



# **Malta:**

# **Draft Budgetary Plan**

# **2019**

**Ministry for Finance**  
**October 2018**

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.

Figures may not add up due to rounding.

This document is based on statistical information available up to the  
12<sup>th</sup> of October, 2018

## 1. Overall Policy Framework and Objectives

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The forthcoming budget will continue to address the new challenges brought by the economic success, while at the same time addressing social obligations. Indeed, the Government will 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 environment will be better protected with increased uses of greener and cleaner energy, sustainable water sources, as well as better waste management. The budget will continue focusing on improving Malta's housing stock while addressing the challenges of the household rental market. Concurrently, it will continue to target a fiscal surplus net of IIP whilst ensuring that the debt burden on future generations continues to be minimised. Hence, the 2019 Budget will further support the robust growth momentum and insulate the economy from major economic imbalances while also promoting long-term economic sustainability.

## 1.1 Macroeconomic Scenario

In the first half of 2018, growth moderated to 5.4 per cent, although it is expected to pick up momentum in the second half of the year as a number of investment projects accelerate and export growth strengthens. Growth in 2018 is estimated at 5.8 per cent, consistent with an output gap of 0.9 per cent.

The economic outlook for 2019 is expected to continue to be underpinned by a stronger element of domestic demand, driven in particular by strong investment activity in real-estate, accommodation, aviation, technology and telecommunications and supported by a strong public investment. Exports are also expected to pick up momentum, though the external situation is expected to remain fragile and conditioned by rising protectionist tendencies and vulnerabilities to global capital flows. The Maltese economy is forecasted to grow at a more moderate pace of 5.3 per cent, sufficiently below the potential growth estimate of 6.2 per cent to allow the output gap to close.

The growth outlook for 2019 is expected to be underpinned by rising productivity, moderate wage growth, relatively low inflationary pressures and a persistent current account surplus. Together with a more modest output gap, these indicators suggest that the positive outlook can be sustained over the medium-term. This notwithstanding, risks to the growth outlook cannot be underestimated. However, both the sensitivity analysis and the alternative model projections suggest that risks are fairly balanced in 2018 and still marginally positive for 2019.

## 1.2 Fiscal Policy Objectives

Given the present phase of the economic cycle and the positive state of public finances, both in terms of structural balances and debt ratio, the overall objective is to maintain fiscal stability by targeting a structural budget balance net of IIP in 2019 and ensuring a further reduction in the debt burden. This objective is to be balanced with the need for further investment in infrastructure whilst addressing the distributional imbalances which persist. Indeed, Government is aware that the pace of economic activity can create social pressures on certain vulnerable segments of the population, including pensioners, single earner households with children, disabled persons and low-income households

who are at risk as a result of the booming rental market. A number of budget measures are expected to address these pertinent concerns of social policy. Economic growth has also brought to the fore both skill and labour market bottlenecks as well as a number of infrastructural constraints which need to be addressed in order to ensure that the present rate of potential economic growth can be maintained over the medium to long-term.

In this context, Government is targeting a budget balance of 1.3 per cent of GDP in 2019. This is consistent with a structural budget balance of 1.2 per cent of GDP. This exceeds the structural target presented in the Government's Medium-Term Fiscal Strategy submitted to Parliament in May 2018. This target is also consistent with the medium-term strategic commitment to continue to ensure compliance with the MTO, net of IIP receipts and expenditure. Gross debt is targeted to decline further to 43.8 per cent of GDP, thus sustaining the downward trend observed in the last few years. The ambitious fiscal target is to be achieved, whilst public investment is expected to reach 3.5 per cent of GDP in 2019, an investment target which is meant to support the needed investment in infrastructure to sustain Malta's growth potential.

### **1.3 Fiscal Governance**

The Fiscal Responsibility Act adopted by the Maltese Parliament in August 2014, marked a significant step in the strengthening of fiscal governance. In March 2018, further changes were made to the Act in order to ensure full transposition of Council Directive 2011/85/EU on the requirements of budgetary framework of Member States.

The further strengthening of the institutional capacity in Malta's fiscal framework continues to be a priority. The Comprehensive Spending Reviews are a core element of the Maltese Government's strategy to ensure the achievement of a more effective approach to public spending, improving decision making and ensuring that public spending is meeting changing priorities and changing social needs. The Comprehensive Spending reviews, which started in 2014, have so far covered the Department for Social Security, Mater Dei Hospital, Primary Health, Pharmacy of your Choice, the Ministry for Education and Employment, the Management and Efficiency Unit as well as the Malta College for Arts, Science and Technology. Furthermore, in line with the Country Specific Recommendation 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 started through assistance from the Structural Reform Support Programme. In 2018, a Directorate was set up within the Budgetary Affairs Division (Ministry for Finance) 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. Draft operational guidelines have been formulated and a training programme has been set. Around 50 officials from various ministries, including officials from the Ministry for Finance, have been selected and will be specifically trained over the course of the end of this year and the beginning of 2019.

In addition, 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 last May and published a report on 27th September presenting and explaining

in detail the results, while also putting forward recommendations that further enhance fiscal transparency. The report, which is the first of its kind for Malta, found that many elements of sound fiscal transparency practices are in place in Malta. Furthermore, Malta obtained results which are similar to other advanced economies in the EU that have undertaken the FTE and compared well with the EU average made up of Ireland, Romania, Portugal, Finland and UK FTE scores.

The targets contained in this Plan fulfill the legal requirements established by virtue of the Fiscal Responsibility Act. In addition, the macroeconomic forecasts underlying this Plan and the 2019 Budget have been endorsed by the Malta Fiscal Advisory Council.

## 1.4 Conclusion

The strength and stability being exhibited by the Maltese economy, mainly underpinned by strong improvements in investment, continued positive developments in the labour market, and subdued inflationary pressures, are supported by the range of structural economic policies presented in various National Reform Programmes and budget measures. These structural reform measures are intended to address the country's main economic challenges, and in particular:

1. Continue to deliver Government's commitment of ensuring public finance sustainability in the short to medium-term, while also addressing the long-term dimension in particular through reduction in Government Debt.
2. Raising potential output, by continuing to direct Malta towards higher value-added, knowledge-based sectors comprising a range of activities including professional, financial, gaming, corporate and fiduciary services, increase the labour force participation, especially of women, raising skill and education levels, promoting lifelong learning and continue addressing labour market shortages.
3. Investing and upgrading the infrastructure in order to support the increased economic activity and pave the way forward for further sustainable growth.
4. Addressing other long-term challenges including in the transport, environment and housing sectors.
5. Ensure a fair and equitable distribution of resources whilst supporting the most vulnerable in society.
6. Continue reducing bureaucracy especially the length of the public procurement process and ensuring that the public service is efficient and cost effective, including through the extension of one-stop shops.
7. Safeguarding the successes achieved by the Maltese financial sector.

As a result of the Government's structural reform initiatives, Malta's potential growth is now estimated to reach 6.1 per cent in 2019. This rate of economic expansion is expected to support the further consolidation of public finances and the reduction of debt burden whilst improving the sustainability of public finances.



## 2. Economic Outlook

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## 2. Economic Outlook

### 2.1 The Short-Term Scenario

Following the robust growth rates recorded in the last three years, the Maltese economy continued to progress at a faster pace than in the European Union (EU28) and the Euro Area (EA) in the first half of 2018. Indeed, during this period, the Maltese economy registered a growth rate of 5.4 per cent in real terms. This strong growth is primarily attributable to a relatively larger contribution from the domestic side of the economy, particularly attributed to growth in both public and private household consumption.

During the first half of 2018, total Gross Value Added (GVA) increased by 7.6 per cent over the same period in 2017. The growth in GVA was mostly attributed to the services sector which registered a contribution rate of 6.9 percentage points to growth, while the primary and secondary sectors provided a positive contribution towards growth equivalent to 0.6 percentage points. The growth in GVA was underpinned by increases registered in all sectors of the economy, with substantial growth rates registered in the real estate activities sector (11.5 per cent), the arts, entertainment and recreation sector (10.7 per cent), the financial and insurance activities sector (10.4 per cent), the public administration, education and human health sector (9.5 per cent), and the professional, scientific and technical activities sector (8.5 per cent). These sectors as well as the wholesale and retail, transportation and accommodation sector, accounted for a contribution of 6.6 percentage points to GVA growth. The lowest contribution to GVA was recorded in agriculture and fishing at 0.03 percentage points.

From the income side, in comparison to the first half of 2017, the factor distribution of income gains between compensation of employees and gross operating surplus and mixed income was more evenly balanced. Specifically, the former grew by 8.2 per cent, while the latter exhibited a growth rate of 7.1 per cent. Meanwhile, taxes on production and imports continued to rise faster than Gross Domestic Product (GDP) growth whilst subsidies became more subdued in the first half of 2018.

The Maltese economy is expected to retain a positive momentum in the second half of 2018, as overall growth is expected to increase by 5.8 per cent in real terms by the end of the year. Growth is expected to be driven by the domestic side, which is expected to contribute 5.4 per cent to GDP growth, while the external side of the economy is expected to contribute negatively to economic growth.

Private consumption is projected to rise by a real rate of 5.6 per cent, supported by employment growth and increases in disposable income, consistent with positive developments in wages. Government consumption is expected to grow by 15.0 per cent in real terms (or equivalently 19.0 per cent in nominal terms), mainly reflecting higher compensation of employees for the public sector. When the Individual Investor Program (IIP) portion of market output is excluded from this figure, public consumption is projected to grow at 13.8 per cent in nominal terms. While gross fixed capital formation declined in the first half of 2018, reflecting a base effect arising from the extraordinary investments in the energy sector and in aircraft equipment in the previous two years, investment growth is expected to recover in the second half of 2018 to reach a real growth rate of 1.3 per cent in 2018. This positive performance reflects the expected acceleration of EU-funded investment towards the end of the year, investments pertaining to the areas

of technology and telecommunication as well as the positive momentum in construction activity. It is worth mentioning, that when forecasting investment, economists within the Ministry for Finance (MFIN) take a relatively prudent approach, factoring in only those projects that have a strong political commitment or a high prospect of realisation. Besides, a relatively high import content of investment is assumed in the forecasts.

From an external standpoint, import growth is expected to outweigh export growth, leading to a negative net trade contribution to growth equivalent to 0.9 per cent. Imports are expected to rise by a real rate of 2.0 per cent, mostly driven by a strong domestic demand, especially investment, and higher oil prices. On the other hand, real exports are forecasted to increase by 1.3 per cent. The moderate growth in exports reflects subdued external demand conditions, stemming from economic activity in Malta's main trading partners which is somewhat weaker than originally anticipated in the previous forecasts of the Ministry. The strength of the Euro is also expected to negatively influence export performance over the course of 2018, though the recent weakening against the US Dollar should support export competitiveness. However, by the end of the year, the Euro is expected to strengthen against the US Dollar. Moreover, the Euro is expected to appreciate against the UK Pound Sterling.

The labour market is expected to continue yielding favourable developments, as employment is projected to rise by 5.0 per cent and the unemployment rate to decline from 4.6 per cent to 4.0 per cent in 2018. Prices are projected to increase by 1.7 per cent in 2018, reflecting higher growth in the prices of services and processed food that is partly offset by lower growth in non-energy industrial goods and services components.

Throughout 2019, real GDP is expected to remain strong, reaching a growth rate of 5.3 per cent. Domestic demand is expected to remain strong. Government expenditure and private consumption are expected to remain robust albeit more balanced due to a pick-up in inflation. Investment is expected to hasten on the back of the materialisation of a number of large-scale investment projects of a construction nature particularly in health, real-estate and tourism.

In contrast to 2018, net exports are expected to contribute positively to economic growth over the course of 2019. Despite the further strengthening of the Euro against the US Dollar and the expected subdued external demand conditions in 2019, exports are forecasted to increase at a relatively faster pace (an increase of 0.9 percentage points), reaching a growth rate of 2.2 per cent, while imports are expected to continue growing even if at a marginally slower pace (a 0.2 percentage points increase), reaching a growth rate of 2.2 per cent during 2019. While imports of capital goods are expected to increase, owing to the accelerated growth in investment activity, imports of consumption goods are expected to decline, as growth in private final consumption expenditure is expected to remain strong even if somewhat slower than in 2018. Such positive external developments are underpinned by strong performance in the services sector, particularly in the financial services, other business services, pharmaceuticals, tourism, and remote gaming sectors.

Table 2.1 presents the main macroeconomic indicators for the period 2015 to 2019. The figures for the 2015 to 2017 period are based on the latest data released by the National Statistics Office (NSO) under the European System of National and Regional Accounts

## Growth in Main Macroeconomic Indicators

Table 2.1

per cent

	2015	2016	2017	2018f	2019f
GDP growth at current market prices	12.5	6.9	9.4	7.7	7.7
GDP growth at Chain Linked Volumes by period (Reference year 2010) <sup>(1)</sup>	9.5	5.2	6.7	5.8	5.3
<b>Expenditure Components of GDP</b>					
<b>at Current Market Prices by period</b>					
Private final consumption expenditure <sup>(2)</sup>	6.8	3.2	4.8	6.3	4.7
General Government final consumption expenditure	5.3	-1.1	4.6	19.0	10.6
: net of Individual Investor Programme (IIP) proceeds	8.4	5.9	8.0	13.8	7.1
Gross fixed capital formation	64.4	3.1	-5.3	5.0	11.1
Exports of goods and services	5.8	5.4	7.3	4.1	3.9
: net of Individual Investor Programme (IIP) proceeds	5.4	4.6	6.9	5.8	3.1
Imports of goods and services	9.4	1.4	0.5	5.3	3.9
<b>Expenditure Components of GDP</b>					
<b>at Chain Linked Volumes by period (Reference year 2010)</b>					
Private final consumption expenditure <sup>(2)</sup>	5.0	2.6	3.7	5.6	4.1
General Government final consumption expenditure	3.7	-2.8	2.8	15.0	8.2
Gross fixed capital formation	56.8	1.7	-7.3	1.3	8.4
Exports of goods and services	3.7	4.2	3.8	1.3	2.2
Imports of goods and services	7.4	0.7	-1.9	2.0	2.2
Inflation rate	1.2	0.9	1.3	1.7	1.9
Employment growth (National Accounts Definition)	3.6	4.8	4.0	5.0	3.7
Unemployment rate (Harmonised definition, Eurostat)	5.9	5.2	4.6	4.0	4.1
Compensation per employee	5.1	2.8	1.8	2.9	2.9
Labour productivity	5.4	1.0	1.4	0.8	1.4
Nominal Unit Labour Cost	-0.3	1.8	0.4	2.1	1.5
Real Unit Labour Costs	-1.5	0.9	-0.9	0.4	-0.4

<sup>(1)</sup> 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.

<sup>(2)</sup> Includes NPISH final consumption expenditure.

(ESA 2010), whereas the figures presented for 2018 and 2019 are forecasts produced by economists within the MFIN.

