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## **Assessment of the 2015 Stability Programme for**

**MALTA**

*(Note prepared by DG ECFIN staff)*

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## **1. INTRODUCTION**

This document assesses Malta's April 2015 Stability Programme (hereafter called Stability Programme), which was submitted to the Commission on 30 April and covers the period 2014-2018. The document is usually not approved by the government nor presented to the national parliament for a debate.

Malta is currently subject to the corrective arm of the Stability and Growth Pact. The Council opened an Excessive Deficit Procedure based on both deficit and debt on 21 June 2013. Malta was recommended to correct the excessive deficit by 2014. After the correction of the excessive deficit, Malta will be subject to the preventive arm of the Pact and should ensure sufficient progress towards its MTO. As the debt ratio in 2015 is projected at 66.8% of GDP, exceeding the 60% of GDP reference value, Malta will also be subject to the debt reduction benchmark.

This document complements the Country Report published on 26 February 2015 and updates it with the information included in the Stability programme. Section 2 presents the macroeconomic outlook underlying the Stability Programme and provides an assessment based on the Commission 2015 spring forecast. The following section presents the recent and planned budgetary developments, according to the Stability Programme. In particular, it includes an overview on the medium term budgetary plans, an assessment of the measures underpinning the Stability Programme and a risk analysis of the budgetary plans based on Commission forecast. Section 4 assesses compliance with the rules of the Stability and Growth Pact, including on the basis of the Commission forecast. Section 5 provides an overview on long term sustainability risks and Section 6 on recent developments and plans regarding the fiscal framework and the quality of public finances. Section 7 summarises the main conclusions.

## **2. MACROECONOMIC OUTLOOK**

The Stability Programme projects real GDP growth to decline gradually over the forecast horizon from the 3.5% peak reported in 2014 to 2.8% in 2018. Domestic demand is projected to be the main driver of growth in 2015-16, in particular underpinned by strong investment on the back of several large-scale projects. The boost to investment is forecast to fade out in the later years of the programme. The corresponding moderation in imports is projected to result in a stronger contribution of net exports to growth. The cyclical position of the economy is relatively strong and the output gap, as recalculated by the Commission based on the information in the programme, following the commonly agreed methodology, is positive in 2014-16.

The real GDP growth projections for 2015-16 are slightly lower than those in the Commission forecast, while for 2017-18 the programme's growth projections are in line with the potential growth of the Maltese economy, as estimated by the Commission. The programme discusses the sensitivity of the underlying macroeconomic scenario to a number of economic shocks, including exchange rate changes, developments in trading partners as well as in key economic sectors and policy developments. The programme concludes that risks are rather tilted to the upside in the short-term, but the balance swings to the downside in the medium term as uncertainty increases. The composition of GDP growth in the Stability Programme is more tax rich than the Commission forecast for 2015 on account of higher wage growth. The

Stability Programme's macroeconomic scenario does not include the macroeconomic impact of structural reforms, which is discussed and quantified in detail in the National Reform Programme. Overall, the macroeconomic scenario underpinning the Stability Programme is plausible.

**Table 1: Comparison of macroeconomic developments and forecasts**

	2014		2015		2016		2017	2018
	COM	SP	COM	SP	COM	SP	SP	SP
Real GDP (% change)	3.5	3.5	3.6	3.4	3.2	3.1	2.8	2.8
Private consumption (% change)	3.4	3.4	3.0	3.4	2.7	2.7	2.5	2.4
Gross fixed capital formation (% change)	14.0	14.0	19.9	23.6	5.5	13.1	-2.8	0.2
Exports of goods and services (% change)	-0.2	-0.2	4.6	2.8	3.0	2.4	1.0	1.9
Imports of goods and services (% change)	0.1	0.1	6.3	5.0	3.2	3.5	-0.3	1.0
<i>Contributions to real GDP growth:</i>								
- Final domestic demand	5.7	5.7	5.7	6.3	3.4	4.6	0.9	1.5
- Change in inventories	-1.7	-0.5	0.0	0.0	0.0	0.0	0.0	0.0
- Net exports	-0.5	-1.6	-2.1	-2.9	-0.3	-1.6	2.0	1.3
Output gap <sup>1</sup>	0.4	0.7	0.4	0.6	0.0	0.0	-0.3	-0.3
Employment (% change)	4.2	3.1	2.4	2.0	2.4	1.8	1.7	1.8
Unemployment rate (%)	5.9	5.9	5.9	5.8	5.9	5.7	5.8	5.8
Labour productivity (% change)	-0.6	-0.1	1.1	1.8	0.8	1.5	1.3	1.2
HICP inflation (%)	0.8	0.8	1.3	1.0	1.9	1.8	2.4	2.4
GDP deflator (% change)	1.5	1.7	1.4	1.3	1.8	2.1	2.4	2.6
Comp. of employees (per head, % change)	0.9	1.9	2.0	3.1	2.0	3.7	3.5	3.5
Net lending/borrowing vis-à-vis the rest of the world (% of GDP)	4.7	4.4	2.3	2.2	1.9	-0.7	0.7	2.4
<i>Note:</i>								
<sup>1</sup> In percent of potential GDP, with potential GDP growth recalculated by the Commission on the basis of the programme scenario, using the commonly agreed methodology.								
<i>Source:</i>								
Commission 2015 spring forecast (COM); Stability Programme (SP).								

### 3. RECENT AND PLANNED BUDGETARY DEVELOPMENTS

#### 3.1. Deficit developments in 2014

In 2014, the budget deficit decreased to 2.1% of GDP, from 2.6% in 2013. The outcome is in line with the targets set in both the previous Stability Programme and the 2015 Draft Budgetary Plan submitted in October 2014. The reduction in the headline deficit of 0.5% of GDP is explained by the improvement in current revenue, which increased by 1.5 percentage points of GDP thanks to both the favourable macroeconomic outlook (since the continuous recovery of domestic demand led to more tax-rich economic growth) and a higher yield from government measures. Current expenditure did not contribute to the consolidation since it increased by 7.3% year-on-year in nominal terms and by 0.8 percentage points as a share of GDP. The increase was driven by higher spending for public wages, intermediate

consumption and subsidies (including the ones to the public transport system). More in detail, the increase in public wages was due to both higher average wages and higher employment in both the health and education sector. The increase in intermediate consumption was linked to higher expenditure for medicines and for residential care for elderly people in private homes. As a result, current expenditure as a share to GDP has reached the second highest level since Malta has joined the EU.

Net capital expenditure increased by 0.2 percentage points of GDP driven by higher public investment linked to the acceleration in the absorption rate of EU funds of the programming period 2007-13 and to higher investments by the Central Government (namely the Extra Budgetary Units). In particular, public investment increased by more than 43% in nominal terms compared to 2013, while subsidies to Air Malta were lower than the ones given in 2013 (0.2% of GDP in 2014 vs 0.5% of GDP in 2013).

While overall the headline deficit in 2014 was in line with the targets set in both the previous programme and the Draft Budgetary Plan submitted in October 2014, in terms of composition there are differences. In particular, the previous programme targeted both lower current revenues and net capital expenditure as a share of GDP, while the reported current expenditure was in line with the target. Therefore, the higher outturn for net capital expenditure was offset by higher than targeted current revenue.

### **3.2. Target for 2015 and medium-term strategy**

#### **The target for 2015**

In 2015, the deficit is targeted to decline to 1.6% of GDP, in line with the previous 2014 Stability Programme and DBP for 2015 against the background of an upward revision in real GDP growth (from 2.1% in the previous programme to 3.4%) driven by domestic demand. The deficit target set in the Stability Programme incorporates the impact of the 2015 budget that was approved by Parliament in November 2014, which included the measures underpinning the revenue and expenditure targets for 2015.

The planned narrowing of the deficit in 2015 is mainly revenue-based, broadly in line with the consolidation effort laid down in the previous programme. The 2015 Stability Programme plans a lower reduction in current expenditure compared to the previous update while net capital expenditure is projected to be reduced. Similarly, the Draft Budgetary Plan set out a consolidation effort that was mainly revenue-based. However, it did not specify in detail the measures underpinning the revenue and expenditure targets for 2015.

