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EUROSISTEMA
CENTRAL BANK OF MALTA

ECONOMIC UPDATE

9/2020

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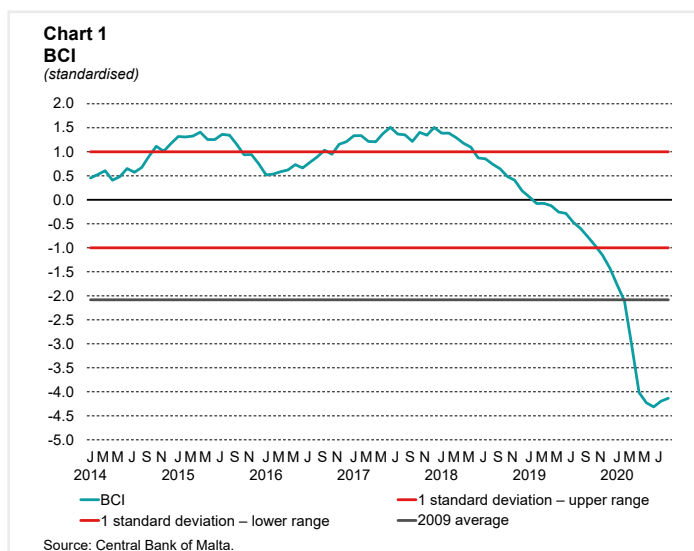
Summary¹

In August, the Bank's Business Conditions Index (BCI) improved only slightly when compared with the previous month, a further suggestion that economic conditions continued to bottom out. The European Commission's Economic Sentiment Indicator (ESI) rose, but remained well below the level recorded before the onset of COVID-19. The increase in sentiment largely reflects improved confidence in the services sector and in industry and, to a lesser extent, among retailers. By contrast, sentiment fell in the construction sector and among consumers. Confidence remained negative in all sectors.

In July, the volume of retail trade and industrial production contracted again in annual terms, though at a somewhat slower pace when compared with June. The number of registered unemployed and the unemployment rate fell when compared with a month earlier, with the latter remaining low from a historical perspective. The annual inflation rate based on the Harmonised Index of Consumer Prices (HICP) decelerated to 0.7% in July, from 1.0% in June, while inflation based on the Retail Price Index (RPI) edged down marginally to 0.6% from 0.7% a month earlier. Maltese residents' deposits grew at a slower annual rate of 5.3% over the year to July, while annual growth in credit to Maltese residents rose by 9.1%. In July, the cash-based Consolidated Fund recorded a deficit compared with a surplus a year earlier, reflecting the impact on revenue from a slowdown in economic activity due to the global spread of COVID-19, and the expense associated with ongoing government support measures to mitigate the economic effects of the pandemic.

Central Bank's BCI²

In August, the Bank's BCI stood at -4.1, a marginal improvement from its updated value of -4.2 for July (see Chart 1). The BCI in August continued to signal low levels of economic activity, reflecting the exceptional economic environment triggered by COVID-19. The estimate continued to be affected by strong negative outturns in almost all variables, especially year-on-year falls in inbound tourists, economic sentiment and government revenue, as



¹ The cut-off date for information in this note is 15 September 2020. Most of the data reported in this issue of the *Economic Update* refer to July 2020, and thus reflect the impact of the lifting of restrictive measures related to COVID-19, as from May. Data for the BCI and the ESI are for August 2020. As from 19 August, some containment measures were re-introduced, affecting the entertainment sector. Tourism data for April, May and June have not been collected by the National Statistics Office (NSO) as airport and seaport were closed in those months. Inbound tourism data for July were collected and published as the airport and seaport were reopened. With effect from 22 August, an amber list was added to the red and green travel lists, requiring tourists arriving from countries on this list to present a negative COVID-19 test result before boarding.

² The methodology underlying the BCI can be found at [here](#). A zero value of the BCI is consistent with average business conditions, which in the case of Malta tends to be consistent with a real GDP growth rate of close to 4%. When the value of the BCI falls repeatedly below -1, economic activity would be significantly below normal. From June 2020, the BCI methodology was updated to include a new variable – monthly development permits.

well as higher unemployment, compared to a year earlier. Overall business conditions were worse than those observed during 2009.

Business and consumer confidence indicators

In August, the European Commission's ESI stood at 75.0, up from 63.4 in July, but still well below the 99.7 recorded a year earlier and its long-run average (see Table 1).^{3,4} The ESI also stood 12.7 points lower than that in the euro area.

The month-on-month increase in sentiment reflects improved confidence across the services sector and, to a lesser extent, in industry and among retailers. By contrast, sentiment among consumers and in the construction sector fell further.

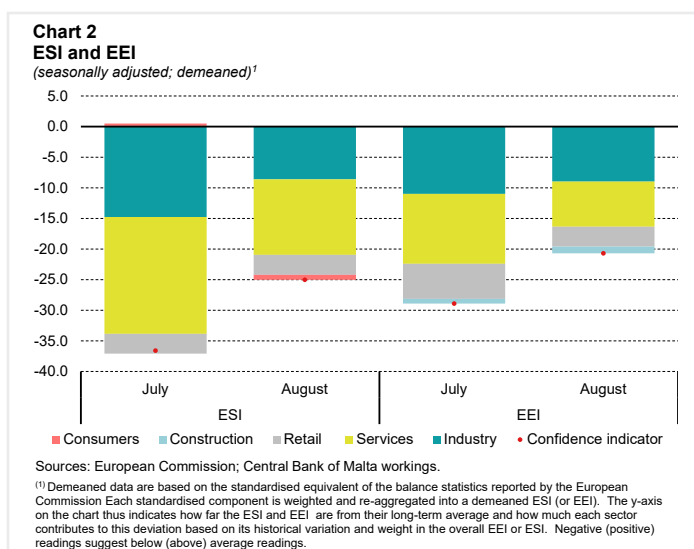
Table 1		BUSINESS AND CONSUMER SURVEYS													
<i>Balances; percentage points; seasonally adjusted</i>		2018		2019		2020									
		Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.						
ESI	112.4	100.7	99.9	93.9	87.5	52.1	56.6	56.5	63.4	75.0					
Services confidence indicator	34.6	20.7	7.9	11.4	0.4	-56.8	-53.5	-57.3	-41.1	-18.7					
Business situation development over the past 3 months	30.7	16.7	-3.8	4.6	-0.3	-59.8	-66.3	-77.4	-68.9	-32.4					
Evolution of the demand over the past 3 months	35.8	21.5	3.8	7.9	11.4	-56.3	-66.0	-78.2	-60.2	-40.2					
Expectation of the demand over the next 3 months	37.2	24.0	23.8	21.7	-9.9	-54.1	-28.3	-16.3	5.7	16.4					
Industrial confidence indicator	6.9	-6.7	-1.1	-15.5	-19.2	-45.4	-40.2	-42.2	-35.6	-24.0					
Assessment of order-book levels	-1.5	-23.0	-19.1	-20.2	-14.7	-56.1	-76.0	-76.9	-73.2	-74.1					
Assessment of stocks of finished products	5.8	15.5	20.0	33.2	13.3	32.5	34.4	31.4	40.4	20.1					
Production expectations for the months ahead	27.9	18.4	35.8	6.9	-29.7	-47.6	-10.2	-18.3	6.8	22.3					
Retail trade confidence indicator	8.2	4.2	0.0	-0.4	-22.3	-31.7	-43.2	-30.1	-53.6	-49.9					
Business activity, past 3 months	15.4	18.9	3.0	4.8	5.8	12.4	-21.1	-28.1	-49.2	-52.5					
Stocks of finished goods	7.7	17.4	7.2	10.0	9.7	65.6	53.0	54.8	46.3	50.6					
Business activity, next 3 months	17.0	11.1	4.1	4.1	-63.1	-42.0	-55.5	-7.4	-65.3	-46.6					
Construction confidence indicator	21.3	26.2	7.9	8.3	14.3	-38.9	-20.3	-19.9	-5.9	-12.7					
Evolution of your current overall order books	16.9	19.7	4.5	2.0	2.1	-38.1	-13.0	-18.8	-5.0	-12.4					
Employment expectations over the next 3 months	25.7	32.6	11.3	14.5	26.5	-39.6	-27.6	-21.1	-6.9	-13.0					
Consumer confidence indicator	10.1	4.5	8.4	7.9	0.1	-15.8	-11.3	-6.9	-3.3	-12.9					
Financial situation past 12 months	16.9	11.3	13.4	11.6	13.8	6.2	0.8	0.8	-2.7	-10.6					
Financial situation next 12 months	17.5	11.2	13.1	10.7	5.1	-14.5	-5.7	-2.1	6.1	-5.6					
Economic situation next 12 months	28.9	20.9	18.0	19.8	-3.0	-36.6	-17.7	-3.9	13.9	-10.6					
Major purchases next 12 months	-22.6	-25.1	-10.9	-10.4	-15.5	-18.4	-22.5	-22.4	-30.5	-24.7					
EI	114.1	101.2	100.2	102.7	90.0	56.2	71.8	71.0	72.3	80.4					
Services	33.9	17.5	6.7	21.6	11.8	-33.0	-16.6	-16.8	-7.1	1.9					
Retail	15.4	4.7	25.2	11.9	-8.6	-14.2	-15.5	-3.3	-25.6	-13.2					
Industry	31.1	12.8	16.5	7.0	-16.7	-61.2	-18.9	-40.3	-34.9	-26.0					
Construction	25.7	32.6	11.3	14.5	26.5	-39.6	-27.6	-21.1	-6.9	-13.0					
ESI demeaned	12.4	0.7	-0.1	-6.1	-12.5	-47.9	-43.4	-43.5	-36.6	-25.0					
EI demeaned	14.3	1.0	0.0	2.1	-11.1	-46.0	-28.7	-30.8	-28.9	-20.7					

