



BANK ĊENTRALI TA' MALTA
EUROSISTEMA
CENTRAL BANK OF MALTA

ECONOMIC UPDATE 6/2015

Date of issue: 26 June 2015

© Central Bank of Malta, 2015

Address

Pjazza Kastilja
Valletta VLT 1060
Malta

Telephone

(+356) 2550 0000

Fax

(+356) 2550 2500

Website

<http://www.centralbankmalta.org>

E-mail

info@centralbankmalta.org

All rights reserved. Reproduction is permitted provided that the source is acknowledged.

The cut-off date for information in this publication is 15 June 2015 unless otherwise indicated. Figures in tables may not add up due to rounding.

ISSN 2410-8294 (online)

ECONOMIC UPDATE 6/2015

Summary¹

Economic activity in Malta continued to expand robustly in the first quarter of 2015, with real gross domestic product (GDP) increasing by 4.0% on a year earlier, driven by net exports, as domestic demand declined. Indicators for manufacturing and tourism point to further growth in the second quarter of 2015. Growth in economic activity is being reflected in the labour market, with employment expanding and the unemployment rate remaining at historically low levels. Price pressures remain contained. The annual rate of HICP inflation eased to 1.3% in May. In April, Maltese residents' deposits increased on a year earlier, but credit to residents continued to fall. As regards fiscal developments, the general government deficit narrowed to 2.1% of GDP during 2014. In the first four months of 2015, the deficit on the Consolidated Fund also decreased compared with the same period of 2014. On the external side, the surplus on the current account of the balance of payments widened during the fourth quarter of the year.

Output, demand and the labour market

Economic activity in Malta continued to grow strongly during the first quarter of 2015, with real GDP rising at an annual rate of 4.0%, a slight deceleration from 4.2% in the previous quarter.

Growth was driven by net exports. While exports fell on a year earlier, imports declined at an even faster pace (see Table 1). As a result net exports turned positive, and contributed 4.2 percentage points to real GDP growth, outweighing a drop in domestic demand (see Chart 1).

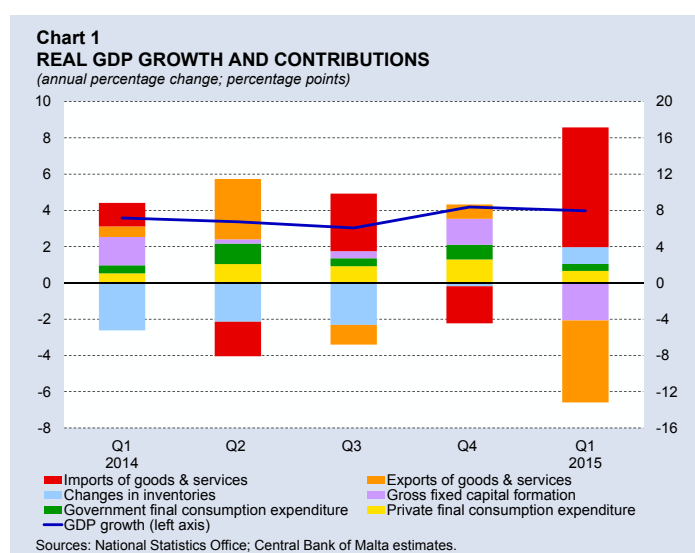
Exports dropped by 5.5%, year-on-year, mostly due to lower foreign sales of goods, while services exports dropped only slightly. Reflecting the reduction in exports and the drop in domestic demand, total imports fell by 7.9%. This drop also stemmed largely from imports of goods.

	2014				2015
	Q1	Q2	Q3	Q4	Q1
	<i>Annual percentage changes</i>				
Private final consumption expenditure	1.8	3.6	3.4	4.6	2.3
Government final consumption expenditure	4.1	11.2	5.0	8.3	3.6
Gross fixed capital formation	15.4	2.6	5.2	14.8	-18.3
Domestic demand	-0.1	0.6	-1.3	7.2	-0.3
Exports of goods & services	0.8	4.3	-1.4	1.0	-5.5
Imports of goods & services	-1.2	2.5	-4.5	2.8	-7.9
Gross domestic product	3.6	3.4	3.0	4.2	4.0

⁽¹⁾ Chain-linked volumes, reference year 2010.
Source: National Statistics Office.