## 2.1.1 Assumptions for Projections

The macroeconomic forecasts presented in this Draft Budgetary Plan are based on the following assumptions:

1. Economic activity in Malta's main trading partners is expected to increase by 1.8 per cent in 2018 and 1.7 per cent in 2019.
2. Oil prices are expected to rise, reaching an average of US \$72.1 per barrel in 2018 and US \$72.2 in 2019.
3. The short-term interest rate is expected to remain at the current spot rate of 0.0 per cent in both 2018 and 2019. On the other hand, the long-term interest rate is expected

to average at 1.3 per cent in 2018 and remain at the same level in 2019.

4. The USD/EUR exchange rate is expected to average 1.1785 in 2018 and 1.1980 in 2019, representing an appreciation of the Euro of 2.7 per cent in 2018 and 1.7 per cent in 2019. The STG/EUR exchange rate is expected to average 0.8873 in 2018 and 0.8868 in 2019, representing an appreciation of the Euro of 1.3 per cent in 2018 and a slight depreciation of the Euro of 0.1 per cent in 2019.
5. It is assumed that, starting from the third quarter of 2018, changes in inventories will not contribute materially to GDP growth.

## **2.1.2 Employment Prospects**

The Labour Force Survey (LFS) reported an employment rate of 70.6 per cent in the second quarter of 2018, which is 1.7 percentage points higher than the corresponding period of last year. Growth in headcount employment is expected to remain strong and increase by 5.0 per cent in 2018 and 3.7 per cent in 2019. Moreover, the unemployment rate (based on the Harmonised definition) is expected to decrease to 4.0 per cent and 4.1 per cent in 2018 and in 2019, respectively, standing well below the EU average rate. This reflects the buoyant state of the economy as well as ongoing efforts in promoting and sustaining active labour market policies.

In 2018, all sectors are expected to register growth in employment. The highest rates of growth are expected to be in the remote gaming and tourism sectors. The overall positive performance is mainly supported by the inflow of foreign workers and a higher female participation rate, reflecting ongoing Government policies aimed at strengthening the supply side of the labour market. These include work-life balance measures, family-friendly measures, in-work benefit and the tapering of benefits, lower taxes on labour, and various tax incentives.

## **2.1.3 Inflation**

The Harmonised Index of Consumer Prices (HICP) inflation rate (twelve-month moving average) which in 2017 stood at 1.3 per cent, increased to 1.5 per cent in the first half of this year, reflecting growth in the prices of services and to a lesser extent in non-energy industrial goods. The HICP is expected to average 1.7 per cent by the end of this year and 1.9 per cent in 2019. The relatively higher oil prices in 2018 and 2019 and higher expected services inflation are expected to increase inflationary pressures, while the strength of the Euro is expected to alleviate these effects.

## **2.2 Comparison to Commission's Latest Forecast**

Prior to comparing the MFIN's Autumn forecasts with those published by the European Commission (EC), it is worth mentioning that the EC's forecast does not include the latest national accounts data published by the NSO, while the MFIN's forecasts incorporate this data. Furthermore, MFIN's forecasts incorporate the latest data and forecasts in the external environment which are important for a small and open economy.

The Spring forecasts published by the EC projected a growth rate for Malta of 5.8 per cent and 5.1 per cent in 2018 and 2019, respectively, with domestic demand expected to be the main driver of growth in both years. Nevertheless, the interim summer forecasts projected by the EC suggest a marginally more moderate expansion of 5.4 per cent for 2018 whilst keeping the growth forecast for 2019 unchanged at 5.1 per cent. Whilst

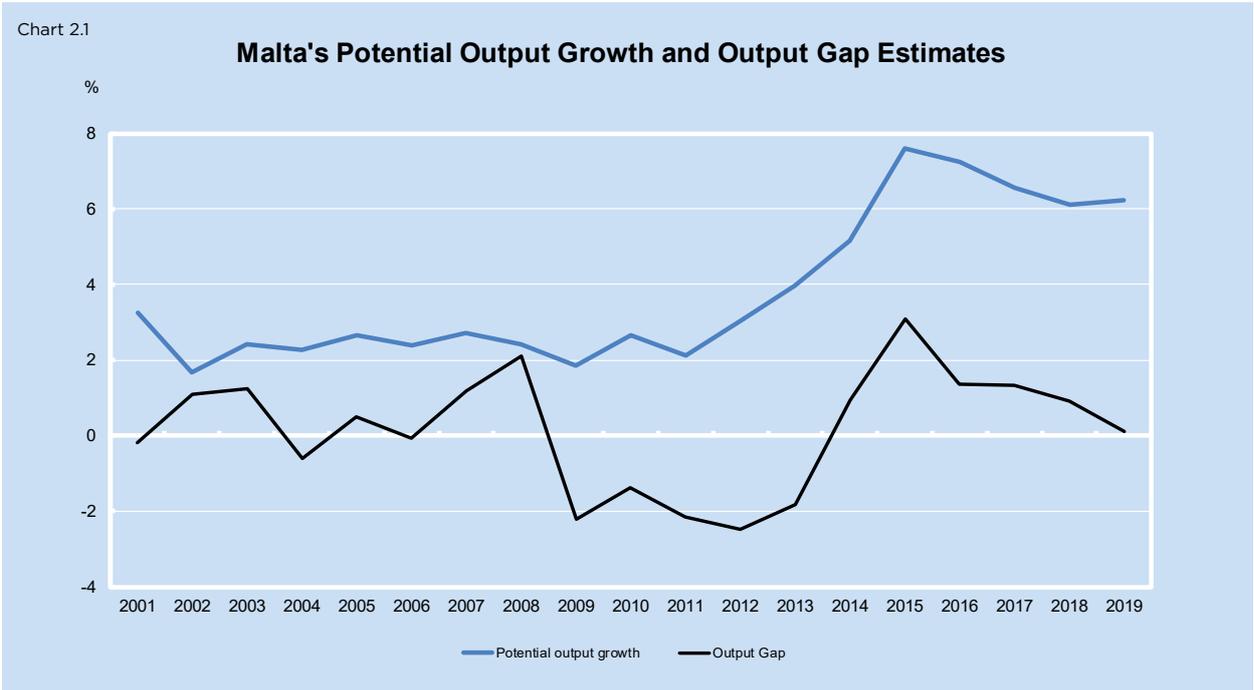
in Autumn the MFIN forecasts have also been revised downwards by 0.3 percentage points compared to the Spring forecasts, MFIN is still more confident of a more positive outlook for 2018 on the back of the outturn for the first half of 2018 and the expected acceleration in investment activity over the second half of 2018.

MFIN forecasts for 2019 are only marginally higher by 0.2 percentage points when compared to the rate of economic expansion forecasted by the EC for 2019 in the two latest forecast vintages.

The EC did not produce nominal GDP growth forecasts in the Interim summer forecast, so this can only be compared to the spring projections. Nominal GDP growth presented in this Draft Budgetary Plan is projected at 7.7 per cent for both 2018 and 2019. For 2018 and 2019, this represents a lower growth of 0.1 percentage points and a higher growth of 0.5 percentage points over the baseline presented by the EC in its Spring forecast, respectively. Moreover, the MFIN forecasts a slightly lower growth in the GDP deflator for 2018, but a slightly higher growth in the GDP deflator for 2019, when compared to the EC Spring forecasts.

### 2.3 Potential Output and the Output Gap

The developments in potential output and in the output gap, both historically and those expected over the forecast horizon are illustrated in Chart 2.1. The average potential output growth stood at 4.8 per cent during the period 2010 to 2017. Over 2018 and 2019, potential output growth is expected to increase to an average growth rate of 6.2 per cent, mainly underpinned by positive employment growth and higher labour market participation rates. Improvements in the total factor productivity and capital accumulation will also contribute positively to potential output growth. The positive output gap for 2017 of 1.3 per cent is expected to decline to 0.9 per cent for 2018, and then to almost close in 2019.



## 2.4 Comparison with the MFIN Spring Forecasts

The economic outlook in this Draft Budgetary Plan has been revised marginally downwards for 2018, whilst the forecast growth for 2019 has been largely retained, when compared to the Spring round of forecasts. The contribution from the external side of the economy has been revised downwards for 2018, reflecting a more moderate growth in exports due to subdued external demand conditions. These stem from a somewhat weaker economic activity by Malta's main trading partners, than that originally anticipated in the MFIN Spring forecasts. The strength of the Euro throughout 2018 is also expected to negatively influence export performance. These have been partly offset by an increase in the contribution to growth from the domestic side of the economy, namely private and Government consumption. Thus, domestic demand remains the main contributor to growth in the Maltese economy.

While growth in 2019 has been maintained in line with the Spring forecasts, the composition is slightly different. The domestic contribution to growth is now stronger. This reflects stronger expected growth in household consumption, government expenditure and investment activity which mitigates the weaker growth in exports expected to result from exchange rate pressures and weaker external demand conditions. Relatively higher expected inflationary pressures are to result in a stronger GDP deflator and hence a higher growth in nominal GDP than forecasted in Spring.

## 2.5 Sensitivity Analysis

The macroeconomic forecast is the economic foundation of the Government's fiscal policy targets presented in this Plan. In this context, the macroeconomic forecasts prepared for the budget balance the need to strive for forecast accuracy with the need to maintain a measure of prudence. This is complemented by the assessment of past forecasting performance and a rigorous and scientific quantification of macroeconomic risk, based on research carried out by the Economic Policy Department (EPD) within the MFIN. While the Maltese economy has proved to be very resilient to the international economic crisis, GDP forecast errors are relatively higher for Malta than those observed for larger and less open economies within the EU<sup>1</sup>. This section provides 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.

### 2.5.1 The Accuracy of Past Forecasting Performance

The updated analysis shows a tendency to underestimate GDP growth and hence a downward bias in the GDP growth projections in previous years. However, this is primarily a result of significant statistical revisions persistently in the upward direction in the national accounts data. While the one-year ahead forecasts display a root-mean squared error (RMSE) of 3.1, it is notable that the sample size employed is rather small and the earliest available forecast is that of 2004. The small sample size, the recession of 2009, the subsequent recovery and the statistical revisions play an undue influence on this evaluation and limit comparability with the forecast accuracy displayed by other economies. It is noteworthy, that over successive vintages of forecasts, the widening of RMSE has been primarily attributed to the relatively large forecast errors in 2014 and 2015 which are symptomatic of significant upward revisions in the national accounts data.

The evaluation of the risk and uncertainty of the current macroeconomic projections underlying this Programme is based on both an ex ante analysis of past forecast errors which determine the level of uncertainty and an ex post assessment of the balance of risk based on a number of alternative but plausible economic scenarios generated with the forecasting model used by the EPD.

## **2.5.2 The Balance of Risks**

To determine the balance of risks surrounding the macroeconomic forecasts, thirteen 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 forecast.
3. Weaker Euro exchange rate against the US Dollar.
4. Stronger Euro exchange rate against the UK Pound Sterling.
5. Higher world prices rising by 2.5 per cent in contrast to the 1.7 per cent growth assumed in the baseline forecast.
6. Higher interest rate scenario resulting into an upward sloping yield curve in 2019.
7. Trade protectionism scenario, where a strong US Dollar coupled with high world prices and higher export and import prices resulting from the imposition of tariffs is modelled.
8. Stronger medium-term investment scenario.
9. Weaker medium-term investment scenario.
10. Higher oil prices, rising to 80.0 US Dollars per barrel in the last quarter of 2018 and reaching 85.0 US Dollars per barrel in 2019.
11. Higher wage inflation scenario where a growth rate of 3.5 per cent is assumed for 2019.
12. Negative manufacturing growth scenario.
13. Lower growth in exports of financial services.

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 also 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.

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.

### **2.5.2.1 Improved Global Economic Growth**

In this scenario, global growth is assumed to be higher, where Malta's key trading partners will have stronger growth than originally anticipated; an increase of 0.1 percentage points in 2018 and an increase of 0.6 percentage points in 2019. The relatively higher than expected economic growth in Germany, Italy, France, the UK, and the US is based on the Consensus Forecasts September 2018 publication, assuming the most optimistic growth figure for each trading partner for the forecast years 2018 and 2019. The outcome of

this scenario is marginal in 2018. On the other hand, real GDP growth is revised upwards by 0.3 percentage points in 2019, reaching a real growth rate of 5.6 per cent, while the budget balance is increased by 0.1 percentage points.

### **2.5.2.2 Weaker Global Economic Growth**

This scenario models the downside risk of a weaker than expected economic growth rate in Malta's main trading partners on the Maltese economy; a decline of 0.2 percentage points in 2018 and a decline of 0.4 percentage points in 2019. The relatively lower than expected growth projections for Germany, Italy, France, the UK, and the US are based on the Consensus Forecasts September 2018 publication, assuming the lowest growth figure for each trading partner for the forecast years 2018 and 2019. The outcome of this scenario is that the Maltese economy will continue yielding roughly the same development in real GDP growth and the budget balance for 2018 as in the baseline forecast. In contrast, real GDP growth is lowered by 0.2 percentage points in 2019, to reach 5.1 per cent, while the budget balance is essentially unaffected.

### **2.5.2.3 Interest Rate Scenario**

This scenario assumes that long-term interest rates are assumed to increase by 50 basis points in 2019, thereby steepening the yield curve compared to the baseline scenario. The effect of this scenario is lower real investment growth leading to a decline of 0.3 percentage points in real GDP in 2019 and a virtually unchanged budget balance.

