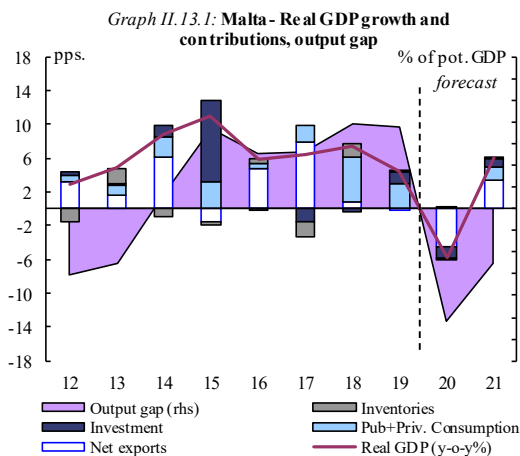


13. MALTA

Economic growth in Malta, which has been strong in recent years, is expected to turn negative in 2020 due to the outbreak of COVID-19. Private consumption and trade are projected to take a significant hit, while increased public spending should partially mitigate the effects of the recession. Employment is forecast to decline temporarily and the unemployment rate to increase. After several years in surplus, the general government balance is expected to slip into deficit and public debt to rise, as the government takes fiscal measures to offset the crisis.

A resilient economic growth model tested

After annual real GDP growth of 7.3% in 2018 and 4.4% in 2019, Malta's economy had already started to show signs of cooling before the COVID-19 outbreak. Domestic demand has been the main growth driver, underpinned by robust private consumption and investment. Economic sentiment had eased in recent months, but remained strong with steady confidence in industry and construction. Although exports have been losing steam, tourism still contributed significantly to GDP growth.



A temporary downturn led by services

Malta's economy will be severely affected by the COVID-19 pandemic this year. GDP is expected to contract by around 5¼% but should rebound by 6.0% in 2021. The lockdown and closure of non-essential businesses since March 26 is weighing on private consumption and service exports, with limited room for expenditure on recreation or food services. However, the initial tightness in the labour market and households' high saving rate may cushion the crisis' impact on consumption. Some large-scale investment projects in health and infrastructure are continuing, while other plans have been postponed.

The external sector is set to contribute negatively this year, reflecting a weaker external environment, elevated global uncertainty and a substantial decline in tourism revenues. A fall in domestic demand is expected to drag imports down at a slower pace than exports in 2020, before imports growth outpaces exports' in 2021. The current account surplus, which peaked in 2017, is projected to gradually narrow over the forecast horizon, but to remain high. An easing in general restrictions is expected to re-stimulate domestic demand in 2021, though it is set to remain below its 2019 level.

As a small open economy, Malta's economic outlook is highly sensitive to global uncertainties and the growth performance of its trading partners. Their economic development in the wake of the COVID-19 pandemic may weigh on Malta's exports and pace of recovery more strongly than assumed in this forecast.

Tight labour market inevitably affected despite the government's financial packages

The fast pace of economic growth in Malta led to a record-low unemployment rate of 3.5% in 2019, but in the wake of the COVID-19 crisis, the temporary closure of tourism-related activities is set to have a harsh impact on employment. Despite the financial aid made available to employees and the government's measures to cushion the impact on corporates, the unemployment rate is projected to increase to around 6% in 2020 before decreasing again in 2021 to 4½ %.

Inflation eases amid recession

Headline inflation is projected to moderate from 1.5% in 2019 to 0.7% in 2020 and 1.1% in 2021. The strong decline in energy prices should contribute to this slowdown with an expected fall in fuel prices in 2020. The interruption of hospitality-related activities will substantially impact services inflation as a result of demand

contraction and wage reductions. In turn, possible disruptions in supply-chains may create inflationary pressures for some imported goods.

Fiscal position set to deteriorate temporarily

In 2019, the government surplus declined to 0.5% of GDP from 1.9% a year earlier. The outcome fell short of the government's plans to assure a balanced budget when discounting for the proceeds of the Individual Investor Programme (citizenship scheme), mainly due to lower-than-budgeted VAT receipts. The favourable economic environment translated into strong growth in income taxes and social contributions. Nevertheless, outlays on intermediate consumption, wages and capital outpaced positive revenue developments.

