

18. MALTA

Solid growth continues

Following exceptional growth rates in 2014 and 2015, and strong growth in 2016, real GDP growth is forecast to remain robust both this year and next. The labour market is performing well, with unemployment set to remain at record lows. The budget balance swung into surplus in 2016, which, thanks to strong revenue growth, is expected to remain.

Malta's economy performed better than expected in 2016. Real GDP growth expanded by 5% following upward data revisions for the first three quarters and a particularly strong final quarter of the year. Growth was driven primarily by services exports, in particular gaming and professional services. Private consumption expenditure also drove growth, fuelled by gains in disposable income and declining unemployment. Following extraordinarily high growth in 2014 and 2015, investment contracted slightly but remains well above the historical average.

Real GDP growth to remain robust

Real GDP growth is set to ease somewhat over the forecast horizon to robust rates of 4.6% in 2017 and 4.4% in 2018. With labour market conditions forecast to remain favourable, private consumption is projected to continue growing strongly over the forecast horizon. Despite a gradual increase in public investment and strengthening residential construction, gross fixed capital formation is forecast to remain modest, reflecting the expiration of one-off equipment investments. Net exports are projected to continue to contribute to growth, in particular due to the expansion of services exports, while goods exports are expected to remain subdued. Exports of services are being given a boost by the proceeds from the government's citizenship programme. As a result, the current account surplus is projected to continue to rise gradually over the forecast horizon.

Favourable labour market conditions continue

The trend of rising labour market participation and employment, in particular among women, is projected to continue over the forecast horizon. This is expected to feed continued strong employment growth averaging 2.9% in 2017-2018, while the unemployment rate stabilises at just below 5%. In line with the supportive macroeconomic conditions, wage growth is forecast to strengthen somewhat, while rising productivity, keeps unit labour costs increases contained.

Price inflation gradually increases

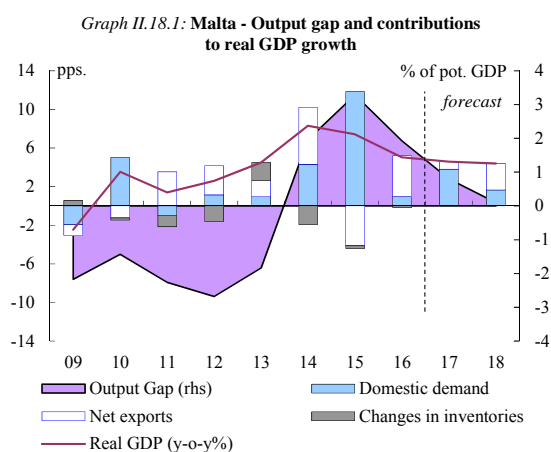
Annual HICP inflation is projected to gradually increase over the forecast horizon, in line with rising international commodity prices as well as growing domestic incomes. A rebound in fuel prices is expected to be the main driver behind the increase in HICP inflation in 2017. A further increase in fuel prices, accompanied by a pick-up in price growth in services is projected to push up inflation in 2018. Thus, HICP inflation is forecast to remain below 2% over the forecast horizon, rising above the euro-area average in 2018.

Risks to the macroeconomic projections are broad-based. On the domestic front, strong economic growth could spur private consumption and investment further, albeit somewhat offset by increased uncertainty due to the announced elections. The launching of the Malta Development Bank could provide an additional boost to investment. The decision to increase the minimum wage may support private consumption further, although the impact on GDP growth could be offset by higher costs for employers. The negotiations between the UK and the EU, which are still shrouded in considerable uncertainty, may also be set to impact Malta's growth prospects.

Government balance turned positive in 2016...

In 2016, the government balance turned positive, registering a surplus of 1% of GDP, up from a deficit of 1.3% in 2015. This better-than-expected outcome is explained by the high growth rate of current revenue. In particular, income tax revenues increased substantially due to both favourable labour market conditions and high corporate profits. In addition, higher-than-expected proceeds from Malta's citizenship programme (1.7% of GDP) contributed to the fiscal surplus. Current expenditure continued to increase but at a slower pace than in previous years. This was despite increases in public sector wages and intermediate consumption, which included costs associated with Malta's presidency of the EU. Finally, despite a

sharp decline in the absorption of EU funds as a result of the start of a new programming period, and a lower capital injection into the national airline, net capital expenditure increased by 0.3 pps. of GDP.