## **2.5.3 Alternative Model Forecasts**

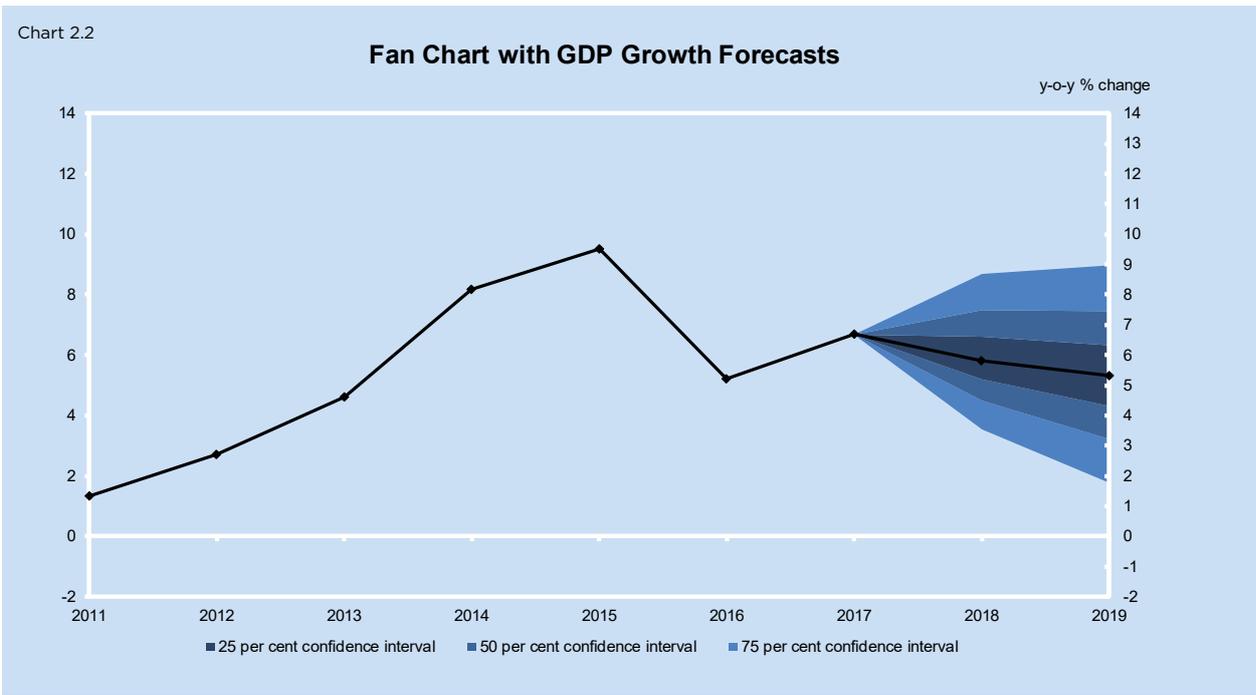
Moreover, the EPD has developed seven alternative forecasting models ranging from model-free statistical forecast (Random Walk and Holt-Winters Seasonal Smoothing Method), model-based univariate forecasts (2 ARIMA models) and model-based multivariate forecasts (2 VAR models and one VECM model). These models help EPD benchmark the results inferred from STEMM and can be used to generate alternative growth forecasts. For 2018, the alternative models give a range of growth forecasts from 5.1 to 6.5 with the average being very close to the baseline forecast. This is indicative of a relatively balanced risk for 2018. For 2019, growth forecasts range from 5.1 per cent to 6.2 per cent, meaning that the baseline forecast is rather prudent.

## **2.5.4 Uncertainty and the Balance of Risk Underlying the Macroeconomic Projections**

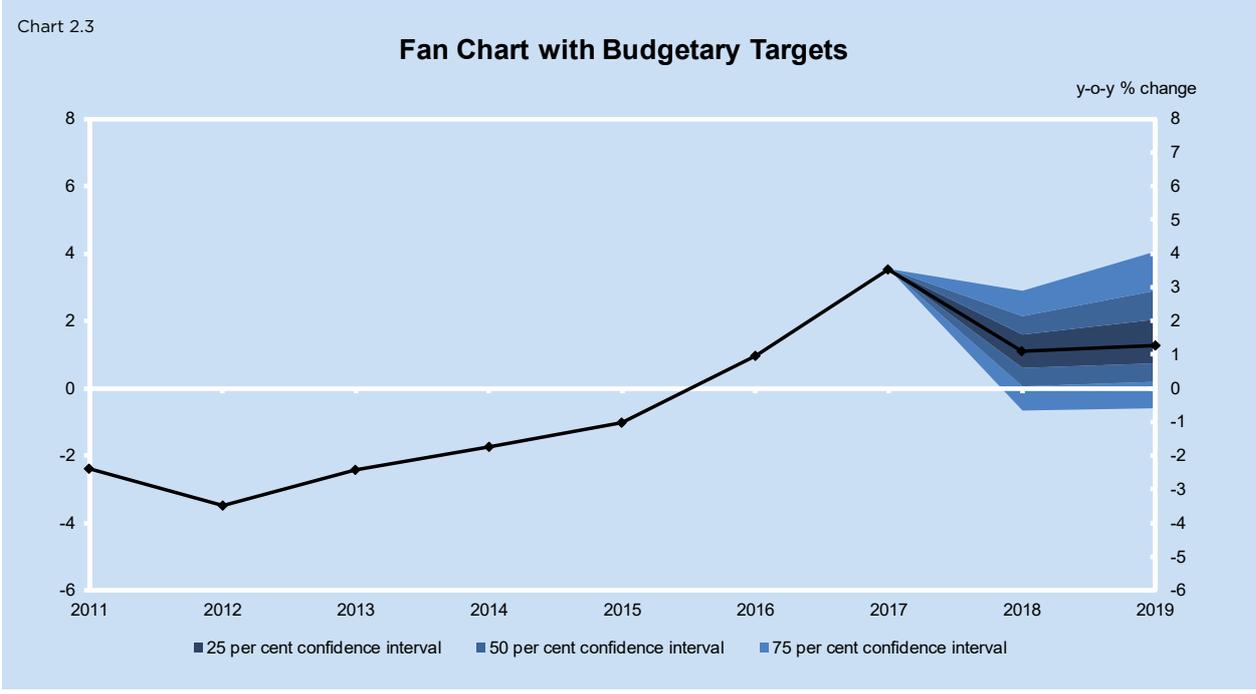
The uncertainty surrounding the macroeconomic projections is based on the past forecast error variance of GDP. This is equal to 2.2 for the current year forecast, and 3.1 for the one-year ahead forecast. The balance of risk is based on the Pearson skewness indicator of the model generating alternative forecast for GDP documented above. The indicator shows a rather balanced risk for 2018, but an upside risk for 2019. The result is consistent with the analysis of alternative model forecasts highlighted earlier. Chart 2.2 represents the uncertainty and the balance of risk surrounding the macroeconomic forecasts presented in this Draft Budgetary Plan.

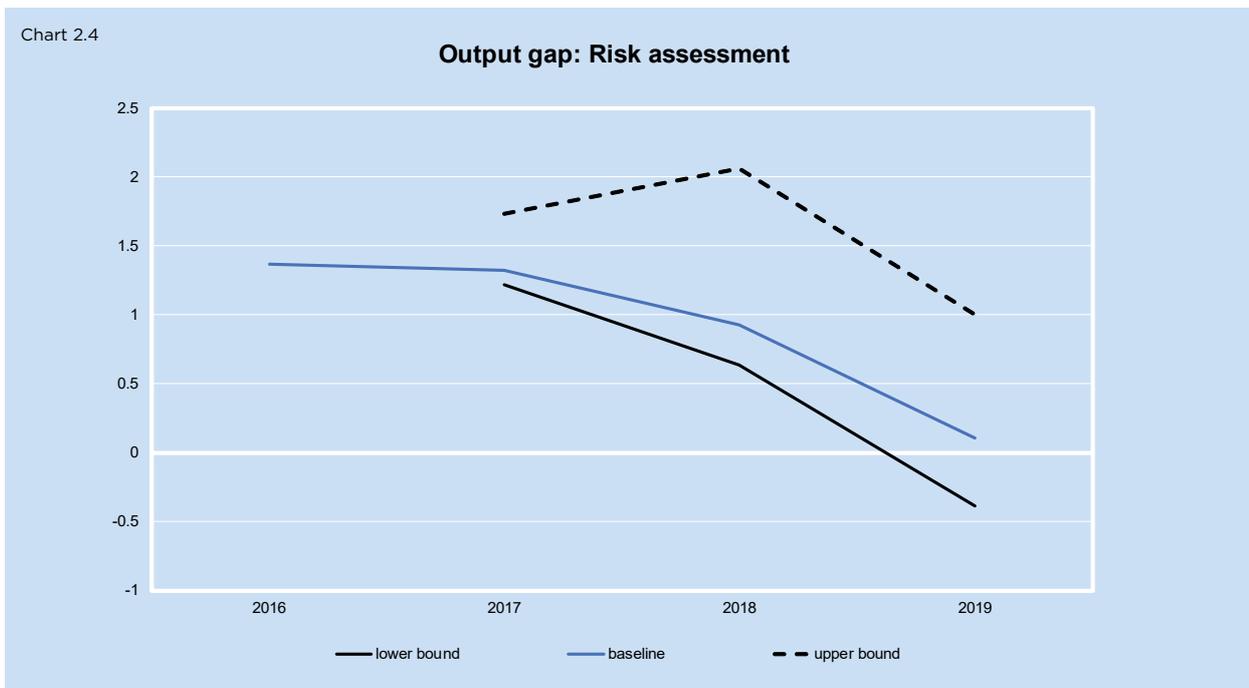
## **2.5.5 Risks to Fiscal Targets**

The alternative macroeconomic scenarios documented above can influence the attainment of the deficit targets thus underpinning alternative fiscal conditions. Chart



2.3 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 balanced risk for the attainment of the surplus target in 2018, while the balance of risk is on the





upside for 2019. Looking at point estimates, under the worst possible cyclical scenarios contemplated, the budget balance would remain in surplus for the period under review.

## 2.5.6 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 been carried out.

Compared to the baseline scenario, as shown in Chart 2.4, alternative output gap projections range from 0.6 in 2018 up to -0.4 in 2019 under the lower-bound scenario and from 2.1 in 2018 down to 1.0 in 2019 under the upper-bound scenario.

### Footnote:

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

**Macroeconomic forecasts**  
(Basic assumptions)

Appendix Table 0.i

	Data Source	2017	2018	2019
Short-term interest rate (annual average)	ECB	0.00	0.00	0.00
Long-term interest rate (annual average)	ECB	1.30	1.30	1.30
USD/€ exchange rate (annual average)	ECB + Consensus Economics (September 2018)	1.148	1.179	1.198
STG/€ exchange rate (annual average)	ECB + Consensus Economics (September 2018)	0.876	0.887	0.887
Real GDP Growth of main trading partners	Eurostat + Consensus Economics (September 2018)	2.0	1.8	1.7
Nominal GDP Growth of main trading partners	Eurostat + Consensus Economics (September 2018)	2.7	3.6	3.5
Oil prices (Brent, USD/barrel)	US Energy Information Administration (EIA) + Consensus Economics (September 2018)	54.20	72.10	72.20

**Macroeconomic forecasts**  
(Macroeconomic prospects)

Appendix Table 1.a		€ million CLV 2010 Prices	rate of change		
	ESA Code	2017	2017	2018f	2019f
<b>1. Real GDP<sup>(1)</sup></b>	B1*g	9,553.3	6.7	5.8	5.3
<b>2. Potential GDP</b>			6.6	6.2	6.2
contributions:					
- labour			3.2	3.0	3.0
- capital			1.7	1.6	1.7
- total factor productivity			1.6	1.5	1.4
<b>3. Nominal GDP</b>	B1*g	11,139.7	9.4	7.7	7.7
<b>Components of real GDP</b>					
<b>4. Private final consumption expenditure<sup>(2)</sup></b>	P.3	4,558.8	3.7	5.6	4.1
<b>5. Government final consumption expenditure</b>	P.3	1,546.4	2.8	15.0	8.2
<b>6. Gross fixed capital formation</b>	P.51	1,847.2	-7.3	1.3	8.4
<b>7. Changes in inventories and net acquisition of valuables (% of GDP)</b>	P.52 + P.53		-0.8	0.7	0.7
<b>8. Exports of goods and services</b>	P.6	12,844.3	3.8	1.3	2.2
<b>9. Imports of goods and services</b>	P.7	11,260.9	-1.9	2.0	2.2
<b>Contributions to real GDP growth</b>					
<b>10. Final domestic demand</b>		7,952.4	0.4	5.4	5.0
<b>11. Changes in inventories and net acquisition of valuables</b>	P.52 + P.53		-1.5	1.4	0.0
<b>12. External demand</b>	B.11	1,583.4	7.8	-1.0	0.3

<sup>(1)</sup> 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.

<sup>(2)</sup> Includes NPISH final consumption expenditure.

**Macroeconomic forecasts**  
(Price developments)

Appendix Table 1.b	Index <sup>(1)</sup>	rate of change			
	ESA Code	2017	2017	2018f	2019f
<b>1. GDP deflator</b>		116.6	2.6	1.8	2.2
<b>2. Private consumption deflator</b>		110.0	1.0	0.7	1.0
3. HICP		102.2	1.3	1.7	1.9
4. Public consumption deflator		112.9	1.7	3.5	1.9
5. Investment deflator		122.4	2.2	3.6	2.2
<b>6. Export price deflator (goods and services)</b>		117.4	3.4	3.3	1.8
<b>7. Import price deflator (goods and services)</b>		114.7	2.5	3.3	1.9

<sup>(1)</sup> Index (base 2010 unless otherwise indicated)

**Macroeconomic forecasts**  
(Labour market developments)

Appendix Table 1.c	€000s	rate of change			
	ESA Code	2017	2017	2018f	2019f
<b>1. Employment, persons<sup>1</sup></b>		218.0	4.0	5.0	3.7
2. Employment, hours worked <sup>2</sup>		440,335.9	4.0	5.0	3.7
<b>3. Unemployment rate (%)<sup>3</sup></b>			4.6	4.0	4.1
<b>4. Labour productivity, persons<sup>4</sup></b>		43.8	1.4	0.8	1.4
5. Labour productivity, hours worked <sup>5</sup>				0.8	1.4
<b>6. Compensation of employees</b>	D.1	4,583.4	7.1	8.0	6.6
<b>7. Compensation per employee</b>		21.0	1.8	2.9	2.9

<sup>1</sup> National accounts definition.

<sup>2</sup> National accounts definition.

<sup>3</sup> Harmonised definition, Eurostat; levels.

<sup>4</sup> Real GDP per person employed.

<sup>5</sup> Real GDP per hour worked.

**Macroeconomic forecasts**  
(Sectoral balances)

Appendix Table 1.d

% GDP

	ESA Code	2017	2018	2019
<b>1. Net lending/net borrowing vis-à-vis the rest of the world</b>	B.9	14.3	10.4	14.6
<i>of which:</i>				
- Balance on goods and services		19.8	16.0	16.8
- Balance of primary incomes and transfers		-6.1	-5.9	-2.3
- Capital account		0.6	0.3	0.1
2. Net lending/net borrowing of the private sector	B.9	9.7	8.1	12.8
3. Net lending/net borrowing of General Government	B.9	3.5	1.3	0.9
<b>4. Statistical discrepancy</b>		1.1	0.9	0.9

### **3. General Government Budgetary Developments**

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### 3. General Government Budgetary Developments

During the past five years, the Government has managed to successfully consolidate public finances, turning a deficit of 3.5 per cent of Gross Domestic Product (GDP) in 2012 to a surplus in the last two years. The gradual but consistent improvement in the budget balance positively impacted on the Government debt ratio which fell below the 60.0 per cent target in 2015 and has continued to decline in the last two years. These developments were primarily supported by a strong and sustainable rate of economic growth and growing primary surpluses.

Government considers the recent fiscal developments as an essential pillar of the sustainability of economic policies, while facilitating the recovery of the necessary fiscal space to allow fiscal policy to act in a countercyclical manner should the need arise. The achievement of the Medium-Term Objective (MTO) is also an important step in safeguarding the of 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 further strengthens potential growth and supports the process of convergence to higher living standards.

