# 18. MALTA
Robust growth outlook

Real GDP growth peaked in 2015 on the back of strong investment and supported by private consumption. Growth is expected to moderate in 2016 and 2017 with the phasing out of the major investment projects. The general government deficit and debt are forecast to decline further also thanks to the favourable macroeconomic conditions.

Growth strengthens further in 2015 and moderates thereafter

Malta's economy grew by 5.4% (y-o-y) in the third quarter of 2015, slightly less than the 5.8% increase reported in the second quarter. The latest national accounts release features notable upward revisions to the growth figures of recent quarters, which will result in an even stronger carryover going forward. The main engine of growth continued to be investment, particularly machinery and equipment investment associated with large ongoing energy investment projects. Private consumption expanded by 5.1% on the back of strong wage growth and record-low unemployment. The high import-dependence of domestic demand resulted in a negative contribution of net exports to growth. Favourable developments in the traditionally volatile primary income account fully offset this. As a result the current account surplus increased further.

Graph II.18.1: **Malta - Output gap and contributions to real GDP growth**
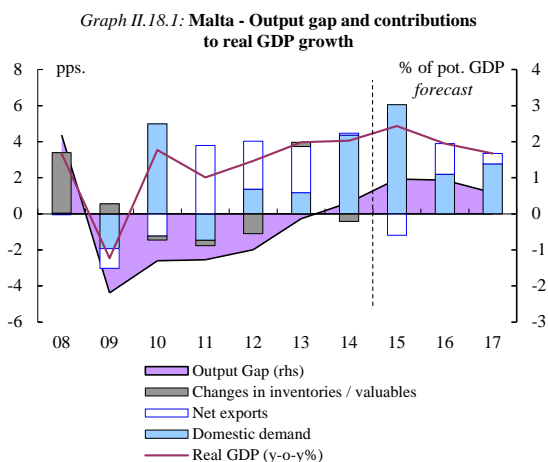
Real GDP growth is forecast to reach 4.9% in 2015 before moderating to 3.9% in 2016 and further to 3.4% in 2017. The expected slowdown primarily reflects the planned completion of large-scale energy investment projects in 2016 and the expiration of the 2007-13 programming period of EU funding. Private consumption is therefore projected to become the main driver of growth over the forecast horizon, contributing on average

over 1.5 pps. per year to growth in 2016 and 2017. Export growth is expected to continue recovering gradually, helping Malta to regain export market shares. As demand for capital goods slows down in line with the decrease in investment and oil prices remain subdued, net exports are expected to make a positive contribution to GDP growth in 2016-17.

The risks to this macroeconomic forecast are balanced. Upside risks are related mainly to the investment outlook due for example to the materialisation of additional infrastructure projects linked to the Investment Plan for Europe and the potential impact of the establishment of a development bank to help SMEs access financing. At the same time, protracted weakness in emerging markets could hamper the recovery of exports, given Malta's large exposure to trading partners outside the EU.

Unemployment continued dropping over the third quarter of 2015 thanks to sustained job creation. The unemployment rate is projected to average 5.4% for the year as a whole and to remain broadly unchanged until the end of the forecast horizon. The very low unemployment rate points to some tightness in the labour market, which, combined with strong productivity gains, are forecast to result in some upward pressure on wage growth.

HICP inflation is forecast to return to above 2% by 2017 on the back of higher energy inflation, reflecting the expiration of the low base effect from cutting electricity tariffs for households in 2016 and a gradual recovery in oil prices in 2017. Services inflation is also projected to accelerate. Inflation is forecast to be among the highest in the euro area over the forecast horizon.

Budget deficit decreases further

In 2015 the general government deficit is projected to have decreased further to 1.6% of GDP, from 2.1% of GDP in 2014, supported by strong nominal GDP growth. Revenue growth is expected to benefit from the positive outlook for the labour market and consumer demand, as well as the

proceeds from the citizenship programme (0.9% of GDP). Despite the moderation in the growth rate for social transfers and interest, current expenditure is expected to increase by 5.5% (y-o-y) in nominal terms. Net investment is expected to remain at levels close to 2014, while subsidies to investment are set to increase on the back of a further capital injection into Air Malta (0.5% of GDP).

