



Medium-Term Fiscal Strategy for Malta:

**Update of Stability Programme
2019 - 2022**

The following symbols have been used throughout this document:

... to indicate that data are not available;

— to indicate that the figure is negligible;

0 to indicate that the figure is zero;

- to indicate that data are not applicable or cannot be determined;

n/c to indicate that there is no change in the data.

f to indicate that it is a forecast

Figures may not add up due to rounding.

Introduction

This Programme constitutes the tenth update of Malta's Stability Programme. The first Update for Malta was submitted in December 2008.

The present submission has been prepared in accordance with Council Regulation (EC) No. 1466/97 as amended by Council Regulation (EC) No. 1055/05 and Council Regulation (EC) No. 1467/97 as amended by Council Regulation (EC) No. 1056/05.

This document is also in line with the new requirements of the Stability and Growth Pact, namely the amendments to Council Regulation (EC) No. 1466/97 by Council Regulation (EU) No. 1175/2011 of the European Parliament and of the Council of 16th November 2011 and the amendments to Council Regulation (EC) No. 1467/97 by Council Regulation (EU) No. 1177/2011 of 8th November 2011. The programme also takes into account Council Directive 2011/85/EU of 8th November 2011 on the requirements for budgetary frameworks of the Member States.

The Stability Programme now also meets the reporting requirements under Article 15 of the Fiscal Responsibility Act, 2014 and will therefore constitute Malta's Medium-Term Fiscal Plan. It is the intention of the Government to submit this Plan to the House of Representatives together with the fiscal risk assessment to be provided by the Malta Fiscal Advisory Council (MFAC) in line with Article 15(1) of the Fiscal Responsibility Act, 2014.

The document is in line with the 'Specifications on the Implementation of the Stability and Growth Pact and Guidelines on the format and content of Stability and Convergence Programmes', endorsed by the Economic and Financial Affairs Council on 24th January 2012. Nevertheless, it contains additional information as required by the Fiscal Responsibility Act.

The Ministry for Finance compiled this document, with important contributions from the National Statistics Office as well as from other Ministries and entities across Government. It was prepared on the basis of policies proposed in the 2019 Budget and updated with the latest macroeconomic projections and more recent fiscal data.

The outline of the programme is as follows:

- Chapter 1 presents Government's Medium-Term Fiscal Policy Strategy including the public expenditure priorities and the public investment programme in order to fulfil the requirements of Article 15(7) of the Fiscal Responsibility Act;
- Chapter 2 presents the main macroeconomic projections for the medium-term as well as the potential impact of a selection of structural reform measures;

- Chapter 3 outlines the overall fiscal policy strategy and updated budgetary plans for the current year, followed by a presentation of the medium-term fiscal projections and debt developments;
- Chapter 4 contains an analysis of forecast uncertainty and the balance of risk surrounding macroeconomic projections and an evaluation of the risks to the achievement of fiscal targets conditional on alternative plausible macroeconomic conditions;
- Chapter 5 reviews the long-term sustainability of public finances;
- Chapter 6 analyses the quality of public finances;
- Chapter 7 reviews recent institutional developments related to public finances.

The macroeconomic forecasts underlying this Programme have been submitted to the Fiscal Advisory Council for its endorsement. The Council concluded that, “Based on the information available to the Malta Fiscal Advisory Council, and after taking due consideration of the uncertainty inherent in macroeconomic forecasts, the Council considers the full set of macroeconomic forecasts for the period 2019 to 2022 prepared by the Ministry for Finance as part of the Update of Stability Programme 2019 – 2022 to lie within its endorsable range”. The fiscal projections underlying this Programme will be submitted to the Council for its evaluation and endorsement in line with the requirements of the Fiscal Responsibility Act. This exercise is expected to be concluded in the coming weeks.

1. Medium-Term Fiscal Policy Strategy

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The year 2018 was another positive year where the pace of economic expansion continued to excel thus allowing for the further build up of fiscal buffers. A fiscal surplus of 2.0 per cent of Gross Domestic Product (GDP) and a debt ratio of 46 per cent of GDP were indeed achieved. This Medium-Term Fiscal Strategy continues to build on past achievements with robust economic growth and a structural budget surplus net of the Individual Investors Programme (IIP) planned over the coming three years. The projections underlying this Programme suggest that these targets are realistic and sustainable. This notwithstanding, macroeconomic risks justify the maintenance of additional fiscal buffers as an over-arching objective of this Strategy.

In the context of the requirements of the Fiscal Responsibility Act, this Programme is being submitted to the Malta Fiscal Advisory Council for its endorsement thus elevating it to the status of Malta's Medium-Term Fiscal Plan. The Medium-Term Fiscal Policy Strategy includes the expenditure priorities and the public investment programme highlighted in this chapter in order to fulfil the requirements of Article 15(7) of the Act. In the process of its assessment, the Malta Fiscal Advisory Council will carry out a fiscal risk assessment. Once this is completed, the report of the Malta Fiscal Advisory Council will be considered by Government and will then be submitted to the House of Representatives in conjunction with the Stability Programme.

1.1 Economic Situation and Risks to the Outlook

Economic conditions supporting the fiscal performance in 2018 remained strong, underlined by a robust rate of actual growth of 6.6 per cent and potential growth of 6.8 per cent in 2018. It is clear that the rate of economic growth in Malta is predominantly structural and buoyed by supply-side developments and a strong improvement in competitiveness. In particular, the significant rise in the export market shares in services is consistent with substantial improvements in regional competitiveness registered in accommodation and food services, remote gaming and professional services (Borg and Vella, 2019). Another development is the strong and positive contribution to potential growth of total factor productivity, which is estimated to have reached 1.9 per cent in 2018. These indicators suggest that the real rate of economic growth of 6.6 per cent in 2018 can be sustained over the short to medium-term without generating any significant macroeconomic imbalances.

These developments will continue to support the strong pace of potential growth albeit some moderation is expected over the forecast period. It is also interesting to note, that the substantial increase in the investment-to-GDP ratio was achieved at a time when the economy was registering successive surpluses in the current account of the balance of payments. This suggests that the overall savings ratio in the economy was increasingly financing the rise in investment activity. The improvement in the current account is also underlined by the gradual improvement in the fiscal position. In particular, it is worth noting that Government has been registering a primary surplus (budget balance excluding interest payments) and a current surplus (budget balance excluding investment) since 2013. This increase in public savings has also contributed

to the correction of the twin deficits, thus confirming that the Maltese economy is not suffering any major external imbalances.

Growth in 2018 was driven by domestic demand mitigating the weak external demand conditions. This outcome was underpinned by a general weakening of growth among Malta's trading partners as well as an appreciation of the Euro against major currencies which slowed down the pace of growth of Maltese exports. On the domestic side, the strength of the labour market supported the strong momentum in household consumption coupled with a strong expansion in public investment, as Government embarked on a determined effort to absorb European Union (EU) funds.

Economic performance manifested itself in a sturdy and relatively broad-based growth in sectoral gross value added. This was generally a continuation of the performance of 2017, albeit stronger in the case of real-estate and construction, remote gaming and financial services. Tourism experienced another record year. Manufacturing and Wholesale and Retail trade activity also recorded another positive year of growth, albeit more moderate than last year.

Furthermore, the import content of domestic production kept diminishing in 2018, though perhaps for different reasons than previous years. In particular, the stronger element of construction activity in investment, a lower imported energy component of production and lower financial services imports were the main contributors to the decline in imports as a share of GDP. On the other hand, the import content of services (other than financial services) remained at the same ratio as last year. The decline in the import content of production is a key phenomenon of the Maltese economy in the last few years and generally explains why all forecasts of the Maltese economy have tended to underestimate growth year after year. Nevertheless, it is difficult to determine future trends based on last year's developments as such data is often subject to statistical revisions which inevitably demands an element of restraint on the part of forecasters.

From the income side, economic growth is supported by strong growth in profits of 9.7 per cent whilst compensation of employees rose by 7.2 per cent.

From a fiscal perspective, the composition of growth was tax rich, with a solid growth in household consumption and incomes. The Harmonised Index of Consumer Prices (HICP) inflation was also stronger than what was recorded in 2017. The property market also expanded robustly in 2018 and generated substantial tax revenue. These factors supported a strong performance in indirect tax revenue. The more moderate growth in incomes, particularly corporate profits, underlined the more moderate growth in taxes on income.

The macroeconomic forecasts underlying this Programme suggest a gradual moderation in economic activity and a measured correction in the positive output gap expected over the next three years. This is in part due to the conservative forecasts surrounding this three-year plan, in line with past practices. Nevertheless, the Government is of the view that Malta will continue to experience a positive economic situation over the forecast period and will register a growth of 6.2 per cent in 2019. Growth is expected to moderate to 5.7 per cent in 2020 and reach 5.0 per cent by 2022. These macroeconomic

projections have been submitted to the Malta Fiscal Advisory Council, as required by the Fiscal Responsibility Act, and subsequently endorsed.

Like all forecasting exercises, this largely positive macroeconomic outlook is conditional on a number of assumptions. External demand conditions this year are assumed to be slightly weaker than last year but will recover slowly over the medium-term. In the baseline scenario, a soft BREXIT is expected to materialise while further escalation of trade protectionist measures is not envisaged. Monetary policy is expected to remain largely accommodative. Despite the external situation, domestic demand is expected to remain the main driver of growth supported by a continued growth in production and employment, which is mainly supply driven and hence not overly constrained by the generally weak global demand conditions. Service oriented sectors will continue to grow robustly. Investment activity will be driven by a number of large-scale investment projects stimulating construction activity, though there are still a number of projects which are not taken completely on board in the baseline forecast.

The baseline scenario underpinning this Programme has been subjected to a series of exogenous shocks producing alternative growth scenarios. Based on these scenarios and an evaluation of past forecast accuracy, the risks surrounding macroeconomic forecasts have been quantified. Based on the established methodology, this risk assessment suggests exposure to both upside and downside risks though the risk profile is balanced on the downside for short-term, due primarily to the uncertainty related to weaker global trade activity resulting from protectionist trade policies. The balance of risk turns on the upside over the medium-term period. The alternative macroeconomic scenarios have also been used to gauge the fiscal response to the materialisation of such risks. It is encouraging to note, that under the worst case macroeconomic scenarios contemplated, the budget balance remains well within the 3 per cent of GDP benchmark of the corrective arm of the Stability and Growth Pact.

1.2 Fiscal Performance and Stance

Over the last six years, Government managed to turn a deficit of 3.5 per cent of GDP in 2012 to a surplus of 3.4 per cent of GDP in 2017. In 2018, the surplus reached 2.0 per cent of GDP compared to a surplus of 1.1 per cent of GDP targeted in the previous Update. The gradual but consistent fiscal effort positively impacted the debt ratio which fell below the 60 per cent target to 46.0 per cent of GDP in 2018. The fiscal strategy presented in this Programme will reduce the debt burden even further to 33 per cent of GDP by 2022. The Government considers fiscal developments over the last four years as an important achievement, particularly the recovery of the necessary fiscal space to allow fiscal policy to act in a countercyclical manner. The achievement of the Medium-Term Objective (MTO) was also an important step in safeguarding long-term sustainability of public finances. The budget surplus also allows more room for manoeuvre to address other structural challenges such as infrastructural bottlenecks and further investments in human capital and technology. This reinforces potential growth and supports the process of convergence to higher living standards. In this context, it is opportune to note that in 2017, GDP per capita in Purchasing Power Standards had already reached 96 per cent of the EU average, up from 83 per cent in 2010. At the same time, Government is conscious of persistent challenges in the external environment which support the need for continued prudence in the fiscal targets and the creation of additional buffers.

Whilst recognising the minimum binding constraint of maintaining a fiscal position within the MTO, the medium-term fiscal strategy portrayed in this Programme is one that essentially aims to maintain a surplus net of IIP. The budget balance is targeted to reach 0.9 per cent of GDP in 2019 and to remain close to 1.0 per cent of GDP over the medium-term. Such targets are themselves based on prudent fiscal assumptions which create an extra buffer in these projections. The targets presented in this Programme are consistent with the allocation of around 3.9 per cent of GDP towards public investment programmes in 2019 and around 3.2 per cent of GDP over the medium-term in order to address infrastructural bottlenecks. These investments do not include additional investment devoted to the improvement of human capital to meet the challenges in the education sector, which are generally classified elsewhere in the ESA categorisation.

1.2.1 Government's Expenditure Priorities

The Government is committed to implement its work programme on the basis of the Electoral Manifesto. It is also committed to make the best use of EU funds from the 2014-2020 Programming period.

Whilst consolidating earlier achievements, the 2019 Budget focused primarily on addressing infrastructural bottlenecks to growth, particularly in transport, social housing and waste management whilst addressing distributional challenges. Economic growth has also brought to the fore both skill and labour market bottlenecks which are being addressed in order to ensure that the present rate of potential economic growth can be maintained over the medium to long-term.

In the context of the increasing financial sophistication of the economy, the fight against tax evasion and money laundering is high on the Government's agenda. Health, Education and Social Protection continue to be a priority in line with Government's commitment to improve the standard of living of the Maltese population, including the most vulnerable individuals and families whilst at the same time ensuring equality of opportunity for everyone willing to further their education or to contribute directly in the labour market.

Notwithstanding these expenditure priorities, the Government is constantly striving to ensure that expenditure leads to high quality outcomes. Given the positive budgetary developments, this year's Programme continues to focus on the quality of public spending. Indeed, ensuring that expenditure growth does not exceed the economy's growth potential remains an intermediate target in this Programme. As outlined in this programme, gains in public sector productivity can play a role in enhancing the quality of public expenditure. Furthermore, the spending review process has shown that incremental benefits are possible not just in terms of expenditure savings but more importantly with respect to better public sector outcomes and productivity.

The Government remains committed to continue with the pension reform process. Important steps were adopted in 2016 through measures intended to strengthen the sustainability of pensions, particularly through the lengthening of the contribution period and the introduction of incentives to defer retirement. Measures were also adopted to strengthen adequacy of contributory pensions, particularly through increases in pensions. In reforming the pension system, the Government seeks to tie in with the contours of the

recommendations to be laid on the Table of the House of Representatives by not later than end-2020. A report by the Pensions Strategy Working Group shall be reviewing the state of public pensions together with recommendations with a view of achieving further adequacy, sustainability and social solidarity in such manner that a stable proportion is kept between the contribution periods. The Pension Strategy Group set up a number of working groups addressing matters such as pensions and divorce, demographics and fertility, pension economic modelling, and review of voluntary pensions framework. Government has introduced over recent years a number of measures intended to diversify retirement income, such as voluntary third pillar pension products, voluntary occupational pensions and the Home Equity Release Scheme.

The conduct of comprehensive reforms in the public health system to ensure the delivery of a cost-effective and efficient service has been high on the political agenda over the past few years. This has been mainly driven by strategic investments to underpin the revision of existing processes, whilst shifting the focus of care away from hospital and towards the primary health care setting. The review of existing processes is also highlighting which areas are best suited for structural expansion in capacity with a view to maximising return on investment. Progress has also been registered with respect to strengthening health promotion and disease prevention. These developments reflect the adoption of a new National Health Systems Strategy covering 2014-2020 and Strengthening of Primary Care.

1.2.2 Public Investment Programme

Malta's Partnership Agreement presents the overarching strategy and identifies the priorities in the allocation of EU funds. In this regard, the Partnership Agreement has identified three funding priorities which are considered as the main overarching objectives for the 2014-2020 programming period, namely:

1. Fostering competitiveness through innovation and the creation of a business-friendly environment;
2. Sustaining an environmentally-friendly and resource efficient economy; and
3. Creating opportunities through investment in human capital and improving health and well-being.

The main overarching objectives will be addressed through two Operational Programmes and their respective priority axis. The Priority Axes of the first Operational Programme are the following:

1. Investing in research, technological development and innovation;
2. Consolidating investment within the ICT sector;
3. Enhancing Malta's competitiveness through investment in Small and Medium-Sized Enterprises (SMEs);
4. Shifting towards a low-carbon economy;
5. Protecting our environment - investing in natural and cultural assets;
6. Sustainable Urban Development;
7. Shifting towards a more low-carbon transport sector;

8. Investing towards a more socially-inclusive society;
9. Developing our future through education, training and lifelong learning;
10. Investing in a more environmentally-friendly society;
11. Investing in TEN-T Infrastructure; and
12. Technical Assistance.

The second Operational Programme targets employment, education, social inclusion and health and is aimed at achieving inclusive growth. The priority axes of the second Programme are:

1. Investing in the employability and adaptability of human capital;
2. Towards a more inclusive society;
3. Investing in people through Education, Training and Life Long Learning;
4. Building the Institutional Administrative Capacity; and
5. Technical Assistance.

These objectives and priority axes in general also apply to the national funds earmarked for capital investment. In addition to the co-financing element of EU-funded projects, locally financed investments are mostly targeted to road, education and health infrastructure, waste management and environmental management.

1.3 Structural Reforms

The Government's priority remains that of simultaneously securing sustainable economic growth and sustainable public finances. The Government is undertaking measures targeting infrastructural bottlenecks, strengthening the labour market and investing in education and technology as well as implementing further initiatives pertinent to the pension reform process. In addition, it will continue implementing measures to enhance the governance framework across all economic sectors and continue with the drafting and implementation of different climate and energy policies. The 2020 National Reform Programme and this Update of the Stability Programme outline Government's strategy and policy measures intended to address challenges in the structural and fiscal policy domains.

On the fiscal side, the Government is enhancing the spending review process by strengthening the institutional framework. Several amendments were affected with a view to ensure full consistency with the Directive on Budgetary Frameworks as well as other amendments intended to ensure clarity in the administration of the Fiscal Responsibility Act. An internal process is underway to assess the recommendations outlined by the International Monetary Fund (IMF) in its Fiscal Transparency Evaluation which generally established that many practices in place are sound from a fiscal transparency perspective. The Government is also committed to continue the simplification of the tax system which in turn will alleviate the administrative costs associated with the computation of tax liability. A legal notice containing the EU Anti-Tax Avoidance Directives Implementation Regulations has been published in a bid to address tax avoidance. All but one of the

regulations have entered into force as of January 2019, with the regulation on the Exit tax coming into effect as from January 2020.

The Government is seeking to amend the Malta Financial Services Authority (MFSA) Act in a bid to strengthen both the regulatory and the supervisory roles with respect to the financial services sector. The Authority's resource capacity is being strengthened. In connection with the supervision of Anti-Money Laundering/Combating the Financing of Terrorism (AML/CFT), the MFSA and the Financial Intelligence Analysis Unit (FIAU) are in the process of enhancing the Money Laundering/Financing of Terrorism (ML/FT) risk assessment procedures for financial institutions and other Designated Non-Financial Businesses and Professions (DNFBPs) (namely trustees and company service providers). The Government also launched the AML/CFT strategy prepared on the basis of the National Risk Assessment (NRA) and a thorough gap assessment of Malta's AML/CFT framework in a bid to further strengthen and raise the profile of the local supervisory framework locally and internationally. The National Coordinating Committee on Combating Money Laundering and Funding of Terrorism was established in April 2018, with the objective of drawing up, implementing and carrying out follow-up action with respect to a national strategy and policies to combat money laundering and the funding of terrorism. The Asset Recovery Bureau (ARB) became operational in mid-2018 and is responsible for efficient identification, tracing, collection, storage and disposal of proceeds of crime or property in favour of Government.

In the context of good governance, over recent years, Government embarked on various initiatives that sought to reform the national justice system. These include extensive use of ICT and setting up of a specialised Court presided by a specialised member of the judiciary who hears and decides cases falling within its jurisdiction. The Government is also enacting institutional reforms to address a number of the recommendations made by the Council of Europe's Venice Commission.

A number of measures are also being implemented in a bid to encourage diversification of retirement income, thus reducing the sole dependency on state pensions. The Malta Stock Exchange is actively contributing towards the increase in the level of financial literacy through the Strategy on Retirement and Financial Capability. In the 2019 Budget, the Government continued to strengthen the incentives for the Third Pillar Pension Scheme and the Voluntary Occupational Pension Scheme. Moreover, the Government has recently launched the voluntary Home Equity Release Scheme enabling financial institutions to start providing this facility to retirees. The scheme is intended to provide pensioners with an alternative method to supplement their income.

Long-term economic sustainability also depends on an effective health care strategy. The Government seeks to maintain an efficient healthcare system which is free and accessible to all, while also curtailing expenditure. The National Health System Strategy (NHSS) targeted health promotion and disease prevention through a number of sectoral strategies that have been launched over recent years. A new one-stop facility for community care which will also provide specialised care for several diseases and conditions, is being developed. The Southern Regional Hub is expected to become operational by 2023. Furthermore, by 2020, the Primary Health Care Services will be introducing an Electronic Patient Record system to replace the current paper-based

system, in order to decrease the cost of the health care service while also reducing the administrative burden and improving health care provision.

Various infrastructural projects are underway, most notably numerous road work projects, as part of the TEN-T core network, which include the building and upgrading of various main roads in Malta. Furthermore, the Government is committed to mitigate the developmental obstacles Gozo faces arising from double-insularity and detachment from core economic and social activities. The possibility of a tunnel is being studied in order to create a permanent link between the two islands. A study is also being carried out to evaluate the introduction of a Mass Rapid Transport System (MRT) for Malta in a bid to facilitate and provide an alternative public transport system while lowering the carbon footprint. Furthermore, the Government acknowledges the importance of the contribution of SMEs to the economy, in particular their potential to drive innovation in the Maltese economy. In this respect, it is assisting existing SMEs and start-ups through public as well as EU funds.

A number of initiatives attest to the Government's commitment to foster the use and development of disruptive technologies. In October 2018, the Malta Digital Innovation Authority (MDIA) was set-up with the aim of promoting and developing the innovative technology sector in Malta by means of proper recognition and regulation of relevant innovative technology arrangements and related services. Its remit also covers the certification of Distributed Ledger Technologies (DLT) platforms, thus providing legal certainty for users, whilst at the same time increasing the prospects for investment in innovative technology. Moreover, the Government has established a MALTA.AI Taskforce through which it aims to develop a National Strategy for Artificial Intelligence (AI).