Against the background of persistent challenges and risks in the external environment, continued prudence in the fiscal targets and the creation of additional buffers are warranted. In this context, the 2019 Draft Budget targets a surplus net of Individual Investor Programme (IIP) and a structural surplus (also net of IIP). Indeed, the budget balance is targeted to reach 1.3 per cent of GDP in 2019, which also includes an allocation of around 3.5 per cent of GDP towards gross fixed capital formation in 2019. These investments do not include additional investment devoted to the improvement of human capital to meet the challenges of a changing economy, which are generally classified elsewhere in the European System of Accounts (ESA) categorisation. Meanwhile, the debt ratio is also expected to decrease by 3.1 percentage points of GDP to 43.8 per cent of GDP in 2019. Further improvements in the underlying debt dynamics are expected to be secured through positive growth prospects, sustained investor confidence, and an efficient and effective debt management system.

The Budget outlined for 2019 builds on the achievements of the previous Budgets of this administration, while also outlining new initiatives on infrastructure and other social investments in a context of higher living standards, improving on social justice and a more inclusive society that cares for those in need and accepts increased social diversity. In the forthcoming year's budget, the Government will continue to address new challenges brought by economic prosperity, while at the same time addressing social obligations. In the 2019 Budget and over the coming years, the Government will continue to ensure that the environment is better protected with increased uses 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, thus further strengthening potential growth and supporting the process of convergence to higher living standards. Backed by a stronger economy, the Maltese Government endeavours to guarantee and improve the income and care for

senior citizens and people with disability, people at risk of poverty and those materially deprived, including through higher investment in social housing and creating pathways towards affordable housing.

This Chapter provides an analysis of planned developments in revenue, expenditure and debt during 2019, including details of the main discretionary measures underpinning the expenditure and revenue targets for 2019, and is based on the ESA 2010 methodology. Indeed, data provided in this Chapter covers the General Government sector, which is composed of the central and local Government subsectors. In turn, the central Government subsector comprises the operations of Government Ministries and Departments and of Extra Budgetary Units (EBUs). Appendix Table 6b provides a list of established EBUs as at 31 December 2017.

### 3.1 Budgetary Targets

Revisions were carried out to the components of both revenue and expenditure for 2019, compared to the projections outlined in the Medium-Term Fiscal Strategy (MTFS). Indeed,

<b>Budgetary Targets</b>			
(General Government budgetary targets broken down by subsector)			
Table 2.a		% GDP	
	ESA Code	2018	2019
<b>Net lending (+) / net borrowing (-) by sub-sector<sup>1</sup></b>	B.9		
<b>1. General Government</b>	S.13	1.1	1.3
<b>2. Central Government</b>	S.1311	1.1	1.3
<b>3. State Government</b>	S.1312	-	-
<b>4. Local Government</b>	S.1313	-0.0	-0.0
<b>5. Social security funds</b>	S.1314	-	-
<b>6. Interest expenditure</b>	D.41	1.6	1.5
<b>7. Primary balance<sup>2</sup></b>		2.7	2.7
<b>8. One-off and other temporary measures<sup>3</sup></b>		0.0	0.0
<b>9. Real GDP growth (%) (=1 in Table 1.a)</b>		5.8	5.3
<b>10. Potential GDP growth (%) (=2 in Table 1.a)</b>		6.2	6.2
<b>11. Output gap (% of potential GDP)</b>		0.9	0.1
<b>12. Cyclical budgetary component (% of potential GDP)</b>		0.4	0.0
<b>13. Cyclically-adjusted balance (1 - 12) (% of potential GDP)</b>		0.6	1.2
<b>14. Cyclically-adjusted primary balance (13 + 6) (% of potential GDP)</b>		2.3	2.7
<b>15. Structural balance (13 - 8) (% of potential GDP)</b>		0.6	1.2

<sup>1</sup> TR-TE= B.9.

<sup>2</sup> The primary balance is calculated as (B.9) plus (D.41, item 6).

<sup>3</sup> A plus sign means deficit-reducing one-off measures.

**Budgetary Targets**  
(General Government debt developments)

Table 2.b	% GDP	
	2018	2019
<b>1. Gross Debt<sup>(1)</sup></b>	46.9	43.8
<b>2. Change in gross debt ratio</b>	-4.0	-3.1
<b>Contribution to changes in gross debt</b>		
<b>3. Primary Balance</b>	-2.7	-2.7
<b>4. Interest Expenditure</b>	1.6	1.5
<b>5. Stock-flow adjustment</b>	0.7	1.6
<b>p.m. Implicit interest rate on debt<sup>(2)</sup></b>	3.4	3.3

<sup>(1)</sup> As defined in Regulation 479/2009

<sup>(2)</sup> Proxied by interest expenditure divided by the debt level of the previous year

in 2019, in view of the relatively similar macroeconomic growth composition yet more representative elasticity assumptions, and a higher expected turnout in 2018, higher proceeds are expected from taxation. On the expenditure side, higher than expected outlays on compensation of employees, intermediate consumption, and social payments are anticipated, and to a lesser extent, higher capital expenditure. On account of these revisions, in 2019, the budget balance is targeted to increase marginally to 1.3 per cent of GDP. In structural terms, the General Government balance is expected to increase from 0.6 per cent in 2018 to 1.2 per cent in 2019. General Government budgetary targets are outlined in Table 2a.

The General Government gross debt ratio is expected to decrease by 4.0 percentage points of GDP in 2018 and by a further 3.1 percentage points in 2019, reaching 43.8 per cent of GDP, 16.2 percentage points below the European Commission's 60 per cent Maastricht threshold. In particular, the positive impact of nominal growth and the projected primary surplus will more than offset the upward pressure that the interest burden and the stock flow adjustment are expected to have on the debt ratio. The stock-flow adjustment, is mainly due to the contribution to the Malta Government Stock sinking fund. Additionally, in 2018 part of the positive stock flow is attributed to the positive balance in the IIP which does not feature in the Central Government Deficit. Developments in gross Government debt are presented in Table 2b.

A detailed account of the Stock-Flow adjustments can be found in Appendix Table 7.

### 3.1.1 Discretionary Measures

A list of the main discretionary measures included in the Draft Budgetary Plan and underpinning the expenditure and revenue targets for 2019 are presented in Table 5.a. The net impact on the budget balance of temporary and permanent discretionary revenue measures for 2019 (including those implemented in previous budgets but which will still have an impact in 2019) is estimated at -0.8 per cent of GDP. Meanwhile, incremental discretionary expenditure measures (including those implemented in previous budgets but which will still have an impact in 2019), are expected to have a negative impact on the budgetary balance of 2019 of -0.3 per cent of GDP.

In the Budget for 2019, the Maltese Government continues to be committed to the principle that economic prosperity and wealth should be felt and enjoyed by all. Indeed, the Budget is introducing measures addressing the following:

1. Sustaining investment in road infrastructure;
2. A number of family supporting measures relating to housing, pensions, school transport, disabilities and other social needs;
3. Measures intended to minimise waste generation;
4. Enhance economic diversification.

The annual contribution to the 'Contingency Reserve' account is expected to increase to €12.9 million in 2019.

### 3.2 Expenditure and Revenue Projections under the No Policy Change Scenario

In 2019, tax revenue is expected to broadly follow economic developments. Tax revenues are expected to grow by around 9 per cent, with an implied elasticity of tax revenue to GDP under the no-policy change scenario estimated at 1.2. This is supported by historical developments in elasticity estimates for revenue components relative to their respective tax base. As a result, the tax burden would increase by 0.3 of a percentage point to 34.2 per cent of GDP under a no-policy change scenario, as shown in Table 3. This development mainly reflects a higher ratio for current taxes on income, in part offset by a marginal decline in the ratios to GDP of social contributions and of taxes on production and imports, as the ratio to GDP of capital taxes is expected to remain relatively stable. At unchanged policies, 'other revenue' would increase marginally by 0.2 of a percentage point of GDP.

At unchanged policies, total expenditure would decline from 38.4 per cent of GDP in 2018 to 37.5 per cent in 2019. Social payments as a share of GDP would decrease by 0.4 percentage points, primarily reflecting low inflationary developments as well as measures legislated in previous years encouraging further participation in the labour market. The decline in the expenditure to GDP ratio is also set to come from a decline in capital transfers by 0.3 of a percentage point of GDP. It is nevertheless worth noting that in 2018, this item of expenditure included €63.5 million or 0.5 per cent of GDP primarily for the capitalisation of Malta Air Travel Ltd (MAT Ltd) for the purchase of Air Malta's landing slots which will not be repeated in 2019. Meanwhile, at unchanged policies, compensation of employees as a share of GDP would decrease by 0.1 percentage points, mainly as a result of a lower wage growth compared to GDP growth, as well as

### Discretionary measures taken by General Government

Table 5.a

List of measures	Detailed description	Target (Expenditure / Revenue component) ESA Code	Accounting principle	Adoption Status	Introduced in Budget for...	Incremental Budgetary Impact	
						2018 % of GDP	2019 % of GDP
VAT	Impact from VAT directive on electronic commerce	D2 - R	Accruals	Permanent & Adopted	2019	0.00	-0.12
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	0.00
Personal income tax	Change in income tax thresholds for low income earners, including pensioners	D5 - R	Accruals	Permanent & Adopted	2017 - 2019	-0.04	-0.01
	Fiscal incentives for private pensions	D5 - R	Accruals	Permanent & Adopted	2015 - 2019	0.00	-0.01
Individual Investor Programme (IIP)	Revenue from the Individual Investor Programme	P10 - R	Accruals	Permanent & Adopted	2014	-0.65	-0.60
Other revenue measures legislated in previous budgets			Accruals	Permanent & Adopted		-0.09	-0.05
EU Presidency	Intermediate consumption in respect of Malta's EU Council Presidency in 2017	P2 - E	Accruals	Permanent & Adopted	2016 - 2017	0.24	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	0.08	-0.02
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	0.02
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	-0.07	-0.14
School transport	Extension of the school transport network to children in independent and church schools	D6 - E	Accruals	Permanent & Adopted	2018 - 2019	-0.04	-0.11
Tax relief measure		D6 - E	Accruals	Permanent & Adopted	2018 - 2019	-0.10	0.01
Compensation payments		D7 - E	Accruals	Permanent & Adopted	2017 - 2019	-0.01	0.05
Other expenditure measures legislated in previous budgets			Accruals	Permanent & Adopted		-0.13	-0.07
						<b>-0.82</b>	<b>-1.06</b>

the planned recruitment as envisaged in the Ministries and Departments' Business and Financial Plans, including HR Plans, within the parameters of the approved budgetary estimates. Against the background of historically low interest rates, interest expenditure is also expected to decline by 0.1 of a percentage point of GDP. Such declines are expected to be in part offset by higher gross fixed capital formation, in order to address the infrastructural bottlenecks and further investments in human capital and technology outlined in this Chapter.

### 3.3 Expenditure and Revenue Targets

General Government expenditure and revenue targets are presented in Table 4a. Both the revenue and expenditure ratios to GDP are expected to decline marginally in 2019, although a more pronounced decline in expenditure is expected to result in an improvement in the budget surplus by 0.2 of a percentage point of GDP.

Total revenue is expected to decline by 0.3 of a percentage point to 39.1 per cent of GDP in 2019 as a higher tax revenue ratio is expected to be in part offset by lower property income and 'other' revenue, the latter primarily reflecting lower market output. The marginal decline in the ratio of taxes on production and imports by 0.2 of a percentage point of GDP reflects the loss in retained revenue during the transitory period of the regulation on Value Added Tax (VAT) on electronic services, as well as the extension of ongoing measures targeting stamp duty. The ratio of current taxes on income and

**Expenditure and Revenue Projections under the no-policy change scenario <sup>1</sup>**  
(General Government expenditure and revenue projections at unchanged policies  
broken down by main components)

Table 3

% GDP

	ESA Code	2018	2019
<b>General Government (S13)</b>			
<b>1. Total revenue at unchanged policies</b>	TR	39.4	39.7
<i>Of which:</i>			
1.1. Taxes on production and imports	D.2	12.7	12.6
1.2. Current taxes on income, wealth, etc	D.5	14.5	15.0
1.3. Capital taxes	D.91	0.2	0.2
1.4. Social contributions	D.61	6.3	6.2
1.5. Property income	D.4	0.7	0.5
1.6. Other <sup>2</sup>		5.0	5.2
<b>p.m.: Tax burden</b>		33.9	34.2
<i>(D.2+D.5+D.61+D.91-D.995)<sup>3</sup></i>			
<b>2. Total expenditure at unchanged policies</b>	TE <sup>3</sup>	38.4	37.5
<i>Of which:</i>			
2.1. Compensation of employees	D.1	11.5	11.4
2.2. Intermediate consumption	P.2	6.9	6.9
2.3. Social payments	D.6M	10.1	9.7
of which Unemployment benefits <sup>4</sup>		0.3	0.3
2.4. Interest expenditure	D.41	1.6	1.5
2.5. Subsidies	D.3	1.4	1.4
2.6. Gross fixed capital formation	P.51	3.3	3.5
2.7. Capital transfers	D.9	1.5	1.2
2.8. Other <sup>5</sup>		2.1	2.0

<sup>1</sup> Data for 2018 (current year) is equivalent to the data presented in Table 4.a. The no-policy change scenario for the forthcoming year (2019) involves the extrapolation of revenue and expenditure trends after deducting the impact of temporary measures of the current year and before adding the impact of the measures included in the forthcoming year's budget.

<sup>2</sup> P.10 + D.39rec + D.7rec + D.9rec (other than D.91rec).

<sup>3</sup> Tax revenue, including those collected by the EU and including an adjustment for uncollected taxes and social contributions D.995), if appropriate.

<sup>4</sup> Includes cash benefits (D.621 and D.624) and in kind benefits (D.632) related to unemployment benefits.

<sup>5</sup> D.29pay + D.4pay (other than D.41pay) + D.5pay + D.7pay + P.5M + NP + D.8.

wealth is expected to increase by 0.5 of a percentage point of GDP, mainly on account of the lagged effects on income tax revenue from strong increases in corporate profits registered in previous years. Meanwhile, a lower ratio to GDP of property income from 0.7 per cent in 2018 to 0.5 per cent in 2019 is primarily on account of lower anticipated profits from the Central Bank of Malta and lower dividends from public listed companies.

Alongside lower capital transfers, which are expected to decline by 0.3 of a percentage point of GDP, moderate declines of 0.1 of a percentage point of GDP each for compensation of employees, interest, social payments and 'other' expenditure as a share of GDP are expected to more than offset higher gross fixed capital formation. Increases in capital expenditure will be devoted to roads, the environment, health and education, and include higher infrastructure expenditure financed from both the European Union and local funds.