In 2015, total current revenues in nominal terms are expected to increase slightly above nominal GDP, thus increasing only marginally (0.1 percentage points) as a share of GDP. The increase includes also the proceeds of the International Investor Programme (0.6% of GDP). Total current taxes are expected to increase by 4.3% in nominal terms compared to 2014, due to a very prudent estimate of the growth rate of current taxes related to very conservative elasticities for tax revenues and the incorporation of the gradual reduction of the overall income tax levels (that have been introduced with the budget for 2013). Current expenditure, in turn, is projected to decrease by around 0.2 percentage points of GDP, compared to an increase of 0.8 percentage points of GDP reported in 2014. In fact, the increase in intermediate consumption and subsidies is compensated by a reduction in compensation of employees, social transfers (reflecting the low Cost-of-living adjustment and the expected

savings from the Youth Guarantee and the tapering of social benefits) and interest expenditure (thanks also to the lower yields that have been registered since the beginning of the year). In particular, the high increase in public wages reported in 2014 (7.6%, explained by both high average wages and dynamic employment in the health and the education sector) is anticipated to decelerate markedly (2.9%) due to a lower/contained growth rate of employment in the public sector, including health and education. Net capital expenditure is set to increase marginally in terms of GDP since higher subsidies (due to a further capital injection into Air Malta of 0.5% of GDP) are compensated by a higher EU co-finance in investments for the programming period 2007-13 (that have to be spent by end-2015) and, to a minor extent, 2014-20.

The Commission 2015 spring forecast projects the 2015 deficit to be at 1.8% of GDP. The 0.2 pp of GDP gap with the authorities' target is explained by higher net investments (by 0.2 percentage points of GDP) due to a lower EU co-financing. Current expenditure in the Commission forecast is higher due to the more dynamic compensation of employees and subsidies, although partly compensated by higher current revenue, with the Commission projecting higher income taxes in line with a somewhat more dynamic labour market.

The programme plans an improvement in the (recalculated) structural balance<sup>1</sup> of 0.8 percentage points of GDP in 2015, slightly higher than the change in the structural balance based on programme data at face value (0.7 percentage points of GDP). Based on the Commission forecast, the deficit in structural terms is expected to register a lower improvement of ½ percentage points of GDP in 2015.

### **The medium-term strategy**

Malta plans to further reduce the deficit over the period covered by the Stability Programme, to 0.2% of GDP in 2018, with the smallest adjustment in 2018. This implies gradual progress towards the medium-term objective (MTO), which is defined as a balanced budgetary position in structural terms, to be achieved by 2019 (beyond the programme period). The medium-term objective is more stringent than what the Stability and Growth Pact requires. In addition, according to the Stability Programme, the path of the structural balance is consistent with the requirements of the national fiscal rules.

The programme plans to reduce the headline deficit by around 0.5% of GDP annually in 2016-2017, followed by a slightly lower pace of consolidation in 2018 (0.4% of GDP). The primary surplus is planned to improve from 1.1% of GDP in 2015 to 2.3% of GDP in 2018.

When looking at the entire programme period, the revenue and expenditure projections point to a consolidation effort that is primarily expenditure-based, in line the previous programme. Due to lower EU- financed investments, both the revenue and expenditure ratios are planned to drop significantly in 2016 while, in 2017-2018, net capital expenditure is set to stabilize. The bulk of the consolidation is due to a planned reduction of current expenditure which is set to decrease by 2.7 percentage points of GDP in the period 2015-2018, while current revenue are set to decrease by 1.7 percentage points of GDP over this same period as a result of a prudent elasticity assumption and of a slower growth in the tax base than nominal GDP in the later years of the programme.

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<sup>1</sup> Cyclically adjusted balance net of one-off and temporary measures, recalculated by the Commission on the basis of the information provided in the programme, using the commonly agreed methodology.

However, the planned consolidation effort is underpinned by measures only for 2015, while for the remaining years the programme provides details on the quantification of some specific items and confirms the continuation of the restrictive policy on recruitment in the public sector as well as of measures targeted at tapering social benefits. However, these specific measures are not sufficient to underpin the programme targets as of 2016.

In structural terms, the planned (recalculated) fiscal effort for 2016 is estimated at 0.9 percentage points. After 2016, the programme projects a (recalculated) structural adjustment effort of 0.6 and 0.4 percentage points respectively in 2017 and 2018. The path of the (recalculated) structural balance shows that Malta would be close to its medium-term objective of a balanced budget in structural terms already in 2018. Namely, in 2018 the (recalculated) structural balance is estimated at 0.1% of GDP, in the vicinity of the MTO by a margin of 0.25 percentage points.

The Commission 2015 spring forecast expects Malta's structural balance to improve by 0.6 percentage points of GDP in 2016 under a no-policy-change assumption. This is below the adjustment foreseen in the programme because of a higher headline deficit projected in the Commission forecast.

**Table 2: Composition of the budgetary adjustment**

(% of GDP)	2014	2015		2016		2017	2018	Change: 2014-2018
	COM	COM	SP	COM <sup>1</sup>	SP	SP	SP	SP
<b>Revenue</b>	<b>41.7</b>	<b>42.5</b>	<b>42.6</b>	<b>40.9</b>	<b>40.6</b>	<b>39.9</b>	<b>39.4</b>	<b>-2.3</b>
<i>of which:</i>								
- Taxes on production and imports	13.7	13.9	13.9	13.9	13.7	13.5	13.3	-0.4
- Current taxes on income, wealth, etc.	14.5	14.5	14.1	14.4	14.0	14.0	14.1	-0.4
- Social contributions	7.0	7.0	7.1	6.9	7.0	7.0	6.8	-0.2
- Other (residual)	6.5	7.1	7.5	5.7	6.0	5.5	5.2	-1.3
<b>Expenditure</b>	<b>43.8</b>	<b>44.3</b>	<b>44.2</b>	<b>42.4</b>	<b>41.7</b>	<b>40.5</b>	<b>39.6</b>	<b>-4.2</b>
<i>of which:</i>								
- Primary expenditure	40.9	41.6	41.5	39.7	39.1	38.0	37.2	-3.8
<i>of which:</i>								
Compensation of employees	13.2	13.1	13.0	13.0	12.8	12.6	12.3	-0.9
Intermediate consumption	6.6	6.8	6.8	6.9	6.5	6.3	5.9	-0.7
Social payments	12.7	12.5	12.5	12.4	12.1	11.9	11.7	-1.0
Subsidies	1.3	1.6	1.5	1.6	1.4	1.4	1.3	0.0
Gross fixed capital formation	3.8	3.8	4.1	2.7	3.2	3.1	3.0	-0.8
Other (residual)	3.4	3.7	3.7	3.2	3.1	2.8	3.1	-0.4
- Interest expenditure	2.9	2.7	2.7	2.6	2.6	2.5	2.5	-0.4
<b>General government balance (GGB)</b>	<b>-2.1</b>	<b>-1.8</b>	<b>-1.6</b>	<b>-1.5</b>	<b>-1.1</b>	<b>-0.6</b>	<b>-0.2</b>	<b>1.9</b>
<b>Primary balance</b>	<b>0.8</b>	<b>0.9</b>	<b>1.1</b>	<b>1.1</b>	<b>1.5</b>	<b>2.0</b>	<b>2.3</b>	<b>1.5</b>
One-off and other temporary	0.3	0.1	0.1	0.1	0.1	0.1	0.1	-0.3
<b>GGB excl. one-offs</b>	<b>-2.4</b>	<b>-2.0</b>	<b>-1.7</b>	<b>-1.6</b>	<b>-1.1</b>	<b>-0.6</b>	<b>-0.3</b>	<b>2.2</b>
Output gap <sup>1</sup>	0.4	0.4	0.6	0.0	0.0	-0.3	-0.3	-0.6
Cyclically-adjusted balance <sup>1</sup>	-2.3	-2.0	-1.9	-1.5	-1.1	-0.4	-0.1	2.2
<b>Structural balance (SB)<sup>2</sup></b>	<b>-2.6</b>	<b>-2.1</b>	<b>-2.0</b>	<b>-1.6</b>	<b>-1.1</b>	<b>-0.5</b>	<b>-0.1</b>	<b>2.5</b>
Structural primary balance <sup>2</sup>	0.3	0.6	0.7	1.0	1.4	2.0	2.3	2.0
<b>Notes:</b>								
<sup>1</sup> Output gap (in % of potential GDP) and cyclically-adjusted balance according to the programme as recalculated by the Commission on the basis of the programme scenario, using the commonly agreed methodology.								
<sup>2</sup> Structural (primary) balance = cyclically-adjusted (primary) balance excluding one-off and other temporary measures.								
<b>Source:</b>								
Stability Programme (SP); Commission 2015 spring forecasts (COM); Commission calculations.								