¹ The cut-off date for information in this note is 15 June 2015.

Domestic demand contracted by 0.3% on a year earlier, dampening real GDP growth by 0.2 percentage points. Investment fell sharply when compared with the first quarter of 2014. It dropped by 18.3%, reversing the increases registered in the previous five quarters. Thus, investment reduced real GDP growth by 4.1 percentage points. The fall in investment can be largely attributed to lower spending on non-residential construction and machinery. Conversely, investment in dwellings rose, as did expenditure on transport equipment.



The decrease in investment offset growth in the other components of domestic demand.

Private consumption continued to rise, sustained by further growth in employee compensation, contributing 1.3 percentage points to GDP growth. However, at 2.3%, the annual growth rate halved compared with the last quarter of 2014.

Government consumption growth also slowed down significantly, with the annual growth rate down to 3.6% from 8.3% in the previous three month period. The deceleration reflected more moderate growth in both compensation of employees and intermediate consumption.

At the same time, changes in inventories had a large positive impact on growth.²

Nominal GDP growth moderated slightly in the first quarter of 2015, standing at a rate of 6.0%, compared with 6.4% in the last quarter of 2014. The annual rate of growth of gross value added (GVA) remained unchanged, at 5.2%. Sectoral data show that services continued to drive the expansion in GVA. The strongest contributions came from the sectors incorporating professional & scientific activities and public administration, health & education, which together accounted for almost half of the increase in GVA. Strong increases were also recorded from the sectors incorporating wholesale & retail trade, financial services and utilities. Meanwhile, GVA in the construction sector increased marginally, whereas that in manufacturing declined.

Data going into the second quarter of 2015 show signs of recovery in manufacturing and continued growth in tourism.

² Changes in inventories include acquisitions and disposals of valuables as well as the statistical discrepancy. In the absence of NSO data, the contribution of changes in inventories is based on the Bank's calculations.

As regards manufacturing, the index of industrial production increased by 2.3% in year-on-year terms during April 2015.³ The three-month moving average of the index rose by 2.1% when compared with the corresponding period last year. The increase mainly reflected a strong pick-up in the production of pharmaceuticals. Manufacturing of food products, electricity, rubber & plastic products, computer, electronic & optical products also increased, although more modestly. On the other hand, output declined in the printing & reproduction of recorded media and the beverages sectors.

Turning to tourism, the positive performance observed in 2014 extended into 2015. In April, tourist arrivals rose at an annual rate of 2.5%, with expenditure also increasing, whereas nights spent declined marginally. As a result, during the first four months of 2015, tourist numbers increased by 5.7% on a year earlier, while nights stayed and total spending went up by 3.5% and 6.8%, respectively. All major expenditure components went up on a year earlier.

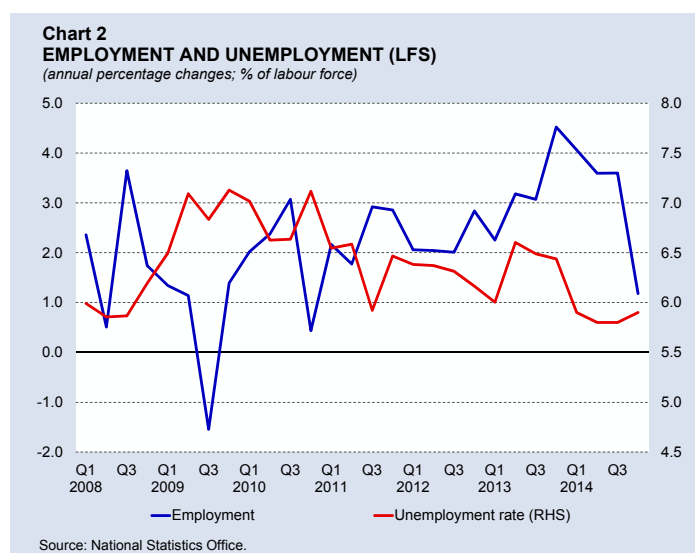
In the first three months of 2015, however, the number of foreign cruise passengers amounted to 20,652, a decrease of 45.8% over the exceptionally high number of visitors a year earlier.