Source: European Commission.

³ The ESI summarises developments in confidence in five surveyed sectors: industry, services, construction, retail and consumers. Weights are assigned as follows: industry 40%, services 30%, consumers 20%, construction 5% and retail trade 5%.

⁴ Long-term averages are calculated over the entire period for which data are available. For the consumer and industrial confidence indicators, data became available in December 2002, while the services and construction confidence indicator data became available in May 2007 and May 2008, respectively. The long-term average of the retail confidence indicator is calculated as from May 2011, when it was first published. However, the long-term average of the ESI is computed from December 2002.

Demeaned data – which account for the variation in weights assigned to each sector in the overall index – show that most of the amelioration in overall sentiment in August can be attributed to developments in the services sector and in industry (see Chart 2). Although still relatively low from a historic perspective, sentiment in these two sectors was much less negative than in July. While sentiment in the retail sector was less negative than before, the impact on the overall ESI was similar to that estimated for the previous month. By contrast, the contribution of consumers turned slightly negative.



In August, sentiment within the services sector stood at -18.7, up from -41.1 a month earlier, but still below its long-term average of 20.4.⁵ Enhanced sentiment largely reflected an improvement in respondents' assessment of the business situation and demand over the past three months. Their expectations of demand for the next three months also improved, although to a lesser extent. Additional survey data show that a marginally smaller share of firms anticipated falling prices in the months ahead.

Industrial confidence rose to -24.0, from -35.6 a month earlier.⁶ The recent improvement in sentiment was driven by a smaller share of participants reporting above normal stock levels and more positive production expectations. Meanwhile, firms' assessment of order book levels weakened slightly. Supplementary data show that, on balance, a smaller share of respondents anticipated a fall in selling prices in the coming months.

Confidence within the retail sector rose to -49.9, from -53.6 in July.⁷ The recent rise in sentiment was driven by retailers' expectations of business activity over the next three months. By contrast, firms' assessment of business activity over previous months deteriorated further. At the same time, a higher share of respondents reported above normal stock levels compared to July.⁸ Additional survey data indicate that price expectations turned positive in the month under review.

⁵ The services confidence indicator is the arithmetic average of the seasonally-adjusted balances (in percentage points) of replies to survey questions relating to the business climate, the evolution of demand in the previous three months and demand expectations in the subsequent three months.

⁶ The industrial confidence indicator is the arithmetic average of the seasonally-adjusted balances (in percentage points) of replies to a subset of survey questions relating to expectations about production over the subsequent three months, to current levels of order books and to stocks of finished goods.

⁷ The retail confidence indicator is the arithmetic average of the seasonally-adjusted balances (in percentage points) of replies to survey questions relating to the present and future business situation and stock levels.

⁸ Above normal stocks of finished goods have a negative effect on the overall indicator. Thus, a rise in the balance of firms reporting above normal stock levels has a negative effect on the overall indicator.

Confidence in the construction sector stood at -12.7 in August, down from -5.9 in July. Following this decrease, sentiment returned below its long-term average of -11.7.⁹ This decrease was due to more negative employment expectations and falling orders. Additional survey data indicate that a considerably higher share of respondents expected prices to decrease over the next three months.

Consumer confidence also weakened remarkably in August. It fell to -12.9 from -3.3 in the previous month.¹⁰ Following this decline, sentiment stood below its long-term average of -11.2. The recent fall in sentiment was largely driven by weaker expectations of the general economic situation over the next 12 months and, to a lesser extent, by consumers' expectations of the financial situation over the same period. On balance, participants' assessment of the financial situation in previous months also weakened. These developments offset improved consumers' expectations of major purchases over subsequent months, although these remained negative on balance. Supplementary data show that price expectations were less negative in July. Meanwhile, a significantly higher share of respondents anticipated unemployment to rise in the coming months.

The European Commission's Employment Expectations Indicator (EEI) – which is a composite indicator of employment expectations in industry, services, retail trade and construction – increased in August.¹¹ The EEI stood at 80.4, up from 72.3 in July, but remained below its long-run average of around 100.0. Moreover, in August, Malta's EEI stood 9.2 points below the euro area average. Employment prospects improved considerably across almost all sectors, barring construction. Employment expectations remained negative in most sectors surveyed, except services where it turned positive.

When accounting for the variation in weights assigned to each sector in the overall index, it appears that the increase relative to July was largely driven by the services sector and, to a smaller extent, by the retail sector and industry. The evolution of sentiment in the services sector and, to a lesser degree, in industry, largely explains why the overall EEI has remained below its long-term average in recent months (see Chart 2).

Activity indicators

In July, annual growth in the index of industrial production – which is a measure of economic activity in the quarrying, manufacturing and energy sectors – remained negative for the fourth consecutive month. The index fell by 2.6% in annual terms, following a contraction of 3.8% in June (see Table 2).¹²

⁹ The construction confidence indicator is the arithmetic average of the seasonally-adjusted balances (in percentage points) of replies to two survey questions, namely those relating to order books and employment expectations over the subsequent three months.

¹⁰ The consumer confidence indicator is the arithmetic average of the seasonally-adjusted balances (in percentage points) of replies to a subset of survey questions relating to households' assessment and expectations of their financial situation, their expectations about the general economic situation and their intention to make major purchases over the subsequent 12 months. The computation of this indicator was changed as reflected in the [January 2019 release](#) of the European Commission.

¹¹ The EEI is based on question 7 of the industry survey, question 5 of the services and retail trade surveys and question 4 of the construction survey, which gauge the respondent firms' expectations as regards changes in their total employment over the next three months. Before being summarised in one composite indicator, each balance series is weighted on the basis of the respective sector's importance in overall employment. The weights are applied to the four balance series expressed in standardised form. Further information on the compilation of the EEI is available in: European Commission. (2020), *The Joint Harmonised EU Programme of Business and Consumer Surveys User Guide*.

¹² The annual growth rates of the overall industrial production index are based on working-day adjusted data. Unadjusted data, however, are used for the components.