### **Measures underpinning the programme**

The 2015 budget was approved by Parliament in November 2014. The government's 2015 budget includes mostly revenue-increasing measures (0.5% of GDP), such as increases in indirect taxation, fees, a revision in the taxation on immovable property transfers and measures to fight tax evasion and avoidance. On the expenditure side, the budget envisages several (deficit-increasing) social measures among which, child and in-work benefits for low income households, a compensation for those who do not qualify for income tax cuts and a bonus for those who have retired from work and are not entitled to receive a pension but who have paid at least 5 years of contributions, and revisions of the maternity benefits. These



higher expenditures are only partly compensated by some restraint on public wages and on social benefits coming from measures such as the tapering of social benefits and the Youth Guarantee which aim to incentivise and reward work effort as well as discourage dependency on the social security system.

### Main budgetary measures

Revenue	Expenditure
<b>2015</b>	
<ul style="list-style-type: none"> <li>• Increase in several excise duty rates (0.3% of GDP)</li> <li>• Widening of tax base due to International Registration Scheme (0.1% of GDP)</li> <li>• Anti avoidance measures (0.2% of GDP)</li> </ul>	<ul style="list-style-type: none"> <li>• Conditional children's allowance (0.1% of GDP)</li> <li>• Social measures (0.2% of GDP)</li> <li>• Tapering of benefits and Youth Guarantee (-0.1% of GDP)</li> <li>• Restrictions on recruitment in the public sector (-0.1% of GDP)</li> </ul>
<b>2016</b>	
<ul style="list-style-type: none"> <li>• Other Revenue Measures to be specified (0.1% of GDP)</li> </ul>	<ul style="list-style-type: none"> <li>• Tapering of benefits and Youth Guarantee (-0.1% of GDP)</li> </ul>
<b>2017</b>	
<ul style="list-style-type: none"> <li>• Other Revenue Measures to be specified (0.2% of GDP)</li> </ul>	<ul style="list-style-type: none"> <li>• Tapering of benefits and Youth Guarantee (-0.1% of GDP)</li> </ul>
<b>2018</b>	
<ul style="list-style-type: none"> <li>• Other Revenue Measures to be specified (0.2% of GDP)</li> </ul>	<ul style="list-style-type: none"> <li>• Tapering of benefits and Youth Guarantee (-0.1% of GDP)</li> </ul>
<p><u>Note:</u> The budgetary impact in the table is the impact reported in the programme, i.e. by the national authorities. A positive sign implies that revenue / expenditure increases as a consequence of this measure.</p>	

### 3.3. Debt developments

The general government debt-to-GDP ratio increased to 69.2% of GDP in 2013, also on account of a debt-increasing stock-flow adjustment related to tax arrears from Enemalta (the public energy utility corporation). Following the repayment of these tax arrears, the debt decreased to 68.0% of GDP in 2014.

In the Stability Programme, the general government gross debt ratio is expected to decrease by 1.2 percentage points of GDP in 2015, reaching 66.8% of GDP. In particular, the projected primary surplus and the positive impact of nominal growth are sufficient to offset the stock-flow adjustment (0.5 percentage points) due to a high cash buffer.

The debt-to-GDP ratio is projected to decrease further over the programme period, reaching 61.2% in 2018. The stock-flow adjustment is projected to be sizeable, especially in 2016-2017, due to the contribution to the Malta Government Stock sinking fund. Despite this, the projected increasing primary surplus, the acceleration of inflation and the positive (even if moderating) impact of real growth as well as the planned decrease in interest expenditure are sufficient to keep the debt ratio on a declining path. Finally, a sizeable reduction in the debt ratio is planned in 2018, explained also by a lower (but still debt-increasing) stock-flow adjustment.

Compared to the Draft Budgetary Plan, the debt-to-GDP ratio for 2014 was revised downwards by 2.1 percentage points to 68.0 per cent of GDP. In addition, the Draft Budgetary Plan projected a slightly more gradual pace of debt reduction in 2015. While a precise comparison among figures for the debt-to-GDP ratio in different programmes is not possible due to the recent switch to ESA 2010, it is worth noting that in the previous programmes the debt was expected to reach the same level in 2017 but with a different pace of reduction and despite a significantly higher debt ratio in 2014<sup>2</sup> and a less buoyant macroeconomic environment.

According to the Commission forecast, the debt ratio is projected to decrease further and reach 65.4% of GDP in 2016. The difference compared to the Stability Programme targets is due to the lower expected primary surplus (on a no-policy-change basis), which more than compensate for a lower projection for the stock-flow adjustment, while nominal GDP growth projections are broadly similar.

Overall, both in the Stability Programme and in the Commission forecast, the debt rule is projected to be respected as of 2015 (in its forward-looking configuration).

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<sup>2</sup> Compared to the previous update, for 2014, the debt-to-GDP ratio was revised downwards by 1.4 percentage points. to 68.0% of GDP.

**Table 3: Debt developments**

(% of GDP)	Average 2009-2013	2014	2015		2016		2017	2018
			COM	SP	COM	SP	SP	SP
<b>Gross debt ratio<sup>1</sup></b>	<b>68.3</b>	<b>68.0</b>	<b>67.2</b>	<b>66.8</b>	<b>65.4</b>	<b>65.6</b>	<b>63.8</b>	<b>61.2</b>
Change in the ratio	1.3	-1.2	-0.9	-1.2	-1.7	-1.2	-1.8	-2.6
<i>Contributions<sup>2</sup>:</i>								
<b>1. Primary balance</b>	<b>0.0</b>	<b>-0.8</b>	<b>-0.9</b>	<b>-1.1</b>	<b>-1.1</b>	<b>-1.5</b>	<b>-2.0</b>	<b>-2.3</b>
<b>2. “Snow-ball” effect</b>	<b>0.3</b>	<b>-0.5</b>	<b>-0.5</b>	<b>-0.3</b>	<b>-0.6</b>	<b>-0.7</b>	<b>-0.7</b>	<b>-0.8</b>
<i>Of which:</i>								
Interest expenditure	3.1	2.9	2.7	2.7	2.6	2.6	2.5	2.5
Growth effect	-1.1	-2.3	-2.3	-2.2	-2.0	-2.0	-1.7	-1.7
Inflation effect	-1.7	-1.0	-0.9	-0.8	-1.2	-1.3	-1.5	-1.5
<b>3. Stock-flow adjustment</b>	<b>1.0</b>	<b>0.1</b>	<b>0.5</b>	<b>0.2</b>	<b>0.0</b>	<b>1.1</b>	<b>0.9</b>	<b>0.5</b>
<i>Of which:</i>								
Cash/accruals diff.								
Acc. financial assets								
<i>Privatisation</i>								
Val. effect & residual								

Notes:

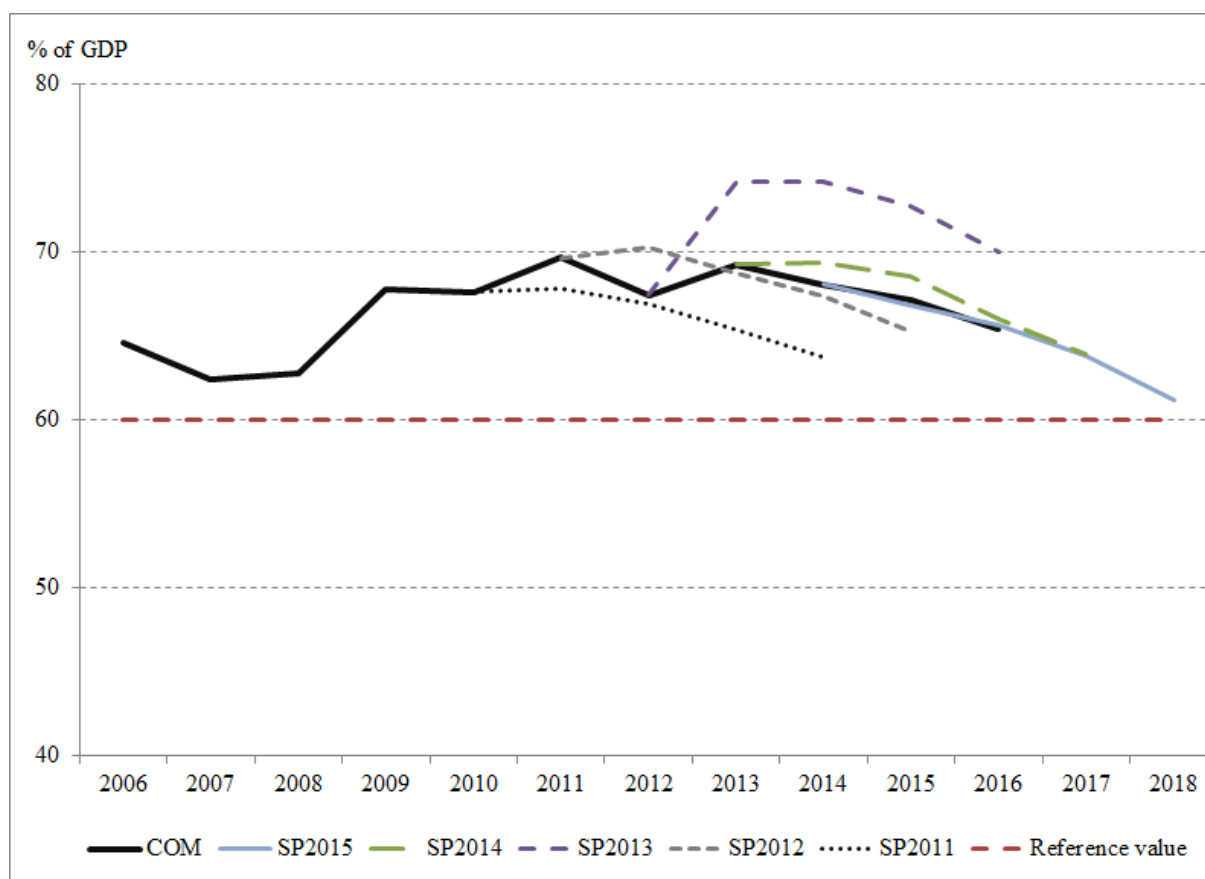
<sup>1</sup> End of period.

<sup>2</sup> The snow-ball effect captures the impact of interest expenditure on accumulated debt, as well as the impact of real GDP growth and inflation on the debt ratio (through the denominator). The stock-flow adjustment includes differences in cash and accrual accounting, accumulation of financial assets and valuation and other residual effects.

Source:

*Commission 2015 spring forecast (COM); Stability Programme (SP); Commission calculations.*

**Figure 1: Government debt projections in successive programmes (% of GDP)**



Source: Commission 2015 spring forecast; Stability Programmes.

### 3.4. Risk assessment

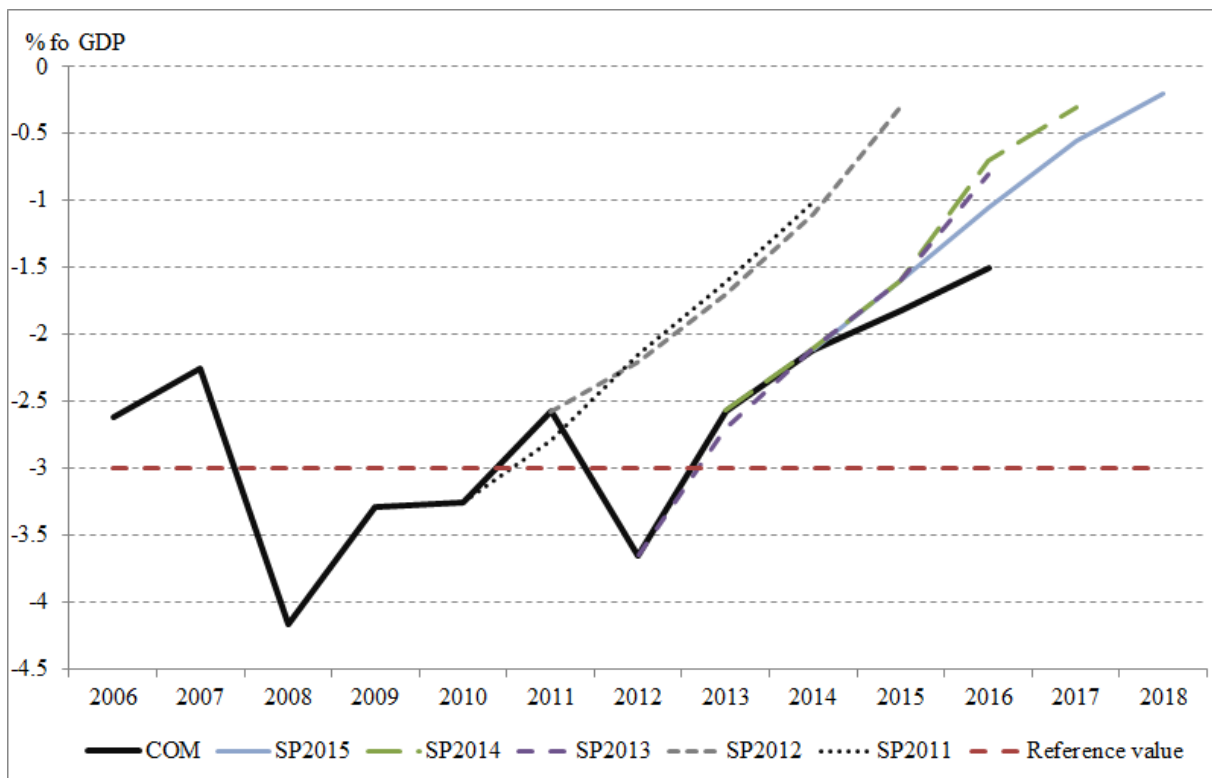
#### Deficit developments

There are risks related to the deficit targets in the Stability Programme. In particular, there are risks related to slippages in current expenditure, especially in the public sector wage bill, intermediate consumption and subsidies, given past experience. In addition, the public transport service could require additional subsidies on top of what is already budgeted. Finally, net capital expenditure could also be higher than planned since 2015 is the final year in which the EU funds from the programming period 2007-2013 can be spent, thus putting pressure on public investments coming also from projects financed from national sources. Furthermore, the revenue targets for 2016-2018 are not underpinned by measures.

On the other hand, revenue projections in the Stability programme seem cautious, relying on very conservative elasticities, thus pointing to an upside risk to the revenue projections. Moreover, the revenue targets include also the impact of a revenue measure introduced with the 2014 Budget, namely the Individual Investor Programme, that could bring in higher than expected revenue.

Overall, while risks related to the deficit targets seem balanced, there could be differences in the composition of the adjustment.

**Figure 2: Government balance projections in successive programmes (% of GDP)**



Source: Commission 2015 spring forecast, Stability Programmes

### **Debt developments**

The same risks highlighted for the deficit targets apply to the debt projections of the Stability programme. Moreover, despite a decrease in 2013 (to 15.8% of GDP from 16.4% of GDP in 2012), the government-guaranteed debt in Malta have increased again in 2014 to 16.4% of GDP and remains high compared to other Member States.

#### 4. COMPLIANCE WITH THE PROVISIONS OF THE STABILITY AND GROWTH PACT

##### **Box 1. Council recommendations addressed to Malta**

On 21 June 2013, the Council recommended Malta under Art. 126(7) of the Treaty to correct its excessive deficit by 2014. To this end, Malta should:

(a) reach a headline general government target of 3.4% of GDP for 2013 and 2.7% of GDP in 2014, which is consistent with an annual improvement of the structural balance of 0.7% of GDP in 2013, and 0.7% of GDP in 2014. This adjustment path would allow bringing the headline government deficit below the 3% of GDP reference value by 2014 while at the same time ensuring that the government gross debt ratio will approach the 60%-of-GDP reference value at a satisfactory pace;

(b) specify and rigorously implement the measures that are necessary to achieve the correction of the excessive deficit by 2014, and use all windfall gains for deficit reduction.