...and is expected to remain positive over the forecast horizon.

In 2017, the fiscal surplus is expected to decline to 0.5% of GDP. In line with robust GDP growth and a strong labour market performance, tax revenues are expected to continue growing. Yet, following

lower proceeds from the citizenship scheme, overall current revenue growth is expected to slow down. Current expenditure growth is projected to strengthen, mainly resulting from higher outlays for public wages related to the renewal of the public sector wage agreement and costs associated with Malta's presidency of the EU. By contrast, interest expenditure is set to marginally decrease. Net public investment is forecast to remain broadly unchanged as the implementation of investment projects co-financed by the EU and by the revenues received from the citizenship scheme seems to lag behind. In 2018, under a no-policy-change assumption, the budget surplus is projected to improve further to 0.8% of GDP. The structural balance is estimated to have improved in 2016 by 3 pps., reaching a surplus of 0.4% of GDP. It is projected to remain positive in 2017 and 2018, thanks to a swift closure of the positive output gap. The government debt-to-GDP ratio, which fell below the 60% threshold in 2016, is forecast to decline further to 52.5% in 2018.

Risks to the fiscal outlook are balanced as higher current expenditure, related to the recently-called early elections and slippages in budgetary execution, may be compensated by higher proceeds from the citizenship programme.

Table II.18.1:

Main features of country forecast - MALTA

	2015			Annual percentage change						
	mio EUR	Curr. prices	% GDP	97-12	2013	2014	2015	2016	2017	2018
GDP	9275.8		100.0	2.7	4.5	8.3	7.4	5.0	4.6	4.4
Private Consumption	4652.0		50.2	2.2	2.3	2.8	5.2	3.8	3.5	3.3
Public Consumption	1690.3		18.2	1.8	-0.3	6.5	3.8	-3.1	11.8	4.1
Gross fixed capital formation	2291.1		24.7	1.4	-1.7	8.8	48.8	-1.3	0.5	-3.0
of which: equipment	1242.7		13.4	-	-4.5	15.2	117.6	0.3	-	-
Exports (goods and services)	13356.1		144.0	5.7	1.4	5.3	4.1	4.0	3.6	4.5
Imports (goods and services)	12629.8		136.2	4.9	0.4	1.6	7.5	1.1	3.4	2.8
GNI (GDP deflator)	8898.2		95.9	2.4	3.8	8.6	8.0	3.2	5.0	4.8
Contribution to GDP growth:										
		Domestic demand		2.1	1.0	4.3	11.9	1.0	3.9	1.7
		Inventories		-0.2	1.8	-1.9	-0.2	-0.2	0.0	0.0
		Net exports		0.8	1.6	5.8	-4.3	4.3	0.7	2.8
Employment				1.0	3.7	5.1	3.8	3.7	3.0	2.8
Unemployment rate (a)				6.8	6.4	5.8	5.4	4.7	4.9	4.9
Compensation of employees / head				3.8	2.0	1.5	3.3	2.4	3.0	3.1
Unit labour costs whole economy				2.2	1.3	-1.4	-0.2	1.1	1.4	1.5
Real unit labour cost				-0.2	-0.7	-3.4	-2.5	-0.5	-0.2	-0.3
Saving rate of households (b)				-	-	-	-	-	-	-
GDP deflator				2.4	2.0	2.0	2.4	1.6	1.6	1.8
Harmonised index of consumer prices				2.7	1.0	0.8	1.2	0.9	1.6	1.8
Terms of trade of goods				0.2	1.7	6.6	1.4	1.2	1.1	0.3
Trade balance (goods) (c)				-16.2	-13.6	-12.3	-19.4	-18.4	-19.1	-18.5
Current-account balance (c)				-3.9	2.8	9.7	5.3	7.9	6.5	9.0
Net lending (+) or borrowing (-) vis-a-vis ROW (c)				-2.8	4.6	11.3	7.1	8.7	8.1	10.5
General government balance (c)				-4.9	-2.6	-2.0	-1.3	1.0	0.5	0.8
Cyclically-adjusted budget balance (d)				-4.8	-1.7	-2.7	-2.5	0.3	0.2	0.7
Structural budget balance (d)				-	-1.8	-3.2	-2.6	0.4	0.4	0.7
General government gross debt (c)				64.0	68.7	64.3	60.6	58.3	55.8	52.5

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