Table 2		ACTIVITY INDICATORS															
<i>Annual percentage changes</i>																	
	2018	2019	2019									2020					
			June	July	Aug.	Sep.	Oct.	Nov.	Dec.	Jan.	Feb.	Mar. ⁽¹⁾	Apr. ⁽²⁾	May ⁽²⁾	June ⁽²⁾	July ⁽³⁾	
Industrial production	1.3	1.2	0.2	1.4	6.4	4.0	1.8	-2.8	8.8	12.0	13.6	6.4	-6.8	-9.0	-3.8	-2.6	
Commercial permits	14.5	-2.4	19.9	-0.3	-12.9	-10.8	-7.4	-12.8	-8.1	-24.2	-31.9	-56.8	-8.2	-25.2	-26.2	-9.8	
Residential permits	43.1	-3.1	-25.5	-45.3	-56.0	11.0	-6.5	12.3	34.4	22.2	-23.3	-19.6	-73.3	-53.6	-60.2	-8.1	
Retail trade	0.9	5.0	5.9	6.0	4.9	7.6	4.8	4.2	5.1	4.5	7.9	-1.9	-23.5	-13.1	-8.4	-8.1	
Number of tourist arrivals	14.3	5.9	8.0	5.2	7.2	5.5	6.2	9.1	19.3	16.8	16.5	-56.5	-	-	-	-84.0	
Number of nights stayed	12.5	4.1	5.1	1.6	5.8	2.1	6.5	9.0	15.1	3.5	10.1	-60.2	-	-	-	-75.3	
Rented accommodation	10.7	4.6	6.7	-1.7	7.4	2.8	12.1	9.6	13.9	7.7	11.1	-62.2	-	-	-	-84.3	
Collective ⁽⁴⁾	7.1	-0.1	2.0	-2.9	3.2	4.5	4.2	2.9	9.9	11.0	14.9	-61.7	-	-	-	-85.4	
Other rented ⁽⁵⁾	18.0	13.5	15.3	0.0	13.0	0.3	28.5	26.6	19.7	1.0	3.1	-63.5	-	-	-	-82.7	
Non-rented accommodation ⁽⁶⁾	22.7	1.6	-3.9	21.6	-2.0	-3.8	-19.8	6.3	20.8	-8.3	3.9	-47.7	-	-	-	-31.4	
Tourist expenditure	8.0	5.7	10.7	1.8	2.8	5.9	7.1	10.3	25.4	11.2	22.0	-62.6	-	-	-	-88.1	
Package expenditure	16.6	-8.2	6.4	-20.0	-10.1	-1.8	-6.2	4.9	7.9	-7.8	25.8	-69.8	-	-	-	-93.5	
Non-package expenditure	13.3	17.1	17.1	21.4	15.1	18.4	14.8	13.5	41.3	33.1	22.8	-58.8	-	-	-	-88.7	
Other	-2.2	5.9	7.8	3.8	0.9	-0.1	11.1	10.8	22.0	4.7	19.1	-60.2	-	-	-	-83.7	

Sources: National Statistics Office; Eurostat.

⁽¹⁾ Tourism data for March 2020 should be interpreted in the context of the unprecedented containment measures and travel restrictions introduced in response to COVID-19.

⁽²⁾ As a result of the COVID-19 situation, it was not possible for the NSO to issue the April, May and June 2020 news releases for Inbound Tourism.

⁽³⁾ The inbound tourism news release was issued for July following the reopening of Malta International Airport in the beginning of July.

⁽⁴⁾ Collective accommodation comprises hotels, guesthouses, hostels, tourist villages, holiday complex, bed & breakfast and campsites.

⁽⁵⁾ Other rented accommodation comprises holiday furnished premises (farmhouses, flats and villas), host families, marinas, paid-convents, rented yachts and student dormitories.

⁽⁶⁾ Non-rented accommodation includes own private residence, staying with friends or relatives and other private accommodation (e.g. free-convents or timeshare).

This decline largely reflected lower output by firms involved in the repair and installation of machinery and equipment as well those in the 'other manufacturing' sector, which includes firms involved in the production of medical and dental instruments, toys and related products. It also reflected a decline in output of firms that produce textiles and clothing, beverages, computer, electronic and optical products as well as rubber and plastic goods. On the other hand, production of food and pharmaceutical products increased. Firms involved in printing and recording of recorded media also reported higher activity, though to a lesser extent.

Meanwhile, production in the energy sector posted the first positive annual increase since April.

In July, annual growth in development permits for both commercial and residential buildings remained negative, though the pace of contraction was much slower than in the second quarter of the year. Commercial permits fell by an annual rate of -9.8%, while those for residential purposes declined by -8.1%. The latter, however, remain above the historical average.

The volume of retail trade, which is a short-term indicator of final domestic demand, contracted for the fifth consecutive time in July, although the rate of contraction eased compared to the previous month. It declined by an annual rate of 8.1%, following a fall of 8.4% in June.

The number of inbound tourists, nights stayed and expenditure declined substantially during July relative to the amounts recorded a year earlier, as several measures were enacted to limit the spread of COVID-19. Tourist arrivals declined by 84.0% on a year earlier. Nights stayed declined by 75.3%, driven primarily by a decrease in rented accommodation, although nights spent in non-rented accommodation also contracted. Furthermore, tourist spending in Malta fell by 88.1% in annual terms.

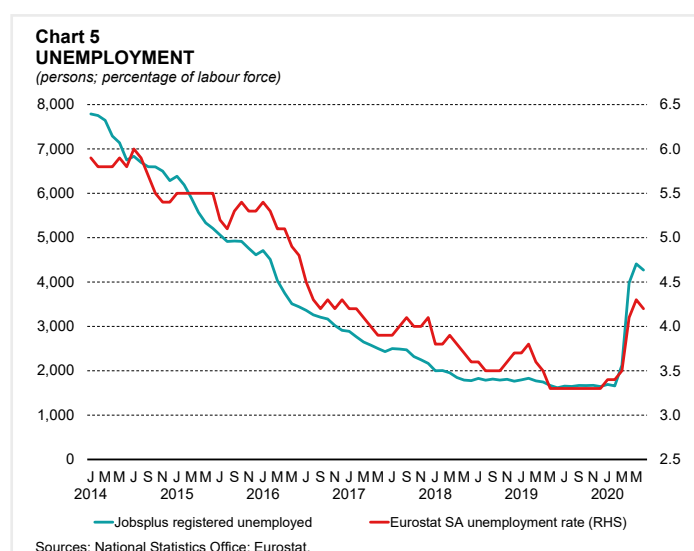
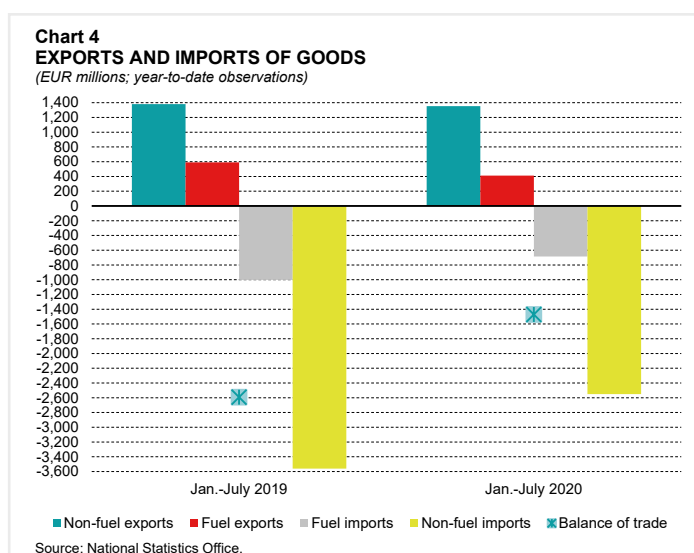
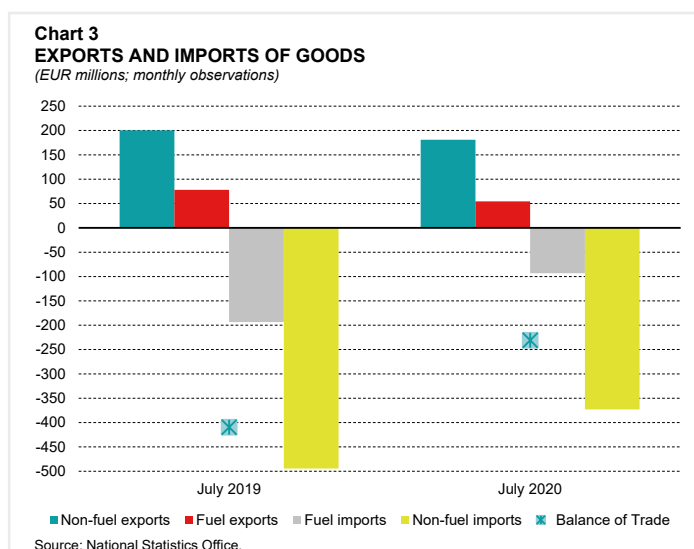
Customs data show that the merchandise trade deficit stood at €231.0 million in July, down from €409.7 million a year earlier. The significantly smaller deficit reflected a €221.7 million fall in imports, which offset a €43.1 million decline in exports (see Chart 3). Lower imports were observed across most categories. However, the fall in imports mainly reflected a substantial decrease in the fuel import bill, fewer registrations of aircraft and sea vessels, and, to a lesser extent, lower imports of machinery and mechanical appliances, electric machinery and organic chemicals. The decline in exports was due to lower re-exports of mineral fuels and related products, machinery and mechanical appliances, electrical machinery, and aircraft parts. Together these outweighed a rise in exports of pharmaceutical products and printed material.