In 2016 the deficit is forecast to further decrease to 1.1% of GDP. Despite the increase in excise duty on various products, current revenue is expected to grow less than nominal GDP. This reflects the lowering of income tax for low income earners, the phasing out of the eco contribution and the high base effect for the proceeds linked to the citizenship programme. Current expenditure is expected to continue growing due to measures introduced with the 2016 Budget, including an upward adjustment of the minimum contributory pension and the partial funding of the cost of home

care for the elderly. Public investment is expected to decrease on the back of the phasing out of the capital injection to the national airline, while the sharp decline in the absorption of EU funds due to the beginning of a new programming period should be partially compensated for by a higher reliance on national funds. In 2017, under a no-policy-change assumption, the deficit is expected to decline further to 1.0% of GDP thanks to favourable nominal GDP growth.

The structural deficit ratio is estimated to have remained stable in 2014. It is projected to improve by ½ pp. of GDP in both 2015 and 2016 and by ¼ pp. of GDP in 2017.

From 66.9% of GDP in 2014, the debt ratio is projected to fall further in 2015 to 64% of GDP, also thanks to the expected repayment of some tax arrears from the public energy utility corporation. It is expected to follow a downward path and to reach 58.7% of GDP by 2017.

Table II.18.1:

Main features of country forecast - MALTA

		2014		Annual percentage change						
	mio EUR	Curr. prices	% GDP	96-11	2012	2013	2014	2015	2016	2017
GDP		8106.1	100.0	2.8	2.9	4.0	4.1	4.9	3.9	3.4
Private Consumption		4366.3	53.9	2.7	-0.2	2.0	2.8	4.0	3.4	2.6
Public Consumption		1614.8	19.9	2.0	6.3	0.2	7.8	2.5	4.9	6.3
Gross fixed capital formation		1445.5	17.8	0.6	1.4	-0.2	7.6	19.1	-2.6	1.0
of which: equipment		518.4	6.4	-	-17.3	9.0	-0.7	-	-	-
Exports (goods and services)		11977.7	147.8	4.8	6.7	0.8	0.0	2.7	4.5	4.8
Imports (goods and services)		11329.3	139.8	4.1	5.2	-0.8	-0.1	3.7	3.5	4.7
GNI (GDP deflator)		7896.9	97.4	2.6	1.7	3.2	6.8	5.6	3.8	3.5
Contribution to GDP growth:	Domestic demand			2.2	1.3	1.2	4.3	6.1	2.2	2.8
	Inventories			0.0	-1.1	0.2	-0.4	0.0	0.0	0.0
	Net exports			0.7	2.6	2.5	0.1	-1.2	1.7	0.5
Employment				1.0	2.5	3.7	5.0	2.1	2.4	2.4
Unemployment rate (a)				6.7	6.3	6.4	5.8	5.4	5.4	5.4
Compensation of employees / head				3.8	3.7	1.3	0.6	3.1	3.4	3.4
Unit labour costs whole economy				1.9	3.2	1.1	1.5	0.4	1.9	2.4
Real unit labour cost				-0.4	1.2	-0.8	-0.2	-2.0	-0.6	-0.2
Saving rate of households (b)				-	-	-	-	-	-	-
GDP deflator				2.4	2.0	1.9	1.8	2.4	2.5	2.6
Harmonised index of consumer prices				-	3.2	1.0	0.8	1.2	1.7	2.1
Terms of trade of goods				0.3	-1.9	2.6	1.7	0.9	-0.3	0.0
Trade balance (goods) (c)				-16.7	-14.2	-13.1	-12.8	-15.5	-14.2	-13.5
Current-account balance (c)				-5.2	1.3	3.6	3.9	4.3	5.9	6.5
Net lending (+) or borrowing (-) vis-a-vis ROW (c)				-4.2	3.2	5.3	5.6	6.1	7.6	8.1
General government balance (c)				-5.1	-3.6	-2.6	-2.1	-1.6	-1.1	-1.0
Cyclically-adjusted budget balance (d)				-5.1	-3.1	-2.5	-2.2	-2.0	-1.5	-1.3
Structural budget balance (d)				-	-3.4	-2.7	-2.5	-2.2	-1.6	-1.3
General government gross debt (c)				62.1	67.4	68.5	66.9	64.0	61.2	58.7

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