### Expenditure and Revenue Targets

(General Government expenditure and revenue targets, broken down by main components)

Table 4.a % GDP

	ESA Code	2018	2019
<b>General Government (S13)</b>			
<b>1. Total revenue target</b>	TR	39.4	39.1
<i>Of which:</i>			
1.1. Taxes on production and imports	D.2	12.7	12.5
1.2. Current taxes on income, wealth, etc	D.5	14.5	15.0
1.3. Capital taxes	D.91	0.2	0.2
1.4. Social contributions	D.61	6.3	6.2
1.5. Property income	D.4	0.7	0.5
1.6. Other <sup>1</sup>		5.0	4.7
<b>p.m.: Tax burden</b>		33.9	34.1
(D.2+D.5+D.61+D.91-D.995) <sup>2</sup>			
<b>2. Total expenditure target</b>	TE <sup>3</sup>	38.4	37.8
<i>Of which:</i>			
2.1. Compensation of employees	D.1	11.5	11.4
2.2. Intermediate consumption	P.2	6.9	6.9
2.3. Social payments	D.6M	10.1	10.0
of which Unemployment benefits <sup>3</sup>		0.3	0.3
2.4. Interest expenditure (= item 6 in Table 2.a)	D.41	1.6	1.5
2.5. Subsidies	D.3	1.4	1.4
2.6. Gross fixed capital formation	P.51G	3.3	3.6
2.7. Capital transfers	D.9	1.5	1.2
2.8. Other <sup>4</sup>		2.1	2.0

<sup>1</sup> P.10 + D.39rec + D.7rec + D.9rec (other than D.91rec).

<sup>2</sup> Tax revenue, including those collected by the EU and including an adjustment for uncollected taxes and social contributions D.995), if appropriate.

<sup>3</sup> Includes cash benefits (D.621 and D.624) and in kind benefits (D.632) related to unemployment benefits.

<sup>4</sup> D.29pay + D.4pay (other than D.41pay) + D.5pay + D.7pay + P.5M + NP + D.8.

**Expenditure and Revenue Targets**  
(Amounts to be excluded from the expenditure benchmark)

Table 4.b % GDP

	2017	2017	2018	2019
	Level (€ millions)			
<b>1. Expenditure on EU programmes fully matched by EU funds revenue</b>	69.5	0.6	1.4	1.6
<b>1.a of which 'Investment fully matched by EU funds revenue</b>	49.5	0.4	0.8	1.0
<b>2. Cyclical unemployment benefit expenditure <sup>1</sup></b>	-0.7	-0.0	0.0	0.0
<b>3. Effect of discretionary revenue measures <sup>2</sup></b>	85.3	0.6	-0.8	-0.8
<b>4. Revenue increases mandated by law</b>	-	-	-	-

<sup>1</sup> The cyclical unemployment benefit expenditure is calculated by multiplying the gap between the Non-Accelerating Wage Rate of Unemployment (NAWRU) and the unemployment rate (expressed in terms of the unemployment rate) by the total unemployment benefit expenditure. Data for the NAWRU and the unemployment rate is obtained from the latest update of the AMECO Database, while data for the total unemployment benefit expenditure is as defined in COFOG under the code 10.5.

<sup>2</sup> Revenue increases mandated by law is not included in the effect of discretionary revenue measures: data reported in rows 3 and 4 are mutually exclusive.

**Divergence from latest SP**

Table 7 % GDP

	ESA Code	2017	2018	2019
<b>Target General Government net lending/ net borrowing</b>	B.9			
<b>Stability Programme</b>		3.9	1.1	0.9
<b>Draft Budgetary Plan</b>		3.5	1.1	1.3
<b>Difference</b>		-	-	0.3
<b>General Government net lending projection at unchanged policies</b>	B.9			
<b>Stability Programme</b>		3.9	2.7	2.6
<b>Draft Budgetary Plan</b>		3.5	1.1	2.2
<b>Difference <sup>1</sup></b>		-	-1.6	-0.4

<sup>1</sup> This difference refer to both deviations stemming from changes in the macroeconomic scenario and those stemming from the effect of policy measures taken between the submission of the SP and the submission of the DBP. Differences are also due to the fact that the no-policy change scenario is defined differently for the purpose of this Code of Conduct with respect to the Stability Programme.

## Stock Flow Adjustment Statement

Appendix Table 7

€ million

	2018	2019
<b>Deficit (ESA)</b>	<b>-127.0</b>	<b>-165.0</b>
ESA Adjustments	116	131.7
Contribution to Sinking Fund (Local)	-89.4	0.0
Contribution to Sinking Fund (Foreign)	0.1	0.0
Contribution to Special MGS Sinking Fund	50.0	50.0
Equity Acquisition	65.9	10.6
EFSF/ESM Credit Line Facility	4.5	4.5
Stock Premium paid to Church	0.7	1.4
Sale of Assets	-0.9	-0.9
Sale of Non-Financial Assets	-	-
EBUs	-3.9	0.0
Currency	9.7	8.2
Movement in Bank Account	-3.5	-
Other Statistical Discrepancies	-	-
Increase/(Decrease) in cash balance	-7.9	-0.2
<b>Increase/(Decrease) in Non-Consolidated Debt</b>	<b>14.3</b>	<b>40.3</b>
<i>MGS Consolidation</i>	<i>-60.2</i>	<i>-4.9</i>
<b>Increase/(Decrease) in Consolidated Debt</b>	<b>-45.9</b>	<b>35.4</b>
<b>SFA</b>	<b>81.1</b>	<b>200.4</b>

**Indications on how the measures in the DBP address CSR and  
the targets set by the Union's Strategy for growth and jobs  
CSR recommendations**

CSRs	Relevant measures
<p><b>CSR 1: Strengthen the overall governance framework by enhancing the national supervision of internationally oriented businesses licensed in Malta, by ensuring the effective enforcement of the Anti-Money Laundering framework and by continuing to step up the fight against corruption.</b></p>	<p><b>During the year, various measures have been implemented to reinforce the overall governance framework, including the effective enforcement of the Anti-Money Laundering framework and measures earmarked to curtail corruption practices.</b></p> <p><i><u>Enhancing the national supervision of internationally oriented businesses licensed in Malta</u></i></p> <p>While the supervision of internationally-oriented businesses in the insurance, investment services and in the banking sectors can be challenging for a relatively small supervisory authority, the Malta Financial Services Authority (MFSA) is strengthening its human resource capacity and is also reviewing its IT systems in order to ensure continued rigorous supervision which can keep up with the technological developments in the financial services industry. In fact, an increase in personnel recruitment for the years 2018-2019 is envisaged with respect to the teams responsible for the authorisation, regulation and supervision of entities falling within the regulatory and supervisory remit of the MFSA.</p> <p>The European Insurance and Occupational Pensions Authority (EIOPA) issued a Decision on the collaboration of the insurance supervisory authorities, which is applicable to all Member States. In accordance with this Decision, where the applicant intends to operate exclusively (or almost exclusively) in another Member State, the MFSA engages with that Member State even at application stage in order to facilitate its understanding of the situation and the circumstances of the undertaking before the MFSA makes a decision on the authorisation.</p> <p>With regards to European Union (EU) cooperation, the local supervisor makes use of the EIOPA initiatives for National Competent Authorities cooperation and also participates in various insurance groups cross border Colleges of Supervisors. Besides, there are regular cooperation meetings and/or conference calls with the host supervisors, in particular with those host supervisors where Maltese insurance undertakings carry out significant activities.</p> <p>Following feedback from stakeholders to a consultation held in the second half of 2017, the Government of Malta proposed to amend the MFSA Act, to reflect the objective of reorganising the authority by separately and clearly framing both roles of regulation and supervision in the financial services sector. Greater levels of efficiency and effectiveness of the MFSA were called for during the consultation, in line with the views of international authorities.</p> <p>The amendments to the Act saw the creation of a Chief Executive Officer responsible for the MFSA's overall performance in terms of the achievement of its objectives and implementation of its strategy and policies as set out by the Board of Governors.</p> <p>At present, the Government of Malta is proposing further amendments to the MFSA Act (Bill no 49 of 2018) reflecting the proposed changes in the structure of the MFSA which are intended to strengthen the MFSA and to make it a more efficient, proactive and dynamic regulator.</p>

### Regulation and supervision of financial institutions

The MFSA is the single financial regulator in Malta responsible for the prudential regulation, monitoring and supervision of financial services in Malta. The Financial Intelligence Analysis Unit (FIAU), is the authority tasked with the monitoring and supervision of financial institutions and Designated Non-Financial Business and Professions (DNFBPs) for compliance with the AML/CFT requirements established under the Prevention of Money Laundering Act (PMLA) and the Prevention of Money Laundering and Funding of Terrorism Regulations (PMLFTR). The FIAU and MFSA have established common joint examination procedures to streamline the supervision methodology and are currently in the process of reviewing the Memorandum of Understanding (MoU) signed between them to reflect the recent developments in their cooperation.

Earlier this year, Government 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. The Maltese Authorities carried out the NRA during the course of 2017 on the basis of collaborative process involving all key stakeholders and using the World Bank National ML and TF Risk Assessment Tool.

The Strategy comprises seven key initiatives:

- Establish a national coordination mechanism responsible for defining the overall AML/CFT strategy and overseeing its implementation;
- Strengthen and clarify the supervisory framework by extending the breadth and depth of supervision and increasing resources;
- Enhance internal capabilities of the financial intelligence unit, especially in terms of staff number and training, access to additional databases and use of analytical tools;
- Enhance investigation and prosecution capabilities with increased resources, specialisation and tools, in order to improve the number of investigations and their translation into legal enforcement;
- Establish an effective asset recovery unit with a well-equipped agency dedicated to tracing, confiscating and managing assets;
- Increase transparency of legal entities and arrangements, in particular with regards to their beneficial ownership;
- Build on the existing international cooperation setup, in particular to improve the effective implementation of targeted financial sanctions and to raise the role of Malta's supervisors in international fora.

Financial Institutions are regulated and supervised for AML/CFT purposes. The FIAU is responsible for ensuring that subject persons comply with their AML/CFT obligations under the PMLA and the PMLFTR. The FIAU is assisted by the MFSA in the AML/CFT supervision of financial institutions that fall under the regulatory competence of the MFSA.

The FIAU and the MFSA are currently in the process of enhancing the ML/FT risk assessment procedures for financial institutions as well as other DNFBPs (namely trustees and company service providers). This will entail a complete overhaul of the current Annual Compliance Report (ACR) system, developing ACRs that are sector-specific and requiring more detailed information and data.

This will enable the FIAU and the MFSA to carry out more in-depth analysis. In 2017, the FIAU and the MFSA carried out an extensive data collection exercise on all credit institutions to strengthen the authorities' risk understanding of this sector and the respective operators, and the 2018 supervision plan factors in the results of this data collection exercise.

Apart from investing in its human resources, the FIAU has embarked on a project to strengthen its technical resources by acquiring and deploying a new software to upgrade the FIAU compliance databases. With this upgrade, the FIAU's Compliance Section will have at its disposal a fully automated risk tool through which it may rapidly assess and keep updated ML/FT risks within the sectors and individual subject persons it supervises. The new system will also provide a tool to support other qualitative analysis and will also serve as a portal for more effective communication with subject persons. The new compliance software is intended to be operational by the end of 2019 and technical meetings are currently underway between the Compliance Section and the contractor who is developing the system.

The MFSA continued to strengthen its anti-money laundering procedures with the publication of Guidance on Politically Exposed Persons (PEPs). This is another step in the MFSA's efforts to enhance AML supervision and tackle international challenges posed by money laundering in line with international best practice and commitments with international counterparts and supervisory bodies.

The Markets in Financial Instruments Regulation (MiFIR) and Markets in Financial Instruments Directive II (MiFID II) were transposed in 2017 and became applicable as from 2018. These frameworks strengthen the transparency and improve the functioning of the internal market for financial instruments through enhanced regulatory and supervisory convergence with respect to the requirements applicable to investment firms, trading venues, data reporting services providers and third country firms providing investment services or activities in the Union. The regulatory framework, as amended, shall improve transparency and supervisory oversight with the main changes inter alia including additional transaction reporting requirements and enhanced conduct of business rules. In turn, the increase in transparency generates investor confidence and allows the MFSA to maintain a healthier market integrity.

To be noted, that during September, the International Monetary Fund completed a Financial Sector Assessment Programme, a comprehensive and in-depth analysis of a country's financial sector. Furthermore, another review is to be carried out by the Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism (MONEYVAL) is being envisaged during the fourth quarter of 2018.

### **Ensuring the effective enforcement of the Anti-Money Laundering framework**

*Amendments to the Prevention of Money Laundering (PMLA) Act and the Prevention of Money Laundering and Funding of Terrorism Regulations (PMLFTR)*

In December 2017, Malta transposed the fourth Anti-Money Laundering Directive (AMLD IV) into national law, and now incorporates the latest Financial Action Task Force (FATF) Recommendations in the field of anti-money laundering and counter-terrorist financing. Amendments to the PMLA and PMLFTR were introduced in 2017 to transpose the 4<sup>th</sup> EU AML Directive and to strengthen the Maltese Anti-Money Laundering/Combating the Financing of Terrorism (AML/CFT) framework. A number of amendments were specifically aimed at enhancing the AML/CFT supervisory and enforcement regime, in particular:

- Amendments to Article 26 and Article 27 of the PMLA requiring the FIAU (as the main AML/CFT supervisor) to ensure that AML/CFT supervision is carried out on a risk-sensitive basis and to further strengthen the co-operation between Maltese supervisory authorities on AML/CFT supervision, by specifically providing for the carrying out of joint (on-site and off-site) AML/CFT supervisory examinations between Maltese supervisory authorities (namely the FIAU, the MFSA and the Malta Gaming Authority (MGA)).
- Amendments to Article 13(3), 13(4), 16(1)(k), and 27(1) of the PMLA enhance the level of international cooperation on supervisory matters between the FIAU and foreign regulators/supervisors. Among others, these include an express obligation requiring the FIAU to notify the relevant European Supervisory Authorities of any administrative sanctions imposed on subject persons and the responsibility enabling the FIAU to co-operate with foreign supervisory authorities to co-ordinate the imposition of administrative penalties in cross-border cases of AML/CFT infringements, apart from a general power to cooperate with foreign regulatory and supervisory authorities upon request or on the FIAU's own instructions.
- An overhaul and significant strengthening of the sanctioning measures for AML/CFT breaches aligning Regulation 21 of the PMLFTR to the requirements envisaged under Section 4 of the 4<sup>th</sup> EU Anti-Money Laundering Directive. The revised Regulation 21 which came into force on the 1<sup>st</sup> January 2018, provides for the imposition of administrative sanctions which may range from a reprimand in writing or a minimum penalty of €250 up to a maximum of €46,500. The Regulation enables the FIAU to impose heftier penalties in the case of breaches considered to be serious, repeated or systematic, in particular:
  - (i) where the subject person committing such contravention carries out a relevant activity (hence a DNFBP), penalties of up to €1,000,000 or twice the amount of the benefit derived from the breach (where the benefit can be quantified) may be imposed; and
  - (ii) where the subject person committing such contravention carries out a relevant financial business (hence financial institutions) the maximum penalty that may be imposed increases up to €5,000,000 or 10 per cent of the total annual turnover of the institution.