In the seven months to July, the visible trade gap narrowed to €1,470.9 million from €2,591.4 million in the corresponding period of 2019, driven by a sharp fall in imports (see Chart 4).

Labour market

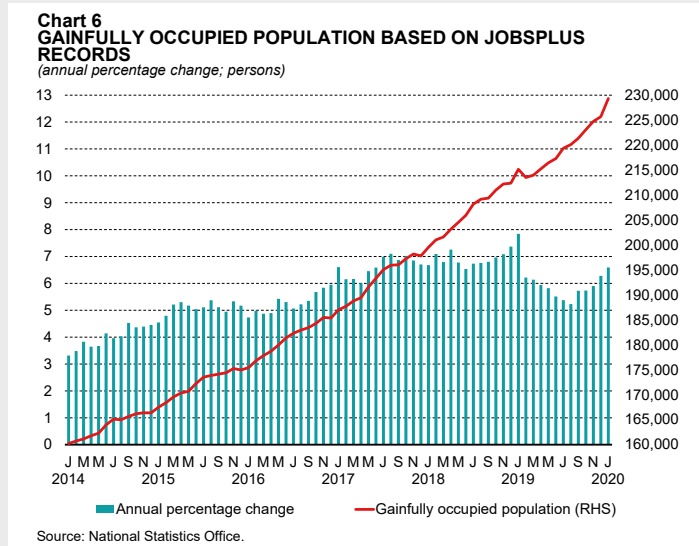
Jobsplus data show that the number of persons on the unemployment register stood at 3,981 in July, down from 4,270 in June but higher than 1,654 a year earlier (see Chart 5).

The seasonally-adjusted unemployment rate stood at 4.1% in July, down from 4.3% in the previous month, but still higher than the rate of 3.6% registered in the same month of 2019.



BOX 1: GAINFULLY OCCUPIED POPULATION

Jobsplus records show that in January 2020, the gainfully occupied population – defined as all persons in full-time employment – rose by 6.6% on a year earlier to 229,325 persons (see Chart 6 and Table 3). Annual growth was faster than the 6.3% registered in the preceding month, but lower than the 7.8% observed a year earlier.



As in recent months, growth in employment continued to be mainly driven by the private sector.

The number of full-timers in the private sector went up by 13,038, or 7.8%, compared with January 2019. Employment growth in this sector continued to be driven by market services, where the number of full-time job holders increased by 10,128, or 7.8% in annual terms. This increase was distributed across all major sectors within this category.

The sector incorporating real estate, professional and administrative activities registered the largest absolute increase. Employed persons in this sector went up by 4,159 in the year to January 2020 and accounted for slightly more than 40% of the overall rise in private market services employment. Employment also rose strongly in accommodation and food services activities – by 1,417 persons. The number of persons employed in ‘other services’ rose by 1,130, mostly reflecting increased employment in the sectors incorporating human health and social work activities, and the other service activities. Meanwhile, 884 additional persons were recruited in the arts, entertainment and recreation sector.

The number of persons employed in direct production rose by 2,910, or 8.0%, on a year earlier. Growth was mainly recorded in the construction sector, although employment in manufacturing also increased.

Public sector employment rose by 1,140, or 2.4%, on a year earlier. Employment increased mostly in the health and education sectors as well as in public administration and defence. Notwithstanding, the share of public sector employment in the total gainfully occupied population fell to 21.5%, from 22.4% a year earlier.

Table 3
LABOUR MARKET INDICATORS BASED ON JOBSPLUS RECORDS

Persons; annual percentage changes

	2019	2020	Annual change	
	January	January	Number of persons	%
Labour supply	216,943	231,016	14,073	6.5
Gainfully occupied ⁽¹⁾	215,147	229,325	14,178	6.6
Registered unemployed	1,796	1,691	-105	-5.8
Unemployment rate (%)	0.8	0.7		
Private sector	166,902	179,940	13,038	7.8
Direct production⁽²⁾	36,363	39,273	2,910	8.0
Of which:				
Manufacturing	21,663	22,220	557	2.6
Construction	11,823	13,902	2,079	17.6
Market services	130,539	140,667	10,128	7.8
Wholesale and retail trade	27,540	28,506	966	3.5
Transportation and storage	9,501	10,140	639	6.7
Accommodation and food service activities	14,363	15,780	1,417	9.9
Information and communication	7,211	7,515	304	4.2
Financial and insurance activities	10,285	10,527	242	2.4
Real estate, professional and administrative activities ⁽³⁾	34,230	38,389	4,159	12.2
Arts, entertainment and recreation	9,607	10,491	884	9.2
Education	5,875	6,262	387	6.6
Other	11,927	13,057	1,130	9.5
Public sector	48,245	49,385	1,140	2.4

Source: National Statistics Office.

⁽¹⁾ This category measures full-time employment.

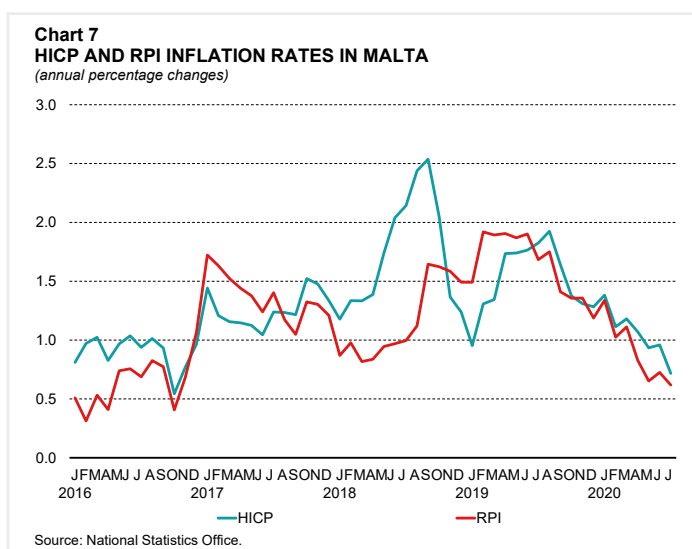
⁽²⁾ This includes employment in agriculture, fishing, mining and quarrying, manufacturing, electricity, gas and water supply, and construction.

⁽³⁾ This includes employment in real estate activities, professional, scientific and technical activities, and administrative and support service activities.

Prices, costs and competitiveness

Annual HICP inflation decelerated to 0.7% in July, from 1.0% in the previous month (see Chart 7). This was largely driven by lower growth in unprocessed food prices. At the same time, energy prices contracted, reflecting the mid-June cut in fuel prices.

Services inflation also fell slightly, reflecting a larger fall in prices of miscellaneous services. Meanwhile, processed food inflation declined marginally when compared with June. By contrast, non-energy industrial goods' prices rose, particularly due to an increase in prices of semi-durables.



Annual RPI inflation declined to 0.6% in July, from 0.7% in June (see Chart 7).¹³

Producer output inflation, measured by the producer price index, recovered to 1.2% in July, from -0.3% in June.¹⁴ This reflected positive growth in intermediate goods, which offset the marginally lower growth rates in producer prices of consumer and capital goods. Energy inflation remained nil.