2. Economic Outlook

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2.1 Economic Conditions for 2018

In 2018, the Maltese economy recorded a real growth rate of 6.6 per cent, equivalent to 8.9 per cent in nominal terms. This growth figure was 4.7 percentage points higher than that of the European Union (EU) of 2.0 per cent, which means that Malta remained among the top performers in the European economy. While the rate of growth of the Maltese economy was broad-based, the domestic demand component was the main driver for growth, contributing to 4.3 percentage points. Net exports also contributed 1.4 percentage points towards growth, while there was also a positive contribution of 0.9 percentage points from changes in inventories in 2018.

Underpinning this positive performance was the consistent growth in household and Government consumption. Buoyant private consumption in 2018 was supported by strong employment growth, increases in disposable income and a large accumulation of savings in recent years. In the meantime, the growth in Government consumption mainly reflected higher compensation of employees including the impact of the new collective agreements for public sector employees. There was also an improvement in investment activity compared to 2017, which mainly reflected the acceleration in EU-funded investment projects. From an external standpoint, export activity in real terms and export prices moderated due to weaker external demand conditions. An increase in real imports was also registered, mostly driven by strong domestic demand, and higher oil prices.

Gross Value Added (GVA) at basic prices increased by 8.3 per cent in 2018. The output side confirms that this growth is primarily attributed to the services sector, which contributed 7.2 percentage points to growth in GVA. The industry sector was responsible for the rest of the growth in GVA. Overall, all sectors recorded a positive growth rate. Indeed, the services sector maintained a strong share in GVA at 89.0 per cent, while the industry sector maintained a share of 10.0 per cent of GVA. Delving deeper into the individual sectors shows that the highest growth rates were recorded in Real Estate, which grew by 13.0 per cent over the year, followed by Arts, Entertainment and Recreation (11.3 per cent), Construction (10.3 per cent), and Professional Services (9.8 per cent) sectors. The sector that contributed the most towards GVA growth was Arts, Entertainment and Recreation with a contribution of 1.6 percentage points, followed by the Professional, Scientific and Technical sector, and Public Administration, Education and Health sector (both with a contribution of 1.5 percentage points).

On the income side in 2018, compensation of employees increased by 7.2 per cent in nominal terms to reach €4,972.2 million. Gross operating surplus and mixed income growth remained strong at 9.7 per cent, reaching €5,920.7 million. Meanwhile, subsidies on production and imports experienced an increase of 23.9 per cent reaching €181.4 million, while revenue from taxation on production and imports rose by 13.0 per cent reaching €1,608.3 million.

During 2018, the global economy continued to expand, albeit at a moderate and uneven pace. According to the International Monetary Fund's (IMF) most recent Economic Outlook, the global economy expanded by 3.6 per cent in 2018, which is 0.2 percentage points lower than the growth recorded in 2017. The moderation is expected to further persist in 2019, as global Gross Domestic Product (GDP) is expected to grow by 3.3 per cent and recover to 3.6 per cent in 2020. These growth figures are relatively low

when compared to the previous forecasts, reflecting a slowdown in the expected global growth momentum.

Global and EU cross-border investment slowed down in 2017 and in the first half of 2018, whilst capital flows moderated compared to previous years. Ongoing trade tensions and cross border uncertainty were the key elements behind the slowdown in investment. Compared to the pre-crisis period current account balances across the world have moderated and a shift of imbalances towards advanced economies was noted.

Downside risks have increased for the Euro Area (EA) due to a combination of external and internal factors, including slower global trade growth, high trade policy uncertainty, global manufacturing weaknesses, and domestic growth impediments. There is also a lot of uncertainty surrounding Brexit, with the outcome of the Brexit process set to impact the financial sector and investors alike. Consequently, the Euro started to depreciate in the second half of 2018 against most of the major currencies, as well as against some of the emerging markets currencies. This trend has continued in the first quarter of 2019. According to the European Commission (EC), the lower momentum in economic activity is expected to persist in 2019, and subsequently, growth is expected to stabilise in 2020. On the positive side, labour market conditions improved in 2018, which together with more muted inflation and declining oil prices since Autumn of last year, should help in the economic expansion of the EA.

In the local scene, the current account surplus in 2018 was primarily driven by significant increases in the services net export balance. The personal, cultural and recreational services, together with the tourism sector were the largest contributors towards the net export figure in the services balance. Furthermore, the goods and services balance continued to register a strong net export balance owing to a decrease in the net import balance in the goods account and the increasing service orientation of the Maltese economy coupled with the resulting drop in the import content of exports.

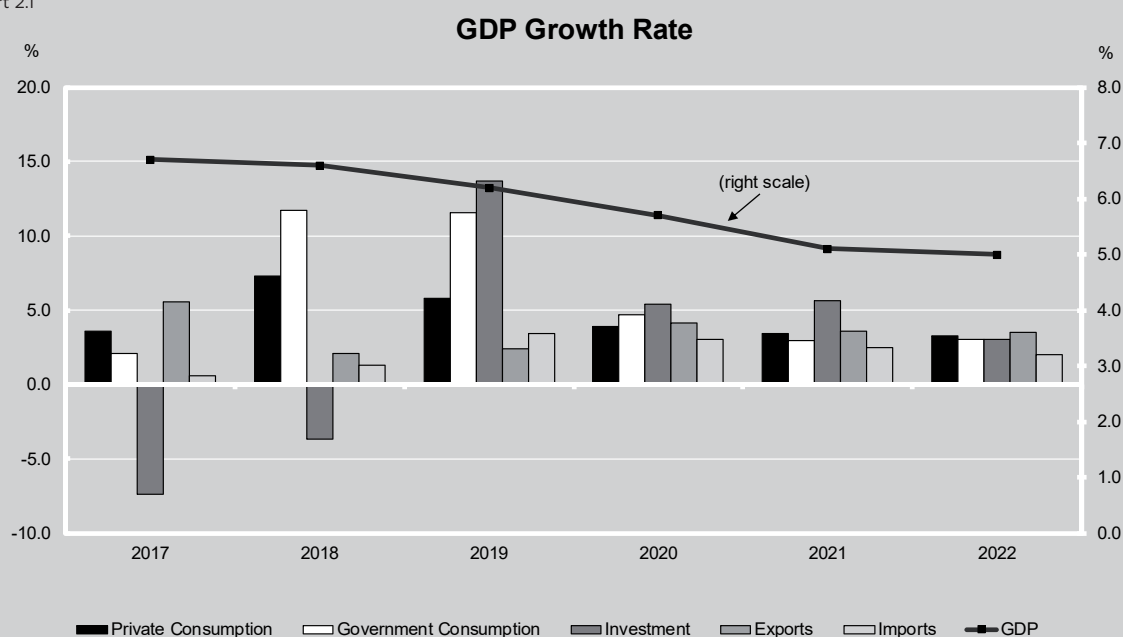
In terms of income flows, the primary income balance net payments increased from €0.6 billion in 2015 to €1.1 billion in 2018 owing to increases in net payables in direct investment and a drop in net receivables with respect to portfolio investments.

Despite the substantial increase in investment, the growth in the Maltese economy supported an even greater increase in savings resulting in capital outflows and a net accumulation of foreign assets. The net asset position has stabilised at €28 billion as from 2015, with the increase in net direct investment liabilities of €128 billion being largely offset by the combined increase of €127 billion in net portfolio and other investment assets since then.

2.2 The Medium-Term Scenario

Over the projection period, the Maltese economy is expected to continue growing at a strong pace, with real GDP projected to reach a growth rate of 6.2 per cent in 2019 and 5.7 per cent in 2020. Economic growth is expected to be primarily driven by the domestic component of the economy, which is projected to contribute 7.0 percentage points to growth in 2019 and 3.7 percentage points to growth in 2020, underpinned by robust growth in investment, as well as growth in both private and public consumption. External developments are expected to negatively contribute to growth in 2019, with a strong growth in imports reflecting the positive developments in investment activity. However, the net trade contribution is expected to turn positive in 2020, contributing

Chart 2.1



Main Macroeconomic Indicators

Table 2.1

	2017	2018	2019f	2020f	2021f	2022f
GDP growth at current market prices (%)	9.4	8.9	9.3	8.3	7.4	7.2
GDP growth at Chain Linked Volumes by period (Reference year 2010) (%) ⁽¹⁾	6.7	6.6	6.2	5.7	5.1	5.0
Expenditure Components of GDP						
at Current Market Prices by period (%)						
Private final consumption expenditure ⁽²⁾	4.7	8.2	7.6	5.1	4.9	4.8
General Government final consumption expenditure	3.9	15.9	15.8	6.8	5.6	5.7
: net of Individual Investor Programme (IIP) proceeds	7.3	11.0	11.4	6.6	5.3	5.4
Gross fixed capital formation	-5.4	0.6	17.3	9.0	8.7	5.6
Exports of goods and services	8.6	4.3	4.7	6.4	5.9	5.7
: net of Individual Investor Programme (IIP) proceeds	8.2	4.7	5.1	6.5	6.0	5.7
Imports of goods and services	2.6	3.6	5.8	4.9	4.7	4.0
Expenditure Components of GDP						
at Chain Linked Volumes by period (Reference year 2010) (%)						
Private final consumption expenditure ⁽²⁾	3.6	7.3	5.8	3.9	3.4	3.3
General Government final consumption expenditure	2.1	11.7	11.6	4.7	2.9	3.0
Gross fixed capital formation	-7.4	-3.7	13.7	5.4	5.7	3.0
Exports of goods and services	5.6	2.1	2.4	4.1	3.6	3.5
Imports of goods and services	0.6	1.3	3.4	3.0	2.5	2.0
Inflation rate (%)	1.3	1.7	1.9	2.0	1.8	1.8
Employment growth (National Accounts Definition) (%) ⁽³⁾	7.8	5.6	4.6	4.3	4.0	3.8
Unemployment rate (Harmonised definition, Eurostat) (%)	4.0	3.7	3.8	3.9	4.0	4.0
Compensation per employee (% change) ⁽⁴⁾	2.9	2.9	3.3	3.2	3.2	3.1
Labour productivity (% change)	2.5	1.4	1.5	1.3	1.0	1.1
Nominal Unit Labour Cost (% change)	0.4	1.5	1.8	1.9	2.1	1.9
Real Unit Labour Costs (% change)	-0.9	-0.2	-0.1	-0.1	0.3	0.1

⁽¹⁾ Users should note that chain-linking gives rise to components of GDP not adding up to the aggregate real GDP series. This non-additivity, similar to that in other countries' national accounts, is due to mathematical reasons and reflects the fact that chain-linked volumes are calculated by separately extrapolating both totals and their sub-components.

⁽²⁾ Includes NPISH final consumption expenditure.

⁽³⁾ Total Employment based on National Accounts Definition.

⁽⁴⁾ Compensation per employee actual figures and forecasts based on unpublished FTEs.

2.1 percentage points to real GDP growth, supported by a growth recovery in exports, as global conditions improve.

Over the outer years, economic growth is expected to be more balanced and reach 5.1 per cent in 2021 and 5.0 per cent in 2022. In 2021, economic growth is expected to be mainly driven by domestic demand, which is expected to contribute 3.1 percentage points to growth, while the contribution of net exports is also expected to remain strong, contributing 2.0 percentage points to growth. This positive development in external demand is expected to further strengthen in 2022, as the contribution of net exports is projected to equal 2.4 percentage points, while domestic demand is expected to contribute 2.6 percentage points. Therefore, in the outer years, the contribution of domestic demand is expected to be more contained. This reflects a moderate growth in investment activity and Government expenditure as well as a gradual moderation of private consumption attributed to a somewhat slower growth in employment.

Chart 2.1 illustrates the forecasted growth rates of GDP, together with a detailed breakdown of the expenditure aggregates. Table 2.1 presents the main macroeconomic indicators for the years 2017-2022. The figures for 2017 and 2018 represent actual data published by the National Statistics Office (NSO), while the data from 2019 onwards represent the projections of the Ministry for Finance (MFIN). The macroeconomic forecasts take into account the latest available data and are provided in Table 1a, 1b, 1c and 1d of the Statistical Appendix.

2.2.1 Assumptions for Projections

The macroeconomic forecasts presented in this Stability Programme are based on the following assumptions:

- Economic activity in Malta's main trading partners is expected to increase by 1.2 per cent in 2019, then stabilise at a growth rate of 1.3 per cent until 2022.
- World prices are projected to increase by 1.4 per cent in 2019, before growing by a yearly average rate of 1.6 per cent over the outstanding years.
- Oil prices are assumed to fall from an annual average price of \$71.1 per barrel in 2018 to \$65.1 in 2019, then marginally increase to \$66.5 in 2020 and stabilise at this level until 2022.
- The Dollar/Euro exchange rate is expected to depreciate from a yearly average of 1.1751 Dollars per Euro in 2018 to 1.1430 Dollars per Euro in 2019 and then appreciate in 2020 to 1.1760 Dollars per Euro before stabilising at 1.1790 Dollars per Euro in the outer years.
- The Sterling/Euro exchange rate is expected to depreciate from an annual average of 0.8857 Pounds per Euro in 2018 to 0.8613 Pounds per Euro in 2019 and 0.8578 Pounds per Euro in 2020. In the outer years, a slight appreciation over the previous year to 0.8600 Pounds per Euro is projected.
- The short-term interest rate is projected to remain virtually unchanged at around 0.0 per cent over the projection horizon in line with the European Central Bank (ECB)

projections, while the long run interest rate is assumed to remain stable during the forecast horizon at 1.5 per cent.

- Changes in inventory are assumed not to contribute to GDP growth.

These assumptions are outlined in Table 8 of the Statistical Appendix.

2.2.2. Risks to Outlook

The medium-term outlook for the Maltese economy is expected to remain robust. Nevertheless, there are a number of factors that could either boost or limit growth prospects. These risk factors will be explored in more detail in Chapter 4. Nevertheless, it is worth highlighting that the balance of risks shows downside risk for 2019, and upside risks for the outer years.

2.2.3. Private Final Consumption Expenditure

Following the strong growth in 2018, private consumption is expected to continue growing, although gradually moderating over the forecast horizon, on the back of a buoyant labour market coupled with a moderate appreciation in wages. Indeed, private consumption is forecasted to grow by 5.8 per cent in 2019 and at a slower pace of 3.9 per cent in 2020, while over the outer years, it is projected to grow by an average rate of 3.4 per cent.

2.2.4 General Government Final Consumption Expenditure

Government consumption expenditure is expected to continue growing at a strong pace, partly reflecting increases in proceeds from the Individual Investor Programme (IIP). Indeed, public consumption is forecasted to increase by 11.6 per cent in 2019, reflecting strong growth in both compensation of employees and intermediate consumption. In 2020, Government consumption is expected to stabilise and increase by 4.7 per cent, while over the outer years, it is projected to grow by an average rate of 3.0 per cent. This implies that the share of public consumption in real GDP will average at 17.0 per cent over the projection period.

2.2.5 Gross Fixed Capital Formation

It is worth mentioning, that the inherently volatile nature of gross fixed capital formation makes it relatively challenging to forecast. Hence, when forecasting investment, economists within MFIN take a relatively prudent approach, factoring in only those projects that have a strong political commitment or a high probability of realisation, while assuming a relatively high import content.

Over the forecast horizon, gross fixed capital formation is projected to increase by 13.7 per cent in 2019 and by 5.4 per cent in 2020, as several large-scale investment projects particularly in the transport and aviation, tourism, information technology, telecommunications, real-estate, and health sectors are expected to materialise. The lower growth rate in investment projected for 2020 reflects a base effect arising from public investment in the previous year, due to the expected acceleration of EU-funded projects. In the outer years, investment activity is expected to gradually moderate and increase by 5.7 per cent in 2021 and 3.0 per cent in 2022. Moreover, the investment-to-

GDP ratio is expected to increase and average at 18.5 per cent over the forecast horizon, from the ratio of 17.3 per cent recorded in 2018.

2.2.6 External Balance of Goods and Services

In 2018, increases in domestic demand underpinned economic growth. While over the forecast horizon the contribution of domestic demand is expected to remain strong especially in 2019, the contribution of net exports is set to turn positive and strengthen from 2020 onwards, on the back of stronger export growth. The external balance as a percentage of GDP is expected to marginally decline from 21.4 per cent in 2018 to an average of 21.1 per cent over the forecast horizon.

Although the growth in Malta's main trading partners will increase more moderately in 2019 compared to the previous year, the weakening of the Euro against both the US Dollar and the UK Pound Sterling, and improved competitiveness of Malta's services exports are expected to support the increase in Malta's exports of 2.4 per cent in 2019. This growth performance is further supported by the projected increase in IIP proceeds in 2019. In 2020, real exports are projected to grow by 4.1 per cent on the back of improvements in the growth of Malta's main trading partners. Goods exports are expected to increase, while the growth in services exports will be sustained from the previous year. Growth in real exports will then gradually moderate to 3.6 per cent in 2021 and 3.5 per cent in 2022.

In 2019, import growth is expected to outweigh export growth, leading to a negative net trade contribution to GDP growth. Specifically, imports are expected to increase by 3.4 per cent, reflecting the substantial increase in investment activity. However, from 2020 onwards, the contribution of net exports is set to turn positive and remain strong over the forecast horizon, as growth in imports is set to gradually moderate in line with the expected moderation in investment activity. In particular, imports are projected to increase by 3.0, 2.5, and 2.0 per cent in 2020, 2021, and 2022, respectively.

It is worth mentioning, that in Malta, investment activity tends to be highly import-intensive, and thus, year-on-year movements in investment are offset by imports of capital goods, thereby minimising the impact of volatile investment flows on GDP in the medium-term. Furthermore, over recent years, the import intensity of exports has been showing signs of a steady decline consistent with the strong increase in gross value added from the services sector.

2.2.7 Sectoral Balances

The current account forecasts are shown in Table 1d. In 2019, the current account surplus is expected to be lower than in 2018 due to decreases in the goods and services balance, but still remain in surplus. This is mostly owing to higher imports of investment goods as well as external shocks related to goods exports. In the outer years, the current account as a percentage of GDP will continue on an upwards trajectory, mainly due to expected decreases in primary income net payments coupled with moderate increase in the goods and services balance. The expected decrease in the primary income net payments is due to an expected increase in asset holdings, which is expected to exceed the increase in liabilities. Indeed, the decline in the net asset position recorded since 2015 is expected to be reversed by 2022 mainly in view of a strong rise in portfolio investment asset holdings. In addition, in comparison to the last four years, the rate of return on portfolio investments is expected to rise more strongly over the medium-term, supporting a stronger increase in the return on foreign assets than on liabilities. As a result, returns

on foreign assets are expected to increase more than the payments on liabilities, thus reducing the negative primary income account balance over the medium-term.

2.2.8 Productivity and Employment Growth

The labour market continued to yield positive developments in 2018, as employment growth stood at 5.6 per cent (as per National Accounts definition). This reflected strong labour demand conditions and the robust state of the Maltese economy, supported by the inflows of migrant workers and improved business prospects. Employment growth was further supported by ongoing efforts by the Government in promoting and sustaining active labour market policies. These include work-life balance measures, family-friendly measures, in-work benefit and the tapering of benefits, and lower taxes on labour.

Employment prospects are expected to remain favourable, while somewhat moderating over the outer years to edge closer to the long run average. Specifically, employment growth is expected to stand at 4.6 per cent in 2019 and 4.3 per cent in 2020. Over the outer years, employment growth is set to further moderate, increasing by 4.0 per cent in 2021 and 3.8 per cent in 2022. This positive development is expected to be supported by the inflows of foreign workers as well as the increasing female and older worker participation rate. Moreover, the unemployment rate based on the Harmonised definition is projected to stand at 3.8 per cent in 2019 and 3.9 per cent in 2020, before stabilising at 4.0 per cent in the outer years, meaning that expansion in labour demand is expected to be counterbalanced by an increase in labour supply.

Compensation of employees increased by 7.2 per cent in 2018. It is anticipated that this growth momentum will be maintained throughout the forecast horizon, as compensation of employees is forecasted to increase by 8.1 per cent in 2019 and by 7.7 per cent in 2020. Over the outer years, compensation of employees is expected to slightly moderate, growing by 7.3 per cent in 2021 and by 7.0 per cent in 2022, in line with the projected growth in employment. Following an increase in income per head of 2.9 per cent in both 2017 and 2018, further tightening of the labour market over the forecast period is expected to put marginal upward pressures on wages. Concomitantly, growth in compensation per employee is projected to grow by 3.3 per cent in 2019, before stabilising at around 3.2 per cent in the outer years.

Real labour productivity increased by 1.4 per cent in 2018 and it is expected to increase by 1.5 per cent this year. In 2020, real labour productivity is set to grow at a slightly slower pace, increasing by 1.3 per cent, before slowing down in the remaining years, growing at an average rate of 1.1 per cent, in line with the expected moderation of economic activity. Nominal unit labour costs increased by 1.5 per cent in 2018 and are projected to continue increasing at an average rate of 1.9 per cent over the forecast horizon. Moreover, real unit labour costs registered a negative growth of 0.2 per cent 2018 and are projected to increase by an average growth rate 0.1 per cent over the forecast horizon.

2.2.9 Inflation

In 2018, the inflation rate (measured as the twelve-month moving average of the Harmonized Index for Consumer Prices (HICP)) was 1.7 per cent. This was primarily driven by relatively high oil prices, increases in processed food prices and services prices, and moderate growth in energy prices and unprocessed food prices. The inflation rate is expected to increase to 1.9 per cent in 2019 and 2.0 per cent in 2020. It is expected to be mainly driven by food prices (both processed and unprocessed), services prices, and

a moderate growth in energy prices. In the outer years, inflation is projected to increase by 1.8 per cent in both years.