#### Malta Police Anti-Money Laundering Squad

The Malta Police Anti-Money Laundering Squad is the unit in charge of investigating and prosecuting cases involving money laundering and funding of

terrorism. It receives reports directly from FIAU or other Police Units and carries out its investigations using a number of legal tools and powers.

The Police Anti-Money Laundering Squad works very closely with various authorities and institutions, including the FIAU, the MFSA, the Attorney General's Office, the Law Courts, the Malta Secret Service and all the licensed financial institutions.

The Malta Police cooperate and exchange information with counterparts using both formal (INTERPOL, EUROPOL and SIRENE (SIENA)), and other informal networks (such as, CARIN and Swedish Initiative). Malta is signatory to all EU Directives in this respect. The Malta Police can also exchange information with foreign liaison officers that are assigned to foreign missions/embassies in Malta.

#### Beneficial ownership information

The Companies Act (Register of Beneficial Owners) Regulations require every company to obtain and at all times hold adequate, accurate and up to date information in respect of beneficial owners. Furthermore, every company constituted in Malta, must also provide a declaration to the Registrar of Companies containing information on all the beneficial owners of the company. This beneficial ownership information is held in the Registry for Companies for new companies incorporated after the 1<sup>st</sup> January 2018 and will also become gradually available for other companies which were already incorporated before that date. Competent authorities, including the FIAU, the Malta Police and other authorities may access information on beneficial owners of companies held in the Registry of Companies.

Meanwhile, the Trusts and Trustees Act (Register of Beneficial Owners) Regulations, 2017 ("the Regulations") were published on 20 December 2017 by virtue of Legal Notice 373 of 2017. The provisions of these Regulations are aimed at implementing the relevant provisions on beneficial ownership information, emanating from article 31 of AMLD IV in so far as they are applicable to trusts and trustees. The provisions and requirements emanating from these Regulations came into force on 1 January 2018, other than the provisions of regulation 6 related to access to such beneficial ownership information, as the latter enter into force on 1 April 2018. Trustees authorised or registered in terms of the Trusts and Trustees Act were required to submit the beneficial ownership information of trusts which generate tax consequences, which were under their administration prior to the coming into force of the Regulations, by 1 July 2018. With respect to trusts which generate tax consequences for which the trustees were appointed to act as such following the coming into force of the said Regulations, trustees were required to submit the relevant beneficial ownership information within 14 days.

#### The National Coordinating Committee on Combating Money Laundering and Funding of Terrorism

AML/CFT policy development and implementation at national level is entrusted to the National Coordinating Committee on Combating Money Laundering and Funding of Terrorism (NCC), which was established by means of the National Coordinating Committee on Combating Money Laundering and Funding of Terrorism Regulations (NCC Regulations) on the 13 April 2018.

The Committee's functions are outlined in Article 12A(2) of the PMLA and Regulation 5 of the NCC Regulations and include the responsibility to:

- draw up a national strategy and policies to combat money laundering, the funding of terrorism and the financing of the proliferation of weapons of mass destruction;
- co-ordinate any action to be taken to develop, implement and review the national strategy and policies; including
- co-ordination of national risk assessments; and
- actions to be taken to address any threats, vulnerabilities and risks identified.

Regulation 5(1)(c) of the NCC Regulations moreover specifically tasks the NCC to conduct any necessary follow-up action to monitor and ascertain the effective implementation of the national strategy and policies and the actions intended to address any threats, vulnerabilities and risks identified following the carrying out of national risk assessments.

#### Asset recovery bureau

The Asset Recovery Bureau, which became operational in mid-2018, is entrusted with the efficient identification, tracing, collection, storage, preservation, management and disposal of proceeds of crime or property, in favour of Government. Moreover, the ARB aims at cooperating with local and foreign Competent Authorities as a means to strengthen the fight against corruption and other organised crime.

#### Voluntary Organisations (VOs)

Once amendments to the Act are enacted later on this year, the Voluntary Organisations Act will widen the functions and responsibilities of the Commissioner for Voluntary Organisations, who will be assigned the function to review periodically new information on the voluntary sector's potential vulnerabilities to money laundering and the funding of terrorism. Moreover, in case the Commissioner discovers facts or obtains information which raise suspicion that funds received by a voluntary organisation could be proceeds of criminal activity, or that the activities of a voluntary organisation could be related to money laundering or funding of terrorism, he shall promptly disclose the facts or that information, supported by any relevant documentation that may be available to him, to the FIAU.

#### Updates in the Gaming services

With effect from 1<sup>st</sup> January 2018, all gaming operators have become subject persons under the PMLFTR. In anticipation of this entry into force of new laws, the MGA has completed a sectoral ML/TF risk assessment of the gaming sector, as part of a National Risk Assessment for the Gaming Industry in Malta. The main ML/TF risks identified were:

- rogue remote gaming operators undertaking or facilitating (unknowingly) money laundering;
- industry targeted by players seeking to engage in money laundering;
- minimal face to face contact between operators and players;
- certain player account funding mechanisms may be interpreted as being riskier; and

- certain game types present higher risk;
- geographical market risk

The Authority has embarked on a number of initiatives in order to ensure that these risks are effectively mitigated:

- The Authority has enhanced its collaboration with the FIAU in order to ensure an effective AML/CFT framework with the required levels of co-ordination across public and private bodies. In this context, on the 19<sup>th</sup> of July 2018, the FIAU & MGA published the AML/CFT Implementing Procedures for the Remote Gaming Sector – Part 2;
- The Authority has established its own risk-based approach at regulation and supervision, with AML/CFT forming a crucial part of the risk analysis conducted on operators;
- The Authority has built a well-trained and skilled AML unit tasked with the monitoring of ‘Subject Persons’ in terms of AML/CFT compliance by executing offsite and onsite examinations;
- The Authority has also embarked on a number of initiatives aimed at reaching out to the industry on AML/CFT matters;
- The Authority had issued two questionnaires to gaming operators;
  - a controlled questionnaire and
  - a data questionnaire.

The results of these questionnaires will serve the authority to evaluate the risk of gaming operators and compile the Supervisory Plan for examining its operators jointly with FIAU

### **Continuing to step up the fight against corruption**

#### *Overview of the Key Legislative Developments*

Over the past years, the Government introduced reforms to strengthen good governance; targeting issues such as corruption, through inter alia the enhancement and further improvement of the quality, independence and efficiency of the national justice system, the regulation of political party financing, the safeguarding of whistle blowers, the removal of the prescriptive period over corruption offences committed by politicians, the regulation of public appointments, further regulation of judicial appointments and judicial accountability, the enactment of the Media and Defamation Act strengthening one’s freedom of expression as well as through the joining in on the establishment of the European Public Prosecutor’s Office (EPPO).

Since 2013, the Government of Malta has embarked upon an ambitious project intended to reform the national Justice system through a number of measures intended to address backlogs and to further facilitate access to Justice. This has been done through the extensive use of ICT technologies and e-Justice solutions intended to reduce bureaucracy and delays in the civil courts. Other reforms include the promotion of alternative methods of dispute resolution; through an increased number of members of the judiciary; an improved and accurate system of data collection and data analysis of the case load faced by our judiciary. In addition, the Department has introduced the adoption of a case-weighting system, the assignment of a full-time experienced lawyer (court attorney) with pre-defined performance indicators and the adoption of timeframes and performance indicators for all members of the judiciary; the extension and renovation of judicial

facilities to increase the number of halls to address the shortage of halls available in view to the constant increase in the number of sittings held; through a redistribution of duties within the judiciary itself - where two members of the judiciary were tasked to tackle pending case load without being assigned new cases until the pending case load was tackled according to timeframes and performance indicators; and through the establishment of a Commercial section of the Civil Court (which specialised Court shall be assigned applications falling within the competence of the Civil Court and which relate to matters regulated by the Companies Act).

Some of the key legislative and constitutional developments in Malta include:

- the removal of the prescription of corruption offences committed by politicians (as implemented through the Criminal Code (Amendment) Act and the Protection of the Whistleblower Act both enacted in 2013);
- the introduction of the right of appeal from decisions of the Attorney General on the choice of court in the case of arraignment for drug and money laundering crimes (enacted in 2014 through the Various Laws (Criminal Matter) (Amendment No 2) Act enacted in 2014);
- the enactment of the legal regulation of political party financing (through the Financing of Political Parties Act enacted in 2015);
- the enactment of the Media and Defamation Act in 2018 intended at updating and re-writing the Maltese law on libel and slander in a manner which strengthens respect for the right to freedom of expression in a substantial manner.

During 2016, the Government also adopted Act 44 of 2016, entitled 'Constitutional Reforms (Justice Sector) Act', which passed through Parliament on 20 July 2016. This Act seeks:

- to promote the separation of powers between the executive and the judiciary through a new system of judicial appointments;
- enhance the accountability of the judiciary as a result of the extension of disciplinary proceedings in case of breach of ethics; and,
- further uphold the independence of the judiciary through the introduction of an adequate pension scheme that honours the service of retired members of the judicial bench and their widows/ widowers.

In addition, this piece of legislation also makes provision for the setting up of two new Committees working under the remit of the Commission for the Administration of Justice, namely the:

- sub-Committee on the appointment of members of the Judiciary;
- sub-Committee on the discipline of the Judiciary (this sub-Committee is completely made up of sitting members of the Judiciary which are elected by the members of the Judiciary itself.)

The overall aim of the Act is to increase transparency in the method of appointment of members of the Judiciary and to increase the accountability of the members of the Judiciary. Recently, the Government also passed a law providing for pre-appointment parliamentary hearings with respect to important public appointments to Ambassadorships and to leading roles in regulatory authorities. Government has also implemented a set of regulations, through Legal Notice, principally aimed at ensuring notaries' good conduct and diligence during the performance of their duties. The Notaries' Code of Ethics adopts a holistic approach and is spread over five main Titles, dealing with Conduct and Diligence, Independence and Impartiality, Professional Relationships, Unlawful Competition and Professional Secrecy and Confidentiality. This would ensure high-quality

service to several Maltese and Gozitan individuals and families who resort to notaries' services in distinct life circumstances.

On 2 February 2018, Government enacted Act 2 of 2018 (Act amending the Public Administration Act). This Act is intended to provide for pre-appointment parliamentary hearings with respect to important public appointments to Ambassadorships and to leading roles in regulatory authorities. Pre-appointment hearings of persons nominated for certain public appointments will now be undertaken by the Committee on Public Appointments. This Committee shall be a Standing Committee which shall consist of seven members appointed by the House of Representatives of whom four shall be appointed by the Government, one of whom shall be appointed as Chairperson, and the other three shall be appointed by the Opposition.

#### *Permanent Commission Against Corruption*

The Permanent Commission Against Corruption is competent to investigate cases which fall under the thirteen articles of the Criminal Code specified in section 6 of Chapter 326. In addition, it may also investigate attempts, complicity and conspiracy when these are connected with the thirteen articles indicated. Twelve of the articles deal with the various forms of bribery – for example, bribery of Members of Parliament, of Members of the Judiciary, of court experts and other public officers (please refer to article 2 of Chapter 326). One article deals with abuse of power.

The Commission has dealt with a number of reports filed by private persons and has carried out its investigations in accordance with the provisions of Chapter 326. The main principles are secrecy, the observation of the rules of natural justice and reporting to the Minister responsible for Justice. Indeed, in its activity the Commission is guided by the application of the principle of 'beyond reasonable doubt'.

CSRs	Relevant measures
<p><b>CSR 2: Ensure the sustainability of the healthcare and the pension system, including by increasing the statutory retirement age and by restricting early retirement.</b></p>	<p><b>Over the years, Government has consistently sought to provide an efficient health care system which is free and is accessible to all, both at a regional and at national level.</b></p> <p>Primary Healthcare plays a key role in delivering better health; it represents the gateway to healthcare, supported by easy access to care and preventive services. The improvements of a number of health centres located around the Maltese Islands will strengthen access to healthcare at a community level. The continued modernisation will reflect the excellence of the service offered by contributing towards a cleaner and more hygienic environment. Indeed, the overarching intent is to ensure that primary care becomes the first choice of the patients thus relieving pressure on acute hospital services.</p> <p><i><u>The Introduction of the Southern Regional Hub – Paola</u></i></p> <p>The Southern Regional Hub will serve as a one-stop facility for community care, while offering specialised care for several prevalent diseases and conditions. This Hub will introduce within the Primary Healthcare several new outreach clinics and specialised services. It will also incorporate health promotion and disease prevention and will offer treatment for urgent minor conditions which do not require hospital services but are not easily treated by the family doctor in a small clinic or home setting. This Hub will also allow minor operations to be performed outside the main national hospital setting. The Primary Healthcare will thus be able to cater for the increasing demands in the southern region of Malta which has an average higher demand due to the socio-economic status of the habitants. The Southern Regional Hub is expected to become operational by 2023.</p>
	<p><i><u>Introduction of Electronic Patient Record System</u></i></p> <p>By 2020, the Primary Health Care Services will be introducing an Electronic Patient Record (EPR) system to replace the current paper-based methodology. The tender in this respect has already been adjudicated. This information communication technology (ICT) solution will enhance continuity of care and coordination between primary and secondary care as general practitioners would be able to access the patients’ records even when patients attend other health centres (other from theirs) and in the future, it would also be possible to access records of hospital attendances through interphasing.</p> <p>Through this modern ICT system, healthcare professionals will have updated patient information for the correct indication and administration of treatment. This system would also provide much more secure data protection than the present manual files which presently are also handled by patients. Access would also be password protected. The EPR system will also be able to provide analytical data on health services thereby allowing for timelier and more effective informed decision-taking in respect of current services and the introduction of new ones. In addition, it is expected that through the introduction and the utilisation of innovative ICT solutions, the cost of the healthcare service and the present administrative burden will markedly decrease, while the healthcare provision will considerably improve.</p>

	<p><b>Long-term sustainability</b></p>
	<p><b><i>Securing sustainability of the Pension system</i></b></p> <p>During 2018, the Family, Children’s Rights, and Social Solidarity (MFCS) established a Pension Strategy Group through the participation of the Ministry for Finance, and tasked the Group with the preparations for the 2020 Strategic Review. The Pension Strategy Group set up a number of working groups addressing matters such as pensions and divorce, demographics and fertility, pension economic modelling, review of voluntary pensions framework. As established by the Article 64B of the Social Security Act, the Government is to submit a report to the House of Representatives outlining recommendations for achieving further adequacy and sustainability in such a manner that a stable proportion is kept between contribution periods and periods in retirement by not later than December 2020.</p>
	<p><b><i>Diversifying Retirement Income</i></b></p> <p>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 also introduced. Accordingly, there are now a number of providers offering personal pension plans. 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).</p> <p>In the Budget for 2019, Government will seek to strengthen the fiscal incentives for private pension savings and voluntary occupational retirement pensions with a view to encourage further take-up of such products. Furthermore, Government has adopted the recommendations of the working group that over the course of the last year, studied the introduction of a regulatory framework for home equity release in Malta. The main elements of this framework shall be made public shortly.</p> <p><b><i>Strategy on Retirement and Financial Capability</i></b></p> <p>Following the post-consultation strategy on the National Strategy for Retirement Income and Financial Literacy, the Strategy on Retirement and Financial Capability was launched on 25<sup>th</sup> January 2017 and implementation initiated. A number of initiatives are underway – including:</p> <ul style="list-style-type: none"> <li>- design and piloting of a financial education Level 3 certification programme with the Malta Council for Arts, Science, and Technology (MCAST);</li> <li>- design of a long-term awareness education and knowledge campaign targeting 14 different target groups (self-employed, single parents, widows, divorcees, etc.);</li> <li>- design, together with the National Institute for the Maltese Language, a definitive glossary of financial terms in the Maltese language;</li> <li>- active knowledge, information, and tools dissemination on retirement and financial education through <a href="http://www.financialcapability.gov.mt">www.financialcapability.gov.mt</a>.</li> </ul>

***Further initiatives supporting Financial Literacy***

The Malta Stock Exchange is taking an increasingly active role in increasing the level of financial literacy by organising the Annual Investor Education Conference which was first held in 2015. The objective of these conferences is to provide educational information for the small investor. The 3rd and most recent Annual Investor Education Conference was held on 4 November 2017 in partnership with the MFSA.