As regards the labour market, Labour Force Survey (LFS) data for the fourth quarter of 2014 indicate an increase of 1.2% in employment compared with the same period of 2013, slowing down from 3.6% in the previous quarter (see Chart 2). The increase in the fourth quarter mainly reflected a rise in part-time employment, although full-time employment also went up. In 2014 as a whole, employment expanded by 3.1%.

ETC records show that in December the gainfully occupied population rose by 3.8% on a year earlier, the same increase registered in November.⁴

According to the LFS, the unemployment rate stood at 5.9% in the fourth quarter of 2014, compared with 6.4% a year earlier. Eurostat's estimate of the seasonally-adjusted unemployment rate for the first quarter of 2015 also stood at 5.9%. In April, the unemployment rate based on this measure fell to 5.7%.

ETC data show that in April 2015 the number of people on the unemployment register fell by 1,723 compared with a year earlier, to 5,568.



³ Based on the industrial production index adjusted for working days.

⁴ The LFS is a household survey conducted by the National Statistics Office (NSO) on the basis of definitions set by the International Labour Organization and Eurostat. ETC data are based on administrative records according to definitions established by domestic legislation on employment and social security benefits.

Prices, costs and competitiveness

In May, the annual rate of HICP inflation fell slightly to 1.3%, from 1.4% a month earlier. The twelve-month moving average rate edged up by 0.1 percentage point, to 0.8% (see Chart 3).

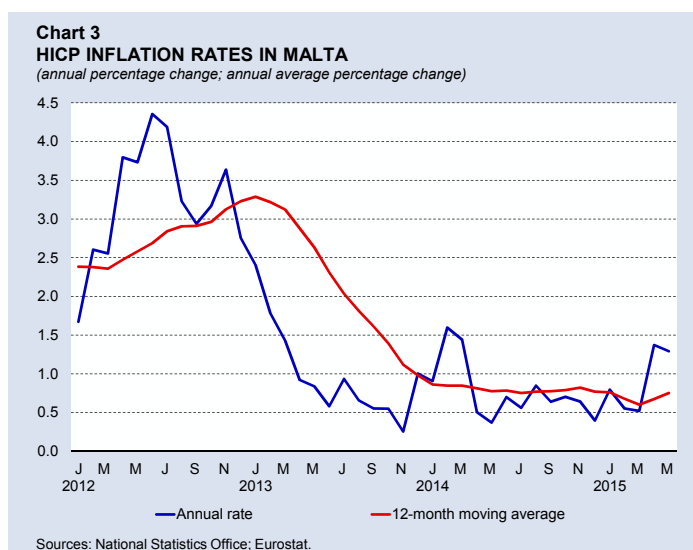
The marginal slowdown in the annual rate of change of the HICP was primarily the result of a deceleration in unprocessed food price inflation. This moderated from 4.9% in April to 2.8% in May, mainly reflecting developments in the prices of fruit and vegetables. Prices of non-energy industrial goods also rose at a slower pace, with the annual rate of change falling from 1.6% in April to 1.4% in May, largely on the back of significantly slower growth in the prices of garments and a drop in the prices of durables.

On the other hand, processed food price inflation picked up to 1.8% in May, from 1.5% a month earlier, partly reflecting a faster increase in alcohol prices. In addition, services price inflation edged-up by 0.1 percentage point to 1.7%, mainly propelled by higher airfares. This was partially offset by a slower rate of change of prices charged by restaurants, as well as a larger drop in the prices of communications services.

Meanwhile, energy prices continued to decline, falling by 4.4% in annual terms in May, compared with a decrease of 5.1% a month earlier. This smaller decline reflected the fact that petrol and diesel prices remained unchanged during the month under review, following the decline in April.

During the first quarter of 2015 Malta's unit labour costs, which track the labour cost of a unit of output, continued to rise. When measured as a four-quarter moving average, they increased by 1.1% on a year earlier, up from 1.0% in the previous quarter. Compensation per employee rose by 0.7%, while productivity fell by 0.5%.