On 8 July 2014, the Council also addressed recommendations to Malta in the context of the European Semester. In particular, in the area of public finances, the Council recommended to Malta to correct the excessive deficit in a sustainable manner by 2014. In 2015, significantly strengthen the budgetary strategy to ensure the required structural adjustment of 0.6% of GDP towards the medium-term objective and, thereafter, pursue a structural adjustment of at least 0.5% of GDP each year, and more in good economic conditions or if needed to ensure that the debt rule is met in order to keep the general government debt ratio on a sustained downward path. In addition, the Council recommended to finalise the adoption of the Fiscal Responsibility Act with a view to putting in place a binding, rule-based multiannual fiscal framework and establishing an independent institution charged with monitoring of fiscal rules and endorsing macroeconomic forecasts underpinning fiscal planning. Finally, to continue improving tax compliance and fighting tax evasion by ensuring the continued roll-out and evaluation of measures taken so far, while taking additional action, notably by promoting the use of electronic means of payment.

##### **4.1. Compliance with EDP recommendations in 2014**

The headline deficit decreased to 2.1% of GDP in 2014, from 2.6% of GDP in 2013, well below the EDP target (2.7% of GDP). Moreover, given that the debt-to-GDP ratio was above the 60% reference value of the Treaty, compliance with the forward-looking debt rule is a necessary condition for the abrogation of an EDP. In 2014, the forward-looking debt rule is met with a margin of 1.9% of GDP. On this basis, it appears that Malta has durably corrected its excessive deficit by the recommended deadline. On this basis, on 13 May 2015, the Commission has issued a Recommendation for a Council Decision abrogating the Decision of 21 June 2013 on the existence of an excessive deficit in Malta.<sup>3</sup>

<sup>3</sup> See [http://ec.europa.eu/economy\\_finance/economic\\_governance/sgp/pdf/30\\_edps/126-12\\_commission/2015-05-13\\_mt\\_126-12\\_commission\\_en.pdf](http://ec.europa.eu/economy_finance/economic_governance/sgp/pdf/30_edps/126-12_commission/2015-05-13_mt_126-12_commission_en.pdf).

## 4.2. Compliance with the debt criterion

Following the abrogation of the EDP, as of 2015 Malta would be subject to the preventive arm of the Pact and, as the debt ratio exceeds 60% of GDP, will need to respect the debt rule (debt reduction benchmark). Namely, Malta has to ensure that the debt ratio is sufficiently diminishing and approaching 60% at a satisfactory pace.

According to the Commission 2015 spring forecast, the debt reduction benchmark is expected to be met in the period 2015-2016, with a margin above 2 percentage points. In addition, according to national plans, the debt benchmark is expected to be met in the period 2015-2016 in three configurations (the backward looking version, the forward-looking one and by taking into account the impact of the cycle), with an increasing margin over the period.

**Table 4: Compliance with the debt criterion**

	2015		2016	
	SP	COM	SP	COM
Gap to the debt benchmark <sup>1,2</sup>	-2.3	-2.3	-3.9	-2.2
<b>Notes:</b>				
<sup>1</sup> Not relevant for Member States that were subject to an EDP procedure in November 2011 and for a period of three years following the correction of the excessive deficit.				
<sup>2</sup> Shows the difference between the debt-to-GDP ratio and the debt benchmark. If positive, projected gross debt-to-GDP ratio does not comply with the debt reduction benchmark.				
<sup>3</sup> Applicable only during the transition period of three years from the correction of the excessive deficit for EDP that were ongoing in November 2011.				
<sup>4</sup> Defines the remaining annual structural adjustment over the transition period which ensures that - if followed - Member State will comply with the debt reduction benchmark at the end of the transition period, assuming				
<i>Source:</i>				
<i>Commission 2015 spring forecast (COM); Stability Programme (SP); Commission calculations.</i>				

## 4.3. Compliance with the MTO or the required adjustment path towards the MTO as of 2015

Following the abrogation of the EDP, Malta will have to comply with the requirements under the preventive arm. The requirement for Malta, that is not yet at its MTO, neither in good nor in bad times and with a general government debt ratio above 60% of GDP, is to deliver a structural adjustment of at least 0.6 percentage points of GDP per year so as to make sufficient progress towards the MTO.

According to the Stability Programme, in 2015, the annual change in the (recalculated) structural balance of 0.8% of GDP is above the required adjustment and the growth rate of government expenditure, net of discretionary revenue measures is in line with the applicable expenditure benchmark rate. Therefore the planned adjustment is in line with the requirements. Based on the Commission 2015 spring forecast, in 2015 the projected 0.5% of GDP improvement in the structural balance would lead to some deviation from the required 0.6% of GDP adjustment towards the MTO. In addition, the growth rate of government expenditure net of discretionary revenue measures is expected to exceed the benchmark by

1.5% of GDP in 2015, thereby breaching the threshold for significance. Therefore, an overall assessment needs to be carried out. Namely, the difference between the structural balance and the expenditure benchmark is explained by several factors. The annual potential GDP growth rate used in the computation of the structural balance is significantly higher than the medium term rate (1.8%) used in the calculation of the expenditure benchmark (frozen based on Commission 2013 winter forecast). Given that the macroeconomic outlook in Malta turned out much better than expected in 2013, the structural balance pillar is found to be based on a more accurate estimate of potential growth. In addition, one-off transactions have had a negative impact on the expenditure benchmark (partly due to the higher-than-expected revenues in 2014 coming from the Investment Registration Scheme). On the other hand, the estimated structural effort is inflated by sizable windfall revenues, but part of the revenue windfalls could possibly point to permanent increase in tax revenues, being a result of efforts to increase efficiency in revenue collection. This possible permanent increase in revenues is not reflected in the assessment based on the expenditure pillar, leading to an underestimation of the fiscal effort under the expenditure benchmark. Therefore, following an overall assessment, Malta is expected to be at risk of some deviation from the adjustment path towards the MTO in 2015.

In 2016 based on the Stability Programme, the annual change in the (recalculated) structural balance of 0.9% of GDP is well above the required adjustment, but the growth rate of expenditure would slightly exceed the benchmark pointing to some deviation (gap of 0.1% of GDP). Over two years (2015-2016), the analysis points to the same conclusion, since the structural balance pillar points to compliance while the expenditure benchmark is expected to deviate somewhat from required adjustment. This calls for an overall assessment. The deviation from the expenditure benchmark (both in 2016 and over two years) is mainly explained by two elements. The annual potential GDP growth rate (3.7%) used in the computation of the structural balance in 2016 is significantly higher than the medium term rate (2.7%) used in the calculation of the expenditure benchmark (based on the 10-years average). In addition, the increase in the adjusted expenditure in 2016 is not matched by discretionary revenue measures since the measures to support the planned deficit targets from 2016 onwards are not yet specified. Therefore, the overall assessment points to compliance based on the government plans in 2016.

In 2016, according to the Commission forecast prepared on a no-policy-change basis, while the improvement in the structural balance is in line with the required 0.6% of GDP adjustment towards the MTO, the growth rate of government expenditure net of discretionary revenue measures is expected to exceed the expenditure benchmark by 0.1% of GDP. However, over the years of 2015 and 2016 taken together, the structural balance pillar points to some deviation (average gap of 0.1% of GDP) and the expenditure benchmark suggests a significant deviation (average gap of 0.8% of GDP). The difference of the two indicators originated from the deviations forecast for 2015. In addition, in 2016, besides the different potential GDP growth rate used as a benchmark in the computation of the two indicators, the lack of discretionary revenue measures (since they have not been specified yet) to match the increase in the adjusted expenditure explains part of the difference between the two indicators. Therefore, according to the Commission forecast, the overall assessment points to a risk of some deviation from the adjustment path towards the MTO in 2016.

Following an overall assessment, based on the Stability Programme, the adjustment path towards the MTO seems to be appropriate and compliant with the requirement of the preventive arm of the Pact in both 2015 and 2016. However, based on the Commission 2015



spring forecast, there is a risk of some deviation from the adjustment path towards the MTO both in 2015 and over 2015-2016 taken together.