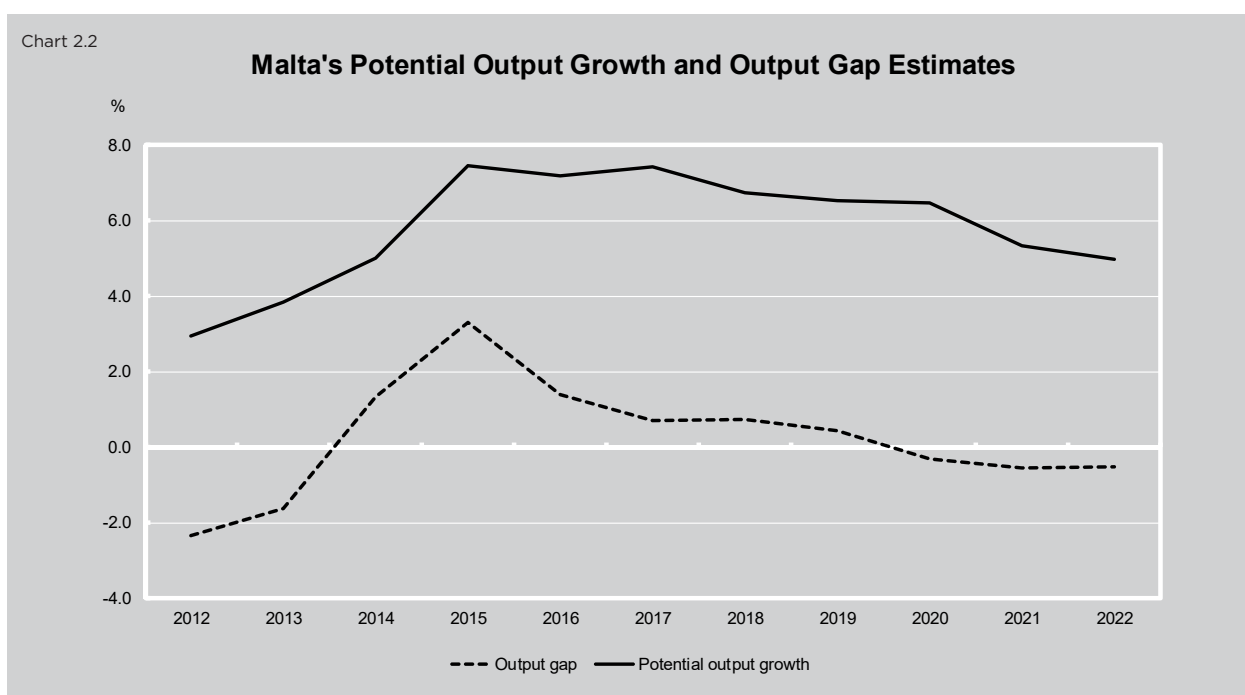
2.2.10 Comparison with the Commission’s Winter Forecast

The 2019 Winter Forecast published by the EC in February, projected a growth rate for Malta of 5.2 per cent and 4.6 per cent in 2019 and 2020, respectively. For 2019, this is 1.0 percentage point below this forecasts’ expectations, while for 2020, this is 1.1 percentage points lower. However, it should be noted that the EC’s Winter Forecast does not use the latest statistical data and that the EC forecasts are currently in the process of being revised. Both the EC’s forecast and the MFIN’s forecast agree that domestic demand will be the key driver of Malta’s growth over both 2019 and 2020. In terms of outlook, a similar outlook to the MFIN’s forecast is foreseen by the EC for private and public consumption, while investment is expected to pick-up on the back of large-scale infrastructure projects. In addition, the EC forecasts the net exports contribution to be slightly negative in both 2019 and 2020. Although this is in line with the MFIN forecast for 2019, the EC forecast assumes a relatively higher import content in both years.

2.3 Potential Output and Output Gap

The estimation of potential output and the output gap within this Update of the Stability Programme is based on the commonly-agreed Production Function method. The main differences between the EC’s and MFIN’s estimation pertain to differences in the macroeconomic forecasts. Developments in the potential output and output gap are presented in Chart 2.2.

During the period 2002 and 2010, potential output growth averaged 2.3 per cent, rising to 5.1 per cent in the following seven-year period. In 2018, the rate of growth of potential output stood at 6.8 per cent and is expected to average around the 5.9 per cent level over the forecast period. The labour market contribution is expected to be the main contributor to potential GDP growth reflecting a higher participation rate. Concomitantly,



growth is supported by Total Factor Productivity and capital accumulation as a result of higher investment. Potential growth is expected to stand at 5.0 per cent in 2022.

The output gap is indicative of the cyclical developments prevailing in the Maltese economy. With the exception of the year 2004, the period 2002 to 2008 has been a period where the Maltese economy operated above its potential level. The output gap turned negative between 2009 and 2013 following the international recession and the subsequent contraction of the domestic economy in 2009. The output gap turned positive as from 2014 and was estimated at 0.6 per cent in 2018. The output gap is expected to close down in 2020 and to remain marginally negative over the forecast horizon as the expansion gradually stabilises.

3. Fiscal Outlook and the Medium-Term Fiscal Strategy

3. Fiscal Outlook and the Medium-Term Fiscal Strategy

The Government succeeded in successfully consolidating public finances turning a deficit of 3.5 per cent of Gross Domestic Product (GDP) in 2012 into a surplus in each of the last three years.

The Maltese Government remains committed to maintain public finance sustainability in the short to medium-term, while also addressing the long-term dimension in particular through the continued reduction in Government debt. The budget surplus also allows more room for manoeuvre to address other structural challenges such as infrastructural bottlenecks and further investments in human capital and technology. This further strengthens potential growth and supports the process of convergence to higher living standards.

As documented in Malta's 2019 National Reform Programme, the Government will continue to address new challenges brought by economic prosperity, while at the same time addressing social obligations. Over the coming years, the Government will continue to ensure that the environment is better protected with increased use of greener and cleaner energy, sustainable water sources, as well as better waste management. The Government will also continue with its programme of upgrading Malta's infrastructure by investing in roads, ensuring sustainable development and providing incentives for alternative forms of commuting. The Government will continue to invest in the upgrading and refurbishing of the health infrastructure and undertake investments in human capital and technology. Backed by a strong economy, the Maltese Government endeavours to improve the income and care for senior citizens and people with disability, people at risk of poverty and those materially deprived, supported by higher levels of investment in social and affordable housing.

The fiscal situation transcends the normal fiscal rules of the Stability and Growth Pact (SGP) and the Fiscal Responsibility Act (FRA). Over the medium-term, the Maltese Government is also committed to ensure compliance with the Medium-Term Objective (MTO). In addition, ensuring that expenditure growth does not exceed the economy's growth potential remains an intermediate target in this Programme. Further improvements in the underlying debt dynamics are expected to be attained through positive growth prospects, sustained investor confidence, and an efficient and effective debt management system. In this respect, the debt-to-GDP ratio is expected to remain well below the 60 per cent threshold, and decline further, until the end of the forecast horizon.

In line with the practice of the previous three Updates of the Stability Programme, the Government's medium-term budget framework, as outlined in this Programme, constitutes Malta's national medium-term fiscal plan as required by Article 4(1) of the European Union (EU) Regulation No. 473/2013 on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member States in the Euro Area.

3.1 Fiscal Developments in 2018

In 2018, the General Government surplus stood at 2.0 per cent of GDP. This exceeded the surplus target of 0.5 per cent of GDP planned in the 2018 Budget, which was subsequently revised to 1.1 per cent of GDP in the 2018 Update of the Stability Programme. The Government also succeeded in recording a General Government surplus net of proceeds from the Individual Investor Programme (IIP).

3.1.1 General Government Revenue in 2018

In 2018, the General Government revenue-to-GDP ratio declined by 0.4 percentage points to 38.8 per cent of GDP, as the ratio to GDP of 'other revenue' declined by the same amount reflecting lower market output.

The tax revenue ratio remained relatively stable at 26.5 per cent of GDP in 2018. The strong developments in the property market and record labour market performance supported strong domestic demand conditions. As a result, revenue from taxes on production and imports registered an increase of 0.5 percentage points of GDP, mainly due to the positive performance from Value Added Tax (VAT) and taxes on financial and capital transactions. Meanwhile, the ratio to GDP of current taxes on income and wealth declined by 0.5 percentage points, mainly underpinned by lower net revenue transferred from income tax. This performance was underlined by a more efficient and expedient administrative process of refunds which reduced the amount of funds transferred to Central Government despite the increase in gross receipts, thus rendering the results not directly comparable to 2017.

Meanwhile, the ratios of social contributions, property income and capital taxes remained relatively unchanged in 2018.

3.1.2 General Government Expenditure in 2018

In 2018, the ratio of General Government expenditure to GDP increased by 1.1 percentage points to 36.8 per cent, as a marginal decline of 0.1 percentage points of GDP in current expenditure was more than offset by a 1.2 percentage points increase in capital expenditure.

Intermediate consumption increased by 0.4 percentage points to 6.8 per cent of GDP in 2018 mainly due to increased outlays by Extra Budgetary Units (EBUs), as well as higher contributions to government entities operating in the energy, waste and financial sectors, and higher expenditure towards health and residential care related activities.

Reviews of Government spending are contributing to the achievement of improved efficiency in public spending, reduction of waste and value for money. As a result of these efforts, as well as the expenditure-reducing effect of measures legislated in previous Budgets, in particular the tapering of social benefits, and the further extension of the retirement age in 2018 by virtue of the 2006 pension reform initiatives, the ratio of social payments declined by a further 0.5 percentage points to 9.5 per cent of GDP. Indeed, the lower ratio for social payments resulted in spite of a number of 2018 Budget

measures addressing the adequacy of pensions, including disability pensions, and other vulnerable groups.

Against the background of the ensuing low interest rate environment and the Treasury's debt management strategy, expenditure on interest payments declined in both absolute and relative terms in 2018.

Expenditure on subsidies and on compensation of employees as a share of GDP remained relatively unchanged in 2018. Developments in the latter reflect moderate increases in civil service salaries, as well as less buoyant than planned recruitment.

Meanwhile, the increase in the expenditure to GDP ratio mainly resulted from higher capital expenditure, as gross fixed capital formation and capital transfers increased by 1.2 percentage points of GDP. Higher capital expenditure was directed to roads, the waste management, health and education and included higher infrastructure expenditure financed from both the EU and local funds.

3.1.3 Meeting the 2018 targets as established in the 2018 Medium-Term Fiscal Plan

This section assesses the fiscal and budgetary policies in 2018 against the medium-term objectives outlined in the 2018 Medium-Term Fiscal Plan published on 30 April 2018. It is pertinent to note that the targets for 2018, as outlined in Spring 2018, were different from those underlying the 2018 Budget presented in October 2017 due to updated fiscal information available and revised macroeconomic assumptions upon which the fiscal projections are based. Developments in the General Government budgetary execution in 2018, between subsequent forecasts, are outlined in Table 3.1.

During 2018, the General Government recorded a surplus of €250.8 million, compared to the target surplus of €132.0 million outlined in the 2018 Update of the Stability Programme. In terms of GDP, the General Government balance has improved from a planned surplus of 1.1 per cent of GDP to a surplus of 2.0 per cent of GDP.

The better than expected outturn mainly reflected a stronger than anticipated revenue outcome, amounting to €128.1 million. Revenue from taxes on production and imports was more buoyant by €106.6 million, mainly reflecting a stronger performance in domestic consumption patterns and a significantly more buoyant property market. Market output also turned out €99.5 million higher than forecasted. The stronger nominal growth and the robust growth registered in the labour market, resulted in higher proceeds amounting to €60.4 million from taxes on individual and household income (including holding gains) recorded under current taxes on income and €5.2 million more revenue from social contributions. Nevertheless, as outlined earlier in this Chapter, lower than expected net revenue from taxes on the income and profits of corporations (including holding gains) was recorded.

General Government expenditure was marginally higher than projected by €9.3 million, as higher than targeted expenditure on intermediate consumption and current transfers

General Government Budgetary Execution and Prospects

Table 3.1

€ millions

ESA Code	2018	2018	2018	2019	2019	2019	
	Budget Forecast	USP 2018- 2021 Forecast	Actual	USP 2018- 2021 Forecast	Budget Forecast	USP 2019- 2022 Forecast	
Net lending (+)/net borrowing (-)							
1. General Government	S.13	54.0	132.0	250.8	120.0	165.0	120.3
2. Central Government	S.1311	55.2	133.2	252.1	121.2	166.2	121.5
3. State Government	S.1312	-	-	-	-	-	-
4. Local Government	S.1313	-1.2	-1.2	-1.2	-1.2	-1.2	-1.2
5. Social Security funds	S.1314	-	-	-	-	-	-
For the General Government							
6. Total Revenue	TR	4,369.3	4,655.2	4,783.3	4,917.8	5,054.0	5,124.4
Of which							
Taxes on Production and Imports	D.2	1,424.1	1,484.0	1,590.6	1,540.6	1,613.8	1,665.8
Current Taxes on Income, Wealth, etc.	D.5	1,626.4	1,743.4	1,650.4	1,885.4	1,935.4	1,796.4
Capital Taxes	D.91	20.5	21.5	20.7	21.3	26.5	27.2
Social Contributions	D.61	723.8	759.6	764.8	804.9	807.3	817.5
Property Income	D.4	105.0	103.4	96.0	101.7	66.2	68.5
Other ^(a)		469.5	543.4	660.8	563.9	604.8	749.0
7. Total Expenditure	TE	4,315.3	4,523.2	4,532.4	4,797.8	4,889.0	5,004.1
Of which							
Compensation of employees	D.1	1,314.3	1,367.3	1,376.1	1,429.7	1,467.7	1,490.3
Intermediate Consumption	P.2	773.9	807.7	834.3	867.2	888.1	936.9
Social Payments	D.6	1,188.2	1,207.7	1,175.4	1,252.3	1,290.9	1,275.1
Interest Expenditure	D.41	199.6	191.1	187.7	186.5	187.8	186.5
Subsidies	D.3	130.8	142.2	157.6	158.9	176.8	165.4
Gross Fixed Capital Formation	P.51	361.0	358.3	370.6	429.5	464.2	525.1
Capital Transfers	D.9	113.1	204.1	168.6	176.7	157.0	168.6
Other ^(b)		234.4	244.8	262.0	296.9	256.5	256.2
8. Gross Debt ^(c)		5,874.9	5,506.3	5,664.7	5,500.8	5,660.1	5,755.8

Notes:

^(a) P.11 + P.12 + P.131 + D.39rec + D.7rec + D.9rec (other than D.91rec).

^(b) D.29 + D.4pay (other than D.41pay) + D.5pay + D.7pay + P.5M + NP + D.8.

^(c) As defined in Council Regulation (EC) No 479/2009 (OJ L 145, 10.6.2009, p. 1).

was for the most part offset by lower than planned expenditure on social payments and capital transfers. Expenditure on intermediate consumption was €26.7 million higher than targeted, mainly reflecting higher than planned expenditure towards residential care, operations and maintenance expenditure, capital expenditure classified under this category of expenditure, and a higher than planned contribution to government entities operating in financial intelligence, water and waste water operations and higher expenditure towards health care related activities. Higher than planned current transfers amounting to €20.4 million were primarily related to compensation payments, public social partnerships and EU own resources. Meanwhile, lower than expected expenditure on social payments was mainly on account of lower unfunded and retirement pensions

expenditure as less beneficiaries resorted to early retirement, as well as lower than estimated outlays for the direct provision of pharmaceutical products and students' maintenance grant. Total capital outlays were €30.6 million lower than projected due to lower than projected expenditure in 2018 on projects financed from the National Development and Social Fund.

3.2 Fiscal Outlook in 2019

During the current fiscal year, developments in the revenue and expenditure ratios to GDP are expected to result in a General Government surplus of 0.9 per cent of GDP. It is nevertheless worth noting, that the 2019 General Government balance includes statistical reclassifications within General Government as recommended by Eurostat amounting to €20 million and pre-financed EU funded expenditure of which the national

Main Fiscal Projections (per cent of GDP)						
Table 3.2						
	2017	2018	2019	2020	2021	2022
Revenue	39.2	38.8	38.1	36.7	35.7	35.2
Components of revenue						
Taxes on production and imports	12.4	12.9	12.4	12.1	11.7	11.5
Current taxes on income and wealth	13.9	13.4	13.3	13.3	13.2	13.1
Capital taxes	0.2	0.2	0.2	0.2	0.2	0.2
Social contributions	6.2	6.2	6.1	6.0	6.0	5.9
Property income	0.8	0.8	0.5	0.5	0.5	0.4
Other revenue	5.7	5.4	5.6	4.7	4.2	4.0
Expenditure	35.7	36.8	37.2	35.7	34.7	34.1
Components of expenditure						
Compensation of employees	11.2	11.2	11.1	10.8	10.7	10.5
Intermediate consumption	6.4	6.8	7.0	6.8	6.6	6.4
Social payments in cash and in kind	10.0	9.5	9.5	9.1	8.9	8.7
Interest expenditure	1.8	1.5	1.4	1.2	1.2	1.1
Subsidies	1.2	1.3	1.2	1.2	1.1	1.1
Gross fixed capital formation	2.3	3.0	3.9	3.3	3.1	3.2
Capital Transfers Payable	0.9	1.4	1.3	1.2	1.1	1.1
Other expenditure	1.9	2.1	1.9	2.0	2.0	2.0
General Government Balance	3.4	2.0	0.9	1.0	1.1	1.1
Primary Balance	5.2	3.6	2.3	2.2	2.2	2.2

Discretionary Factors Underpinning Budgetary Developments

Note: The impact of the measures is reported on accruals basis. The impact is recorded in cumulative terms. A positive represents an improvement in the budget balance.

Table 3.3

List of measures	Detailed description	Target (Expenditure / Revenue component) / ESA Code	Accounting principle	Adoption Status	Introduced in Budget for...	Incremental Budgetary Impact					
						2017 % of GDP	2018 % of GDP	2019 % of GDP	2020 % of GDP	2021 % of GDP	2022 % of GDP
VAT	Impact from VAT directive on electronic commerce	D2 - R	Accruals	Permanent & Adopted	2019	0.00	0.00	-0.11	0.00	0.00	0.00
Duty on documents	Extension of reduced rate of stamp duty chargeable on the transfer of immovable property and of a family business	D2 - R	Accruals	Temporary & Adopted	2014 - 2019	0.05	-0.04	0.00	0.04	0.00	0.00
Personal income tax	Change in income tax thresholds for low income earners, including pensioners	D5 - R	Accruals	Permanent & Adopted	2017 - 2019	-0.03	-0.04	-0.02	0.00	0.00	0.00
	Fiscal incentives for private pensions	D5 - R	Accruals	Permanent & Adopted	2019	0.00	0.00	-0.01	0.00	0.00	0.00
Individual Investor Programme	Revenue from the Individual Investor Programme	P10 - R	Accruals	Permanent & Adopted	2014	0.62	-0.42	-0.50	-0.05	0.00	0.00
Other revenue measures legislated in previous budgets			Accruals	Permanent & Adopted		0.11	-0.04	-0.00	0.00	0.00	0.00
EU Presidency	Intermediate consumption in respect of Malta's EU Council Presidency in 2017	P2 - E	Accruals	Permanent & Adopted	2016 - 2017	-0.14	0.22	0.00	0.00	0.00	0.00
Pension reform initiatives	The pension reform initiative legislated in 2006 is expected to lead to lower pension expenditure primarily as the increase in retirement age leads to lower retirees	D6 - E	Accruals	Permanent & Adopted	2006	0.01	0.09	0.00	0.00	0.00	0.00
Tapering of Social Benefits	Tapering of Social Benefits to beneficiaries who become engaged in employment or start working as self-occupied	D6 - E	Accruals	Permanent & Adopted	2015	0.03	0.03	0.03	0.00	0.00	0.00
Re-distribution measures	Measures to address housing affordability, pension adequacy and the integration of vulnerable individuals in society	D6 - E	Accruals	Permanent & Adopted	2016 - 2019	-0.09	-0.05	-0.11	0.00	0.00	0.00
School transport	Extension of the school transport network to children in independent and church schools	D6 - E	Accruals	Permanent & Adopted	2018 - 2019	0.00	-0.04	-0.11	0.00	0.00	0.00
Tax relief measure		D7 - E	Accruals	Permanent & Adopted	2018 - 2019	0.00	-0.09	0.00	0.00	0.00	0.00
Compensation payments		D7 - E	Accruals	Permanent & Adopted	2017 - 2019	-0.07	-0.02	0.04	0.00	0.00	0.00
Other expenditure measures legislated in previous budgets, including projects financed from the National Development and Social Fund			Accruals	Permanent & Adopted		0.00	-0.14	-0.14	-0.14	-0.15	-0.09
						0.49	-0.54	-0.93	-0.15	-0.15	-0.09

The impact is recorded in incremental terms - as opposed to levels - compared to the previous year's baseline projection. The total figure is the Total impact on the budget balance, as a revenue increasing measure is listed as positive, while an expenditure decreasing measure is also positive. The contrary applies for negative figures, such that a revenue decreasing measure is negative and an expenditure increasing measure is also negative. Simple permanent measures are recorded as having an effect of +/- X in the year(s) they are introduced and zero otherwise (the overall impact on the level of revenues or expenditures does not cancel out). If the impact of a measure varies over time, only the incremental impact is recorded in the table. By their nature, one-off measures are recorded as having an effect of +/- X in the year of the first budgetary impact and +/- X in the following year, i.e. the overall impact on the level of revenues or expenditures in two consecutive years is zero. The measures may not add up to the total due to the marginal impact of measures legislated in previous years Budget, but which might nonetheless have a marginal impact on the budget balance.

co-financing element influences the fiscal balance in 2019. The annual contribution to the 'Contingency Reserve' account is expected to increase to €12.9 million in 2019.

Table 3.2 presents the main fiscal projections, while Table 3.3 presents the measures supporting the fiscal developments envisaged over the medium-term.

3.2.1 General Government Revenue in 2019

General Government revenue is expected to decline by 0.7 percentage points of GDP, from 38.8 per cent of GDP in 2018 to 38.1 per cent of GDP in 2019, primarily reflecting developments in taxes on production and imports and property income.

Tax revenue, including social contributions, is expected to broadly follow economic developments in 2019. Taxes on production and imports are expected to stand at 12.4 per cent in 2019.

At unchanged policies, tax revenues, including social contributions, are expected to grow at 7.0 per cent, with an implied elasticity of tax revenue to GDP estimated conservatively at 0.7.

Meanwhile, a lower ratio to GDP of property income from 0.8 per cent in 2018 to 0.5 per cent in 2019 is related to lower anticipated profits from the Central Bank of Malta and lower distributed dividends from public listed companies.

3.2.2 General Government Expenditure in 2019

The ratio of General Government expenditure to GDP is expected to increase by 0.4 percentage points, from 36.8 per cent in 2018 to 37.2 per cent in 2019. The increase in the expenditure-to-GDP ratio is mainly set to come from a higher ratio of capital expenditure, in part offset by lower ratios for most current expenditure components.

Increases in capital expenditure will be devoted to roads, the environment, health and education and include higher infrastructure expenditure financed from both the EU and local funds. These also include an element of pre-financed expenditure of €100.6 million in 2018 which is accrued to 2019.