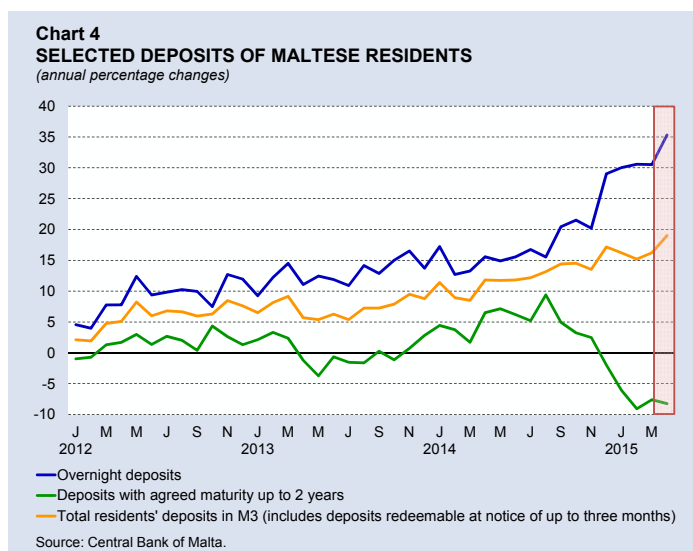
Based on the Central Bank of Malta's advertised property price index, the price of residential properties rose at an annual rate of 4.7% in the fourth quarter of 2014, mainly driven by developments in prices of apartments. This follows four consecutive quarters of strong growth, with the average for 2014 standing at 7.0%. Although they indicate trends, advertised property prices may not accurately reflect the prices at which sales actually take place.



Deposits, credit and financial markets⁵

The annual rate of growth of residents' deposits in M3 accelerated from 16.2% in March to 19.0% in April. This follows an increase in residents' deposits of €348.6 million during the month, which was spread across most types of deposits.

Overnight deposits accounted for most of the April increase, with the annual growth rate reaching 35.3%, from 30.5% in March (see Chart 4). Households accounted for more than half the annual increase.

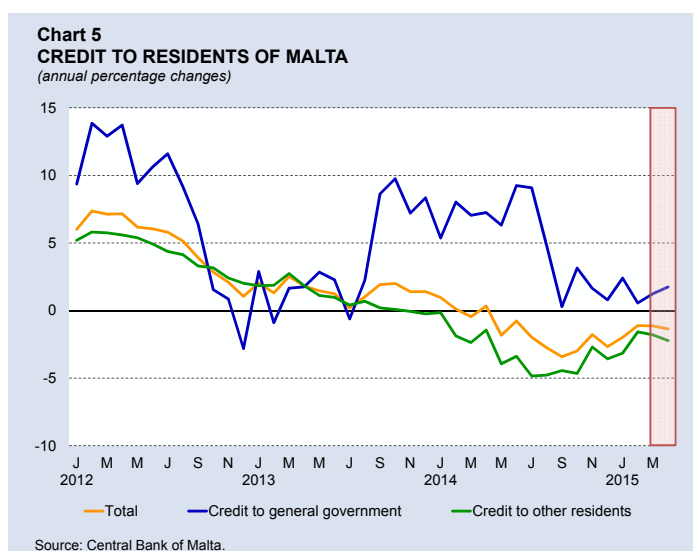


On the other hand, deposits with an agreed maturity of up to two years contracted marginally in April. Consequently, their annual rate of change declined to -8.2% from -7.6%. Meanwhile, deposits redeemable at a notice of up to three months went up by 11.8% in April on an annual basis, up from 8.2% a month earlier.

On the asset side of MFI balance sheets, credit to Maltese residents expanded marginally between March and April. Nonetheless, credit contracted by 1.4% year-on-year, following a contraction of 1.1% during the year to March (see Chart 5). Although credit to government grew at a faster annual rate, the decline in credit to other residents gathered pace.