**Table 5: Compliance with the requirements under the preventive arm**

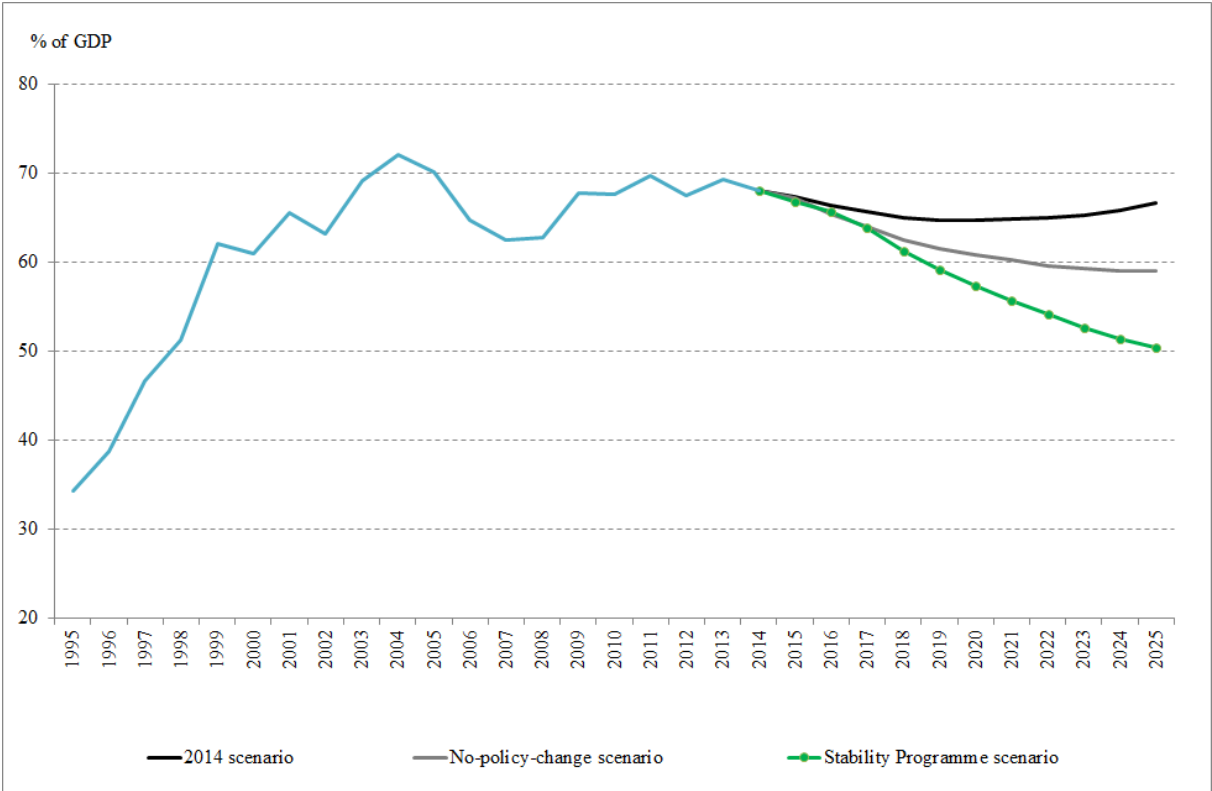
(% of GDP)	2015		2016	
<b>Initial position<sup>1</sup></b>				
Medium-term objective (MTO)	0.0		0.0	
Structural balance <sup>2</sup> (COM)	-2.1		-1.6	
Structural balance based on freezing (COM)	-2.1		-	
<b>Position vis-a-vis the MTO<sup>3</sup></b>	Not at MTO		Not at MTO	
(% of GDP)	2015		2016	
	SP	COM	SP	COM
<b>Structural balance pillar</b>				
Required adjustment <sup>4</sup>	0.6		0.6	
Required adjustment corrected <sup>5</sup>	0.6		0.6	
Change in structural balance <sup>6</sup>	0.8	0.5	0.9	0.6
<i>One-year deviation from the required adjustment<sup>7</sup></i>	0.2	-0.1	0.3	0.0
<i>Two-year average deviation from the required adjustment<sup>7</sup></i>	In EDP	In EDP	0.2	-0.1
<b>Expenditure benchmark pillar</b>				
Applicable reference rate <sup>8</sup>	0.3		1.3	
<i>One-year deviation<sup>9</sup></i>	0.0	-1.5	-0.2	-0.1
<i>Two-year average deviation<sup>9</sup></i>	In EDP	In EDP	-0.1	-0.8
<b>Conclusion</b>				
Conclusion over one year	Compliance	Overall assessment	Overall assessment	Overall assessment
Conclusion over two years	In EDP	In EDP	Overall assessment	Overall assessment
Notes				
<sup>1</sup> The most favourable level of the structural balance, measured as a percentage of GDP reached at the end of year t-1, between spring forecast (t-1) and the latest forecast, determines whether there is a need to adjust towards the MTO or not in year t. A margin of 0.25 percentage points is allowed in order to be evaluated as having reached the MTO.				
<sup>2</sup> Structural balance = cyclically-adjusted government balance excluding one-off measures.				
<sup>3</sup> Based on the relevant structural balance at year t-1.				
<sup>4</sup> Based on the position vis-à-vis the MTO, the cyclical position and the debt level (See European Commission: Vade mecum on the Stability and Growth Pact, page 28.).				
<sup>5</sup> Required adjustment corrected for the clauses, the possible margin to the MTO and the allowed deviation in case of overachievers.				
<sup>6</sup> Change in the structural balance compared to year t-1.				
<sup>7</sup> The difference of the change in the structural balance and the required adjustment corrected.				
<sup>8</sup> Reference medium-term rate of potential GDP growth. The (standard) reference rate applies from year t+1, if the country has reached its MTO in year t. A corrected rate applies as long as the country is not at its MTO.				
<sup>9</sup> Deviation of the growth rate of public expenditure net of discretionary revenue measures and revenue increases mandated by law from the applicable reference rate in terms of the effect on the structural balance. The expenditure aggregate used for the expenditure benchmark is obtained following the commonly agreed methodology. A negative sign implies that expenditure growth exceeds the applicable reference rate.				
<i>Source:</i> Stability Programme (SP); Commission 2015 spring forecasts (COM); Commission calculations.				

**5. LONG-TERM SUSTAINABILITY**

The analysis in this section includes the new long-term budgetary projections of age-related expenditure (pension, health care, long-term care, education and unemployment benefits) from the 2015 Ageing Report<sup>4</sup> published on 12 May. It therefore updates the assessment made in the Country Reports<sup>5</sup> published on 26 February.

Malta’s general government debt stood at 69% of GDP in 2014. Under a no-policy-change assumption (based on the Commission Spring 2015 forecast), it is expected to gradually decline to 59% in 2025, below the 60% of GDP Treaty threshold. The full implementation of the programme would put the general government debt on a clearly decreasing path, reaching 50.4% of GDP in 2025, well below the 60 % of GDP reference value.

**Figure 3: Gross debt projections (% of GDP)**



Source: Commission 2015 spring forecast, Stability Programme, Commission calculations.

While Malta does not appear to face sustainability risks in the short term, these risks increase in the medium and long term.

The medium-term sustainability gap is at 0.1 % of GDP based on the Commission 2015 spring forecast, which indicates a medium risk. This is primarily related to the negative contributions given by the 2015 structural primary balance despite the projected ageing costs until 2030. Based on the (recalculated) government plans enshrined in the Stability Programme, the medium-term sustainability gap becomes negative, at -1.3 %, indicating no

<sup>4</sup> See [http://ec.europa.eu/economy\\_finance/publications/european\\_economy/2015/ee3\\_en.htm](http://ec.europa.eu/economy_finance/publications/european_economy/2015/ee3_en.htm)

<sup>5</sup> See [http://ec.europa.eu/europe2020/making-it-happen/country-specific-recommendations/index\\_en.htm](http://ec.europa.eu/europe2020/making-it-happen/country-specific-recommendations/index_en.htm)

risk, since the positive contribution from projected ageing costs until 2030 is compensated by a lower initial budgetary position.