Malta's nominal harmonised competitiveness indicator (HCI) increased by 2.3% in the year to July.¹⁵ This suggests a continued deterioration in the country's international competitiveness due to movements in the euro exchange rate against currencies of trading partners. The real HCI, which also takes into account relative price changes, rose by 2.2%, suggesting that favourable developments in relative prices vis-à-vis trading partners partly offset unfavourable exchange rate movements.

Public finance

In July 2020, the Consolidated Fund recorded a deficit of €156.2 million, a deterioration of €186.4 million when compared to the €30.2 million surplus registered in July 2019. This was mainly a result of a significant drop in government revenue (see Table 4). In turn, the primary balance registered a deficit of €142.7 million, in contrast to the €45.1 million primary surplus registered in July 2019.

¹³ The RPI and the HICP both measure changes in consumer prices but through different methodologies. The HICP index weights are based on total expenditure in Malta, including that by tourists. In contrast, RPI weights only take into account expenditure by Maltese households.

¹⁴ The Industrial Producer Price Index measures the prices of goods at the factory gate and is commonly used to monitor inflationary pressures at the production stage.

¹⁵ HCIs act as an effective exchange rate measure for countries operating within the euro area monetary union. The nominal HCI tracks movements in the euro exchange rate against the currencies of Malta's main trading partners, weighted according to the direction of trade in manufactured goods. On top of this, the real HCI also takes into account the relative inflation rate of Malta vis-à-vis its main trading partners. A higher (or lower) score in the HCI indicates a deterioration (or improvement) in Malta's international price competitiveness.

Table 4
CONSOLIDATED FUND BALANCE

EUR millions

	2019	2020	2019	2020	Change	
	Jan.-July	Jan.-July	July	July	Amount	%
Revenue	2,466.8	1,960.9	450.7	263.5	-187.2	-41.5
Direct tax	1,254.8	1,012.8	247.4	165.6	-81.8	-33.1
Income tax	877.8	671.1	192.7	114.1	-78.5	-40.8
Social security contributions ⁽¹⁾	377.0	341.6	54.8	51.5	-3.3	-6.0
Indirect tax	906.5	678.9	102.7	51.4	-51.3	-50.0
Value Added Tax	493.9	378.6	45.8	16.9	-28.9	-63.0
Customs and excise duties	182.9	126.6	29.3	8.4	-21.0	-71.4
Licences, taxes and fines	229.8	173.8	27.6	26.1	-1.5	-5.5
Non-tax⁽²⁾	305.5	269.2	100.6	46.5	-54.1	-53.8
Expenditure	2,592.8	3,012.6	420.5	419.7	-0.8	-0.2
Recurrent	2,310.4	2,534.5	357.7	328.4	-29.3	-8.2
Personal emoluments	511.5	527.9	69.9	73.6	3.7	5.3
Operational and maintenance	122.0	147.0	17.2	15.8	-1.4	-7.9
Programmes and initiatives ⁽¹⁾	1,271.2	1,410.7	182.0	183.7	1.7	0.9
Contributions to entities	296.6	342.3	73.7	41.8	-31.9	-43.3
Interest payments	109.1	106.6	14.9	13.5	-1.4	-9.5
Capital	282.4	478.1	62.9	91.3	28.5	45.3
Primary balance⁽³⁾	-16.8	-945.1	45.1	-142.7	-187.8	-
Consolidated Fund balance	-126.0	-1,051.7	30.2	-156.2	-186.4	-

Source: National Statistics Office.

⁽¹⁾ Government contributions to the social security account in terms of the Social Security Act 1987 are netted out from both revenue and expenditure.

⁽²⁾ Includes grants but excludes proceeds from sale of assets, sinking funds of converted loans and borrowings.

⁽³⁾ Revenue less expenditure excluding interest payments.

These developments reflect the impact on revenue of the slowdown in economic activity due to the global spread of COVID-19, and ongoing government support aimed at mitigating the economic effects of this pandemic.

Government revenue declined by €187.2 million or 41.5% in annual terms, driven by a drop in both tax and non-tax income. Revenue from direct taxes declined by €81.8 million, mainly due to a fall in revenue from corporate income. Similarly, indirect tax revenue fell by €51.3 million, predominantly due to lower VAT receipts and customs and excise duties. Moreover, inflows from non-tax revenue declined by €54.1 million, due to lower grants from the European Union.

Government expenditure recorded a marginal decline of €0.8 million, or 0.2% when compared to the corresponding period of 2019, as a drop in recurrent spending was largely offset by a rise in capital expenditure. Recurrent expenditure fell by €29.3 million, chiefly due to the timing of contributions to government entities. On the other hand, capital expenditure increased by €28.5 million, due to a higher subvention to Malta Enterprise, in order to finance the COVID-19 Wage Supplement scheme.

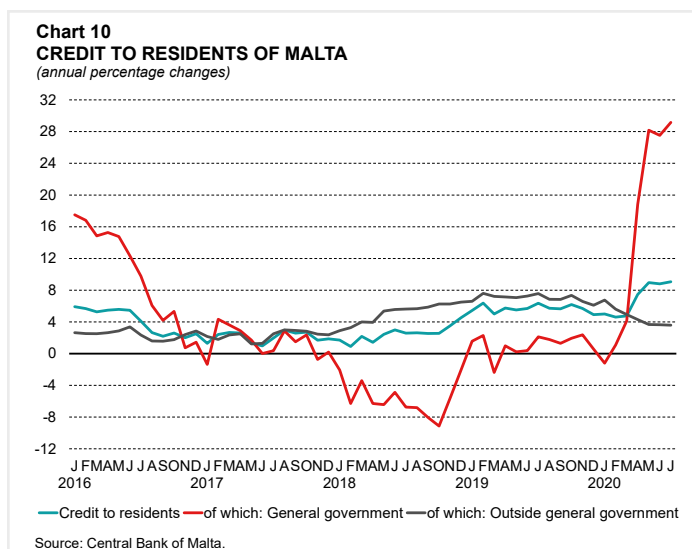
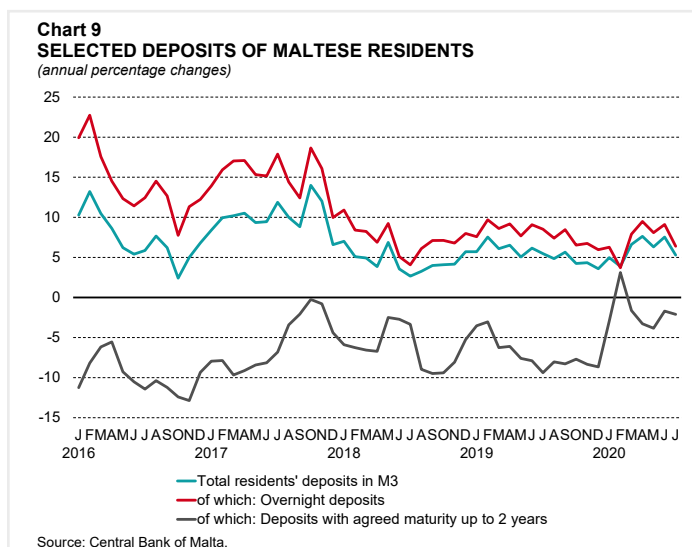
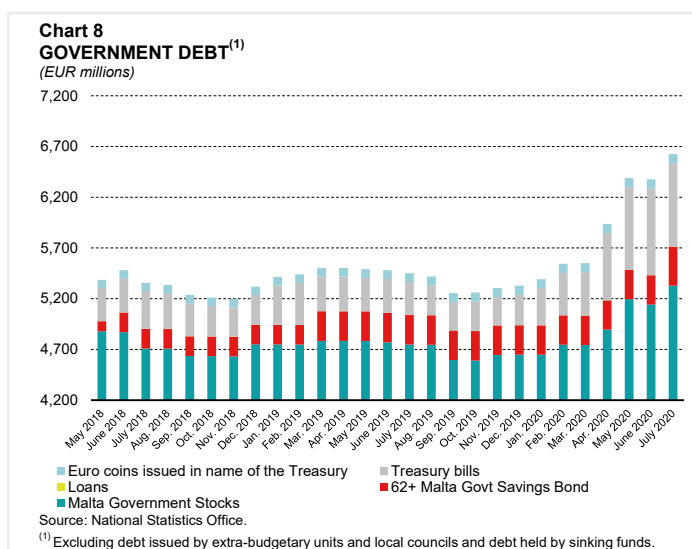
In July 2020, the total stock of government debt amounted to €6,624.2 million, an increase of €247.6 million when compared with a month earlier (see Chart 8). This was mainly due to a higher amount of outstanding Malta Government Stocks and new issues of 62+ Malta Government Savings Bond.