A lower ratio to GDP is expected for most components of current expenditure, except for intermediate consumption, which is expected to increase marginally from 6.8 per cent to 7.0 per cent of GDP. Higher expenditure on intermediate consumption is mainly on account of higher anticipated expenditure by Extra Budgetary Units (EBUs) and by Central Government for residential homes in the social sector, medicines and surgical materials as well as landscaping in urban areas which is one-off in nature, due to an out-of-court settlement relating to previous years.

Lower estimated 'other expenditure' in 2019 by 0.2 percentage points of GDP primarily reflects lower other current transfers within General Government.

Against the background of historically low interest rates and a decline in the stock of debt, interest expenditure is expected to decline both in level terms as well as a share of GDP, by 0.1 percentage points.

The growth in social benefits expenditure is expected to broadly follow GDP growth, since the fiscal impact of the extension of the school transport network and measures addressing the adequacy of pensions and other vulnerable groups, will be for the most part offset by the expenditure-reducing effect of implemented measures that encourage and reward work effort as well as discourage dependency on the social security system.

Meanwhile, expenditure on subsidies and on compensation of employees as a share of GDP are also expected to decline marginally by 0.1 percentage points of GDP. Developments in the latter reflect moderate increases in civil service salaries of around 4.5 per cent in 2019, including the effect of the agreed 8-year collective agreement, as well as the planned recruitment as envisaged in the Ministries and Departments' Business and Financial Plans, including HR Plans, resulting in an estimated 2 per cent increase in employment levels which is in line with the average rate of growth recorded in the last seven years.

3.2.3 Comparison with the 2018 Update of the Stability Programme

During the current fiscal year, the General Government balance is expected to reach a surplus of 0.9 per cent of GDP. Between the 2018 Update of the Stability Programme and this update, fiscal projections were revised to reflect an overall stronger starting fiscal position and revised macroeconomic forecasts, as well as the outlined statistical reclassification. Developments in the General Government budgetary projections for 2019, between subsequent vintages, are outlined in Table 3.1.

In 2019, in view of more buoyant macroeconomic growth yet relatively similar growth composition, the projections for General Government revenue have been revised upwards by €207 million to €5,124.4 million. Higher proceeds are expected from taxation, in particular taxes on production and imports, which have been revised upwards by €125 million to reflect a stronger outturn in 2018 as well as the sustained positive performance of the domestic economy, including household consumption and the property market. In the revised forecasts, revenues from capital transfers have also been revised upwards by €137 million, mainly reflecting higher expenditure related to capital projects financed from EU funds, including the pre-financed expenditure. Meanwhile, in spite of a stronger than anticipated growth in employment and wages when compared to previous forecasts, the fiscal outcome in 2018 warranted a downward revision in 2019 in revenue from current taxes on income and wealth by €89 million. In addition, a downward revision in property income of €33 million in 2019 was also affected.

The projections for General Government expenditure have meanwhile been revised upwards by €206 million. On the expenditure side, higher gross fixed capital formation is anticipated, and to a lesser extent, higher outlays on intermediate consumption, compensation of employees and social payments. Compared with the 2018 Update of the Stability Programme, the main changes to the expenditure forecast in 2019 are due to a combination of the following factors:

1. In view of anticipated developments in capital spending (financed from both national and foreign funds) during the current fiscal year, expenditure on gross fixed capital formation has been revised upwards by €96 million, which primarily includes pre-financed expenditure on EU funded projects.
2. Projections for intermediate consumption have been revised upwards by €70 million, reflecting higher anticipated expenditure for residential homes in the social sector, as well as landscaping in urban areas.
3. An upward revision in expenditure towards compensation of employees amounting to €61 million is expected, reflecting the outlined increases in civil service salaries as well as the planned recruitment for the current year.
4. Social security benefits were revised upwards by €23 million in this update to reflect higher payments expected to fall due this year to cater for the elderly in homes, as well as the extension of the school transport network. These upward pressures were partly mitigated by a downward revision in expenditure in respect of pensions and social security benefits in response to the lower number of beneficiaries recorded in the previous year.
5. Meanwhile, estimated 'other expenditure' in 2019 was revised downwards by €41 million to reflect lower other current transfers within General Government. In the Spring 2018 projections, this category of expenditure included an element of unallocated expenditure items which has subsequently been reclassified to actual ESA categories.

3.3 Medium-Term Fiscal Strategy

Malta's medium-term fiscal strategy envisaged for the 2019-2021 period reflects the baseline macroeconomic projections contained in this Programme. Over the medium-term, the robust performance of the Maltese economy is expected to be sustained, though growth is expected to moderate compared to rates recorded in recent years. The rate of growth of potential output is also expected to moderate over the medium-term, and the output gap is expected to turn slightly negative as from next year.

Inflation is expected to continue to converge to its long-term average. Employment growth is expected to moderate and move closer to the long run average, with unemployment forecasted to remain below the historical average. No major external imbalances are foreseen and the contribution from external demand is projected to remain positive with a higher contribution to GDP growth in the outer years of the forecast horizon.

3.3.1 Structural Budget Balance and the Medium-Term Budgetary Objective

Over the medium-term, the Maltese Government is committed to continue to ensure compliance with the MTO. In addition, ensuring that expenditure growth does not exceed

Analysis of the Developments in the General Government Balance

(percentage points of GDP)

Table 3.4

	2017	2018	2019	2020	2021	2022
Change in Revenue Ratio	1.75	-0.33	-0.77	-1.39	-0.96	-0.54
Discretionary factors underpinning fiscal consolidation	0.55	-0.78	-0.82	-0.11	-0.09	-0.08
Tax revenue buoyancy	0.69	0.22	-0.51	-0.48	-0.39	-0.38
Other revenue	0.51	0.24	0.56	-0.79	-0.48	-0.08
Change in Expenditure Ratio	0.79	-1.06	-0.37	1.46	1.05	0.59
Discretionary factors underpinning fiscal consolidation	-0.24	0.04	-0.25	-0.08	-0.09	-0.03
Change in Gross Fixed Capital Formation	0.16	-0.65	-0.84	0.70	0.29	-0.03
Other expenditure	0.87	-0.45	0.71	0.85	0.85	0.65
Change in the General Government Balance	2.54	-1.39	-1.14	0.08	0.08	0.06

Note: Positive represents an improvement in the general Government balance

the economy's growth potential remains an intermediate target in this Programme. Based on the outlined macroeconomic projections and estimates of the business cycle generated using the commonly agreed methodology, and expected developments in one-off and other temporary measures over the medium-term, the outlined trajectory is translated into a structural balance of 0.7 per cent of potential GDP in 2019 increasing gradually to 1.4 per cent of potential GDP by 2022.

Cyclical Developments

(percentage points of GDP)

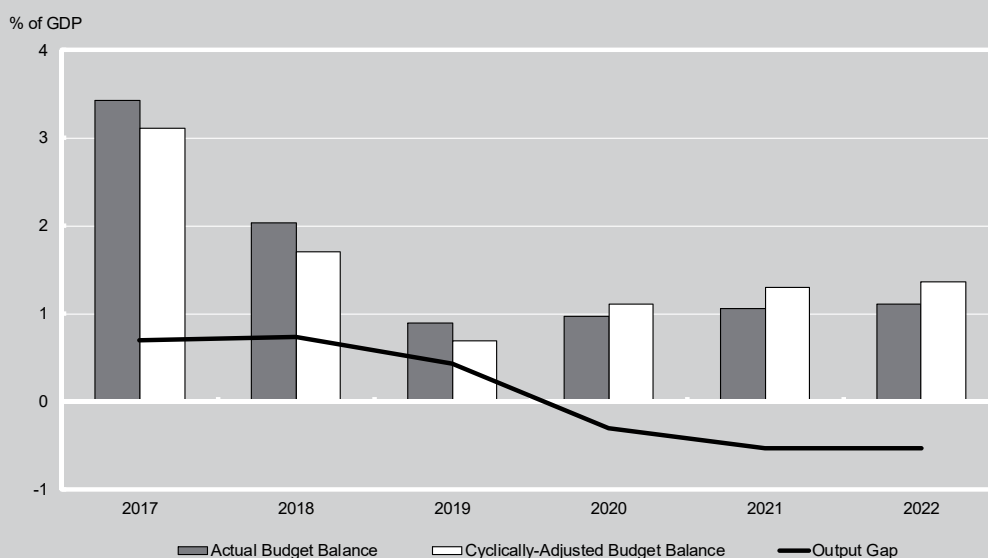
Table 3.5

	2017	2018	2019	2020	2021	2022
General Government Balance	3.4	2.0	0.9	1.0	1.1	1.1
One-off and other temporary measures ⁽¹⁾	-0.2	0.1	0.0	0.0	0.0	0.0
General Government Balance net of One-offs	3.6	1.9	0.9	1.0	1.0	1.1
Output Gap Estimates	0.7	0.7	0.4	-0.3	-0.5	-0.5
Cyclically-Adjusted Budget Balance	3.1	1.7	0.7	1.1	1.3	1.4
Structural Balance	3.3	1.6	0.7	1.1	1.3	1.4
Structural Adjustment	3.0	-1.7	-0.9	0.4	0.2	0.1

⁽¹⁾ A plus sign means deficit-reducing one-off measures

Chart 3.1

Actual and Cyclically-Adjusted Budget Balances



An analysis of the developments in the General Government balance is presented in Table 3.4, while further details on the cyclical developments over the medium-term are illustrated in Table 3.5 and Chart 3.1.

The primary surplus is expected to remain relatively stable at 2.2 per cent of GDP over the medium-term, reflecting a relatively stable ratio to GDP of interest payments and a General Government balance which is expected to increase marginally to 1.1 per cent of GDP over the medium-term forecast horizon. In view of the outlined developments in the primary surplus, the decline in the debt-to-GDP ratio over the medium-term, which is expected to decline significantly below the 60 per cent of GDP reference value, will be primarily supported by the nominal growth trajectory.

3.3.2 Revenue forecasts

Against the background of the outlined medium-term macroeconomic forecasts and plausible elasticity assumptions, the total revenue ratio is expected to decline to 35.2 per cent of GDP by 2022.

Tax receipts are expected to decline by 2.1 percentage points of GDP to 30.7 per cent of GDP by the end of the Programme period. Such developments are partly driven by a slower growth in the indirect tax base than nominal GDP, as a result of which revenue from taxes on production and imports is expected to follow a declining trend to 11.5 per cent of GDP in 2022. Meanwhile, a slower wage growth compared to GDP growth is expected to in part offset the strong growth in gross operating surplus. As a consequence, the ratio to GDP of current taxes on income and wealth is expected to remain relatively stable and decline only marginally in the outer years of the forecast period to 13.1 per cent of GDP. Meanwhile, social security contributions are expected to decline marginally to 5.9 per cent of GDP by the end of the forecast period.

Proceeds from 'other revenue', are expected to increase marginally by 0.2 percentage points to 5.6 per cent of GDP in 2019, before declining to 4.0 per cent of GDP in 2022 as capital transfers related to investment grants are expected to moderate.

3.3.3 Expenditure Targets

As outlined above, over the medium-term, growth in the corrected expenditure aggregate net of discretionary revenue measures is targeted to be lower than the economy's growth potential. Nevertheless, it is worth noting that in 2019, the expenditure aggregate is adversely affected by the negative incremental impact of discretionary revenue measures. The General Government expenditure ratio is expected to amount to 37.2 per cent of GDP in 2019 and to subsequently decline to 34.1 per cent of GDP by 2022.

While the ratio of current expenditure-to-GDP is expected to decline over the medium-term by 2.6 percentage points to 29.8 per cent, capital expenditure is forecast to increase from 4.4 per cent of GDP in 2018 to an average of 4.6 per cent of GDP between 2019 and 2022. Indeed, by means of the planned capital programme, the Maltese Government will give precedence to the national infrastructure needs over the forecast horizon, together with the national economic and social priorities, and consistent with Government's objectives for sustainable economic growth.

Social benefits and social transfers in kind are set to continue on the declining trend relative to GDP recorded in recent years and are expected to decline to 8.7 per cent of GDP by the end of the forecast horizon. Such development reflects savings in social benefits stemming from implemented measures which are aimed to encourage and reward work effort as well as discourage dependency on the social security system.

Expenditure on compensation of employees is expected to decline by 0.7 of a percentage point of GDP to 10.5 per cent in 2022.

Expenditure on interest payments as a share of GDP is expected to follow a declining trend over the medium-term to 1.1 per cent of GDP in 2022.

Meanwhile, the ratio of intermediate consumption to GDP is set to decline to 6.4 per cent of GDP during the period under review,

3.4 Debt levels and developments

Government debt has declined below the 60 per cent Treaty reference value in 2015 and has fallen continuously ever since reaching 46.0 per cent in 2018. As of 2019, the level of public debt relative to GDP is projected to continue with its downward trajectory and reach 33.2 per cent of GDP by 2022. Alongside the strong GDP growth, the healthy state of public finances has also contributed significantly to the reduction in the debt-to-GDP ratio and will continue to have a favourable impact on the debt ratio over the projected period.

Meanwhile, the Government's debt strategy remains that of ensuring that the financing needs of the public sector are met at the lowest possible costs, while simultaneously minimising medium and long-term risks. The Government's reliance on short-term funding remains marginal, in line with the dynamics exhibited in recent years. During 2018, short-term debt accounted for 5.1 per cent of total Government debt and is expected to increase to 5.9 per cent in 2019. Short-term debt funding is predicted to stabilise in the following years and decrease to 4.6 per cent in 2022. Additionally, the share of maturing stocks in total Government debt is expected to increase from a level of 6.9 per cent in 2018 to 7.6 per cent in 2019. Furthermore, the proportion of maturing stocks in total Government debt is projected to remain on an upward trajectory, with the ratio reaching 8.2 per cent in 2021 and decreasing to 6.8 per cent in 2022.

3.4.1 Projected Debt developments

Debt dynamics depend on the net lending which can be decomposed into the contribution from the primary balance, interest expenditure, GDP growth and the stock flow which is made up of financial transactions and accruals that do not affect lending. Developments in the debt ratio for the Programme period and the contributors to developments in the debt-to-GDP ratio are presented in Table 3.6 and Statistical Appendix Table 4. The debt-to-GDP ratio is expected to decrease throughout the forecast horizon reaching 33.2 per cent, mainly on the back of the positive primary surpluses targeted in the coming years. The contractionary impact of the primary balance and the 'snowball effect' will more than offset the expansionary impact of the stock flow adjustment (SFA) on the debt-to-GDP ratio foreseen through the forecast horizon.

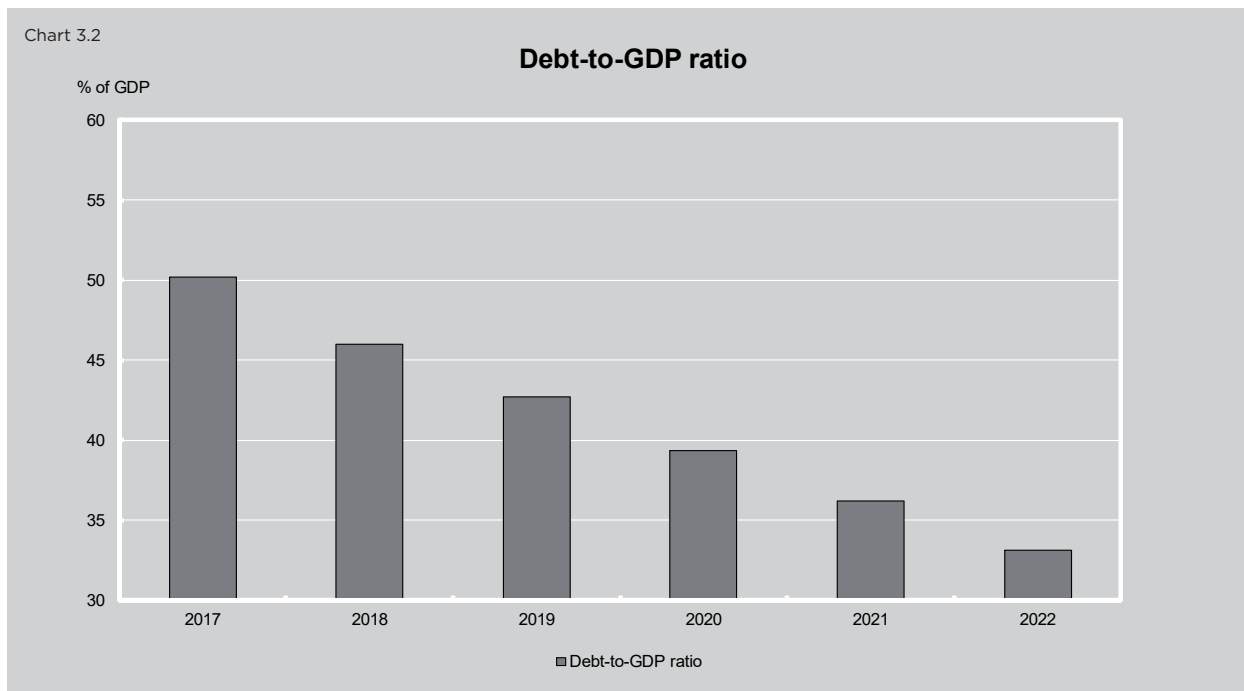
The Dynamics of Government Debt⁽¹⁾

Table 3.6

Percentages of GDP	2017	2018	2019	2020	2021	2022
Gross debt	50.2	46.0	42.7	39.4	36.2	33.2
Change in gross debt ratio	-5.5	-4.2	-3.2	-3.4	-3.2	-3.0
Contributions to changes in gross debt						
Primary balance	-5.2	-3.6	-2.3	-2.2	-2.2	-2.2
Snowball Effect	-2.9	-2.6	-2.5	-2.0	-1.5	-1.3
Interest expenditure	1.8	1.5	1.4	1.2	1.2	1.1
Real GDP growth	-3.5	-3.1	-2.7	-2.3	-1.9	-1.7
Inflation Effect	-1.3	-1.0	-1.2	-1.0	-0.8	-0.7
Stock-flow adjustment	3.0	1.9	1.6	0.9	0.6	0.5
p.m. implicit interest rate on debt	3.6	3.3	3.3	3.1	3.2	3.2

$$^{(1)} \text{ Developments in the debt- to-GDP ratio depend on: } \frac{D_t}{Y_t} - \frac{D_{t-1}}{Y_{t-1}} = \frac{PD_t}{Y_t} + \left(\frac{D_{t-1}}{Y_{t-1}} \cdot \frac{i_t - y_t}{1 + y_t} \right) + \frac{SFA}{Y_t}$$

where t denotes a time subscript, D , PD , Y and SFA are the government debt, primary deficit, nominal GDP and the stock-flow adjustment respectively, and i and y represent the average cost of debt and nominal GDP growth.



After decreasing by €17.8 million over 2017, together with a higher level of GDP, the debt-to-GDP ratio for 2018 fell to 46.0 per cent. The debt ratio is expected to continue to fall by 3.2 percentage points in 2019 and 3.4 percentage points in 2020, and then continue on a declining path to reach 36.2 per cent of GDP in 2021. The fiscal strategy presented in this programme will reduce the debt burden even further to 33.2 per cent of GDP by 2022. The developments in the gross Government debt are illustrated in Chart 3.2. Over the medium-term horizon, the projected reduction in the gross debt ratio is mainly driven by the primary surplus and the nominal growth trajectory. The expansionary contribution of interest expenditure on the debt ratio is expected to moderate throughout the forecast horizon, from 1.5 per cent of GDP in 2018 to 1.1 per cent of GDP in 2022.

In 2018, the SFA is estimated to have resulted in a 1.9 percentage point increase in the debt-to-GDP ratio. This was however mainly underpinned by the adjustments made to the deficit in ESA10 and equity acquisition (€63.5 million) mainly related to the Malta Air Travel Limited and Air Malta Aviation Services Limited. In 2019, stock flow transactions are expected to have a positive impact on the debt ratio while over the medium-term, stock flow transactions are expected to have a marginal impact on debt ratio. Further details on the SFA can be found in Annex Table 10.

3.4.2 Comparison with the April 2018 Update of the Stability Programme

As illustrated in the Statistical Appendix Table 6, the ratios of General Government debt-to-GDP presented in this Programme are expected to be broadly the same as those presented in the previous Update of the Stability Programme. The debt-to-GDP ratios presented in the programme are slightly higher due to higher projected SFA and include the re-classification of certain PPPs within General Government.

For 2018, the debt-to-GDP ratio was revised upwards by 0.2 percentage points to 46.0 per cent of GDP while debt-to-GDP ratios for 2019 and 2020 were revised upwards by 0.2 and 0.1 percentage points, respectively. For 2022, debt-to-GDP was revised upwards by 0.6 percentage points.

In the 2018 Update, the debt-to-GDP ratio was expected to follow a downward path from a level of 45.8 per cent in 2018 to a level of 35.6 per cent in 2021. On the other hand, in this Update of the Stability Programme, the debt-to-GDP ratio is estimated to decline to a level of 36.2 per cent by 2021.

4. Sensitivity Analysis

4. Sensitivity Analysis

The accuracy of macroeconomic forecasts is considered to be a priority, especially in the case of a small and open economy like Malta. Macroeconomic forecasts are the economic foundation of the Government's fiscal targets, hence the professional and objective assessment of past forecasting performance contributes towards the provision of accurate, effective and credible forecast results. While the Maltese economy proved to be resilient to the international economic crisis, Gross Domestic Product (GDP) forecast errors were relatively higher for Malta than for larger and less open economies within the European Union (EU).¹ This is also a reflection of the significant structural change which the Maltese economy has experienced in the last few years.

The macroeconomic forecast presented in Chapter 2 contains the baseline forecast. It is a contingent forecast based on a number of exogenous assumptions regarding the evolution of a number of variables. Since some of these variables have a significant impact on our macroeconomic projections, sensitivity analysis of these variables aids in appropriate risk assessments. Structural pressures may pose an upside or a downside risk.

This Chapter, therefore, seeks to provide an assessment of forecast uncertainty and the balance of risk surrounding the macroeconomic forecasts in this Programme. The analysis is in line with the requirements of Council Directive 2011/85/EU of the EU on the requirements for budgetary frameworks of the Member States.