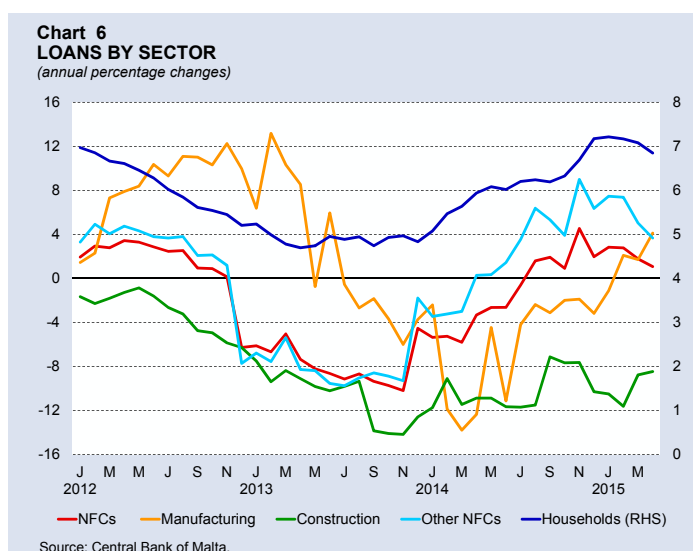
The annual growth rate of credit to general government rose from 1.2% in the previous month to 1.7% in April, partly reflecting increased holdings of Malta Government Stocks by the banking sector.

Meanwhile, credit to all other residents contracted by 2.2% year-on-year, following a drop of 1.8% in the previous month.



⁵ Monetary data for the period from June 2010 onward have been revised to comply with ESA 2010 methodology. The main revisions stem from the reclassification of special purpose entities from residents of the rest of the world to residents of Malta. Consequently, residents' deposits, as well as loans to residents, were revised upwards.

Loans to NFCs decreased slightly in April, driven by a fall in loans to firms operating in the real estate and transportation & storage sectors. Consequently, the annual growth rate declined to 1.1% from 1.8% in March (see Chart 6). Meanwhile, lending to households grew marginally during the month, with the annual rate of growth edging down to 6.8%, from 7.1% in the previous month. This deceleration arose as house loans grew at a slower pace, while consumer and other credit fell more strongly.

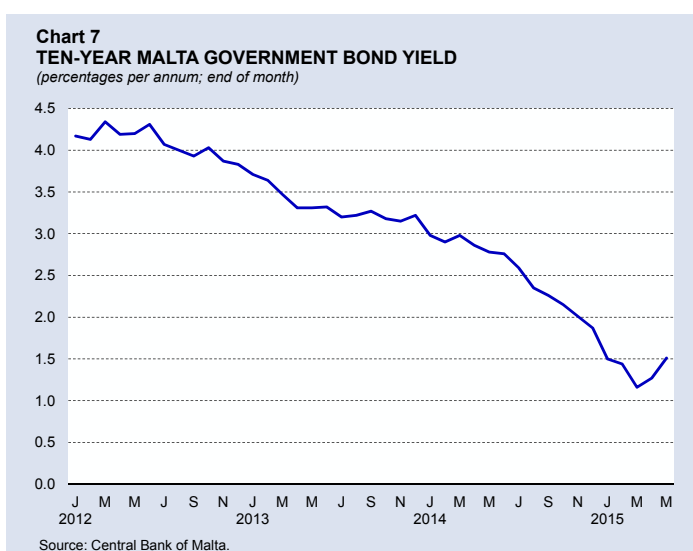


Bank lending and deposit rates fell slightly in April. The composite interest rate paid by MFIs on all euro-denominated deposits belonging to resident households and NFCs dropped by 3 basis points to 0.90%. Meanwhile, the comparable rate charged by MFIs on outstanding loans to resident households and NFCs stood at 3.93%, 5 basis points lower than in March.

The composite deposit rate was 42 basis points below its level a year earlier, while the corresponding lending rate was 26 basis points lower.

In the domestic capital market, the yield on ten-year government bonds rose by 23 basis points in May to 1.5%. The increase, which was in line with developments in sovereign bond yields in the euro area as a whole, brought to a halt the downward trend seen in recent months (see Chart 7). By mid-June, the yield on ten-year government bonds rose to 1.8%.

The Malta Stock Exchange (MSE) index gained 2.9% between the end of April and 29 May.



