country forecast - MALTA

	2019			Annual percentage change						
	mio EUR	Curr. prices	% GDP	01-16	2017	2018	2019	2020	2021	2022
GDP		13390.1	100.0	3.4	8.0	5.2	4.9	**-7.3**	**3.0**	**6.2**
Private Consumption		6233.1	46.6	2.1	3.4	8.5	5.2	**-9.8**	**4.2**	**4.3**
Public Consumption		2299.7	17.2	2.1	1.7	12.0	11.5	**18.4**	**-0.4**	**4.8**
Gross fixed capital formation		2898.4	21.6	5.0	-0.7	3.1	8.8	**-10.1**	**8.0**	**6.8**
of which: equipment		771.1	5.8	7.3	-34.5	-7.7	3.1	**-**	**-**	**-**
Exports (goods and services)		19258.1	143.8	5.3	8.1	-0.5	6.1	**-10.4**	**2.3**	**7.3**
Imports (goods and services)		17392.6	129.9	4.7	4.4	0.4	7.9	**-8.4**	**2.4**	**6.6**
GNI (GDP deflator)		12277.1	91.7	3.0	6.2	7.8	5.8	**-7.5**	**3.0**	**6.2**
Contribution to GDP growth:		Domestic demand		2.7	1.7	6.4	6.1	**-3.6**	**3.5**	**4.5**
		Inventories		-0.2	0.2	0.0	0.0	**0.3**	**-0.5**	**0.0**
		Net exports		1.0	6.0	-1.2	-1.3	**-4.1**	**0.0**	**1.7**
Employment				2.1	8.1	6.0	5.8	**-0.8**	**1.9**	**4.3**
Unemployment rate (a)				6.4	4.0	3.7	3.6	**5.1**	**4.7**	**4.1**
Compensation of employees / head				3.7	0.1	3.7	2.8	**1.0**	**2.0**	**1.1**
Unit labour costs whole economy				2.4	0.1	4.5	3.7	**8.1**	**0.9**	**-0.6**
Real unit labour cost				0.0	-2.1	2.5	1.5	**7.5**	**-0.6**	**-2.7**
Saving rate of households (b)				-	-	-	-	**-**	**-**	**-**
GDP deflator				2.5	2.2	2.0	2.2	**0.6**	**1.5**	**2.1**
Harmonised index of consumer prices				2.1	1.3	1.7	1.5	**0.8**	**1.3**	**1.6**
Terms of trade of goods				-0.2	2.4	3.6	0.1	**-0.3**	**0.7**	**-0.2**
Trade balance (goods) (c)				-17.3	-12.9	-12.2	-12.5	**-6.5**	**-6.2**	**-7.3**
Current-account balance (c)				-2.2	11.2	11.1	4.4	**0.5**	**0.1**	**1.4**
Net lending (+) or borrowing (-) vis-a-vis ROW (c)				-0.9	11.8	12.1	5.2	**1.5**	**1.1**	**2.4**
General government balance (c)				-3.2	3.2	2.0	0.5	**-9.4**	**-6.3**	**-3.9**
Cyclically-adjusted budget balance (d)				-3.2	0.9	-0.3	-1.7	**-6.9**	**-3.7**	**-2.6**
Structural budget balance (d)				-	1.1	-0.3	-1.7	**-6.9**	**-3.7**	**-2.6**
General government gross debt (c)				64.4	48.8	45.2	42.6	**55.2**	**60.0**	**59.3**

(a) as % of total labour force. (b) gross saving divided by adjusted gross disposable income. (c) as a % of GDP. (d) as a % of potential GDP.