4.1 The Accuracy of Past Forecasting Performance

The updated analysis on the accuracy of past forecasting performance as completed by the Economic Policy Department (EPD) within the Ministry for Finance (MFIN) shows a tendency to underestimate GDP growth leading to a downward bias in GDP growth projections. This is partly due to statistical revisions from the first statistical releases of National Accounts and Balance of Payments issued, persistently in the upward direction. While the one-year ahead forecasts display a Root-Mean Squared Error (RMSE) of 3.7, it is notable that the sample size employed is rather small and the earliest forecast available is that of 2004. The recession of 2009, the subsequent recovery, and the statistical revisions play significant influence on this evaluation in such a limited sample and limit comparability with the forecast accuracy displayed by other economies with a longer tradition of forecasts.² It is noteworthy that, the RMSE for the one-year ahead forecast has declined marginally from 3.8³ recorded last year.

The evaluation of the risk and uncertainty of the current macroeconomic projections underlying this Programme is based on an ex ante analysis of past forecast errors which determine the level of uncertainty. Ex post, a number of alternative but plausible economic scenarios generated with the forecasting model used by the EPD are also simulated to determine the balance of risks surrounding the baseline projections.

4.2 The Balance of Risks

To determine the balance of risks surrounding macroeconomic forecasts, fifteen alternative model-based growth projections were carried out as follows:

1. Improved global economic growth based on the upper bound of the Consensus forecasts.

2. Weaker global economic growth based on the lower bound of the Consensus forecasts.
3. Higher world prices based on the upper bound of the Consensus forecasts.
4. Lower World prices based on the lower bound of the Consensus forecasts.
5. Weaker Euro exchange rate against the US Dollar.
6. Stronger Euro exchange rate against the UK Pound Sterling.
7. Higher interest rate scenario resulting into a slightly downwards sloping yield curve in 2019, and an upwards sloping yield curve in the outer years of the forecasts based on recent developments.
8. A Trade protectionist scenario, where a strong US Dollar coupled with high world prices, upper bound growth for the US and lower bound growth for the main trading partners for Malta is modelled.
9. Stronger medium-term investment scenario.
10. Weaker medium-term investment scenario.
11. Higher import content scenario.
12. Stronger Euro exchange rate against the UK Pound Sterling, coupled with weaker global economic growth for Malta's main trading partners.
13. Weaker Euro exchange rate against the UK Pound Sterling, returning to the levels of 2015.
14. Weaker growth in services exports.
15. Model-based scenario, removing any form of economic judgement underlying the baseline forecast thus generating a purely model-based forecast, however still based on a number of exogenous assumptions such as world prices, international economic conditions, interest rates and exchange rates.

These represent scenarios that are considered to be plausible alternatives to the baseline projections. While economic judgement influences the choice of these scenarios, this judgement is also underpinned by the constant monitoring of economic conditions prevailing at the time and informed by the various meetings with economic stakeholders and regulators operating within the Maltese economy, carried out in the early stages of the forecasting exercise. Moreover, the scenarios were assigned probabilities based on the likelihood that such scenarios will materialise. This exercise was based on the expert judgement of a number of economists working within the Public Sector.

Among the alternative forecasts, a more detailed description is provided for the alternative growth and interest rate scenarios as required by the Directive. In the light of the prevailing uncertainty surrounding the global economy, two contrasting growth scenarios are modelled.

4.2.1 Improved Global Economic Growth

This scenario assumes that the international economic outlook strengthens and as a result, Malta's key trading partners will have stronger growth than originally expected. World GDP is assumed to increase by 0.5 percentage points in 2019 from the 1.2 per cent growth assumed in the baseline, while in the outer years, it is assumed to increase by 0.6 percentage points from the 1.3 per cent growth assumed in the baseline. The relatively higher than expected economic growth in Germany, Italy, France, the UK, and the US is based on the Consensus Forecasts March 2019 publication, assuming the most plausible optimistic growth figures for each trading partner. The main effect of this scenario is that of an increase in the demand for Maltese exports leading to a 0.3 percentage points increase in Malta's GDP in 2019, followed by significant upward revisions in real GDP

growth of 0.6, 0.7, and 0.7 percentage points in 2020, 2021, and 2022, respectively. The budget balance would improve in the outer years by 0.1 percentage points in 2021 and 0.2 percentage points in 2022, respectively.

4.2.2 Weaker global economic growth

This scenario models the downside risk of a deterioration in the international economic outlook relative to the baseline forecast. It assumes a permanent weakening in external demand equivalent to 0.7 percentage points each year over the forecast horizon compared to the baseline scenario. The relatively lower than expected growth projections for Germany, Italy, France, the UK, and the US are based on the Consensus Forecasts March 2019 publication, assuming the lowest plausible growth figures for each trading partner. The deterioration in world demand mainly contributes to a reduction in the demand for Maltese exports, which is more pronounced than the decline in imports, resulting in a real GDP decline of 0.5 percentage points in 2019, and then decline by an average of 1.1 percentage points throughout the outer years of the forecast horizon. The budget balance is projected to decrease by 0.1 per cent in both 2019 and 2020, and then to further decline by 0.3 per cent in 2021 and 0.4 per cent in 2022.

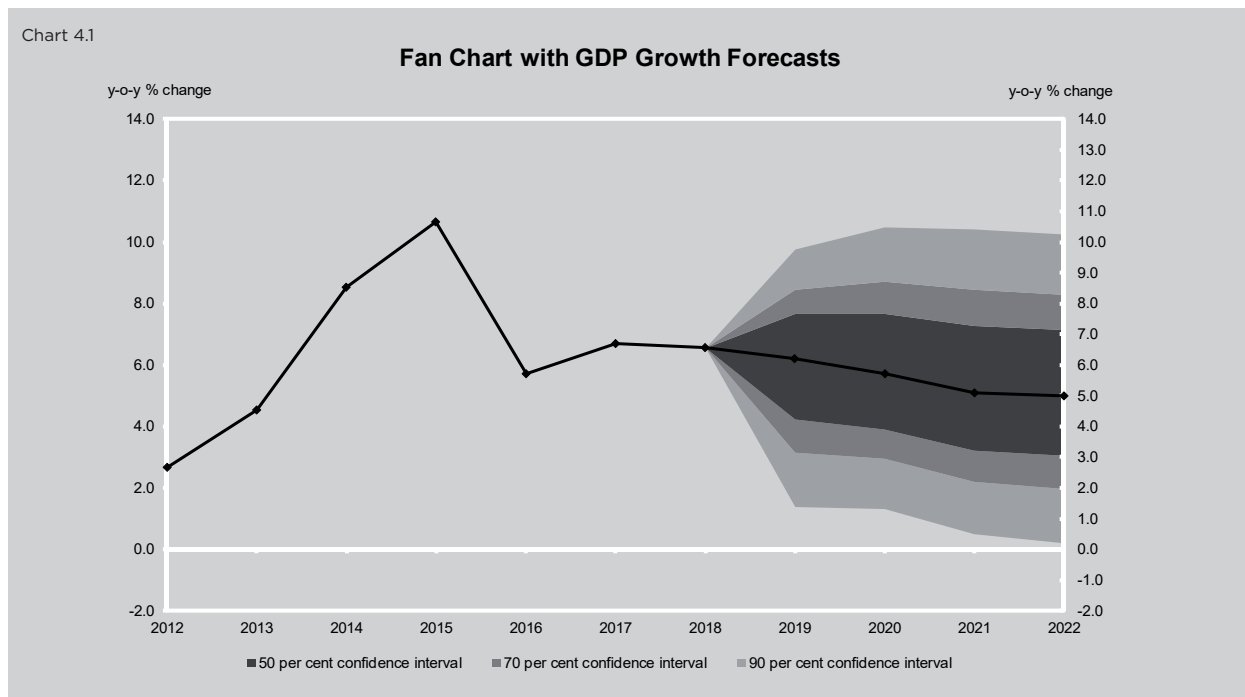
4.2.3 Interest rate scenario

This scenario assumes that the long-run interest rate drops by 10 basis points in 2019, resulting in a less upwards sloping yield curve. On the other hand, in the outer years, this scenario assumes that the long-run interest rate increases by 20 basis points each year till 2022, resulting in a more upwards sloping yield curve. The effect of the former shock is that of a higher real investment leading to an increase in real GDP of 0.1 percentage points, while the effect of the latter shock is that of a real GDP decline of around 0.1 by 2022. The budget balance is expected to decrease by 0.1 per cent in 2019, but then increase by 0.1 per cent in 2020, and is then expected to remain relatively unchanged throughout the outer years of the forecast horizon.

4.3 Alternative Model Forecasts

Six alternative forecasting models were also developed, ranging from model-free statistical forecast (Random Walk and Holt-Winters Seasonal Smoothing Method), model-based univariate forecasts (2 ARIMA models) and model-based multivariate forecasts (2 VAR models and one VECM model). These models help MFIN benchmark the results inferred from STEMM and can be used to generate alternative growth forecasts. On average, these models suggest a slightly higher GDP growth for 2018 of 6.3 per cent, which is very close to the baseline forecast. This is indicative of a relatively balanced risk for 2019. From 2019 onwards, the alternative models suggest higher GDP growth, which on average is around 6.0 per cent, suggesting that the baseline forecast presented in Chapter 2 is rather prudent.

Of special interest are the two VAR models, one which is demand driven with exogenous assumptions and one which is mainly supply driven based on employment and prices. The former is closest to the Keynesian-type baseline model while the latter captures better supply side conditions which in recent years have predominantly determined growth conditions in the Maltese economy. For 2019, both models suggest a growth rate which is very close to the baseline forecast of 6.2 per cent. However, over the medium-term, the demand-driven VAR with exogenous assumptions suggests a growth rate of slightly less than 6 per cent whilst the supply-driven VAR indicates a growth rate slightly above 7 per cent. This indicates the potential upside risks in the outer years of the forecasts.



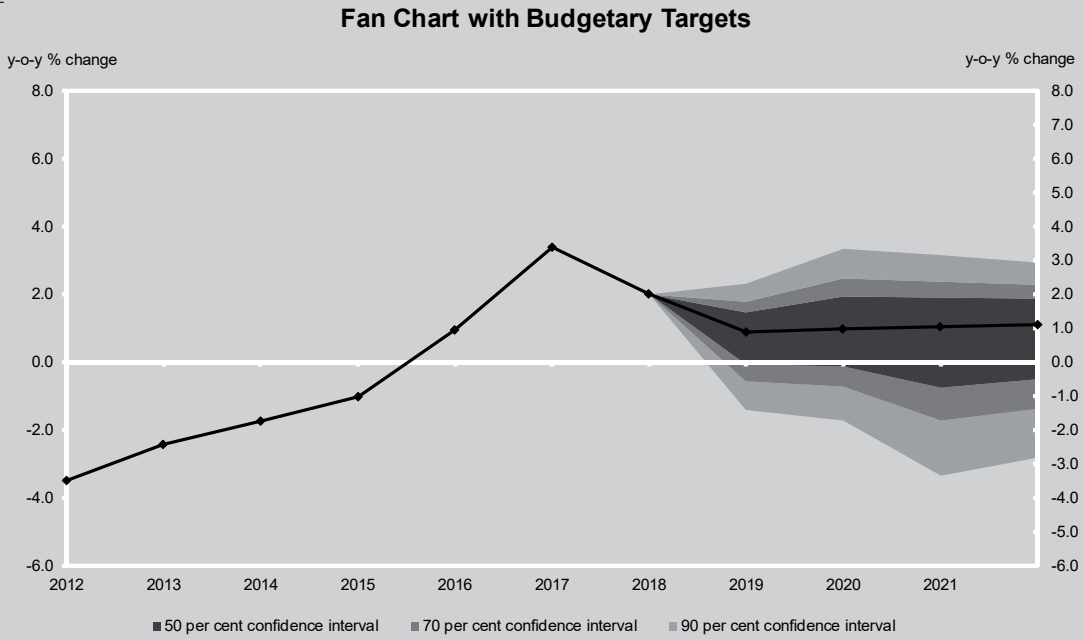
4.4 Uncertainty and the Balance of Risk Underlying the Macroeconomic Projections

The uncertainty surrounding the macroeconomic projections is based on the past forecast error variance of GDP. This is equal to 2.6 for the current year forecast, and 2.8 for the one-year ahead forecast, 3.0 for the two year-ahead forecast, and 3.1 for the three-year ahead forecast. The balance of risk is based on the Pearson skewness indicator of the model generating alternative forecast for GDP documented above. The indicator shows a rather downside risks for 2019, but upside risks for 2020, 2021 and 2022. The results in the outer years of the forecast are somewhat consistent with the analysis of alternative model forecasts highlighted earlier. Chart 4.1 depicts a representation of the uncertainty and the balance of risk surrounding the macroeconomic forecasts presented in this Programme.

4.5 Risks to Fiscal targets

The alternative macroeconomic scenarios documented above, can influence the attainment of the deficit targets thus underpinning alternative fiscal conditions. Chart 4.2 illustrates the range of possible budget balance outcomes conditional upon the realisation of these alternative scenarios. This year, the evaluation of fiscal risk conditional on macroeconomic risks also incorporates the variance resulting from the past forecast error of fiscal projections, based on a methodology similar to that used for deriving the macroeconomic risk assessment. As a result, the risk assessment is presented in the form of a probabilistic fan-chart rather than point estimates. There seems to be a slightly downside risk for the attainment of the surplus target in both 2019 and 2020. The risk will remain in the downside throughout the outer years of the forecast horizon. Looking at point estimates, under the worst possible cyclical scenarios contemplated, the budget balance would be in deficit of around 1.0 percentage points for the period under review, and thus will remain well below the 3 per cent deficit benchmark.

Chart 4.2

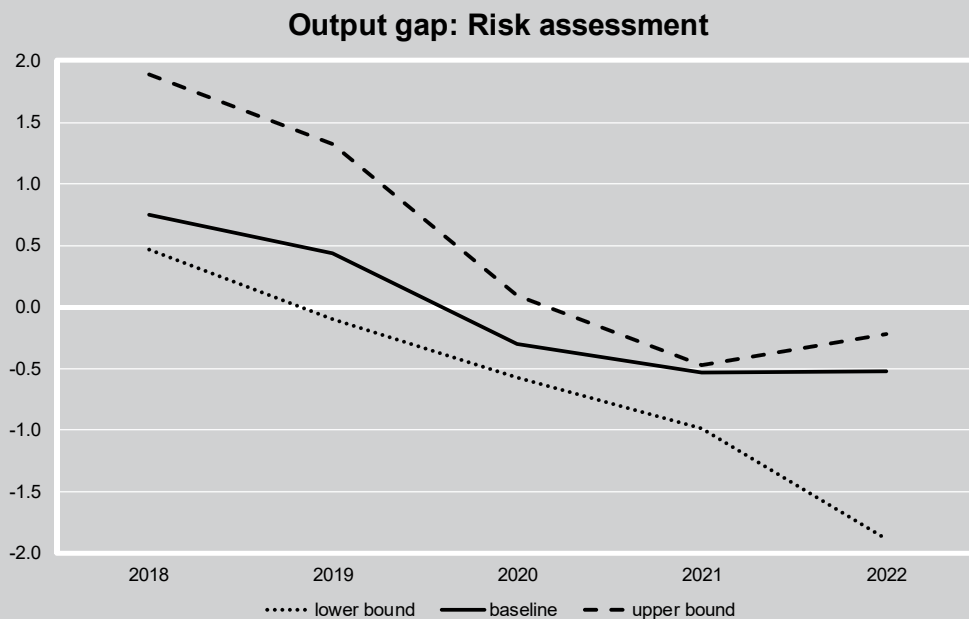


4.6 Alternative Output Gap projections and risks to Structural Fiscal Targets

This assessment has been extended to cover risks to the output gap projections and hence the structural commitments presented in this Programme. Alternative output gap projections consistent with all the above economic scenarios have thus been carried out.

Compared to the baseline scenario, as shown in Chart 4.3, alternative output gap projections range from -0.1 in 2019 up to -1.9 in 2022 under the lower-bound and from 1.3 in 2019 down to -0.2 in 2022 under the upper-bound scenario.

Chart 4.3



Footnotes:

¹ Camilleri, G., and Vella, K. (2015). "Interpolating Forecast Errors for Assessing Uncertainty in Macroeconomic Forecasts: An Analysis for Malta." EPD Working Paper Series, No. 1/2015, March 2015.
http://mfin.gov.mt/en/epd/Documents/Working_Papers/Working_Paper_Full.pdf

² The analysis on past forecast errors has been updated and is different than what is outlined in Camilleri and Vella (2015). The updated analysis features the latest Updates of the Stability Programme as part of the sample data. However, the methodology remains unchanged.

³ This has been recalculated from what was published last year to reflect more recent data on GDP released.

5. Sustainability of Public Finances

5. Sustainability of Public Finances

This Chapter seeks to assess Malta's long-term sustainability of public finances for the period 2016 to 2070. This assessment is based on the public expenditure projection results produced by the Ageing Working Group (AWG) for the 2018 Ageing Report, reflecting a series of population projections as carried out by EUROSTAT. The AWG produced long-term projections ahead of the finalisation of the 2018 Ageing Report, which the Economic and Financial Affairs Council (ECOFIN) mandated the Economic Policy Committee (EPC) to be endorsed and published by the autumn of 2018 at the latest.

The analysis of this Chapter includes pensions, health, long-term care, unemployment and education expenditure projections. These long-term projections provide an indication of the timing and scale of economic changes that would result from an ageing population in a 'no-policy change' scenario. The projections are helpful in highlighting the immediate and future policy challenges for Governments as a result of the expected future challenges caused by demographic change.

5.1 Long-Term Budgetary Projection Results for Malta

This section provides an analysis of the long-term sustainability of public finances for Malta for the period 2016 to 2070 based on commonly agreed assumptions for the European Union (EU) Member States. The modelling work for pension projections assumes a 'no policy change' scenario and reflects as strictly as possible the pension rules, both current as well as those applying in future in reflection of legislative reforms. The model also assumes full wage indexation for non-contributory age (minimum) pensions, even though the current legislation in Malta adjusts age pension with the Cost of Living Allowance (COLA).¹ The projections for pension expenditure exclude the impact of linking the contributory period to life expectancy, in light of the fact that the AWG methodology is based on current legislation.²

The model used in projecting pension expenditure was the World Bank's Pension Reform Options Simulation Toolkit (PROST 15), being the same model used in the projection of pension expenditure for the previous AWG budgetary projections exercise. Staff from the Economic Policy Department within the Ministry for Finance (MFIN) used PROST 15 to model the development of the current pension system and analyse various options for pension reform. The pension projections baseline was prepared by the World Bank with the assistance of expertise from the MFIN and the Ministry for the Family, Children's Rights and Social Solidarity (MFCS). The results obtained were subject to a process of internal review by pension experts within Government and subsequently endorsed by the EPC following a peer review at the AWG. Statistical Appendix Table 7 shows the expenditure components of the long-term budgetary projections as a percentage of Gross Domestic Product (GDP) for the period 2013-2070 and the assumptions used.

5.1.1 Demographic Projections

Population projections as published by EUROSTAT were used as a primary input in the long-term age-related expenditure projections used by the European Commission in the assessment of the sustainability of public finances.³ As shown in Table 5.1, population projections (based on 2015 EUROSTAT projections) indicate that total population in Malta is projected to rise from 436,658 in 2016 to approximately 521,000 in 2070. These

Eurostat Population Projections

Table 5.1

	2016	2020	2030	2040	2050	2060	2070*
2015 Ageing Report							
Total population	429,874	439,341	456,792	462,995	468,528	476,383	:
Old-age dependency ratio (65+ yrs/15-64 yrs)	29.4	33.2	40.5	40.8	45.0	50.9	:
2018 Ageing Report							
Total population	436,658	454,686	489,917	506,385	513,362	519,458	520,761
Old-age dependency ratio (65+ yrs/15-64 yrs)	29.1	33.0	40.4	41.4	46.0	53.9	55.8

* Population projections used for the 2015 Ageing Report are up to 2060.

Source: EUROSTAT

projections are higher than the population projections presented for the 2015 Ageing Report.

5.1.2 Assumptions Applied

In projecting pensions, the demographic assumptions reflect projections by Eurostat, while the macroeconomic assumptions reflect the commonly agreed methodology in the EPC. The assumptions used include the real GDP growth rate, labour productivity (growth rate per hour), inflation rate, labour participation rate by age and gender, unemployment rate by age and gender, population, fertility rate by age, mortality rate by age and gender, and net migration by age and gender.

Life expectancy at birth for men is assumed to rise by 6.8 years from 2016 to reach 86.8 years in 2070. For women, it is expected to reach 90.6 years, an increase of 6.3 years over 2016 which tends to confirm that female life expectancy is projected to remain almost 4 years higher than that of males. Meanwhile, life expectancy at 65 years for males and females is projected to increase by 4.6 and 4.7 years, respectively, over the whole period. Another important variable in the evolution of the demography is net migration, where such inflows are projected to decline from 3,478 in 2016 to 1,015 in 2070. Net migration as a percentage of population is projected to decrease from 0.8 per cent in 2016 to around 0.2 per cent in 2070.

In terms of macroeconomic assumptions, the labour force projections show a substantial rise in the overall participation rates, especially for women and older workers. Potential GDP as well as average growth over the whole period is significantly higher than in the previous round of projections. In the new round of projections, the average potential GDP growth is 2.3 per cent whereas in the 2015 Ageing Report it hovered around 1.7 per cent. Potential GDP growth is projected to decline from 6.1 per cent in 2016 to 1.1 per cent in 2055 and thereby increasing to 1.6 per cent by the end of 2070.

5.1.3 Demographic Developments

Population projections indicate that total population in Malta is projected to rise from 436,658 in 2016 to 520,761 in 2070. As shown in Table 5.2, the age structure of the

population is expected to change significantly. While the share of the very young people (aged 0-14 years) in the total population is projected to hover around the 14.5 per cent share, the share of the people aged 65+ is projected to increase from 19.3 per cent to 30.6 per cent.

From an economic perspective, the most important change in demography concerns the working-age population (aged 15-64 years), which reflects the share of the population that will bear the financial 'burden' of the elderly. From a share of 66.4 per cent in 2016, this ratio is projected to subsequently fall to 54.9 per cent by 2070. The dynamics of the ageing process could be better appreciated by analysing the developments in the dependency ratios, which relate the number of individuals that are likely to be "dependent" on the support of others for their daily living, young people and the elderly, to the number of those individuals who can provide such support. Key indicators of age dependency presented in Table 5.2 are the old-age-dependency ratio (for persons aged 65 years and more) calculated relative to the number of individuals aged 15-64 years and the ageing of the aged ratio (80+ age bracket as a percentage of the 65+ age bracket).