Public finance⁶

In the final quarter of 2014 the general government balance improved on a year-on-year basis. As a result, over the year as a whole, the deficit decreased to €168.3 million from €194.4 million in 2013. The deficit to GDP ratio declined from 2.6% in 2013 to 2.1% in 2014.

Total revenue grew by 10.5% in 2014, buoyed by higher tax revenue, reflecting positive developments in the Maltese economy as well as fiscal measures. Current taxes on income and wealth surged by 10.8%, partly due to revenue from the Investment Registration Scheme, which allowed Maltese residents to regularise their tax position with regard to undeclared assets. Inflows from taxes on production and imports grew by 10.7%, driven by growth in domestic and tourist consumption, as well as increased excise duty rates. At the same time, income from social contributions grew by 6.8%, reflecting continued positive labour market developments.

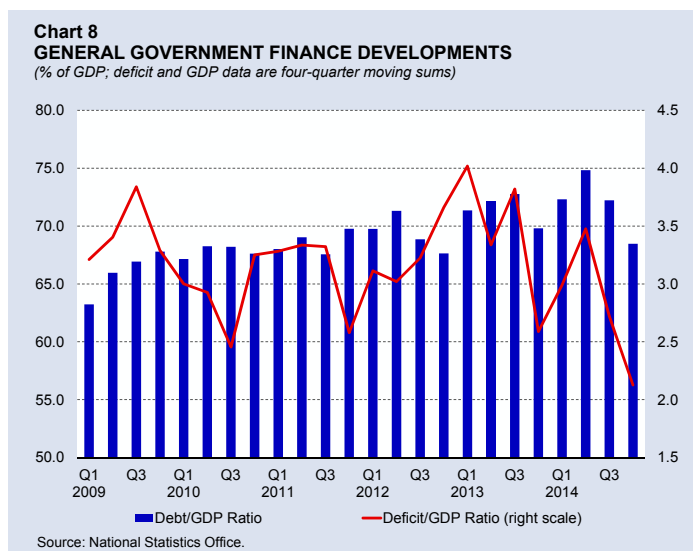
Meanwhile, receipts from capital and current transfers grew by 33.2%, owing to grants received from the European Union (EU).

General government expenditure rose by 9.1%, with recurrent spending accounting for just under three-fourths of the increase. Compensation of employees grew by 7.6%, mainly reflecting increased outlays in the health and education sectors. Intermediate consumption went up by 11.6%, as spending on public administration and health rose. At the same time, outlays on social benefits rose by 4.6%, due to higher spending on retirement pensions and social assistance.

Meanwhile, spending on gross fixed capital formation surged by 43.2%, owing to higher expenditure on infrastructural projects partly funded by the EU. On the other hand, capital transfers declined by 7.1%, as the equity injection into Air Malta was smaller than in the previous year.

The general government debt-to-GDP ratio stood at 68.5% in 2014, down from 69.8% in 2013 (see Chart 8).⁷

In April 2015 the Consolidated Fund deficit stood at €23.2 million, up from €12.7 million in April 2014. However, during the first four months of the year, the Consolidated Fund deficit narrowed by €129.7 million compared with the same period last



⁶ The general government accounts, which are compiled in line with the ESA 2010 methodology, cover central government, including extra-budgetary units, as well as local councils, on an accrual basis. The Consolidated Fund captures most of the transactions of general government on a cash basis.

⁷ These debt ratios are based on the debt levels published in NSO *News Release* 075/2015 and GDP data up to the first quarter of 2015, published in NSO *News Release* 108/2015.

year, to €108.6 million. Revenue surged by 20.0% mainly due to higher grants from the EU, as well as higher indirect tax proceeds. Total expenditure rose by 3.4%, with current and capital spending putting on 2.4% and 11.4%, respectively.

Balance of payments

During the last quarter of 2014, the current account of the balance of payments recorded a surplus of €10.9 million, up from €1.0 million in the same period of 2013.⁸ This increase was mainly driven by an €81.2 million decline in net outflows on the primary income account.⁹ The services balance also improved, by €31.5 million when compared with a year earlier. These favourable developments were partly offset by a widening of €90.5 million in the trade gap in goods and a €12.3 million drop in net secondary income receipts.