In 2020, the general government balance is projected to swing into a large deficit of around 6¾% of GDP. Revenue from indirect taxes is set to decline as household consumption falls. Direct tax revenues are projected to record a slight positive growth given the assumed wage growth and profits recorded by companies in the previous year. The

main drag on the fiscal balance will come from the financial packages adopted to combat the economic impact of COVID-19. Wage supplements, additional spending on healthcare and social benefits, and interest rate subsidies are expected to cost around 4% of GDP. Moreover, the social measures announced in the 2020 budget, which was prepared under a more favourable economic scenario, are expected to be implemented.

Assuming no changes in policies, which implies that the pandemic-related measures would be discontinued after a few months and healthcare spending would decline to pre-2020 levels, the general government balance should improve strongly, but remain in a deficit of around 2½% of GDP.

After declining steadily since 2011, the government debt-to-GDP ratio is forecast to surge to about 51% in 2020 and remain around this level in 2021, driven by adverse developments in the deficit.

Table II.13.1:

Main features of country forecast - MALTA

	2018			Annual percentage change						
	mio EUR	Curr. prices	% GDP	00-15	2016	2017	2018	2019	2020	2021
GDP	12366.3	100.0		3.4	5.8	6.5	7.3	4.4	-5.8	6.0
Private Consumption	5406.0	43.7		2.2	2.4	3.4	7.6	2.4	-5.0	4.0
Public Consumption	1993.9	16.1		2.8	-3.0	1.8	12.7	12.0	12.8	-1.2
Gross fixed capital formation	2335.9	18.9		5.0	-0.3	-6.9	-2.1	7.2	-7.0	5.0
of which: equipment	768.9	6.2		-	13.0	-35.1	-10.7	1.7	-	-
Exports (goods and services)	17922.3	144.9		5.6	4.5	4.8	3.5	1.7	-9.3	12.0
Imports (goods and services)	15314.2	123.8		5.3	1.6	-0.5	3.4	2.1	-7.2	10.8
GNI (GDP deflator)	11352.2	91.8		3.1	2.4	6.0	7.7	4.0	-5.8	6.0
Contribution to GDP growth:										
Domestic demand				2.9	0.6	0.2	4.9	4.3	-1.3	2.4
Inventories				-0.1	0.5	-1.7	1.6	0.2	-0.1	0.1
Net exports				0.7	4.7	8.0	0.9	-0.2	-4.4	3.4
Employment				1.8	4.3	8.1	6.0	5.6	-1.8	2.8
Unemployment rate (a)				6.6	4.7	4.0	3.7	3.4	5.9	4.4
Compensation of employees / head				3.7	2.9	-0.5	2.1	2.4	3.4	2.8
Unit labour costs whole economy				2.0	1.4	1.0	0.8	3.6	7.8	-0.3
Real unit labour cost				-0.4	-0.1	-1.5	-1.3	1.3	5.9	-1.5
Saving rate of households (b)				-	-	-	-	-	-	-
GDP deflator				2.5	1.5	2.5	2.1	2.3	1.8	1.3
Harmonised index of consumer prices				2.2	0.9	1.3	1.7	1.5	0.7	1.1
Terms of trade of goods				0.8	-4.2	4.4	2.7	1.1	3.1	0.4
Trade balance (goods) (c)				-15.8	-18.4	-12.6	-11.7	-11.8	-8.0	-11.4
Current-account balance (c)				-3.2	3.8	11.5	11.3	10.7	7.6	9.7
Net lending (+) or borrowing (-) vis-a-vis ROW (c)				-1.8	4.1	12.1	12.2	11.7	8.6	10.7
General government balance (c)				-3.7	1.0	3.3	1.9	0.5	-6.7	-2.5
Cyclically-adjusted budget balance (d)				-3.6	-0.3	2.1	0.1	-1.3	-4.2	-1.3
Structural budget balance (d)				-	-0.1	2.3	0.0	-1.3	-4.2	-1.3
General government gross debt (c)				65.8	55.5	50.3	45.6	43.1	50.7	50.8

(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.