The old-age dependency ratio (65+ year bracket as a percentage of the 15-64 age bracket) is projected to increase consistently from 29.1 per cent in 2016 to 55.8 per cent in 2070, an increase of 26.7 percentage points. Meanwhile, the ageing of the aged ratio, is projected to increase from 22.0 per cent in 2016 to 43.6 per cent by 2070. The youth dependency ratio is expected to increase from 21.5 per cent in 2016 to 25.1 per cent in 2030, drop to 23.6 per cent in 2040 and subsequently increase to 26.5 per cent by 2070. Thus, by 2070, the total dependency ratio, which is the combined burden of these two components of the economically active population, will amount to 82.3 per cent.

Total Population, by Selected Age Groups

Table 5.2

Age	2016	2020	2030	2040	2050	2060	2070
0-14 yrs	62,250	66,318	74,399	72,405	72,964	76,474	75,761
15-64 yrs	289,920	292,091	295,862	306,922	301,572	287,780	285,676
65+ yrs	84,488	96,277	119,657	127,059	138,827	155,204	159,325
Total	436,658	454,686	489,917	506,385	513,362	519,458	520,761
Share (%)							
0-14 yrs	14.3	14.6	15.2	14.3	14.2	14.7	14.5
15-64 yrs	66.4	64.2	60.4	60.6	58.7	55.4	54.9
65+ yrs	19.3	21.2	24.4	25.1	27.0	29.9	30.6
Ratio (%)							
Youth dependency ratio (0-14 yrs/15-64 yrs)	21.5	22.7	25.1	23.6	24.2	26.6	26.5
Old-age dependency ratio (65+ yrs/15-64 yrs)	29.1	33.0	40.4	41.4	46.0	53.9	55.8
Total dependency ratio	50.6	55.7	65.6	65.0	70.2	80.5	82.3
Ageing of the Aged Ratio (80+ yrs/65+ yrs)	22.0	23.3	32.2	39.4	36.8	37.2	43.6
Support ratio (15-64 yrs/65+ yrs)	3.4	3.0	2.5	2.4	2.2	1.9	1.8

Source: EUROSTAT

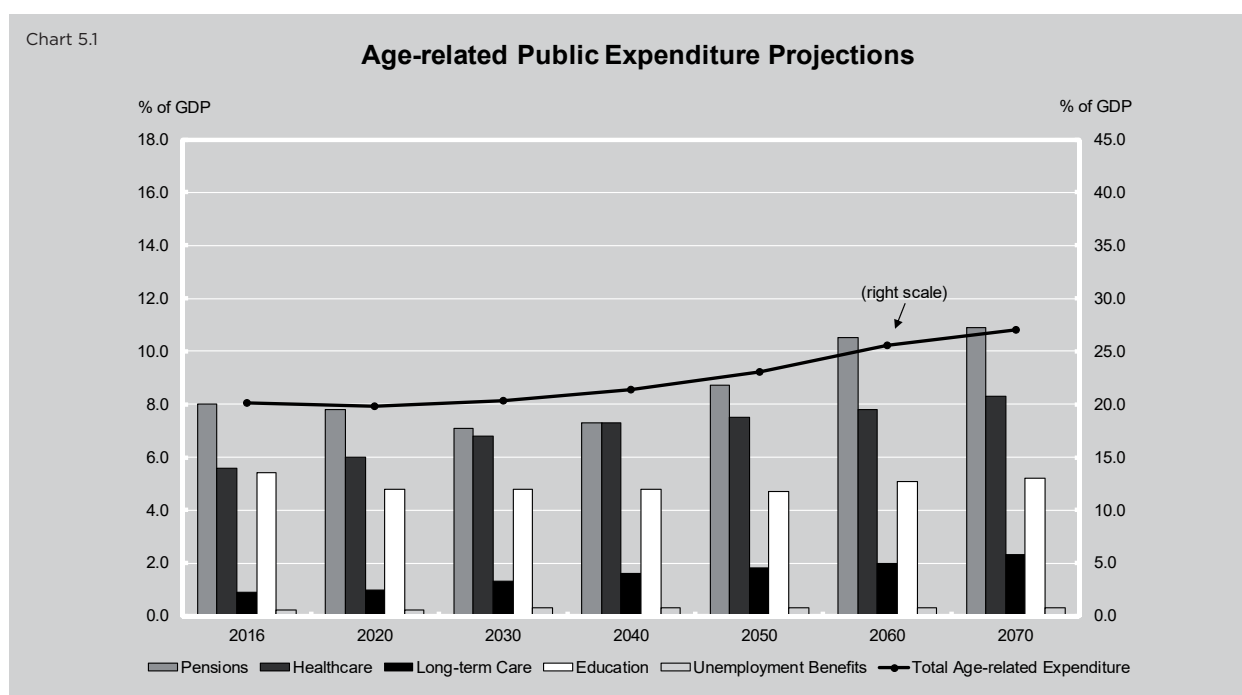
As a result of these demographic developments, the support ratio (persons in the 15-64 years bracket as a proportion of persons aged 65+) is expected to decline from 3.4 per cent in 2016 to 1.8 per cent in 2070. This means that while in 2016 there were more than 3 persons of working-age for every person that reached pension age, by 2070 this ratio is projected to decrease to around 2 persons of working-age for every person of pensionable age.

5.1.4 Age-Related Public Expenditure

Age-related spending including pensions, health care, long-term care, education and unemployment benefits is projected to increase by 6.9 percentage points over the period 2016-2070. Chart 5.1 shows the age-related public expenditure as a share of GDP for this projection period and Table 5.3 shows the revenue from contributions and number of contributors.

Public expenditure on pensions is presently the most important age-related Government expenditure item and is expected to remain so for the foreseeable future. The pension projection exercise covers contributory and non-contributory old-age pension paid under the social security scheme. The coverage of pension schemes includes also the expenditure on non-contributory old-age pension together with the share paid on the contributory and non-contributory bonus payment. The voluntary private pensions system is still in its infancy as regards pension provision for old-aged persons but its uptake is expected to rise in the future.

Over the projection period, pension expenditure is projected to decrease from 8.0 per cent of GDP in 2016 to 7.1 per cent in 2030, and then increase to 10.9 per cent in 2070. Over the period 2016-2070, pension expenditure as a percentage of GDP is projected to increase by 2.9 percentage points. Taking into consideration the entire projection horizon, this increase is entirely driven by the developments in the dependency ratio. However, a decomposition of the projected pension expenditure that allows a better understanding of the underlying drivers, indicates that this increase is counteracted by



Revenue from contributions and number of contributors

Table 5.3

	2016	2020	2030	2040	2050	2060	2070
Revenue from pension contributions (% of GDP)	8.1	7.0	6.9	6.7	6.6	6.5	6.3
Number of contributors (in 1000s)	195	205	224	236	234	224	221

Source: European Commission Services

the employment effect, followed by the labour market intensity effect, which describes the effects of labour market behaviour on pension expenditure.⁴ These two effects lower the ratio of pension expenditure to GDP, which is explained by the fact that in Pay As You Go (PAYG) systems, a higher employment rate helps increasing the sustainability of pension systems by allowing for a larger contribution base, and therefore, as the employment rate increases, the ratio of pension expenditure to GDP falls.

The expected increase in pension expenditure over the entire period is primarily attributable to an increase in expenditure on old-age pensions (earnings-related) that increases from 5.0 per cent of GDP in 2016 to 9.3 per cent in 2070. However, up to 2030, expenditure on old-age pensions is expected to remain contained due to the impact of legislated increases in the pension age and indexation of the maximum pensionable income with the COLA. Thereafter, the increase in old-age pension expenditure is driven by the ageing process, in reflection of the projected demographic developments.

At the same time, one notes that the parametric changes introduced in the pension reform – more dynamic indexation of the ceiling on pensionable income, the statutory changes to indexation for old-age pensions and the crediting of contributions also contribute to raise expenditure. However, the increase in the pension age, the increase in the contribution period for full pension eligibility, the changes to the benefit formula, and the incentives to defer retirement will contain this projected increase in pension expenditure. The incentives to defer retirement enable potential pensioners to postpone their retirement by up to 4 years. At the same time, the lengthening of the contributory period translates into a lower accrual rate because of the relatively longer required length of service to qualify for the full pension benefit rate.

Expenditure on disability pensions and old-age (non-contributory) pensions are projected to stay relatively constant at 0.2 per cent and 0.3 per cent of GDP, while expenditure on survivors' pensions is projected to decrease from 1.4 per cent of GDP to 0.9 per cent of GDP by 2070. This decline reflects faster average economic growth, particularly in the first half of the projection period, which has an accumulating effect on GDP. Furthermore, it is expected that in future, more women will have an old-age pension in their own right in line in reflection of the stronger labour market participation modelled in the projection leading to less reliance on survivorship pensions.

Expenditure on 'other pensions' is projected to decrease from 1.5 per cent of GDP to 0.4 per cent of GDP over the whole period. The decreasing contributions of other pensions (includes 'top-ups' and Treasury pensions) reflect a combination of factors. The 'top-up' pension covers benefits currently payable to persons in receipt of service pensions which

includes former servicemen in receipt of overseas pensions. This expenditure category is projected to decrease in importance over time in line with the life expectancy of the recipients of this pension category. Similarly, expenditure on the Treasury Pension is projected to decrease in importance over time given that it has been closed to new Government of Malta employees since 1979.

Social security contributions are payable by all gainfully occupied persons between the age of 16 and their pension age.⁵ The scheme allows for several types of contributions to extend coverage to all types of persons in employment. Employed persons pay Class One contributions, while the self-occupied pay Class Two contributions. Class One contributions imply that any person employed under a contract of service in Malta is in insurable employment and subject to the payment of these contributions. For each person, a tripartite contribution is payable: the employed person, the employer and the State each pay 10 per cent of the basic salary of the employee; with the contribution capped to the Maximum Pensionable Income. The rate of Class Two contributions is equally shared by the State and self-occupied persons, whereby the self-occupied pays 15 per cent and the State pays 7.5 per cent of their annual income that is subject to the same ceiling that applies for employees. As shown in Table 5.3, revenue from contributions is expected to decrease from 8.1 per cent to 6.3 per cent over the projection period, while the number of contributors is expected to increase from around 195,000 in 2016 reaching around 236,000 in 2040 and thereafter decreasing to around 221,000 in 2070.

Compared with the projections in the 2015 Ageing Report, expenditure on public pensions is foreseen to rise less rapidly over the entire projection horizon. Over the period 2016-2030, public pension expenditure is expected to decline by 1.0 percentage point of GDP. During the 2030-2060 period, the pension expenditure to GDP increases by 3.4 percentage points of GDP, while over the last remaining years expenditure adds-up further by 0.4 percentage points of GDP.

Another important contributor to the increase in age-related spending is healthcare. During the period 2016-2070, projections indicate that Malta is expected to record an increase of 2.7 percentage points of GDP in health care to reach 8.3 per cent and for the long-term care expenditure projections, expenditure is expected to increase by 1.4 percentage points of GDP to reach 2.3 per cent by 2070. These results reflect an ageing society and an increase in life-expectancy at birth over the projection period.

Public spending on unemployment benefits as a share of GDP is projected to remain rather stable rising marginally by 0.1 percentage points relative to the baseline to reach 0.3 per cent of GDP in 2030 and remain unchanged thereafter in reflection of the projected trajectory for the unemployment rate. Additionally, education spending as a percentage of GDP is projected to decrease by 0.2 percentage points during the projection period to reach 5.2 per cent of GDP in 2070 in reflection of developments in the structure of the population.

5.2 Focus on Pension Reforms

The pension projections presented for the 2018 Ageing Report takes into consideration the legislated pension reforms, including measures that are to be phased in gradually. This section outlines briefly the main pension parameters of the contributory old-age pension also known as the two-thirds pension scheme. Pension reform in Malta is an ongoing process. The Government is sustaining its efforts to ensure adequate and sustainable pensions for current and future pensioners, as addressed in the ongoing pension reform

process. The aim is to improve the current system primarily by strengthening further the first pillar and through the introduction of incentives pertaining to third pillar pensions.

In December 2006, the House of Representatives adopted a series of parametric reforms (Act No. XIX of 2006), aimed at enhancing the sustainability of the pension system while improving the adequacy of the pension enjoyed by retirees in the future. These reforms included raising the pension age from 61 to 65 by 2027; lengthening the contributory period from 30 to 40 years; adopting changes to the two-thirds pension, calculation formula, the maximum pensionable income and the crediting of contributions.

In 2016, the Government adopted also a number of reform measures intended to strengthen further adequacy and sustainability. In order to ensure a fair balance between the contributory period and the period spent in retirement across generations, the contribution period for a full pension was based on a stable ratio between years contributing and years drawing pension. Consequently, the contributory period was raised from 40 to 41 years for persons born after 1968.

Incentives to defer early retirement and lengthening working career were also introduced. The scheme is open to all employees, who would have fulfilled the contributory requirements and are eligible to retire at 61 years of age with a full pension. Those who continue working until 62 years will receive an increase of 5 per cent in their pension. The scale increases every year, whereby, a person who works until 63 years would receive an increase of 10.5 per cent. A person deferring retirement by 4 years and 5 years, to retire at 64 and 65, would receive an increase of 16.5 per cent and 23 per cent respectively. In addition, another amendment was effected to Article 64A whereby persons born on or after 1/1/1969, who want to access the early exit option, require 35 years of paid contributions with a maximum of 6 years of credits. Both measures are intended to lengthen careers and deter early retirement.

The two measures, i.e. the incentives to encourage later retirement and the linking of the contributory period to the period spent in retirement, are expected to contribute to the strengthening of the long-term sustainability of public finances.

At the same time, the adequacy element was also safeguarded through the increase in the minimum pension, better credits for child rearing and family growth (which is designed to address gaps in the contributory periods particularly of women, arising due to family responsibilities and as a policy instrument contributing positively toward fertility increases) and the introduction of credits for human capital development and lifelong learning, alongside other measures.

Periodic reviews, within intervals not exceeding 5 years, are to be carried out (next review expected in 2020) with the outcome of the exercise reported to the House of Representatives. The Social Security Act requires the Pensions Strategy Group to put forward recommendations with a view to achieve further adequacy, sustainability and social solidarity in such a manner that a stable proportion is kept between the contribution periods and the period of time that the pension will be paid.

The Government has also focused on diversifying retirement income and reducing dependency on state pensions. Personal private pension schemes were launched in 2015 and tax benefits for such products were introduced. Accordingly, there are now a number of providers offering personal pension plans. Savers undertaking these plans can receive tax rebates on their savings for retirement. In 2017, the Government also

implemented a measure intended to incentivise the take-up of voluntary occupational pensions. The Voluntary Occupational Pension Scheme Rules provide tax credits to both employees and employers (including self-occupied persons). Furthermore, the Government launched the Home Equity Release, which allows home-owners pensioners to raise their annual financial income and improve their standard of living. This will serve as a financial supplement, together with the pension they receive, by allowing pensioners to convert part of their residential value into a stream of income.

During this year, the Government strengthened the incentives for both the Third Pillar Pension Scheme as well as the Voluntary Occupational Pension Scheme, to encourage further take up of such products. In fact, the amount of financial investment that is tax-exempt was raised to a maximum of €2,000 each year and the reduction in taxes was increased from 15 per cent to 25 per cent.

Footnotes:

¹ COLA is a flat rate increase in wages and pensions (the latter granted in full as from Budget for 2008) that reflects the indexation of the basic wage to the average Retail Price Index inflation of the last 12 months to September of that year.

² The Maltese Government believes that the linking of the contributory period to life expectancy remains an important lynchpin in its strategy to ensure sustainable pensions and consequently considers the projections presented for the 2018 Ageing Report as conservative in terms of their potential to generate lower increases in pensions expenditure over the long-term.

³ Following the conclusion of the EUROSTAT projection in February 2018, National Statistics Office (NSO) made a substantial revision in the population, which was not factored in the age related expenditure projections. In 2016, the actual population was revised to 450,415, a difference of 13,757 persons from the population reported in the EUROSTAT projections.

⁴ The employment rate effect is defined as the ratio of population aged 20-64 years over the number of working people aged 20-64 years. The labour market intensity effect is calculated as ratio of the population aged 20-64 years over the hours worked.

⁵ Contributions are also payable by pensioners in gainful employment that retired after 5th January 2008. Pensioners who retired earlier than this date are allowed to work without prejudicing their pension rights in the ages of 61 years to 65 years without paying social security contributions, subject to a ceiling on earnings equivalent to the national minimum wage. For this group, ceiling on earnings is removed at age of 65 years and no further contributions are due.

6. Quality of Public Finances

6. Quality of Public Finances

The Maltese Government is of the view that the framework for better quality public finances should be based on strong links between resources, budgeting, monitoring and intervention, and clear expectations for delivering outcomes.

6.1 Improving the Structure and Efficiency of Revenue Streams

The Government's taxation strategy seeks to ensure that revenue streams from taxation are sustainable and supportive to the attainment of its fiscal targets as specified in this Stability Programme. Since 2013, Government policy reforms have focused on shifting the tax burden away from labour, widening tax bases, further simplifying the tax system and combatting tax evasion and avoidance.

Meanwhile, the Government's tax policy is also directed at tackling environmental concerns. Indeed, the Government focused on shifting the tax burden onto goods that harm the environment or health. Furthermore, through the extension of ongoing measures targeting stamp duty, property owners are encouraged to supply idle properties on the rental market, in a context of an ever-increasing demand for rental units driven primarily by immigration flows.

Priority is also given to tax simplification to alleviate the administrative costs associated with the computation of tax liability. Through Value Added Tax (VAT) grouping, legal independent entities having fixed establishments in Malta and which have financial, economic and organisational ties between them, can register as a single taxable person for VAT purposes. In addition, the Government is also introducing detailed tax consolidation regulations which permit groups of companies to calculate their profits/losses on a group basis.

Furthermore, the Government continued with its fight against tax evasion and unjust competition. Heavier fines have been imposed for both Court and out-of-Court cases related to evasion of excise duty on cigarettes and other tobacco products. In addition, Customs' incessant emphasis on clamping down on tax evasion, in particular, where Malta's borders are concerned, has also included the creation of a new Canine Unit, extensive investment in x-ray scanning facilities, the procurement of an intelligence analytical software for investigation purposes and the creation of a professional Anti-Money Laundering Team. All Customs personnel pertaining to the Canine Unit, Customs Intelligence Service, Scanning Team and Anti-Money Laundering Team has gone through, or are currently undergoing, an extensive professional training programme offered by foreign experts.

A legal notice containing the European Union (EU) Anti-Tax Avoidance Directives Implementation Regulations has been published in a bid to address tax avoidance. All but one of the regulations have entered into force as of January 2019, with the regulation on the exit tax coming into effect as from January 2020.

6.2 Ministries' Business and Financial Plans, including HR Plans

The Ministry for Finance (MFIN) remains responsible for high level business planning, in particular through due consideration of any trade-offs or prioritisation which needs to be made based on a detailed understanding of what resources are at the Government's disposal, and different ways in which they can be deployed. Nevertheless, Ministries and Departments have responsibility in a similar way for lower level business planning. By means of Directive Number 10, which came into effect as from 1st February 2016, Ministries and Departments have an obligation to prepare Business and Human Resource Plans for a period of three years, renewable every year.

In this regard, in 2018, MFIN issued circular MFIN 1/18 to request the submission of the Ministries' 2019–2021 Business and Financial Plans. MFIN assessed the plans received by each Ministry/Department/Entity in order to compile the three-year fiscal projections. Along the budgetary process, two rounds of bilateral meetings were held with each line Ministry, one at Permanent Secretarial level and the second at Ministerial level. The business and financial plans were discussed in detail, clarifications were sought and statements incorporating the three-year revenue and expenditure projections for 2019–2021, at Ministry level, were incorporated into the 2019 Financial Estimates which were approved by Parliament in December 2018.

6.3 The Comprehensive Spending Reviews

During the period 2014 to 2018, the Maltese Government completed a series of reviews in social security, in health and in education. In 2018, following the review at the Management Efficiency Unit (MEU) which was completed in January, the Spending Review exercise was carried out at the Malta College for Arts, Science and Technology (MCAST) and was completed in August 2018. The review identified unnecessary bureaucracy generated by the current academic structure at MCAST and recommended that the structures of teaching, academic staff teaching workloads and academic supervision of students are revised. It was also suggested, that MCAST should update its engineering and science workshops. The recommendations outlined in the report are in the throes of being implemented during 2019.

During the current year, a spending review is being carried out at the Malta Police Force. The terms of reference were agreed at Ministerial level and a panel of experts from both the Malta Police Force and MFIN have now started an in depth Comprehensive Spending Review. The review process started in March with the aim of completing the review by the end of June 2019. The aim is to look at policing in Malta and the policy process and to suggest recommendations for reforms that are sustainable in the long-term.

6.4 Delivering Outcomes

An effective performance measurement system requires information on inputs (monetary and other resources), on outputs delivered and enabling actions achieved, as well as direct measures of outcomes.

6.4.1 Public Sector Productivity

Having met the medium-term budgetary objectives, Malta has been looking more towards the quality of public finances. This section delves into how the various functions of Government are using the resources at their disposal to efficiently deliver public services. This aims to ensure more effective spending through the comprehensive spending review as well as through improvements made in the efficiency and effectiveness of the tax system.

6.4.1.1 Measuring Public Sector Productivity in Malta

This section quantitatively evaluates the productivity growth in Malta's public sector. It is beyond the scope of the study to produce statistical estimates supplementing input-based estimates in the national accounts. However, the various measures of public sector outputs are useful indicators of productivity and are consequently considered an important input in collective bargaining or simply as an assessment of key performance indicators in the public sector.

Assessing public sector productivity is challenging, since in such studies, it is the outcomes which are of interest, and not just of the output itself. To measure the growth in public sector productivity, this study will be using the same methodology applied in last year's Programme. The system takes into account outputs and inputs related to the provision of healthcare, education, social care, public order and safety, defence and other public services. This is achieved by weighting indices of outputs and outcomes per unit of inputs to compute an overall figure for productivity growth within the public sector.

