

What is really driving recent inflation?



In recent months the topic of inflation has reappeared on the local agenda

This perhaps was mostly driven by headline HICP inflation in Malta being above that of the Euro area (EA) since April of this year.

Indeed, the data shows that between the first quarter (Q1) of 2025 and the period of April to August, the year-on-year (to avoid seasonal distortions) rate of inflation in Malta has picked up from 2% to 2.6%, as shown in Table 1. While average inflation for the first eight months stood at 2.4%, which is broadly in line with average inflation over the past 25 years, nevertheless, the readings of April to August show a higher rate than this long-term average.

Moreover, the data shows that whereas during the first quarter inflation in Malta was lower than that of the EA, in the period of April to August inflation picked up, while that in the EA slowed down from 2.3% to 2%.

So, what is driving inflation higher in Malta between Q1 and the period April-August? What is driving the difference in inflation between Malta and the EA average in the latter period? And should we be concerned about these developments? The answer to the latter question is probably no, but close monitoring is war-



ranted and will explain why using the information shown in Table 2.

The middle column of Table 2 shows the underlying factors that have led to the increase of practically 0.6ppts in inflation in Malta between Q1 and April-August. Around half (0.27ppts) of this increase was driven by a pick-up in food inflation. However, the EA also experienced a pick-up in food inflation during this period, although by less (0.10ppt). But when looking at food inflation for the first eight months of 2025 (Table 1), the difference in inflation between Malta (3.2%) and the EA (3%) is relatively small, which indicates that the rise in food prices was broadly driven by higher international food prices, leading to higher prices in the EA, which is an important source of Malta's food imports.

The other half of the increase in inflation between Q1 and the April-August period was driven by inflation in services (0.29ppt). When one digs deeper into this, one finds that this was almost

equally driven by the contribution of higher Air Transport (0.14ppts) and Restaurants & Hotels (0.15ppts) categories. Both components are related to tourism activity which continued to grow strongly during the first seven months of 2025, as the number of tourists, bed-nights, and their expenditure all increased at double-digit rates. With such strong demand from tourism, providers of such services were in a stronger position to extract higher prices.

As shown in Table 2, the contribution of both energy and non-energy industrial goods (NEIG) to the pick-up in inflation in the April-August period was virtually zero, as was the case for the EA with respect to NEIG.

As regards to inflation in Malta in the April-August period becoming higher than that in the EA, the first column of Table 2 shows that energy played an important role, as it accounted for almost half of this difference. As international oil prices fell, energy inflation in the EA declined, and indeed as the last column

in Table 2 shows, this was the major driver of the drop in inflation in the EA after Q1. Of course, in Malta there was no such decline as energy prices remain frozen since 2020. However, a look at the energy index shows that the price level in the EA in August was still 35% higher than the pre-Covid period of December 2019, whereas in the case of Malta it is 3.5% lower than in December 2019, reflecting the government energy subsidies since then.

Apart from the energy element, Table 2 shows that Air Transport (0.39ppts) together with Restaurants & Hotels (0.12ppts) also played a huge role in raising Malta's inflation above that of the EA. Indeed, although overall services do not appear to contribute to the inflation differential between Malta and the EA, the high contribution of Air Transport and Restaurants & Hotels was offset by lower inflation in Malta for all other services combined relative to that of the EA. Indeed, lower inflation in services excluding Air Transport and Restaurants

& Hotels offsets the higher contribution of Energy, Food and NEIG combined.

Thus, the rise in inflation in the April-August period was partly driven by higher imported food inflation and the strong growth in tourism. These factors, together with developments in international energy prices, were also behind inflation in Malta exceeding that of the EA during this period. While the fall in energy prices is of no concern for driving this inflation differential between Malta and the EA, as it actually also reduces the subsidy burden to public finances, the contribution of the tourism components to inflation may reflect to an extent a favourable terms of trade shock to Malta as a major provider of such activity given that real demand continued to grow, although in this regard, going forward, careful monitoring is warranted for tourism competitiveness considerations.

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TABLE 1. HICP Inflation Rates (year-on-year % changes)

	Q1 2025		April to August 2025		Jan. to Aug 2025	
	Malta	Euro Area	Malta	Euro Area	Malta	Euro Area
HICP	2.0	2.3	2.6	2.0	2.4	2.1
HICP excluding Food & Energy	2.0	2.6	2.5	2.4	2.4	2.5
Energy	0.0	0.4	0.0	-2.8	0.0	-1.6
Food (including alcohol & tobacco)	2.4	2.6	3.7	3.2	3.2	3.0
Non-Energy Industrial Goods	0.8	0.6	0.9	0.7	0.9	0.6
Services	2.7	3.7	3.4	3.4	3.2	3.5
Air Transport	21.8	0.6	32.6	2.8	28.5	2.0
Restaurants & Hotels	2.4	4.0	3.4	3.7	3.0	3.8

Source: Eurostat

TABLE 2. Contribution to Inflation differential (ppts)

	April-Aug		April-Aug Q1 2025	
	Malta/EA	Malta	Malta	EA
HICP	0.55	0.58	-0.33	
Energy	0.26	0.00	-0.30	
Food (including alcohol & tobacco)	0.19	0.27	0.10	
Non-Energy Industrial Goods	0.08	0.02	0.02	
Services	0.01	0.29	-0.15	
Air Transport	0.39	0.14	0.02	
Restaurants & Hotels	0.12	0.15	-0.04	

Source: Own calculations based on Eurostat data