In the long-term, the sustainability gap increased to 4.6 % of GDP based on the Commission 2015 spring forecast, which indicates a medium risk. This is primarily related to the costs arising from population ageing (the projected ageing costs), in particular for pensions and health care, despite the negative contribution given by the 2015 structural primary balance. Based on the (recalculated) government plans included in the Stability Programme, the long-term sustainability gap is slightly lower, at 3.5 % of GDP, still characterised by a negative contribution from projected ageing costs. Overall, achieving a debt ratio of 60 % of GDP by 2030 would require further fiscal adjustment over 2017-2020 according to both the government plans and the Commission forecast (in the order of 3.5 and 4.6 percentage points of GDP, respectively). Risks would increase in the event of the structural primary balance reverting to lower values observed in the past, such as the average for the period 2004-2013.

It is therefore appropriate for Malta to continue to implement measures that reduce risks to fiscal sustainability in the long term and to reduce government debt. The projected ageing costs pose a challenge for Malta. In particular, pension and health care expenditure are projected to increase faster than the average for the EU. The focus should therefore be on containing the growth in age-related expenditures in these two sectors in order to ensure the sustainability of public finances in the long term.

**Table 6: Sustainability indicators**

	Malta			European Union		
	2014 scenario	No-policy-change scenario	Stability Programme scenario	2014 scenario	No-policy-change scenario	Stability/Convergence Programme scenario
S2*	5.3	4.6	3.5	1.4	1.7	0.4
<i>of which:</i>						
Initial budgetary position (IBP)	0.6	-0.2	-1.4	0.4	0.5	-0.7
Long-term cost of ageing (CoA)	4.7	4.8	4.8	1.0	1.1	1.1
<i>of which:</i>						
pensions	2.0	2.0	2.1	0.0	0.1	0.1
healthcare	1.7	1.6	1.5	0.8	0.7	0.6
long-term care	0.9	0.9	0.9	0.7	0.7	0.6
others	0.1	0.3	0.4	-0.4	-0.3	-0.2
S1**	1.1	0.1	-1.3	1.4	1.8	0.5
<i>of which:</i>						
Initial budgetary position (IBP)	-0.2	-1.1	-2.3	-0.4	-0.3	-1.6
Debt requirement (DR)	0.5	0.4	0.1	1.7	1.9	1.8
Long-term cost of ageing (CoA)	0.7	0.9	0.9	0.1	0.3	0.4
S0 (risk for fiscal stress)***	0.16	:	:	:	:	:
Fiscal subindex	0.00	:	:	:	:	:
Financial-competitiveness subindex	0.23	:	:	:	:	:
Debt as % of GDP (2014)	68.0			88.6		
Age-related expenditure as % of GDP (2014)	22.6			25.6		
Source: Commission, 2015 Stability Programme						
Note: the '2014' scenario depicts the sustainability gap under the assumption that the structural primary balance position remains at the 2014 position according to the Commission 2015 spring forecast; the 'no-policy-change' scenario depicts the sustainability gap under the assumption that the structural primary balance position evolves according to the Commission 2015 spring forecast until 2016. The 'stability programme' scenario depicts the sustainability gap under the assumption that the budgetary plans in the programme are fully implemented over the period covered by the programme. Age-related expenditure as given in the 2015 Ageing Report.						
* The long-term sustainability gap (S2) indicator shows the immediate and permanent adjustment required to satisfy an inter-temporal budgetary constraint, including the costs of ageing. The S2 indicator has two components: i) the initial budgetary position (IBP) which gives the gap to the debt stabilising primary balance; and ii) the additional adjustment required due to the costs of ageing. The main assumption used in the derivation of S2 is that in an infinite horizon, the growth in the debt ratio is bounded by the interest rate differential (i.e. the difference between the nominal interest and the real growth rates); thereby not necessarily implying that the debt ratio will fall below the EU Treaty 60% debt threshold. The following thresholds for the S2 indicator were used: (i) if the value of S2 is lower than 2, the country is assigned low risk; (ii) if it is between 2 and 6, it is assigned medium risk; and, (iii) if it is greater than 6, it is assigned high risk.						
** The medium-term sustainability gap (S1) indicator shows the upfront adjustment effort required, in terms of a steady adjustment in the structural primary balance to be introduced over the five years after the forecast horizon, and then sustained, to bring debt ratios to 60% of GDP in 2030, including financing for any additional expenditure until the target date, arising from an ageing population. The following thresholds were used to assess the scale of the sustainability challenge: (i) if the S1 value is less than zero, the country is assigned low risk; (ii) if a structural adjustment in the primary balance of up to 0.5 p.p. of GDP per year for five years after the last year covered by the spring 2015 forecast (year 2016) is required (indicating a cumulated adjustment of 2.5 pp.), it is assigned medium risk; and, (iii) if it is greater than 2.5 (meaning a structural adjustment of more than 0.5 p.p. of GDP per year is necessary), it is assigned high risk.						
*** The S0 indicator reflects up to date evidence on the role played by fiscal and financial-competitiveness variables in creating potential fiscal risks. It should be stressed that the methodology for the S0 indicator is fundamentally different from the S1 and S2 indicators. S0 is not a quantification of the required fiscal adjustment effort like the S1 and S2 indicators, but a composite indicator which estimates the extent to which there might be a risk for fiscal stress in the short-term. The critical threshold for the overall S0 indicator is 0.43. For the fiscal and the financial-competitiveness sub-indices, thresholds are respectively at 0.35 and 0.45.						

## **6. FISCAL FRAMEWORK AND QUALITY OF PUBLIC FINANCES**

### **6.1. Fiscal framework**

In line with the 2014 country-specific recommendation to “finalise the adoption of the Fiscal Responsibility Act with a view to putting in place a binding, rule-based multiannual fiscal framework and establishing an independent institution charged with the monitoring of fiscal rules and endorsing macroeconomic forecasts underpinning fiscal planning”, in August 2014, the Maltese Parliament enacted the Fiscal Responsibility Act, which transposed the bulk of the requirements of the Directive 85/2011/EU on budgetary frameworks and the Fiscal Compact.<sup>6</sup>

Besides the introduction of fiscal rules and of a three-year rolling budgetary framework, the Fiscal Responsibility Act provided for the establishment of a Fiscal Council charged among others with endorsing the government’s official macroeconomic and fiscal forecasts as well as ex-ante and ex-post monitoring of the respect of fiscal rules.

Until January 2015, the National Audit Office (NAO) and the Auditor General performed the duties of the Fiscal Council. In January 2015 the Chairperson and two members of the Malta Fiscal Advisory Council (MFAC) were appointed by the Minister of Finance. After that, the Malta Fiscal Advisory Council started to be operational as the newly-established national fiscal monitoring institution and is in the process of hiring additional staff.

The economic growth projections underpinning the Stability Programme were endorsed by the MFAC. The MFAC concluded that the projections may be achievable, albeit dependent upon the investment and private consumption dynamics. The forecasting process was deemed sound and well-documented, but the input received from different government and non-government entities would benefit from more streamlining. The endorsement is available on the website of the Ministry of Finance. At the time the Stability Programme was submitted, the MFAC was still in the process of evaluating the fiscal plans included in the programme.

The budgetary process in Malta is not yet aligned with the European calendar. In particular, Malta has not complied with the information requirements specified in the Regulation (EU) No 473/2013, since, in the last two years, the Draft Budgetary Plan presented on 15 October did not provide sufficient details on the discretionary measures underpinning the budgetary targets. Malta is also in breach of the requirement of the Regulation obliging the euro area Member States to make public their draft annual budgets by 15 October every year. According to the Stability Programme, the Government has announced that it will be adjusting the timing and publication of the forthcoming budget in order to fit the requirements of the common budgetary timeline, which is welcome.

The Stability Programme indicates that it constitutes the national medium-term fiscal plans, as required by Art. 4.1 of Regulation No 473/2013. However, there are no explicit indications on the expected economic returns on non-defence public investment projects that have a significant budgetary impact neither in the Stability Programme nor in the National Reform Programme.

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<sup>6</sup> This section complements the Country Report published on 26 February 2015 and updates it with the information included in the Stability Programme.

## **6.2. Quality of public finances**

The Stability Programme stresses the government's commitment to continue improving the quality of public finances by ensuring a more efficient use of public funds by two channels: reviewing the public expenditure in order to focus on productive spending and continuing to improve the efficiency of the taxation system.