6.4.1.2 Public Sector Inputs

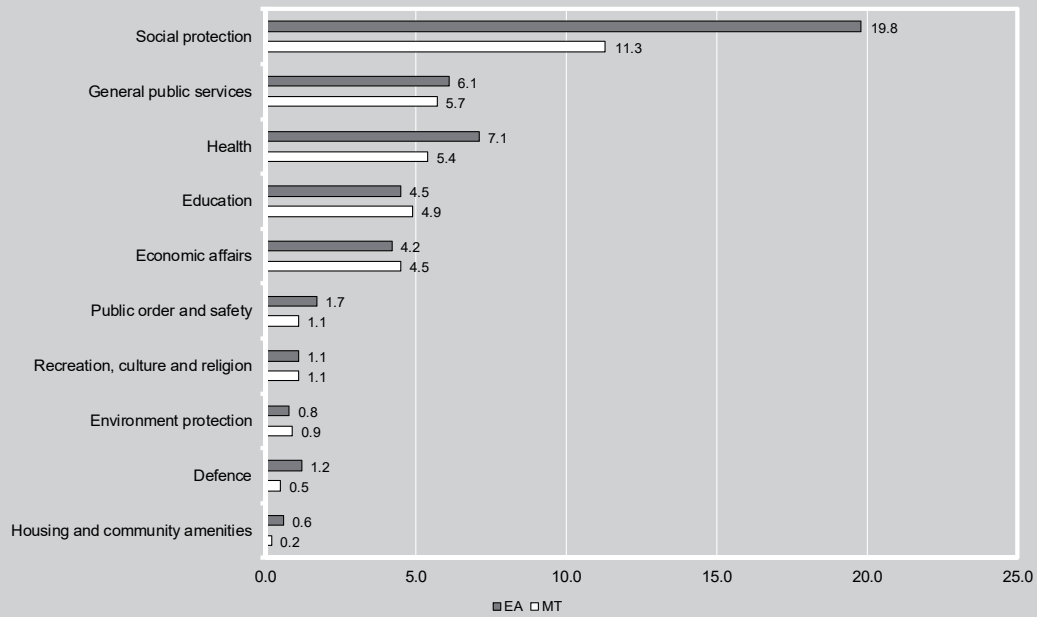
Similar to last year, production inputs considered will be limited to labour inputs and the labour figures are based on estimates provided by the National Statistics Office (NSO) and have been segregated according to the Classification of the Functions of the Government (COFOG). Since a comparative analysis of employment by COFOG within the Euro Area was not possible, a comparison of expenditure as a share of Gross Domestic Product (GDP) was performed. Results show that the Maltese Government expenditure generally follows a somewhat similar pattern to that of the Euro Area with the main exception being social protection.

Chart 6.1 shows that the largest levels of expenditure can be attributed to social protection in both economies. However, expenditure on social protection in the Euro Area, as a per cent of GDP is much higher than that of Malta with the gap widening further compared to 2016. Malta also spends relatively less on Healthcare, Defence, Public Order and Safety, and General Public Services but generally spends relatively more on Education and Economic Affairs. Compared to previous years, Government expenditure as a percentage of GDP has fallen in almost all sectors, primarily reflecting the dynamic economic growth conditions.

In relative terms, the composition of employment in 2017 has remained almost unchanged from the previous year. Chart 6.2 shows that half of Government employment can be attributed to Education and Health, comprising 29.0 per cent and 21.0 per cent of Government employees, respectively. These are followed by Economic Affairs which amounts to 13.0 per cent. Social Protection makes up 10.0 per cent of public employment, whilst General Public Services and Public Order and Safety, respectively constitute 10.0 per cent and 9.0 per cent of total public sector employment.

Chart 6.1

Composition of General Government Expenditure by COFOG

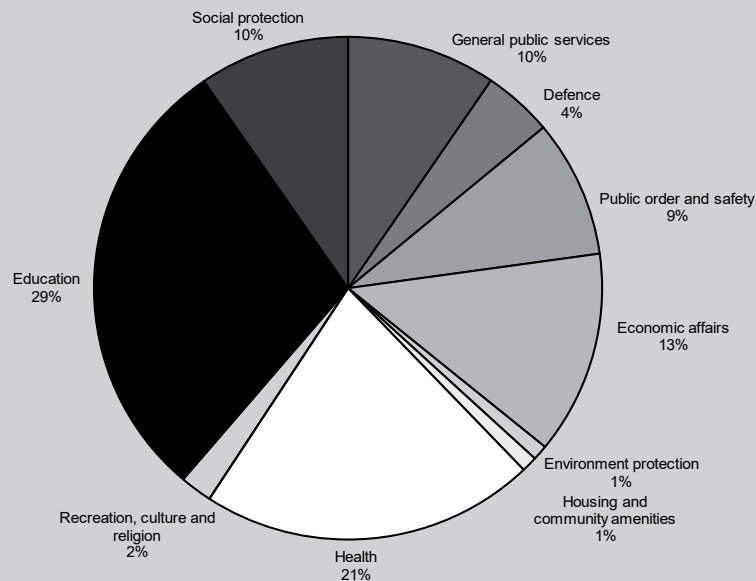


Data Source: Eurostat

Between 2005 and 2017, employment growth averaged at 1.3 per cent per annum (or 2.0 per cent since 2010). The largest growth was recorded in Social Protection and Health with figures rising 4.5 per cent and 2.5 per cent respectively. Chart 6.3 outlines that the largest declines were recorded in the Environment Protection and Housing Community Amenities categories, however this was mainly underpinned by the reclassification of employees to other COFOG categories.

Chart 6.2

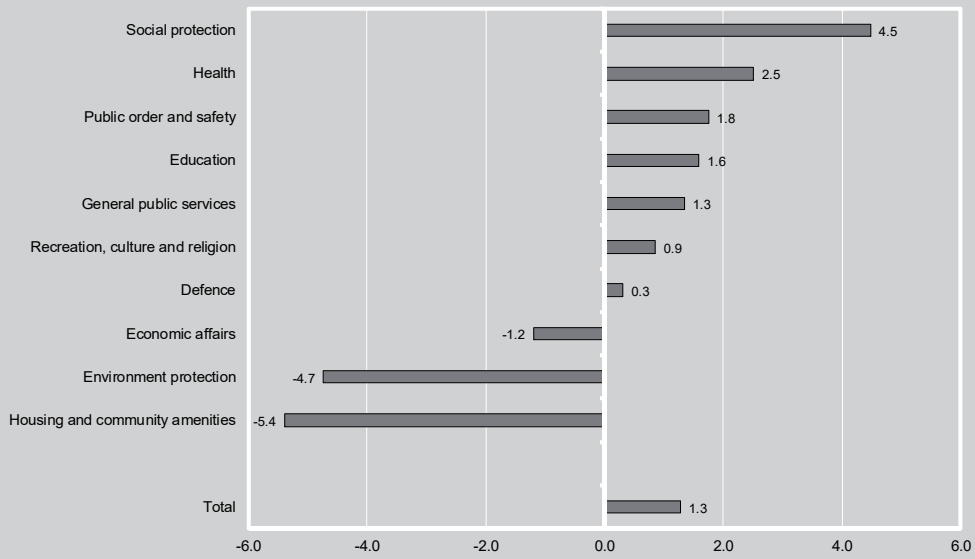
Composition of Public Sector Employment by COFOG



Data Source: NSO/EPD unpublished estimates

Chart 6.3

Average Annual Growth in Public Sector Employment by COFOG (2005 - 2017)



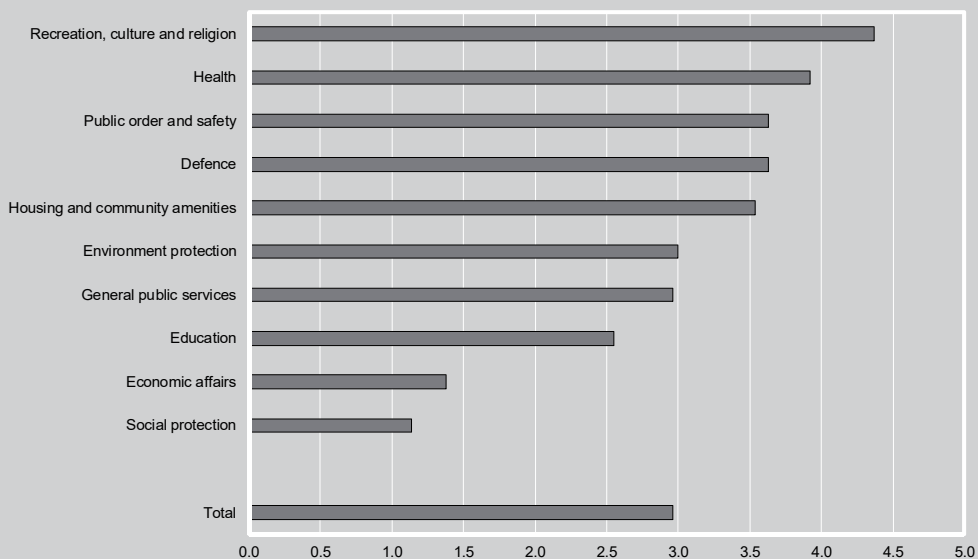
Data Source: NSO/EPD unpublished estimates

6.4.1.3 Public Sector Outputs

A number of indicators, which cover a mix of both volume and quality, were used to construct a measure of output for each of the COFOG categories. The methodology and indicators used for this study were the same as last year’s Programme. Most of the selected indicators, particularly for Health and Social Protection, were only available from 2005, so the index captures productivity gains in the last decade.

Chart 6.4

Average Annual Growth in Public Sector Output by COFOG since 2005



Data Source: NSO/EPD unpublished estimates

Chart 6.4 underlines that output levels grew across all COFOG configurations. The highest increase was recorded in the Recreation, Culture and Religion sector (4.4 per cent), followed by the Health sector (3.9 per cent) whilst the lowest growth in output was registered in the Social Protection category (1.1 per cent). Taking the entire public sector into account, the average annual growth in public sector output since 2005 was of 3.0 per cent.

6.4.1.4 Public Sector Productivity

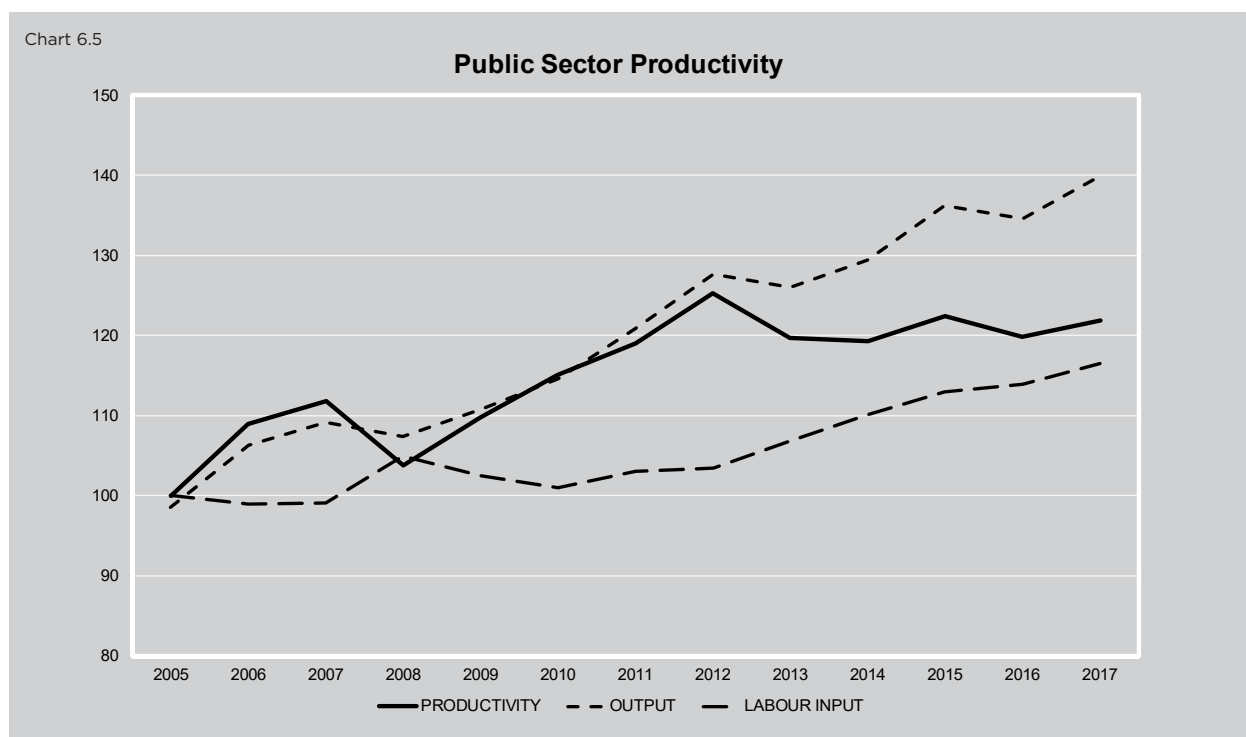
MFIN estimates indicate that real public sector labour productivity has improved by an annual average of 1.7 per cent per annum since 2005. Chart 6.5 illustrates public sector productivity trends and the corresponding developments in output and employment.

The nominal value of public sector labour productivity can be estimated using real public-sector labour productivity together with a measure of any price changes related to public service provision. In the absence of a specific deflator from the output side, the GDP deflator was used as a measure of prices. This indicator is useful when benchmarking wage increases in the public sector. The nominal value of productivity in the public sector was thus estimated to have increased by an annual average of 3.2 per cent per annum since 2005.

6.4.2 Public Service Renewal

In recent years, a programme of constant renewal was implemented for the Public Service, aiming at a more efficient service that seeks to meet the needs and expectations of both the public and the civil servants.

Since 2013, several measures were implemented including the five servizz.gov community hubs enabling easier access to services for citizens, a more concise Public Service Management Code (PSMC), efforts to reduce bureaucracy within the Public Service



while safeguarding accountability, as well as reforms in the fields of public procurement and simplification of financial regulations.

In addition, initiatives were undertaken to improve quality of service and to digitise aspects of the Public Service. A mystery shopper for Government departments was also introduced, in order to identify shortcomings in service delivery and remedy the situation accordingly. In addition, the launch of Key Performance Indicators (KPIs) for the Public Service set clear aims which need to be reached within a specific timeframe.

Meanwhile, the fifth collective agreement for Public Service employees was signed in 2017, covering an eight-year period, thus ensuring more stability while allowing the administration to continue implementing the necessary changes, investing in people and offering a good quality service.

7. Institutional Features of Public Finances

7. Institutional Features of Public Finances

7.1 Fiscal Transparency Evaluation Exercise

In line with its objectives of effective fiscal management and accountability, the Government requested the International Monetary Fund (IMF) to undertake a Fiscal Transparency Evaluation (FTE) of Malta's public finances. The IMF carried out the evaluation in May 2018 and published its report in September 2018 presenting and explaining in detail the results, while also putting forward recommendations that further enhance fiscal transparency.

The report found that many elements of sound fiscal transparency practices were already in place and Malta obtained results which were similar to other advanced economies in the European Union (EU) that have undertaken the FTE. Indeed, the report established that a large number of the principles of the Fiscal Transparency Code are met at good or advanced level.

The evaluation outlined seven recommendations to further enhance fiscal transparency in Malta, and proposed an action plan for implementing these recommendations. Pursuant to this exercise, an internal process is underway which is assessing the recommendations in detail and taking the necessary steps to implement the recommendations where possible, and within the timeframes suggested by the IMF.

Some progress has already been achieved. Pension entitlements were published by the National Statistics Office (NSO) in June 2018, also following the new requirements established in both the European System of Accounts (ESA 2010) and System of National Accounts (SNA 2008). The publication followed a project by NSO, in collaboration with the Research Centre for Generational Contracts (RCG) at Freiburg University to compile a suitable model able to estimate Malta's pension entitlements for its two pension systems; (i) the Social Security Pension system and (ii) the Treasury Pension system. Total entitlements in 2015 were estimated at €24.4 billion. A commitment by NSO to produce a statement of other economic flows of the General Government was also made. NSO is also at an advanced stage in preparing a statement of the operations of corporations based on audited accounts.

Discussions are also underway on how to improve the consistency of fiscal reports and harmonise and consolidate presentations of macroeconomic and fiscal forecasts in different reports to make them more consistent. Specifically, in this Stability Programme a detailed explanation of changes to the forecasts from the Programme of the previous year is being provided, in line with the IMF recommendation.

With a view to strengthen public investment management, multi-year commitments were added to the 2019 business plans, whilst plans are underway to require cost-benefit analysis of major projects to be reported in departmental business plans submitted yearly to the Ministry for Finance (MFIN). The new requirement will apply for prospective projects.

7.2 The Malta Fiscal Advisory Council

The Malta Fiscal Advisory Council (MFAC) is an Independent Fiscal Institution (IFI) established in terms of the Fiscal Responsibility Act (FRA) and began operating in

January 2015. There was a change in the chairmanship of the MFAC during 2018 when Mr. John Cassar White was appointed as chairman from 1 July 2018. In December 2018, the chairman and members of the Fiscal Council were re-appointed to serve for a further period of four years, with effect from 1 January 2019.

The MFAC is mandated to validate the Government's economic and fiscal forecasts; assess performance against the fiscal rules; and provide an assessment of whether the fiscal stance is conducive to prudent economic and budgetary management. Since its establishment in 2015, the Council has always concluded that the macroeconomic and fiscal forecasts presented by the Government in its annual Draft Budgetary Plan and Update of Stability Programme, were within the Council's endorsable range. Legislative amendments to the FRA carried out in 2018 now entrust MFAC to carry out an independent ex post assessment of macroeconomic and fiscal projections, as well as a fiscal risk assessment. It is worth noting that in practice, the MFAC already used to carry out a fiscal risk assessment of the fiscal projections presented in the annual Update of the Stability Programme, which used to be incorporated in the Medium-Term Fiscal Plan submitted by Government to Parliament.

During 2018, the MFAC held twelve formal meetings to discuss economic matters and administrative issues, as well as the MFAC's reports prior to their publication. Indeed, the MFAC published seven reports in 2018. Following the publication of the Annual Report for 2017, the MFAC then issued three reports which focused on the Update of Stability Programme for 2018 - 2021. These dealt respectively with the endorsement of the macroeconomic forecasts, the endorsement of the fiscal forecasts, and the compliance with the fiscal rules. They were followed by a report which assessed MFIN's Annual Report 2017 and another which dealt with MFIN's Half-Yearly Report 2018. The final report focused on the Draft Budgetary Plan for 2019.

Towards the end of 2018, the MFAC, in consultation with MFIN, took the decision to streamline its reports and combine the analysis which previously was spread over different reports. This consolidation process is meant to improve transparency by eliminating unnecessary overlap between successive reports and in so doing improving the presentation of the factual evaluations produced and published by the Council. The MFAC shall supplement these standard reports with other research-oriented working papers in order to both support the MFAC's assessments with more empirical evidence, and to gain deeper insight into macroeconomic developments and public finance issues. To this effect, in 2018, the MFAC published its first working paper, which examined the validity of the Ricardian Equivalence Theorem (RET) for the Maltese economy.

The MFAC issued six press releases during 2018, which at times were followed by requests from the media for interviews. These opportunities should help to raise awareness about the economic and fiscal issues which are most relevant to Malta.

During 2018, various meetings were held with MFIN to discuss issues related to the endorsement of the official macroeconomic and fiscal forecasts. The Ministry also provided feedback on the recommendations made by the MFAC since its establishment. The MFAC also met officials from the Directorate-General for Economic and Financial Affairs within the European Commission in order to exchange views on the latest macroeconomic and fiscal developments and discuss the institutions' short- and medium-term outlook. Other meetings were held with senior officials from the IMF and officials from credit rating agencies.

During the course of 2018, members and staff of the MFAC attended several meetings abroad, mainly related to the MFAC's membership in the EU Network of Independent Fiscal Institutions (EUNIFIS), with the rest being official representation or attendance at seminars. The MFAC participated as member in the Working Group on the Medium-Term Budgetary Framework and the Working Group on the Output Gap.

7.3 Institutionalising Spending Reviews

In line with the Country Specific Recommendation (CSR) endorsed by the European Council in 2017, inviting the Maltese Government to “Expand the scope of the ongoing spending reviews to the broader public sector and introduce performance-based public spending”, the process of institutionalising Comprehensive Spending Reviews has registered substantial progress.

In 2018, a Directorate was set up within the Budgetary Affairs Division (MFIN) and was tasked with the planning and coordination of reviews in collaboration with the respective ministry, department, entity or cost centre as required. This Directorate will be technically assisted by the Economic Policy Department.

The main principles of the spending review process have also been established and a code of conduct has been formulated to consolidate the spending review process and institutionalize it formally based on international best practices and on experience already gained in Malta. The Code of Conduct for Comprehensive Spending Reviews provides the mandate, specifies the objectives, introduces the actors and their respective responsibilities, details the steps to follow and outlines the outputs/outcomes of future spending reviews.

A team was set up to evaluate and monitor progress on the Spending Review's recommendations carried out to date. The Government has secured some €800,000 in funding under the Structural Reform Support Programme. The fund has allowed for the training of some 48 spending review officers, both from MFIN and also finance officers from spending departments in other line ministries and departments. The ongoing programme will also focus on the process of implementing CSR recommendations through the setting up of a traffic lights method of monitoring and evaluation. The process should be completed by June 2020.

Macroeconomic Prospects

Table 1a

Percentages unless otherwise indicated	ESA Code	Level 2017 ⁽¹⁾	Percentage change over previous period					
			2017	2018	2019 ⁽²⁾	2020	2021	2022
1. Real GDP	B.1g	9,699.4	6.7	6.6	6.2	5.7	5.1	5.0
2. Nominal GDP	B.1g	11,313.7	9.4	8.9	9.3	8.3	7.4	7.2
Components of real GDP								
3. Private consumption expenditure ⁽³⁾	P.3	4,550.7	3.6	7.3	5.8	3.9	3.4	3.3
4. Government consumption expenditure	P.3	1,535.5	2.1	11.7	11.6	4.7	2.9	3.0
5. Gross fixed capital formation	P.51	1,862.8	-7.4	-3.7	13.7	5.4	5.7	3.0
6. Changes in inventories and net acquisition of valuables (% of GDP)	P.52+P.53		-0.7	0.1	0.0	0.0	0.0	0.0
7. Exports of goods and services	P.6	14,740.8	5.6	2.1	2.4	4.1	3.6	3.5
8. Imports of goods and services	P.7	12,917.9	0.6	1.3	3.4	3.0	2.5	2.0
Contribution to real GDP growth⁽⁴⁾								
9. Final domestic demand		7,949.0	0.3	4.3	7.0	3.7	3.1	2.6
10. Change in inventories and net acquisition of valuables	P.52+P.53		-1.3	0.9	0.0	0.0	0.0	0.0
11. External balance of goods and services	B.11	1822.9	7.7	1.4	-0.8	2.1	2.0	2.4

⁽¹⁾ € million

⁽²⁾ Forecasts from 2019 onwards

⁽³⁾ Includes NPISH final consumption expenditure

⁽⁴⁾ Users should note that chain-linking gives rise to components of GDP not adding up to the aggregate real GDP series. This non-additivity, similar to that in other countries' national accounts, is due to mathematical reasons and reflects the fact that chain-linked volumes are calculated by separately extrapolating both totals and their sub-components.