Deposits, credit and financial markets

In July, residents' deposits held with monetary financial institutions (MFI) and forming part of broad money (M3) expanded at an annual rate of 5.3%, after growing by 7.5% in June (see Chart 9).

Overnight deposits remained the largest component of residents' M3 deposits, comprising over 85% of their M3 balances. This deposit category – which is the most liquid – grew by 6.4% in the year to July. Meanwhile, time deposits with a maturity of up to two years – the second largest deposit category – fell by 2.1% in annual terms, following a contraction of 1.7% in the year to June.

Credit to Maltese residents grew at an annual rate of 9.1% in July, above the 8.8% recorded a month earlier (see Chart 10). Annual growth in credit to general government rose by 29.2% in July, following an increase of 27.5% in June. At the same time, growth in credit outside general government remained unchanged from the previous month, at 3.6%.

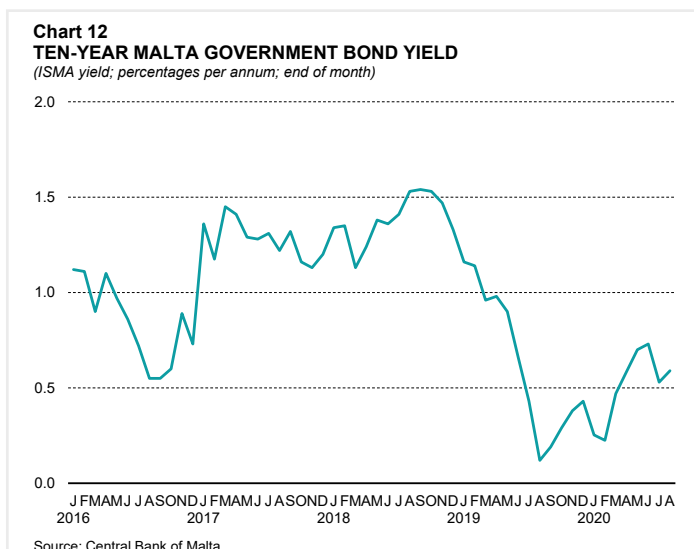
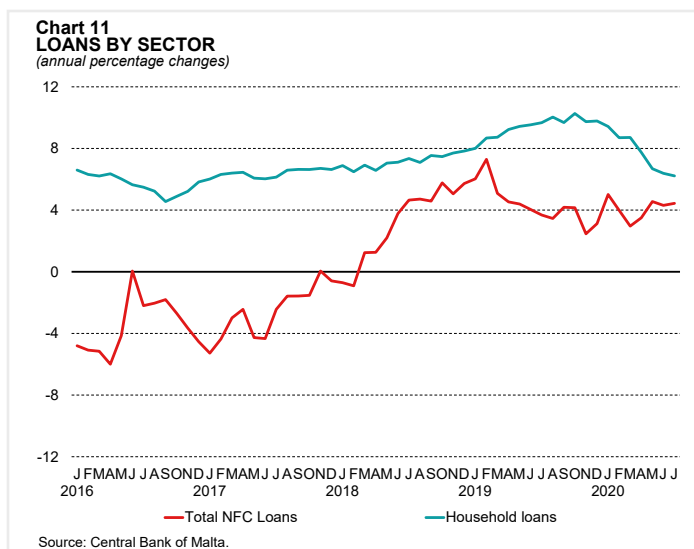


The annual rate of change in loans to non-financial corporations stood at 4.4%, marginally above the 4.3% registered in June (see Chart 11). The marginal increase in growth was largely driven by faster growth in credit to the sector comprising accommodation and food services activities and, to a lesser extent, in loans to the information and communication sector. In addition, loans to the wholesale and retail trade sectors declined at a slower rate. These developments were partly offset by a deceleration in loans to the

construction and real estate sector, the energy sector, and the sector comprising transportation and storage. At the same time, the annual rate of change of loans to households eased to 6.2%, from 6.4% in June. This reflected a faster contraction in consumer credit and other lending, which fell by 4.5%, following a contraction of 1.6% in June. Meanwhile, mortgage loans edged up to 7.4% in July, from 7.3% a month earlier.

As regards interest rates, the composite interest rate paid by MFIs on Maltese residents' outstanding deposits eased marginally to 0.24% in July, from 0.25% in June. The composite rate charged on outstanding loans edged down to 3.41%, when compared with 3.43% a month earlier. Hence, the spread between the two rates narrowed marginally to 317 basis points.

In the capital market, the secondary market yield on 10-year Maltese government bonds rose by six basis points from a month earlier, to 0.59% at the end of August (see Chart 12). Meanwhile, the Malta Stock Exchange (MSE) Equity Price Index declined by 5.9% during the same period. Similar movements were recorded in the MSE Total Return Index, which accounts for dividends as well as changes in equity prices.



BOX 2: LIQUIDITY SUPPORT MEASURES RELATED TO COVID-19

In response to the outbreak of COVID-19 and the subsequent containment measures, a number of businesses and households were faced with liquidity challenges, and thus applied with MFIs in Malta for a moratorium on loan repayments (see Table 5).¹⁶

As at end July, there were 9,624 loans subject to a moratorium on repayments. The total value of loans subject to a moratorium edged up to €1.8 billion, or 16.0% of total outstanding loans to Maltese residents, compared with June – when €1.7 billion, or 15.0% of total loans were subject to a moratorium.

The largest number of loans covered by moratoria was held by households, with the sector accounting for around 77.0% of the total volume of loans subject to a moratorium. Maltese households held €642.0 million, or 35.4%, of the total value of loans subject to a moratorium, equivalent to 10.4% of outstanding household loans.

Meanwhile, the real estate sector held €319.4 million in loans subject to a moratorium, or around 17.6% of such loans and equivalent to a third of this sector's outstanding loans. This was followed by the accommodation and food services activities, which held €230.3 million in loans subject to a moratorium. The latter was the sector most affected by the

Table 5
LOANS SUBJECT TO MORATORIUM – AS AT END JULY 2020

(Number of loans; EUR millions; percentage)

	Volume of loans ⁽¹⁾	Outstanding amounts ⁽²⁾	Share in sector's outstanding loans ⁽³⁾
Households	7,399	642.0	10.4
Manufacturing	154	49.2	22.4
Construction	131	57.1	9.0
Wholesale and retail trade; repair of motor vehicles and motor cycles	492	113.0	17.1
Transportation and storage and information and communication	103	80.4	29.5
Accommodation and food service activities	377	230.3	51.4
Real estate activities	447	319.4	33.0
Other ⁽⁴⁾	522	319.7	16.6
Total	9,624	1,811.1	16.0

Source: Central Bank of Malta.

⁽¹⁾ The number of loans subject to moratorium.

⁽²⁾ Outstanding amounts of loans subject to moratorium as at end of month, in EUR millions.

⁽³⁾ The percentage of loans subject to moratorium in total outstanding loans held by the sector as at end of month.

⁽⁴⁾ Includes loans to agriculture and fishing, mining and quarrying, public administration, education, health and social work, financial and insurance activities (including interbank loans), professional, scientific and technical activities, administrative and support service activities, arts, entertainment and recreation, other services activities and extra-territorial bodies & organisations, and the electricity, gas & water supply sector.

¹⁶ The loans subject to moratorium include both pre and post the Legal Notice 142 of 2020 on the Moratorium on Credit Facilities Regulations in Exceptional Circumstances (see [here](#)) and Central Bank of Malta [Directive No. 18](#). The latter entered into force on 13 April 2020. A number of banks had already started to provide moratorium facilities voluntarily in March 2020.

containment measures and, indeed, more than half – 51.4% – of the loans held by this sector were subject to a moratorium by the end of July. Moreover, as at end July, the wholesale and retail trade sector held €113.0 million in loans subject to a moratorium, making up 6.2% of such loans subject to a moratorium, or 17.1% of loans held by the sector.