The capital account posted net inflows of €9.2 million, down from €49.6 million in the same period of the previous year. Meanwhile, the financial account registered net borrowing of €130.2 million as opposed to net lending of €77.5 million in the last quarter of 2013.

In 2014 as a whole, the surplus on the current account stood at €215.1 million, down from €234.8 million in 2013 (see Table 2). This decline was primarily driven by higher net outflows on the primary income account, though a larger merchandise trade deficit also contributed. Combined, these components offset the positive developments registered on services and the secondary income account. Meanwhile, net inflows on the capital account increased to €138.0 million. The financial account showed net borrowings of €659.1 million, compared with €382.4 million in 2013.

Customs data indicate that in 2014 the merchandise trade deficit widened to €2.6 billion, €0.9 billion more than in 2013.¹⁰ This reflected a decline in exports, mainly driven by lower sales of electrical machinery, though other categories, such as fuel and pharmaceuticals, also fell. At the

	2013 Q4	2014 Q4	2013 Q1-Q4	2014 Q1-Q4
Current account	1.0	10.9	234.8	215.1
Goods	-220.6	-311.1	-1,090.7	-1,120.0
Services	322.4	353.9	1,513.9	1,627.3
Primary income	-158.5	-77.2	-327.4	-484.3
Secondary income	57.6	45.3	138.9	192.0

Source: National Statistics Office.

⁸ As from September 2014, the NSO started publishing the balance of payments statement according to the guidelines provided in the Sixth Edition of the IMF's BOP and IIP manual (BPM6). The most notable difference resulting from the implementation of the latest manual relates to the inclusion of Special Purpose Entities as residents of Malta.

⁹ The primary income account shows income flows related mainly to cross-border investment and compensation of employees. The secondary income account shows current transfers between residents and non-residents.

¹⁰ Goods exports and imports in the balance of payments differ from merchandise trade data from Customs sources due to adjustments for differences in coverage, valuation and timing. For example, Customs data cover all goods which cross Maltese borders, whereas balance of payments data only include transactions involving changes in ownership. These differences are especially pronounced in the case of trade in fuel, aircraft and ships.

same time, imports rose, predominantly on account of a rise in fuels and capital goods, including purchases (and registrations) of ships and boats.

During the first four months of 2015, Customs data show that exports contracted whereas imports increased on a year earlier. As a result, the merchandise trade deficit widened by €265.2 million to €769.0 million. The increase in imports is predominantly attributable to a sharp rise in registrations of aircraft and boats. The negative balance from trade in fuel narrowed on a year earlier, as a decline in fuel imports outweighed a drop in related exports. Excluding fuel, aircraft and boats, the trade gap narrowed as imports contracted, while exports expanded moderately.