MSE is also promoting financial education with the formation of the MSE Institute (MSEI). MSEI is a collaboration between MSE and Thomson Reuters and was inaugurated in 2016 in line with the strategy to improve the level of financial literacy for individual investors as well as industry practitioners. The Institute offers various courses on financial services at introductory, intermediate and advanced level as from January 2017. While the courses can be taken individually, participants have an opportunity to attain a Diploma in Securities and Portfolio Management.

## Extra Budgetary Units as at 31 December 2017

Appendix Table 6.b

	NACE CODE		NACE CODE
Appoġġ	88	Malta Philharmonic Orchestra	90
Arts Council Malta	90	Malta Resources Authority	84
Bord Tal-Koperattivi	84	Malta Statistics Authority	84
Broadcasting Authority	84	Malta Tourism Authority	84
Depositor Compensation Scheme	64	Manoel Theatre Management Committee	90
Environment and Resources Authority	84	Medicines Authority	84
Environment Protection Fund	84	Mental Health Services	87
Fort Security Services Ltd	84	MSE (Holdings) Ltd	64
Foundation for Educational Services	84	National Audit Office	84
Foundation for Medical Services	84	National Commission Persons with Disability	84
Foundation for Tomorrow's Schools	84	National Development and Social Fund	84
Gozo Ferries Co. Ltd	77	Occupational Health and Safety Authority	84
Grand Harbour Regeneration Corporation	71	Office of the Ombudsman	84
Heritage Malta	91	Planning Authority	84
Housing Authority	84	Projects Malta Ltd	84
Identity Malta	84	Projects Plus Ltd	84
International Institute on Ageing	85	Property Management Services	84
Investor Compensation Scheme	64	Protection and Compensation Fund	64
Jobsplus	78	Regulator for Energy and Water Services	84
Libyan Arab Maltese Holdings Ltd	64	Resources Support and Services Ltd	78
Malta College of Arts, Science and Technology	85	Sapport	88
Malta Communications Authority	84	Sedqa - Agency against Drug and Alcohol Abuse	88
Malta Competition and Consumer Affairs Authority	84	SportMalta	93
Malta Council for Economic and Social Development	84	St James Cavalier Creativity Centre	90
Malta Council for Science and Technology	84	Superintendence of Cultural Heritage	84
Malta Enterprise Corporation	84	The Rehabilitation Hospital Karin Grech	86
Malta Gaming Authority	84	Trade Malta Ltd	73
Malta Government Investments Ltd	84	University of Malta	85
Malta Government Technology Investments Ltd	84	Valletta 2018 Foundation	84
Malta Information Technology Agency	63	WasteServ Malta Ltd	38
Malta Investment Management Co. Ltd	84	Yachting Malta Ltd	73

Notes:

1. This list does not include entities which are already accounted for within the Departmental Accounting System (DAS) of Central Government.
2. General Classification of economic activities within the European communities. Industries are grouped into 64 categories (A64) based on NACE Rev 2.

## **4. Distributional Implications of Budget Measures**

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## 4. Distributional Implications of Budget Measures

The benefits arising from sustained economic growth are to be enjoyed by all strata in society, in particular, the most vulnerable groups. However, this is not always automatic and indeed it has been one of the key priorities in Government's programme to address social imbalances, enhance social justice and the making of a more inclusive society. In seeking to achieve these policy objectives, the Government reformed social security, creating incentives for claimants. The In-work benefits, the taper of benefits, free child care services and the breakfast club have provided the pathways for claimants to leave a system of welfare dependency and find employment. Secondly, the Government has, on a year by year basis, increased the minimum pension and has provided tax incentives that benefit those on low incomes. In creating the more inclusive society, it has also increased benefits for those with disability while increasing their opportunities to enter the labour market. Finally, the Government has also reformed the means test which has in turn increased eligibility for patients in need of free prescription drugs and other medical treatments.

The success of these measures in reducing poverty risks, social exclusion and income inequality can be confirmed by the latest SILC statistics which show that from 2013 onwards, the at-risk-of-poverty or social exclusion (AROPE) indicator, which is one of the main indicators used to measure inequality and social exclusion in a country, started to fall steadily. Additionally, the measure of the GINI coefficient remains rather stable and lower than the EU average.

The Budget of 2018 focused on addressing the new challenges brought about by the higher level of economic growth, in particular the need to invest and upgrade the existing infrastructure. The Budget for 2019 will seek to consolidate the achievements of recent years, balancing the need to support growth with social cohesion, while fostering a quality culture. This Chapter shall present an overview of the distributional implications of the Budget for 2019.

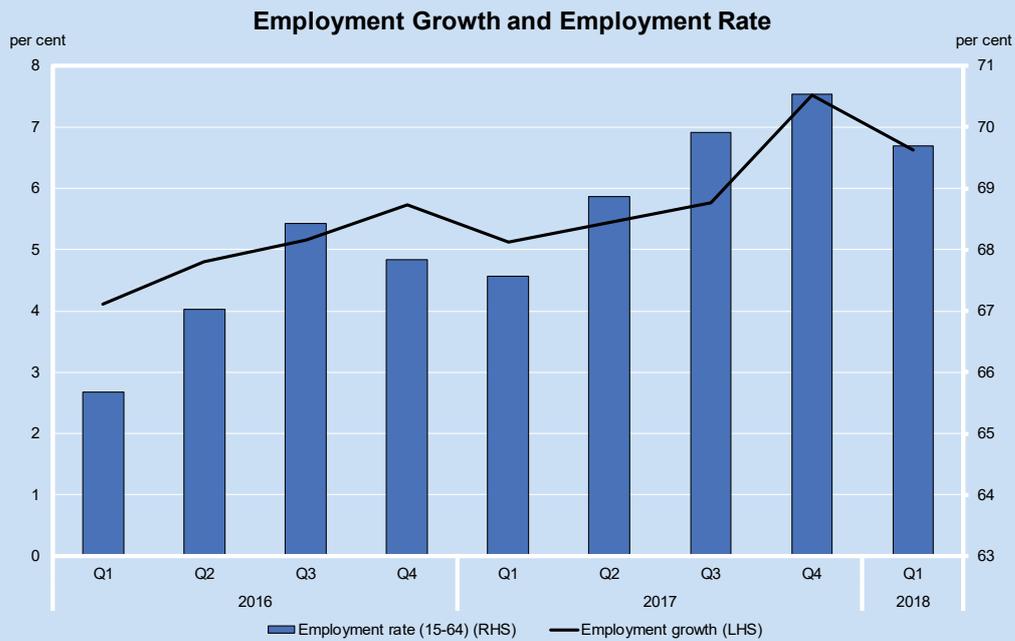
### 4.1 Government Initiatives in Recent Past Legislatures

Over recent years, Budgets sought to strengthen the pillars of the Maltese economy to enhance Malta's productivity and competitiveness potential by particularly focusing on two fronts. The Government has been systematically focused on raising potential output through infrastructural development, namely through reforms in the utility and energy sector and the transport network. Concurrently, the Government focused on strengthening the local workforce while encouraging the vulnerable groups in society to enter the labour market.

As a result, employment growth has been high, reflecting a job-rich economic growth. This was particularly evident in 2016 and 2017, when the number of people employed increased by around 11,000 persons (or 5.4 per cent) on average compared to the previous year. Employment growth remained solid in the first quarter of 2018 at 6.6 per cent.

The employment rate (15-64) during the first quarter of 2018 stood at 69.7 per cent. On average, out of every 100 persons aged between 25 to 54 years, 81 were employed. The male employment rate for this age bracket was 92.1 per cent while that for females was

Chart 4.1



Source: National Statistics Office

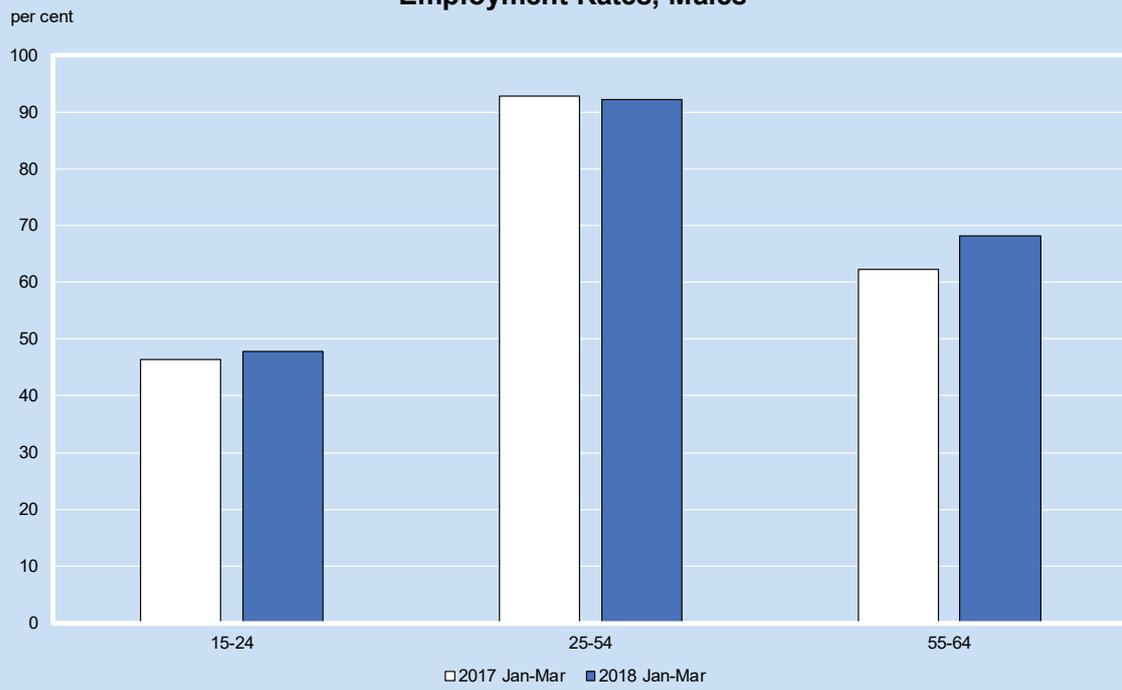
almost 69 per cent. The narrowest gender gap in the employment rate was recorded among persons aged between 15 and 24 years, with the gender employment rate gap increasing with age.

Measures of a social nature that have contributed towards the strengthening of the local workforce include reforms in social security benefits aimed at making work pay, initiatives that increase the female participation rate and measures that reduce households' expenses. These measures include the reduction in utility tariffs, provision of free childcare centres, the maternity leave fund, reductions in income tax rates, the widening of the non-taxable income bracket and extension of the in-work benefit, eligibility for sickness benefit for employed widows, adjustment in treatment of non-contributory benefits with respect to maintenance allowance to children and/or partners and the one-time tax-relief measure granted in 2018.

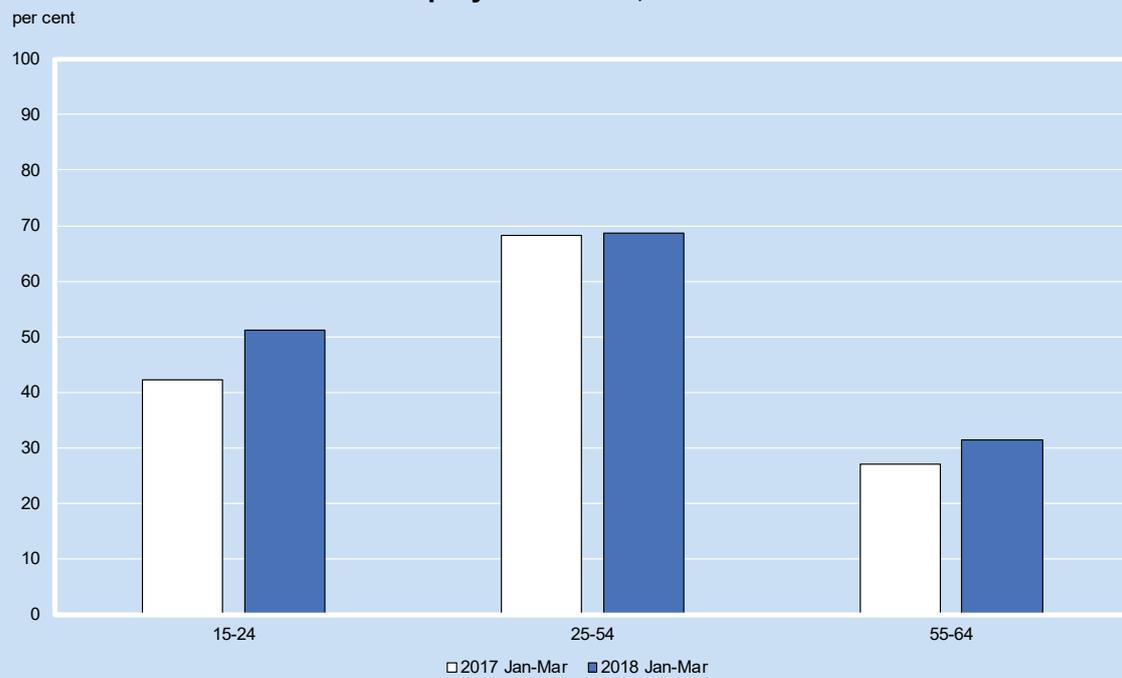
During 2018, following the April 2017 National Agreement between the Unions and employers on the Minimum Wage, employees will also benefit from increases in their minimum wage upon their completion of 12 months in employment. Employees are entitled to mandatory increases of €3.00 per week during the second year of employment, and upon completion of the second year, to an additional €3.00 per week. Employees earning more than the basic minimum wage will be entitled to the portion of increases during the second and third year of employment. The agreement also secures a supplement in the weekly Cost of Living Adjustment (COLA) of €1.00 per week for 2018 and 2019.