In order to further alleviate liquidity challenges, the Government launched the Malta Development Bank (MDB) COVID-19 Guarantee Scheme (CGS) for the purpose of guaranteeing new loans granted by commercial banks for working capital purposes to businesses facing liquidity shortfalls as a result of the pandemic. The scheme enables credit institutions to leverage government guarantees up to a total portfolio volume of €777.8 million.¹⁷

By end July 2020, 340 facilities were approved under the CGS, covering total sanctioned lending of €238.0 million (see Table 6). As the scheme provides loans for working capital, only €88.9 million were disbursed by the end of July, up from the €61.2 million disbursed by the end of June.

In terms of the number of facilities, the sector comprising wholesale and retail activities applied for the largest number of facilities and had the largest value of sanctioned loans at €58.3 million. This was followed by accommodation and food services activities, with 79 facilities making up a total of €45.3 million sanctioned loans, and the sector comprising transportation and ICT, which had a total of €44.4 million.

Table 6
MDB COVID-19 GUARANTEE SCHEME – AS AT JULY 2020

(Number of facilities; EUR millions)

	Total number of facilities ⁽¹⁾	Sanctioned amount ⁽²⁾
Manufacturing	28	11.9
Construction	15	29.8
Wholesale and retail trade; repair of motor vehicles and motor cycles	94	58.3
Transportation and storage and information and communication	27	44.4
Accommodation and food service activities	79	45.3
Professional, scientific and technical activities	25	13.4
Administrative and support service activities	25	8.5
Real estate	9	1.3
Other ⁽³⁾	38	25.0
Total	340	238.0

Source: Malta Development Bank.

⁽¹⁾ The number of facilities taken by various sectors.

⁽²⁾ The total number of loans sanctioned under the scheme as at end month, in EUR millions.

⁽³⁾ Includes loans to education, health and social work, financial and insurance activities, arts, entertainment and recreation, other services activities, activities of households as employers and extra-territorial bodies & organisations, and the electricity, gas & water supply sector.

¹⁷ The MDB COVID-19 Guarantee Scheme was approved by the European Commission on 2 April 2020. See [here](#) for further details.

BOX 3: THE IMPACT OF THE RECENT APPRECIATION OF THE EUR/USD ON MALTA'S MANUFACTURING INDUSTRY¹⁸

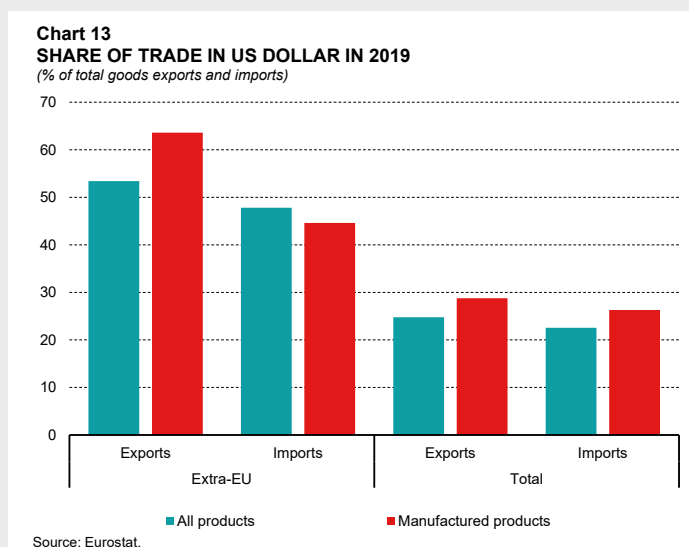
This Box quantifies the potential effects of the recent appreciation of the euro against the US dollar on Malta's manufacturing industry. The first section looks at the prevalence of the US dollar as an invoicing currency in Malta's merchandise exports and, more specifically, manufactured products. The second section outlines recent developments in production in manufacturing output, compared to the euro area. The Box then presents estimates of the possible impact of the appreciation of the euro-dollar exchange rate that occurred from 3 January to 31 August 2020, on GDP, total exports and manufacturing value added.

Trade in US dollars – 2019

International trade data can be classified by invoicing currency. Chart 13 shows the share of Maltese goods exports and imports that were traded in dollars in 2019. It reports such shares for all traded products (including manufacturing goods), and manufactured products¹⁹ as well as those traded with countries outside the EU (extra-EU).

In 2019, the share of the US dollar in goods exports to countries outside the EU stood at 53.4%, while the share in goods imports to these countries was 47.8%. Manufactured products have a higher utilisation of the dollar as an invoicing currency, as the share of dollar in such exports and imports with countries outside the EU stood at 63.6% and 44.6%, respectively. Around 31% of manufactured goods exports with extra-EU countries are invoiced in euro, while around 50% of manufactured goods imports are also invoiced in euro. This suggests that the euro is also a prevalent currency for Malta's international trade.

When including both extra- and intra-EU trade, the share of dollar trades goes down sharply, since – as expected – the use of the euro as an invoicing currency becomes more prevalent. Indeed, the share of total goods exports traded in dollars with all geographical regions stood at 25% in 2019, while that for imports stood at 23%. Manufactured products continue to exhibit a



¹⁸ Prepared by Ian Borg and Noel Rapa. Ian Borg is manager within the Bank's Economic Analysis Department, and Noel Rapa is a principal research economist within the Bank's Research Department.

¹⁹ This section utilises the Standard International Trade Classification (SITC), which is a product classification of the United Nations used for external trade statistics (export and import values and volumes of goods), allowing for international comparisons of commodities and manufactured goods.

stronger dollar utilisation than other products. The dollar was used as an invoicing currency in 29% of manufactured exports and 26% of manufactured imports with all countries.

A deeper investigation of dollar-invoicing patterns across sectors shows that sectors such as those involved in the production of electrical machinery (which includes semiconductors), textiles, wood and paper, as well as the printing sector had between 30% and 50% of their exports invoiced in dollars.

The biggest contributor towards the utilisation of the dollar in Malta's trade in goods (and manufactured products specifically) is the semiconductor industry. Indeed, in 2019, it accounted for more than 40% of all dollar-related goods exports in Malta. Regarding imports, the contribution is slightly more evenly split. Indeed, the sector comprising aircraft had the largest share of dollar-related imports. In addition, minerals and the electrical machinery sector were the second and third largest contributors.

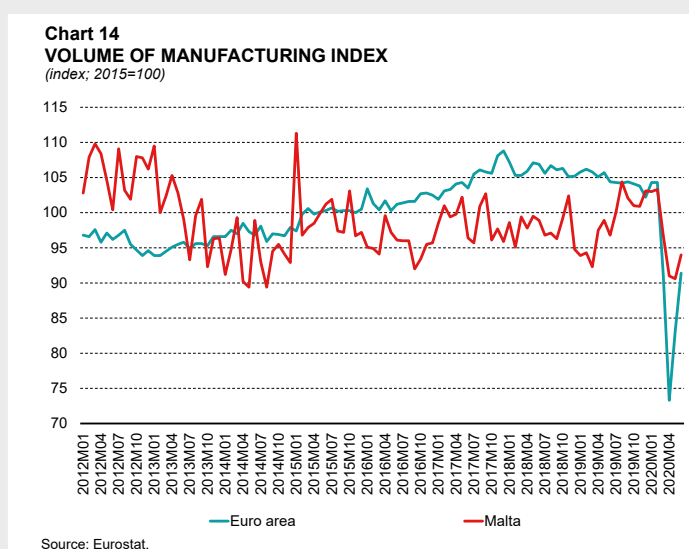
Recent developments in Malta's manufacturing output

Chart 14 shows the volume index of manufacturing since 2012, for the euro area and Malta. It shows that in general Malta's manufacturing performance diverges from the rest of the euro area. Indeed, while manufacturing in the euro area in 2019 declined, Malta registered a small increase.