Price Developments

Table 1b

Percentages unless otherwise indicated	ESA Code	Level 2017 ⁽¹⁾	Percentage change over previous period					
			2017	2018	2019 ⁽²⁾	2020	2021	2022
1. GDP deflator ⁽³⁾		116.3	2.3	2.1	2.9	2.4	2.2	2.0
2. Private consumption deflator		110.0	1.0	0.8	1.7	1.2	1.5	1.5
3. HICP (Average 2015=100)		102.2	1.3	1.7	1.9	2.0	1.8	1.8
4. Public consumption deflator		112.9	1.7	3.8	3.8	2.0	2.5	2.6
5. Investment deflator		123.8	2.1	4.4	3.2	3.5	2.8	2.5
6. Export price deflator (goods and services)		115.8	2.8	2.3	2.3	2.2	2.2	2.1
7. Import price deflator (goods and services)		113.5	2.0	2.2	2.4	1.8	2.1	2.0

⁽¹⁾ Index (base 2010 unless otherwise indicated)

⁽²⁾ Forecasts from 2019 onwards

⁽³⁾ Users should note that chain-linking gives rise to components of GDP not adding up to the aggregate real GDP series. Indeed, summing up the deflators of the components of GDP would not add up to the actual GDP deflator observed for the year. For this reason, the GDP deflator quoted in this table for 2014 and 2015 reflects the actual difference between nominal and real GDP growth rates for the year.

Labour Market Developments

Table 1c

Percentages unless otherwise indicated	ESA Code	Level 2017	Percentage change over previous period					
			2017	2018	2019 ⁽¹⁾	2020	2021	2022
1. Employment, persons (National Accounts Definition, Domestic Concept)		218,464	7.8	5.6	4.6	4.3	4.0	3.8
2. Employment, hours worked (National Accounts Definition, Domestic Concept) ('000s)		438,676	4.1	5.6	4.6	4.3	4.0	3.8
3. Unemployment rate (Harmonised definition, 1000 persons)		9,000	4.0	3.7	3.8	3.9	4.0	4.0
4. Labour Productivity, persons (Real GDP per person employed)		44,398	2.5	1.4	1.5	1.3	1.0	1.1
5. Labour Productivity, hours worked (Real GDP per hour worked)		22.1	2.5	1.4	1.5	1.3	1.0	1.1
6. Compensation of employees (€ million)	D1	4,583.4	7.6	7.2	8.1	7.7	7.3	7.0
7. Compensation per employee (€)		20,980	2.9	2.9	3.3	3.2	3.2	3.1

⁽¹⁾ Forecasts from 2019 onwards

Sectoral Balances

Table 1d

Percentages of GDP	ESA Code	2017	2018	2019	2020	2021	2022
1. Net lending/borrowing		10.9	11.7	10.9	14.0	16.2	19.1
vis-à-vis the rest of the world	B.9						
of which:							
Balance on goods and services		21.3	21.4	19.2	20.5	21.6	23.0
Balance of primary incomes and transfers		-10.9	-10.2	-9.8	-7.9	-6.7	-5.2
Capital account		0.5	0.6	1.5	1.4	1.3	1.2
2. Net lending/borrowing of the private sector	B.9	8.1	9.5	9.9	13.0	15.1	17.9
3. Net lending/borrowing of General Government	EDP B.9	3.5	2.2	0.9	1.0	1.1	1.1
4. Statistical discrepancy		-0.6	0.1	0.0	0.0	0.0	0.0

General Government Budgetary Prospects

Table 2a

Percentages of GDP		ESA code	2017 ^(*)	2018 ^(*)	2017	2018	2019	2020	2021	2022
Net Lending (EDP B9) by sub-sector										
1.	General Government	S13	387.2	250.8	3.4	2.0	0.9	1.0	1.1	1.1
2.	Central Government	S1311	382.6	252.1	3.4	2.0	0.9	1.0	1.1	1.1
3.	State Government	S1312	-	-	-	-	-	-	-	-
4.	Local Government	S1313	4.6	-1.2	0.0	-0.0	-0.0	-0.0	-0.0	-0.0
5.	Social security funds	S1314	-	-	-	-	-	-	-	-
General Government										
6.	Total revenue	TR	4,429.4	4,783.3	39.2	38.8	38.1	36.7	35.7	35.2
7.	Total expenditure	TE	4,042.2	4,532.4	35.7	36.8	37.2	35.7	34.7	34.1
8.	Net lending / borrowing	B9	387.2	250.8	3.4	2.0	0.9	1.0	1.1	1.1
9.	Interest expenditure	D41	205.0	187.7	1.8	1.5	1.4	1.2	1.2	1.1
10.	Primary balance ⁽¹⁾		592.2	438.6	5.2	3.6	2.3	2.2	2.2	2.2
11.	One-off and other temporary measures ⁽²⁾		-17.3	15.2	-0.2	0.1	0.0	0.0	0.0	0.0
Selected Components of Revenue										
12.	Total Taxes (12=12a+12b+12c)		2,990.5	3,261.7	26.4	26.5	25.9	25.5	25.1	24.8
12a.	Taxes on production and imports	D2	1,401.4	1,590.6	12.4	12.9	12.4	12.1	11.7	11.5
12b.	Current Taxes on Income, Wealth, etc.	D5	1,569.8	1,650.4	13.9	13.4	13.3	13.3	13.2	13.1
12c.	Capital Taxes	D91	19.3	20.7	0.2	0.2	0.2	0.2	0.2	0.2
13.	Social Contributions	D61	702.9	764.8	6.2	6.2	6.1	6.0	6.0	5.9
14.	Property Income	D4	90.7	96.0	0.8	0.8	0.5	0.5	0.5	0.4
15.	Other ⁽³⁾		645.2	660.8	5.7	5.4	5.6	4.7	4.2	4.0
16=6.	Total Revenue	TR	4,429.4	4,783.3	39.2	38.8	38.1	36.7	35.7	35.2
p.m.:	Tax Burden (D2+D5+D6111+D6131+D91-D995) ⁽⁴⁾		3,713.7	4,048.5	32.8	32.9	32.2	31.7	31.2	30.7
Selected Components of Expenditure										
17.	Compensation of employees + intermediate consumption	D1+P2	1,987.5	2,210.4	17.6	17.9	18.0	17.6	17.2	16.9
17a.	Compensation of employees	D1	1,268.1	1,376.1	11.2	11.2	11.1	10.8	10.7	10.5
17b.	Intermediate consumption	P2	719.4	834.3	6.4	6.8	7.0	6.8	6.6	6.4
18.	Social payments (18=18a+18b)		1,133.7	1,175.4	10.0	9.5	9.5	9.1	8.9	8.7
	of which Unemployment benefits ⁽⁵⁾		27.0	23.7	0.2	0.2	0.2	0.2	0.2	0.0
18a.	Social transfers in kind supplied via market producers	D632	70.0	83.9	0.6	0.7	0.8	0.8	0.7	0.7
18b.	Social transfers other than in kind	D62	1,063.7	1,091.5	9.4	8.9	8.6	8.3	8.2	8.0
19=9.	Interest expenditure	D41	205.0	187.7	1.8	1.5	1.4	1.2	1.2	1.1
20.	Subsidies	D3	139.9	157.6	1.2	1.3	1.2	1.2	1.1	1.1
21.	Gross fixed capital formation	P51G	264.9	370.6	2.3	3.0	3.9	3.3	3.1	3.2
22.	Capital transfers	D9	98.2	168.6	0.9	1.4	1.3	1.2	1.1	1.1
23.	Other ⁽⁶⁾		213.0	262.0	1.9	2.1	1.9	2.0	2.0	2.0
24=7.	Total Expenditure	TE	4,042.2	4,532.4	35.7	36.8	37.2	35.7	34.7	34.1
p.m.:	Government consumption (nominal)	P3	1,733.9	2,002.8	15.3	16.3	17.2	17.0	16.7	16.4

^(*) € million

⁽¹⁾ The primary balance is calculated as (B9, item 8) plus (D41, item 9)

⁽²⁾ A plus sign means deficit-reducing one-off measures

⁽³⁾ P10 + D39rec + D7rec + D9N (ie D9 other than D91rec)

⁽⁴⁾ Including those collected by the EU and including an adjustment for uncollected taxes and social contributions D995), if appropriate

⁽⁵⁾ Includes social benefits other than social transfers in kind (D62) and social transfers in kind via market producers (D632) related to unemployment benefits

⁽⁶⁾ D29pay + D4Npay (ie D4 other than D41pay) + D5pay + D7pay + P5M + NP + D8

No policy change projections

Table 2b

Percentages of GDP		2018(1)	2018	2019	2020	2021	2022
1.	Total revenue at unchanged policies	4,783.3	38.8	38.7	37.3	36.3	35.7
2.	Total expenditure at unchanged policies	4,532.4	36.8	37.5	36.1	35.2	34.7

⁽¹⁾ € million

Amounts to be excluded from the expenditure benchmark

Table 2c

Percentages of GDP		2017 ⁽¹⁾	2018 ⁽¹⁾	2017	2018	2019	2020	2021	2022
1.	Expenditure on EU programmes fully matched by EU funds revenue	69.5	234.8	0.6	1.9	2.2	1.5	1.0	0.9
1a.	<i>of which</i> Investment fully matched by EU funds revenue ⁽²⁾	49.5	97.3	0.4	0.8	1.3	0.8	0.6	0.5
2.	Cyclical unemployment benefit expenditure ⁽³⁾	3.4	2.3	0.0	0.0	-0.0	0.0	0.0	0.0
3.	Effect of discretionary revenue measures	85.3	-66.4	0.8	-0.5	-0.6	-0.0	0.0	0.0
4.	Revenue increases mandated by law	-	-	-	-	-	-	-	-

⁽¹⁾ € million

⁽²⁾ Based on an estimate of Gross Fixed Capital Formation financed from EU funds

⁽³⁾ The cyclical unemployment benefit expenditure is estimated based on the difference between the unemployment rate and NAWRU. Data for the total unemployment benefit expenditure is defined in COFOG under the code 10.5

General Government Expenditure by Function

Table 3

Percentages of GDP	COFOG Code	2017	2022
1. General public services	1	5.7	5.0
2. Defence	2	0.5	0.6
3. Public order and safety	3	1.1	1.1
4. Economic affairs	4	4.5	4.8
5. Environmental protection	5	0.9	1.3
6. Housing and community amenities	6	0.2	0.3
7. Health	7	5.4	5.1
8. Recreation, culture and religion	8	1.1	1.0
9. Education	9	4.9	5.0
10. Social protection	10	11.3	9.9
11. Total Expenditure	TE	35.7	34.1

General Government Debt Developments

Table 4

Percentages of GDP	ESA Code	2017	2018	2019	2020	2021	2022
1. Gross debt		50.2	46.0	42.7	39.4	36.2	33.2
2. Change in gross debt ratio		-6.0	-4.2	-3.2	-3.4	-3.2	-3.0
Contributions to changes in gross debt							
3. Primary balance		-5.2	-3.6	-2.3	-2.2	-2.2	-2.2
4. Interest expenditure	EDP D.41	1.8	1.5	1.4	1.2	1.2	1.1
5. Stock-flow adjustment		3.0	1.9	1.6	0.9	0.6	0.5
p.m. implicit interest rate on debt ⁽¹⁾		3.6	3.3	3.3	3.1	3.2	3.2

⁽¹⁾ Proxied by interest expenditure divided by the debt level of the previous year.

Cyclical Developments

Table 5

Percentages of GDP	ESA Code	2017	2018	2019	2020	2021	2022
1. Real GDP growth (%)		6.7	6.6	6.1	5.7	5.1	5.0
2. General Government balance	EDP B.9	3.4	2.0	0.9	1.0	1.1	1.1
3. Interest expenditure	EDP D.41	1.8	1.5	1.4	1.2	1.2	1.1
4. One-off and other temporary measures ⁽¹⁾		-0.2	0.1	0.0	0.0	0.0	0.0
<i>of which</i>							
One-offs on the revenue side: General Government		0.1	0.1	0.0	0.0	0.0	0.0
One-offs on the expenditure side: General Government		-0.2	0.0	0.0	0.0	0.0	0.0
5. Potential GDP growth (%)		7.4	6.8	6.5	6.5	5.3	5.0
contributions:							
- labour (hours)		3.6	3.4	2.9	3.0	2.0	1.8
- capital		1.7	1.4	1.7	1.7	1.8	1.7
- total factor productivity		2.1	1.9	1.8	1.7	1.6	1.5
6. Output Gap		0.7	0.7	0.4	-0.3	-0.5	-0.5
7. Cyclical Budgetary Component		0.3	0.3	0.2	-0.1	-0.3	-0.3
8. Cyclically-Adjusted Balance (2-7)		3.1	1.7	0.7	1.1	1.3	1.4
9. Cyclically-Adjusted Primary Balance (8+3)		4.9	3.2	2.1	2.3	2.5	2.5
10. Structural Balance (8-4)		3.3	1.6	0.7	1.1	1.3	1.4

⁽¹⁾ A plus sign means deficit-reducing one-off measures

Divergence from the April 2017 Stability Programme

Table 6

Percentages of GDP	ESA Code	2017	2018	2019	2020	2021	2022
Real GDP growth							
Previous update		6.6	6.1	5.3	4.8	4.6	...
Current update		6.7	6.6	6.1	5.7	5.1	5.0
Difference		0.1	0.5	0.8	0.9	0.5	-
General Government net lending							
	EDP B.9						
Previous update		3.9	1.1	0.9	0.9	1.6	...
Current update		3.4	2.0	0.9	1.0	1.1	1.1
Difference		-0.5	0.9	-0.0	0.1	-0.5	-
Total Revenue							
	TR						
Previous update		40.5	38.7	38.0	37.6	37.4	...
Current update		39.2	38.8	38.1	36.7	35.7	35.2
Difference		-1.3	0.1	0.0	-0.9	-1.7	-
Total Expenditure							
	TE						
Previous update		36.5	37.6	37.1	36.7	35.8	...
Current update		35.7	36.8	37.2	35.7	34.7	34.1
Difference		-0.8	-0.8	0.1	-1.0	-1.2	-
General Government gross debt							
Previous update		50.8	45.8	42.5	39.3	35.6	...
Current update		50.2	46.0	42.7	39.4	36.2	33.2
Difference		-0.6	0.2	0.2	0.1	0.6	-

Long-term Sustainability of Public Finances

Table 7

Percentages of GDP	2016	2020	2030	2040	2050	2060	2070
Total expenditure	20.1	19.8	20.3	21.4	23.0	25.6	27.0
Of which: age-related expenditures							
Pension expenditure	8.0	7.8	7.1	7.3	8.7	10.5	10.9
Social security pension	8.0	7.8	7.1	7.3	8.7	10.5	10.9
Old-age and early pensions	5.0	5.1	5.0	5.6	7.0	8.8	9.3
Disability pension	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Survivors pension	1.4	1.3	1.1	1.1	1.1	1.0	0.9
Other pensions	1.5	1.3	0.7	0.5	0.4	0.4	0.4
Occupational pensions (if in general government)	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.
Health care	5.6	6.0	6.8	7.3	7.5	7.8	8.3
Long-term care (this was earlier included in the health care)	0.9	1.0	1.3	1.6	1.8	2.0	2.3
Education expenditure	5.4	4.8	4.8	4.8	4.7	5.1	5.2
Other age-related expenditures	0.2	0.2	0.3	0.3	0.3	0.3	0.3
Interest expenditure	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.
Total revenue							
Of which: property income	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.
Of which: from pensions contributions (or social contributions if appropriate)	8.1	7.0	6.9	6.7	6.6	6.5	6.3
Pension reserve fund assets	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.
Of which: consolidated public pension fund assets (assets other than government liabilities)	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.
Systemic pension reforms¹⁸							
Social contributions diverted to mandatory private scheme	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.
Pension expenditure paid by mandatory private scheme	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.
Assumptions							
Labour productivity growth	2.5	2.6	2.4	1.8	1.6	1.6	1.5
Real GDP growth	6.1	4.2	3.2	2.0	1.2	1.2	1.6
Participation rate males (aged 15-64)	82.1	82.7	85.4	84.1	84.0	83.9	83.8
Participation rates females (aged 15-64)	55.6	61.0	71.2	74.0	74.8	74.7	75.0
Total participation rates (aged 15-64)	69.2	72.2	78.5	79.2	79.5	79.4	79.5
Unemployment rate (aged 15-64)	4.2	4.6	5.6	5.6	5.6	5.6	5.6
Old-age dependency ratio 15-64	29.1	33.0	40.4	41.4	46.0	53.9	55.8

Source: Ageing Report 2018

Basic Assumptions

Table 8

	2017	2018	2019 ^(a)	2020 ^(a)	2021 ^(a)	2022 ^(a)
Short-term interest rate (annual average)	0.0	0.0	0.0	0.0	0.0	0.0
Long-term interest rate (annual average)	1.3	1.4	1.5	1.5	1.5	1.5
USD/EUR exchange rate (average)	1.148	1.175	1.143	1.176	1.179	1.179
GBP/EUR exchange rate (average)	0.876	0.886	0.861	0.858	0.860	0.860
Malta's main trading partners real GDP growth	2.1	1.5	1.2	1.3	1.3	1.3
Oil prices, (Brent, USD/barrel)	54.3	71.1	65.1	66.5	66.5	66.5
World prices weighted by main trading partners (y-o-y % change)	2.7	2.5	1.4	1.6	1.6	1.6

Basic Fiscal Assumptions

Table 8b

	ESA Code	2017	2018	2019 ^(a)	2020 ^(a)	2021 ^(a)	2022 ^(a)
Implied Elasticity with respect to respective Tax Base							
Taxes on Production and Imports	D2	1.1	2.0	0.9	1.0	0.8	0.9
of which Value Added Taxes	D212	1.1	2.3	1.2	1.1	1.0	0.9
Current Taxes on Income, Wealth, etc. [Personal]	D5	2.1	1.6	1.1	1.0	1.0	0.9
Current Taxes on Income, Wealth, etc. [Corporate]	D5	1.1	-0.3	0.8	0.8	0.7	0.7
Net social contributions	D61	1.4	1.1	0.9	0.9	0.9	0.9
General Government Adjustments (€ millions)		204.5	321.1	118.7	30.9	-15.1	-71.1
Other accounts payable and receivable		-23.4	166.9	41.9	30.9	30.9	29.9
Treasury Clearance Fund & Good Causes Fund		37.2	40.9	32.8	0.0	0.0	0.0
Equity injections		0.0	-62.5	0.0	0.0	0.0	0.0
Social and Investment Fund - IIP - Revenue		169.5	133.1	86.0	81.0	81.0	81.0
Social and Investment Fund - IIP - Expenditure		0.0	-1.0	-10.0	-36.0	-60.0	-75.0
Re-routing/PPP adjustments		-6.9	-20.0	-20.0	-43.0	-65.0	-105.0
Others		28.1	63.6	-12.0	-2.0	-2.0	-2.0
Social Security Benefits							
COLA (€)		1.75	1.75	2.33	3.49	4.08	4.08
Contributory Benefits (€ millions)		749.7	778.9	806.6	844.1	878.6	878.6
Number of CB Beneficiaries (persons)		116,377	116,660	118,929	121,557	124,148	124,700
Non-Contributory Benefits (€ millions)		187.2	186.3	202.9	206.6	206.6	206.6
Number of NCB Beneficiaries (persons)		113,537	113,267	113,935	114,999	116,614	118,317

Contingent liabilities

Table 9

% of GDP

	2017	2018	2019	2020	2021	2022
Public guarantees	9.5	8.7	8.0	7.3	6.8	6.4

Note: The data for Contingent liabilities for 2017 to 2018 is actual, while data for 2019 to 2022 is an estimate

Stock Flow Adjustment Statement

Table 10

Millions of Euros	2018	2019	2020	2021	2022
General Governemnt deficit (-) / surplus (+) (ESA10)	-250.8	-120.3	-141.7	-165.0	-186.3
ESA Adjustments	321.1	118.7	30.9	-15.1	-71.1
Contribution to Sinking Fund (Local)	-89.4	0.0	0.0	0.0	0.0
Contribution to Sinking Fund (Foreign)	0.1	0.1	0.1	0.1	0.1
Contribution to Special MGS Sinking Fund	50.0	50.0	50.0	50.0	50.0
Equity Acquisition	63.5	10.6	0.1	0.1	0.1
EFSF/ESM Credit Line Facility	0.0	4.5	4.5	4.5	4.5
Courts and other deposits	-40.8	-	-	-	-
Stock Premium paid to Church	0.7	1.4	0.0	0.3	0.1
Advances made by Government	-	-	-	-	-
Repayment of Loans to Government	-0.0	0.0	0.0	0.0	0.0
Sale of Assets	-0.9	-0.9	-0.9	-0.9	-0.9
Sale of Non-Financial Assets	-	-	-	-	-
EBUs	25.4	0.0	0.0	0.0	0.0
Currency	6.2	10.6	7.1	7.1	7.1
Movement in Bank Account	-85.2	-	-	-	-
Rerouting/PPP adjustments	20.0	20.0	43.0	65.0	105.0
Increase/(Decrease) in cash balance	-10.9	-0.3	-0.1	-0.1	-1.1
Increase/(Decrease) in Non-Consolidated Debt	9.0	94.4	-7.0	-54.1	-91.5
MGS Consolidation	-26.8	-3.3	-8.6	-17.7	-10.3
Increase/(Decrease) in Consolidated Debt	-17.8	91.1	-15.6	-71.8	-101.8
SFA	233.0	211.4	126.1	93.2	84.5