Chart 4.2

### Employment Rates, Males



### Employment Rates, Females



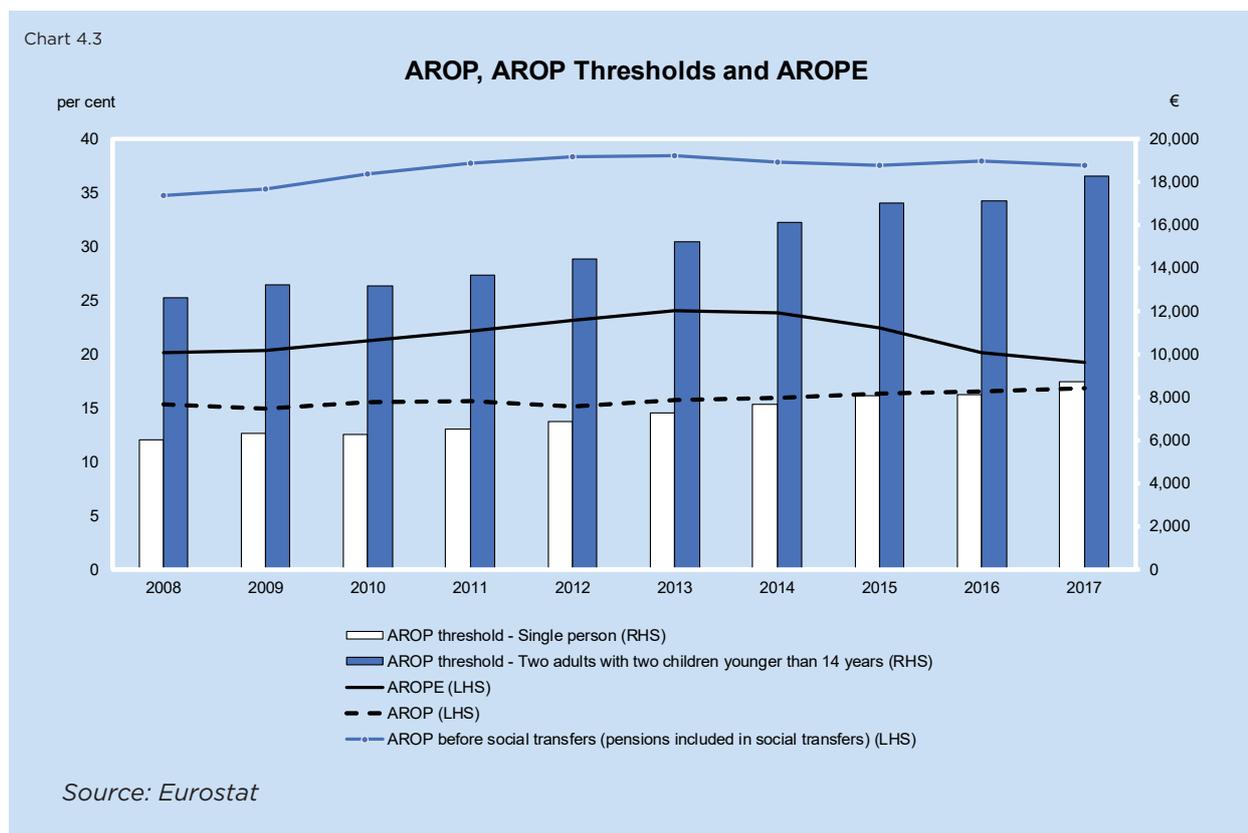
Source: National Statistics Office

## 4.2 Indicators measuring Poverty, Social Exclusion and Inequality

The at-risk-of-poverty or social exclusion (AROPE) indicator is one of the main indicators used to measure inequality and social exclusion in a country. Malta's AROPE maintained its downward trend since 2013, in reflection of labour market outcomes as well as tax-benefit reforms intended to enhance distributional outcomes. This indicator stood at 19.2 per cent for 2017 for Malta, which represents a drop of almost 1 percentage point in the rate when compared to the figure recorded in 2008. The decrease in the AROPE indicator rate is more evident when compared to 2015 figures, with the rate falling 3.2 percentage points from 22.4 per cent. Moreover, Malta's rate was more than 4 percentage points lower than the average European Union (EU) rate for 2016.

One of the elements encompassed within the AROPE indicator is the at-risk-of-poverty (AROP) indicator. This rate before social transfers stood at 37.5 per cent in 2017 for Malta, while the rate for the EU in 2016 stood at 44.5 per cent or 7 percentage points higher than the rate registered in Malta. The AROP rate resumed its downward trajectory, which began in 2013, and only interrupted by a slight increase registered in 2016.

Social transfers contributed to a drop of more than 20 percentage points in the AROP during 2017. At EU level, a more marked drop has been registered for 2016, with the AROP indicator including social transfers dropping a notable 27 percentage points. Malta's AROP rate after the inclusion of social transfers has been rising marginally over the past decade from the 15.3 per cent registered in 2008 to the rate of 16.8 per cent in 2017. Nonetheless, the AROP thresholds for economically-active households such

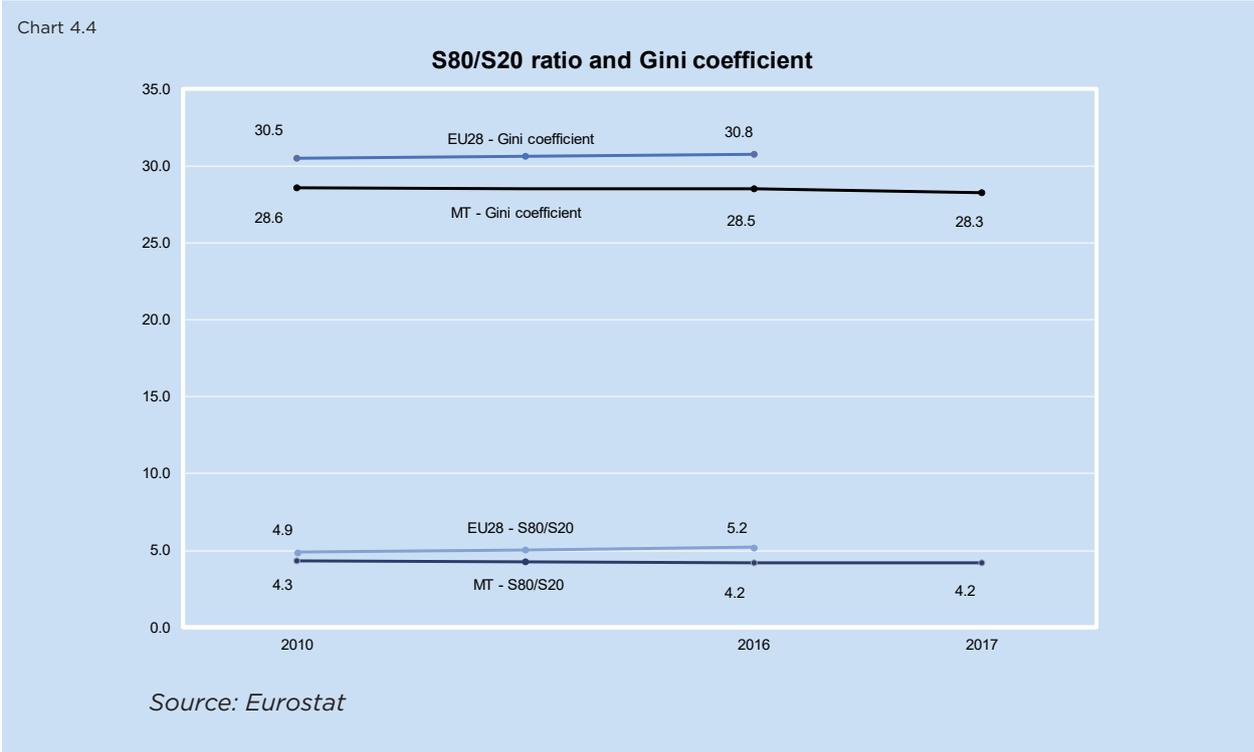


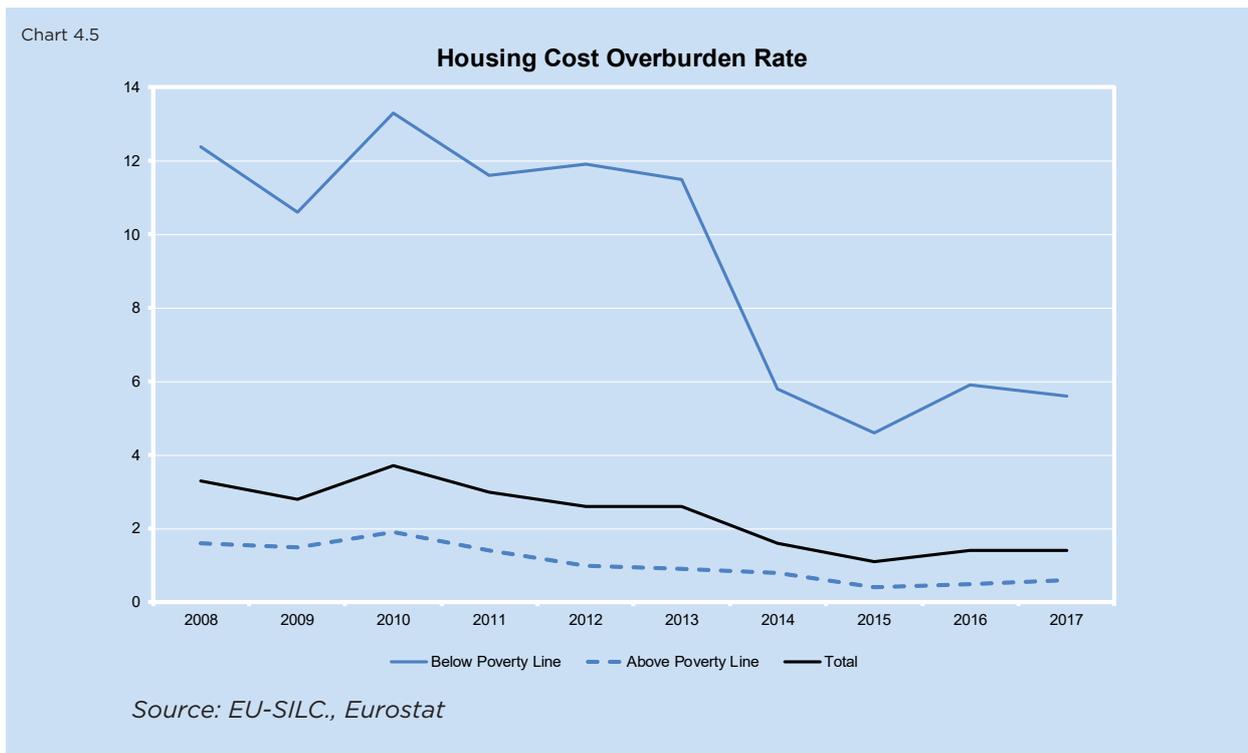
as single person households and households comprising two adults with two children younger than 14 years increased by almost 45 per cent over the same ten-year period under review, thus suggesting that the key contributor for the increase in the AROP is improved labour market outcomes.

When compared to average EU levels, Malta’s average household income is still marginally lower, however it has been converging steadily over the past ten years towards both EU28 levels and Euro Area (EA) levels. Moreover, there seems to be a relatively fairer distribution of income in Malta as evidenced by both the income quintile share ratio (S80/S20) and the Gini coefficient indicators. The latter are two of the main indicators used to assess inequality in a society.

The S80/S20 ratio has been quite stable over the past years and shows that the income of the wealthiest 20 per cent of the Maltese population is on average around 4.2 times higher than the income of the bottom quintile. For persons aged 65 or more, this gap decreases to 3.3 times the income of the top quintile. The S80/S20 ratio for the EU28 in 2016 stood at 5.2.

The Gini coefficient, after the inclusion of social transfers, has also remained rather stable over the past two years, hovering around the 28.4 mark. For 2017, the Gini coefficient stood at 28.3 dropping from the 28.6 registered in 2010, indicating a slight decline in income inequality. At EU level, this coefficient is relatively higher and stood at 30.8 in 2016, increasing slightly from the 30.5 registered during 2010. This, together with the S80/S20 ratio, indicate that income inequality in Malta is less pronounced than that being experienced across the EU as a whole.





The EU-SILC survey indicates that in 2017, approximately three fifths (59.5 per cent) of the Maltese households were owner-occupied dwellings for which there was not an outstanding loan or mortgage, while less than one out of every five households (18.7 per cent) of the population lived in an owner-occupied home with a loan or mortgage. 9.8 per cent of households were accommodations rented at rented rate, 4.6% of households were tenants at the prevailing or market rate, and 3.7% were accommodation free of charge.

The proportion of the Maltese population that spent 40% or more of their equivalised disposable income on housing followed a general negative trend between 2008 and 2017 as shown in Chart 4.5. In 2017, a 1.4 per cent share of the Maltese population lived in households with an overburden cost on housing. This rate was highest for tenants with market price rents (14.9 per cent) and lowest for persons in owner-occupied dwellings with no outstanding mortgage or housing loan (0.4 per cent). The overburden rate for the population that is below 60 per cent of median equivalised income amounted to 5.6 per cent, which was substantially less than the rate recorded in 2008.

### 4.3 Measures targeting inclusive growth in the 2019 Budget

The Budget for 2019 aims to continue to build on distributional policies enacted in recent years with the aim of strengthening social cohesion and social justice, whilst supporting the appropriate conditions for the economy to continue growing and creating jobs.

#### Making Work Pay

Cognisant of the success of the making work pay measures in increasing labour market participation rates and reducing unemployment related poverty, the Government intends

to continue supporting measures which enhance the disposable income of low and middle-income earners.

### **Supporting Families**

The Government aims to continue to build on the legacy of previous budgetary measures regarding families with children on low income. To that effect, a number of measures will be implemented to supplement the income of such families. These measures are expected to address issues of social exclusion affecting families with children.

The demand for dwelling units has increased considerably over the past decade, underpinning the growth in property prices and rental prices. In this context, Government is seeking to strengthen the regulatory framework in the private rental sector with scope of providing certainty and stability for both landlords and tenants, while also assisting in sustaining in affordable housing.

### **Elderly**

The Government will continue to adopt measures intended to reduce the risk of poverty amongst the elderly. The 2019 Budget includes a number of measures aimed at enhancing the pensioners' and the elderly's income and supporting the provision of informal long-term care.