Moreover, although the pandemic has meant that all countries, including Malta, suffered strong declines in production volumes since March 2020, the losses in Malta's manufacturing industry were much lower. In April, manufacturing production in the euro area decreased by almost a third, while in Malta it only declined by 7%. On a month-on-month basis, all countries recovered strongly as containment measures started being lifted in the second quarter.

The impact of the EUR/USD exchange rate appreciation on manufacturing

Between 3 January and 31 August 2020, the euro appreciated by around 6.7% against the dollar, from around 1.11 to 1.18. The negative effect on economic activity is estimated in two steps. Firstly, the Basic Model Elasticities (BMEs) – estimated using the Bank's macroeconomic model



STREAM – are used to derive the effect of the euro’s appreciation on GDP and total exports.²⁰ Since STREAM models aggregate exports, rather than goods exports, this impact needs to be converted to the manufacturing sector’s gross value added. This step is implemented using the Bank’s integrated model, which integrates input-output estimates with STREAM.²¹

According to STREAM, the 6.7% appreciation of the euro against the US dollar that occurred in the first eight months of the year implies a decline of around 0.05% in GDP and a drop of around 0.09% in total exports in 2020.²²

Transposing these results into sectoral impacts using the Bank’s integrated model yields an estimate of the impact of the euro’s appreciation on the manufacturing sector’s gross value added. The latter would decline by around 0.05% in 2020. This decrease is driven by firms that manufacture computer, electronic and optical products. Other sectors such as the manufacture of basic materials, the manufacture of paper and paper products, as well as the manufacture of textiles, also register relatively significant declines.

However, within the context of the significant disruptions related to the pandemic, it is hard to precisely identify the impact of exchange rate shocks. Developments in the manufacturing industry (or any other industry) at the moment, mostly reflect sector-specific consequences of containment measures. For example: supply-chain disruptions may have slowed manufacturing production during the first phase of the pandemic. The demand for certain manufactured products has also declined substantially due to containment measures, which restrict mobility, and the impact of the ongoing world recession on firms’ and households’ finances. In this context, it is challenging to disentangle exchange rate effects from other shocks and, hence, the estimates presented above should be treated with caution. Moreover, the impact of exchange rate movements against the US dollar on the economy can be amplified or offset by movements of the euro against other currencies.

²⁰ See Grech Rapa (2016): *STREAM: A Structural Macro-Econometric Model of the Maltese Economy*. WP/01/2016.

²¹ The Bank’s integrated model was utilised to quantify the impact of COVID-19 on Malta’s economic sectors. The latter was published in Box 1 of the latest forecast publication, see [here](#).

²² According to BMEs estimated for all euro area countries, the impact of a EUR/USD appreciation for Malta is quantitatively and qualitatively similar to that for the euro area.

MACROECONOMIC INDICATORS FOR MALTA

(Annual percentage changes; non-seasonally adjusted data)

	2018	2019	2019	2019	2020	2020	2019	2019	2019	2019	2019	2019	2020	2020	2020	2020	2020	2020	2020	2020
			Q3	Q4	Q1	Q2	July	Aug.	Sep.	Oct.	Nov.	Dec.	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.
Prices and costs																				
HICP inflation	1.7	1.5	1.8	1.3	1.2	1.0	1.8	1.9	1.6	1.4	1.3	1.3	1.4	1.1	1.2	1.1	0.9	1.0	0.7	-
RPI inflation	1.2	1.6	1.6	1.3	1.2	0.7	1.7	1.7	1.4	1.4	1.4	1.2	1.3	1.0	1.1	0.8	0.7	0.7	0.6	-
Industrial producer price inflation	4.4	2.2	1.8	1.8	1.1	0.2	1.8	1.6	2.1	2.3	1.4	1.6	1.8	1.7	0.0	0.6	0.3	-0.3	1.2	-
HCI (nominal)	2.6	-0.7	-1.0	-1.1	-0.2	1.2	-0.7	-0.5	-1.7	-1.1	-1.0	-1.3	-1.1	-1.0	1.7	1.3	0.9	1.3	2.3	-
HCI (real)	2.1	-1.1	-1.0	-1.6	-0.9	1.2	-0.9	-0.5	-1.8	-1.4	-1.4	-2.0	-1.9	-1.9	1.2	1.4	1.0	1.3	2.2	-
Unit labour costs, whole economy ⁽¹⁾	1.7	2.4	3.4	3.6	5.0	10.4	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Compensation per employee ⁽¹⁾	2.9	1.5	3.0	2.8	2.8	2.3	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Labour productivity (per person) ⁽¹⁾	1.3	-1.0	-0.5	-0.8	-2.0	-6.6	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Property Price Index (Eurostat)	5.8	6.1	6.0	5.7	5.6	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Economic activity																				
Nominal GDP	7.3	7.2	5.9	7.4	3.2	-14.9	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Real GDP	5.2	4.9	3.6	5.0	1.4	-16.2	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Real private consumption	8.5	5.2	3.8	4.5	-1.5	-20.7	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Real government consumption	12.0	11.5	8.6	6.7	12.9	11.9	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Real gross fixed capital formation	3.1	8.8	1.9	2.2	-14.5	-11.0	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Real exports of goods and services	-0.5	6.1	8.2	5.6	2.6	-12.8	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Real imports of goods and services	0.4	7.9	9.3	5.2	0.3	-7.9	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Labour market developments																				
LFS unemployment rate (% of labour force)	3.7	3.4	3.4	3.2	3.3	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
LFS employment	7.8	5.8	4.5	5.4	5.5	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Jobsplus gainfully occupied	6.8	5.8	5.4	6.0	-	-	5.4	5.2	5.7	5.7	5.9	6.3	6.6	-	-	-	-	-	-	-
Balance of payments																				
Current account (as a % of GDP) ⁽²⁾	11.1	9.8	8.7	9.8	10.3	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Credit and financial indicators																				
Maltese residents' deposits and loans																				
Overnight deposits	8.0	6.0	8.5	6.0	7.9	9.1	8.5	7.4	8.5	6.5	6.7	6.0	6.3	3.7	7.9	9.5	8.1	9.1	6.4	-
Deposits with agreed maturity up to 2 years	-5.2	-8.7	-8.3	-8.7	-1.6	-1.7	-9.4	-8.0	-8.3	-7.7	-8.3	-8.7	-2.9	3.1	-1.6	-3.3	-3.8	-1.7	-2.1	-
Total residents' deposits in M3	5.7	3.6	5.7	3.6	6.6	7.5	5.5	4.8	5.7	4.2	4.3	3.6	5.0	3.9	6.6	7.6	6.3	7.5	5.3	-
Credit to general government	-2.0	0.6	1.3	0.6	4.1	27.5	2.1	1.8	1.3	1.9	2.4	0.6	-1.2	1.1	4.1	18.8	28.2	27.5	29.2	-
Credit to residents (excl. general government)	6.5	6.1	6.8	6.1	4.9	3.6	7.6	6.8	6.8	7.3	6.6	6.1	6.8	5.6	4.9	4.3	3.7	3.6	3.6	-
Total credit	4.5	4.9	5.6	4.9	4.8	8.8	6.4	5.7	5.6	6.2	5.7	4.9	5.0	4.6	4.8	7.5	9.0	8.8	9.1	-
10-year interest rate (%) ⁽³⁾	1.3	0.4	0.2	0.4	0.5	0.7	0.4	0.1	0.2	0.3	0.4	0.4	0.3	0.2	0.5	0.6	0.7	0.7	0.5	0.6
Stock prices: Malta Stock Exchange Index ⁽⁴⁾	0.1	4.4	2.1	-4.0	-19.5	6.8	0.7	-1.0	2.4	-1.6	-2.5	0.0	-1.2	-0.6	-18.0	6.1	-1.1	1.7	-3.5	-5.9
General government finances (% of GDP)																				
Surplus (+) / deficit (-) ⁽²⁾	1.9	0.5	0.5	0.5	-1.6	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Gross debt ⁽⁵⁾	45.2	42.6	43.2	42.6	43.9	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-

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

⁽¹⁾ Four-quarter moving averages.⁽²⁾ Four-quarter moving sums.⁽³⁾ End of period.⁽⁴⁾ Period-on-period percentage changes, based on end-of-month data.⁽⁵⁾ GDP data are four-quarter moving sums.