Annex 1

MACROECONOMIC INDICATORS FOR MALTA																
<i>(annual percentage changes; non-seasonally adjusted data)</i>																
	2013	2014	2013	2014	2014	2014	2014	2015	2014	2014	2014	2015	2015	2015	2015	2015
			Q4	Q1	Q2	Q3	Q4	Q1	Oct.	Nov.	Dec.	Jan.	Feb.	Mar.	Apr.	May
Prices and costs																
HICP	1.0	0.8	0.6	1.3	0.5	0.7	0.6	0.6	0.7	0.6	0.4	0.8	0.6	0.5	1.4	1.3
Unit labour costs, whole economy ⁽¹⁾	2.0	1.0	2.0	1.3	1.5	1.2	1.0	1.1	-	-	-	-	-	-	-	-
Compensation per employee ⁽¹⁾	0.1	0.1	0.1	-0.5	-0.3	-0.5	0.1	0.7	-	-	-	-	-	-	-	-
Labour productivity (per person) ⁽¹⁾	-1.9	-0.9	-1.9	-1.8	-1.8	-1.7	-0.9	-0.5	-	-	-	-	-	-	-	-
Residential property prices	2.1	7.0	6.4	6.7	8.9	7.6	4.7	-	-	-	-	-	-	-	-	-
Economic activity																
Nominal GDP	4.2	5.4	4.1	5.5	5.0	4.8	6.4	6.0	-	-	-	-	-	-	-	-
Real GDP	2.3	3.5	1.6	3.6	3.4	3.0	4.2	4.0	-	-	-	-	-	-	-	-
Real private consumption	1.8	3.4	3.2	1.8	3.6	3.4	4.6	2.3	-	-	-	-	-	-	-	-
Real government consumption	-0.3	7.1	-2.0	4.1	11.2	5.0	8.3	3.6	-	-	-	-	-	-	-	-
Real gross fixed capital formation	1.1	9.7	9.7	15.4	2.6	5.2	14.8	-18.3	-	-	-	-	-	-	-	-
Real exports of goods and services	-0.9	1.1	-1.6	0.8	4.3	-1.4	1.0	-5.5	-	-	-	-	-	-	-	-
Real imports of goods and services	-1.0	-0.2	-1.8	-1.2	2.5	-4.5	2.8	-7.9	-	-	-	-	-	-	-	-
Tourist arrivals	9.6	6.8	13.4	7.9	9.0	7.2	2.5	7.7	2.7	3.0	1.4	6.8	14.1	4.1	2.5	-
Labour market developments (LFS)																
Unemployment rate (% of labour force)	6.4	5.9	6.4	5.9	5.8	5.8	5.9	-	-	-	-	-	-	-	-	-
Total employment	3.3	3.1	4.5	4.0	3.6	3.6	1.2	-	-	-	-	-	-	-	-	-
Balance of payments																
Current account (as a % of GDP) ⁽¹⁾⁽²⁾	3.1	2.7	3.1	-	-	-	2.7	-	-	-	-	-	-	-	-	-
Credit and financial indicators																
Maltese residents' deposits and loans																
Overnight deposits	13.7	29.0	13.7	13.3	15.6	20.4	29.0	30.5	21.5	20.2	29.0	30.0	30.6	30.5	35.3	-
Deposits with agreed maturity up to 2 years	2.8	-2.0	2.8	1.7	6.2	4.9	-2.0	-7.6	3.2	2.5	-2.0	-6.1	-9.1	-7.6	-8.2	-
Total residents' deposits in M3	8.8	17.2	8.8	8.5	11.8	14.4	17.2	16.2	14.5	13.5	17.2	16.2	15.2	16.2	19.0	-
Credit to general government	8.3	0.8	8.3	7.1	9.2	0.3	0.8	1.2	3.1	1.6	0.8	2.4	0.6	1.2	1.7	-
Credit to other residents	-0.2	-3.6	-0.2	-2.4	-3.4	-4.4	-3.6	-1.8	-4.6	-2.7	-3.6	-3.2	-1.6	-1.8	-2.2	-
Total credit	1.4	-2.7	1.4	-0.5	-0.8	-3.4	-2.7	-1.1	-3.0	-1.8	-2.7	-2.0	-1.1	-1.1	-1.4	-
10-year interest rate (%) ⁽³⁾	3.4	2.6	3.2	3.0	2.9	2.5	2.1	1.5	2.2	2.1	1.9	1.7	1.5	1.3	1.2	1.5
Stock prices: Malta Stock Exchange Index ⁽⁴⁾	14.8	-9.6	7.8	-7.1	-3.7	1.1	-0.1	13.4	-0.9	-0.9	1.8	2.7	0.8	9.5	-0.2	2.9
General government finances (% of GDP)																
Surplus (+) / deficit (-) ⁽⁵⁾	-2.6	-2.1	-2.6	-3.0	-3.5	-2.7	-2.1	-	-	-	-	-	-	-	-	-
Gross debt ⁽⁶⁾	69.8	68.5	69.8	72.3	74.8	72.2	68.5	-	-	-	-	-	-	-	-	-

⁽¹⁾ Four-quarter moving averages.
⁽²⁾ Quarterly data consistent with the latest balance of payments release are unavailable.
⁽³⁾ Period averages.
⁽⁴⁾ Period-on-period percentage changes.
⁽⁵⁾ Four-quarter moving sums.
⁽⁶⁾ GDP data are four-quarter moving sums.

Sources: Central Bank of Malta; European Commission; Malta Stock Exchange; National Statistics Office.