A number of initiatives were launched to improve the efficiency of public spending in Malta. After the first Comprehensive Spending Review completed in 2014, which included all Ministries with the aim of starting to link outputs to expenditure for all line items, another Comprehensive Spending Review is ongoing. As a result of the in depth Comprehensive Review of Social Security expenditure started in February 2014, the 2015 Budget introduced several initiatives, based on the strategy of making work pay, like the Youth Guarantee Programme and the tapering of social benefits. These measures aim at ensuring that the social security system positively incentivises work effort and discourages dependency. In the health sector, several initiatives aimed at improving governance were introduced, namely various internal control mechanisms and monitoring of operational costs, improved financial controls and the centralization of procurement services. On top of these initiatives, a comprehensive spending review, similar to the one undertaken in the social security area is under way within the Ministry for Health with the aim of providing results to be included in the budget of October 2016. Building on these spending reviews, the government aims at limiting the growth in expenditure below the rate of economic growth while shifting expenditure to more productive functions. The areas that the spending reviews target are appropriate. The efficiency of the measures will be judged against their effectiveness in limiting expenditure overruns that have occurred in the past.

In order to improve the efficiency of the taxation system, the Government has embarked on several projects aimed at gradually changing the structure of the tax system, while increasing tax efficiency. More in detail, the shift in the tax burden away from labour has been already introduced in 2013 with a reduction in income tax rate, which has been further strengthened in the 2015 Budget, and the increase of several fees. In order to widen the tax base, several initiatives were introduced aimed at encouraging labour market participation, regularise undeclared work and minimise precarious employment. With the aim of further simplifying taxation and improving tax efficiency, the Government is continuing with the merging of the different revenue departments started in the past, improved the online filing of tax returns by extending the e-filing also to individuals (in addition to companies) and replaced the capital gain tax (35%) with a final withholding tax (ranging from 5% to 10%). Measures to help in fighting tax evasion and avoidance, building on initiatives introduced in previous years, include the obligation for any person carrying out a commercial activity to register with the VAT department irrespective of the turnover and the set up a National Strategy for Electronic Payments Steering Committee to draw up a national strategy for electronic payments in order to increase its use.

## **7. CONCLUSIONS**

In 2014, Malta achieved a headline deficit of 2.1% of GDP, well below the target under the EDP (2.7% of GDP). Also compliance with the forward-looking component of the debt rule was ensured in 2014. On this basis, Malta has timely and durably corrected its excessive deficit.

Malta plans to reduce the headline deficit gradually over the period covered by the Stability Programme, to 1.6% of GDP in 2015 and further to 0.2% of GDP in 2018. The planned progress towards the MTO appears appropriate since the improvement of the (recalculated) structural balance is above the 0.6% of GDP required by the SGP in both 2015 and 2016. Moreover, the structural balance path outlined in the programme, when taken at face value, shows that Malta would be in the vicinity of a balanced budget already in 2018.

However, based on the Commission 2015 spring forecast, there is a risk of some deviation from the adjustment path towards the MTO in 2015, as well as over 2015-2016 taken together.

Finally, according to both the national plans and the Commission forecast, Malta will comply with the debt reduction benchmark in both 2015 and 2016.

## ANNEX

Table I. Macroeconomic indicators

	1997-2001	2002-2006	2007-2011	2012	2013	2014	2015	2016
<b>Core indicators</b>								
GDP growth rate	3.9	2.3	2.1	2.5	2.7	3.5	3.6	3.2
Output gap <sup>1</sup>	0.2	0.3	0.1	-0.2	-0.1	0.4	0.4	0.0
HICP (annual % change)	3.1	2.5	2.4	3.2	1.0	0.8	1.3	1.9
Domestic demand (annual % change) <sup>2</sup>	1.9	3.2	1.2	-0.6	2.8	4.3	6.1	3.6
Unemployment rate (% of labour force) <sup>3</sup>	6.7	7.2	6.5	6.3	6.4	5.9	5.9	5.9
Gross fixed capital formation (% of GDP)	22.4	20.4	19.8	17.4	17.4	18.8	21.9	22.2
Gross national saving (% of GDP)	16.5	14.6	16.3	21.1	21.9	21.5	22.2	22.3
<b>General Government (% of GDP)</b>								
<b>Net lending (+) or net borrowing (-)</b>	<b>-6.9</b>	<b>-4.8</b>	<b>-3.1</b>	<b>-3.6</b>	<b>-2.6</b>	<b>-2.1</b>	<b>-1.8</b>	<b>-1.5</b>
<b>Gross debt</b>	<b>57.2</b>	<b>67.8</b>	<b>66.0</b>	<b>67.4</b>	<b>69.2</b>	<b>68.0</b>	<b>67.2</b>	<b>65.4</b>
<b>Net financial assets</b>	<b>n.a</b>	<b>-43.9</b>	<b>-47.0</b>	<b>-48.4</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>
Total revenue	34.5	37.8	38.4	38.7	39.7	41.7	42.5	40.9
Total expenditure	41.4	42.7	41.5	42.4	42.3	43.8	44.3	42.4
<i>of which: Interest</i>	3.4	3.7	3.3	3.0	2.9	2.9	2.7	2.6
<b>Corporations (% of GDP)</b>								
<b>Net lending (+) or net borrowing (-)</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>
<b>Net financial assets; non-financial corporations</b>	<b>n.a</b>	<b>-84.6</b>	<b>-81.5</b>	<b>-56.7</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>
<b>Net financial assets; financial corporations</b>	<b>n.a</b>	<b>-15.3</b>	<b>-8.1</b>	<b>0.6</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>
Gross capital formation	n.a	n.a	n.a	n.a	n.a	n.a	n.a	n.a
Gross operating surplus	25.9	24.0	25.3	n.a	n.a	n.a	n.a	n.a
<b>Households and NPISH (% of GDP)</b>								
<b>Net lending (+) or net borrowing (-)</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>
<b>Net financial assets</b>	<b>n.a</b>	<b>181.4</b>	<b>163.0</b>	<b>159.2</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>
Gross wages and salaries	n.a	n.a	n.a	n.a	n.a	n.a	n.a	n.a
Net property income	n.a	n.a	n.a	n.a	n.a	n.a	n.a	n.a
Current transfers received	n.a	n.a	n.a	n.a	n.a	n.a	n.a	n.a
Gross saving	n.a	n.a	n.a	n.a	n.a	n.a	n.a	n.a
<b>Rest of the world (% of GDP)</b>								
<b>Net lending (+) or net borrowing (-)</b>	<b>-5.7</b>	<b>-3.2</b>	<b>-3.9</b>	<b>5.3</b>	<b>4.7</b>	<b>4.7</b>	<b>2.3</b>	<b>1.9</b>
<b>Net financial assets</b>	<b>n.a</b>	<b>-35.7</b>	<b>-25.2</b>	<b>-53.1</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>	<b>n.a</b>
Net exports of goods and services	-3.7	-0.4	0.1	5.1	5.5	6.0	3.7	3.4
Net primary income from the rest of the world	-0.8	-1.8	-3.4	-4.3	-4.1	-4.2	-4.0	-3.8
Net capital transactions	0.4	1.5	1.1	1.9	1.7	1.7	1.7	1.6
Tradable sector	52.3	44.1	39.4	37.7	38.0	37.3	n.a	n.a
Non tradable sector	37.2	43.6	48.0	50.1	49.8	49.8	n.a	n.a
<i>of which: Building and construction sector</i>	5.1	6.4	4.2	4.0	3.7	3.6	n.a	n.a
Real effective exchange rate (index, 2000=100)	86.5	92.4	101.6	104.2	106.6	107.7	103.5	103.3
Terms of trade goods and services (index, 2000=100)	97.3	98.3	99.4	99.5	99.8	100.7	100.5	100.6
Market performance of exports (index, 2000=100)	80.3	72.1	94.2	107.1	104.0	100.4	100.7	98.3
<b>Notes:</b>								
<sup>1</sup> The output gap constitutes the gap between the actual and potential gross domestic product at 2005 market prices.								
<sup>2</sup> The indicator on domestic demand includes stocks.								
<sup>3</sup> Unemployed persons are all persons who were not employed, had actively sought work and were ready to begin working immediately or within two weeks. The labour force is the total number of people employed and unemployed. The unemployment rate covers the age group 15-74.								
<b>Source:</b>								
AMECO data, Commission 2015 spring forecast.								