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CENTRAL BANK OF MALTA

INTERIM FINANCIAL STABILITY REPORT

2026

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Unless otherwise stated, the cut-off date for regulatory and prudential returns is 27 August 2026. The general risk assessment in this edition of the Report focuses primarily on developments in the first half of 2026, although in some cases it has been updated to reflect more recent events. Unless otherwise indicated, the source of data in the tables and charts is the Central Bank of Malta.

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ABBREVIATIONS

AI	Artificial Intelligence
AMC	Amortised cost
ASF	Available stable funding
AUM	Assets under management
BCaR	Bank Capital-at-Risk
BoF-PSS3	Bank of Finland Payment and Settlement System Simulator
BPaR	Bank Profitability-at-Risk
CAPM	Capital asset pricing model
CASP	Crypto-asset service provider
CBC	Counterbalancing Capacity
CBM	Central Bank of Malta
CCyB	Countercyclical capital buffer
CET1	Common equity tier 1
CoE	Cost of equity
CRE	Commercial Real Estate
CRP	Country Risk Premium
cSRI	Cyclical Systemic Risk Indicator
DCC	Dynamic Conditional Correlation
EA	Euro area
EBA	European Banking Authority
ECB	European Central Bank
EEA	European Economic Area
EIOPA	European Insurance and Occupational Pensions Authority
ERP	Equity Risk Premium
ESCB	European System of Central Banks
ESRB	European Systemic Risk Board
ETF	Exchange-traded fund
EU	European Union
EUR	Euro
FSR	Financial Stability Report
FV	Fair value
GBP	Great British Pound
GDP	Gross domestic product
GPR	Geopolitical risk index
GWP	Gross written premia
HHI	Herfindahl-Hirschman Index
HICP	Harmonised Index of Consumer Prices
HQLA	High-quality liquid assets
ICT	Information and communications technology
IL	Index-linked
IMF	International Monetary Fund
IRRBB	Interest rate risk in the banking book
LCR	Liquidity coverage ratio
LSTI	Loan service-to-income
LTRO	Longer-term refinancing operation
LTV	Loan-to-value
MFI	Monetary financial institution
MFSA	Malta Financial Services Authority
MGS	Malta Government Stocks
MiCA	Markets in Crypto-Assets Regulation
MMF	Money market fund

MRR	Minimum reserve requirement
MSE	Malta Stock Exchange
NAV	Net asset value
NBFI	Non-bank financial institution
NFC	Non-financial corporation
NII	Net interest income
NPL	Non-performing loan
NSFR	Net stable funding ratio
NSO	National Statistics Office
OFI	Other financial intermediary
O-SII	Other Systemically Important Institution
PDW	Persistent deposit withdrawals
QLP	Quantile local projection
RCR	Redemption Coverage Ratio
RHS	Right-hand scale
ROA	Return on assets
ROE	Return on equity
RRE	Residential real estate
RSF	Required stable funding
RTGS	Real-time gross settlement
RWA	Risk-weighted assets
SCR	Solvency Capital Requirement
sDSTI	Stressed debt service-to-income
sSyRB	Sectoral Systemic Risk Buffer
TPU	Trade policy uncertainty
TREA	Total Risk Exposure Amount
UCITS	Undertakings for the Collective Investment in Transferable Securities
UL	Unit-linked
US	United States
USD	United States dollar
USDC	USD Coin
USDT	Tether
WAIR	Weighted average interest rate

EXECUTIVE SUMMARY

The first half of 2026 was characterised by a challenging external macro-financial environment, amid elevated geopolitical tensions, persistent trade-policy uncertainty (TPU) and renewed volatility in commodity and financial markets. Nevertheless, the global economy remained resilient. Euro area activity was also better than expected at the beginning of 2026, although growth remained modest. Renewed inflationary pressures, fiscal sustainability concerns and political uncertainty in some economies contributed to financial-market volatility, while stretched valuations in certain market segments increased the risk of abrupt repricing.

Against this backdrop, Malta's economy and financial system remained resilient. Economic growth remained robust in the first half of 2026, supported by domestic demand, favourable labour market conditions and continued strength in tourism-related services. At the same time, inflation moderated to 2.0% by mid-year. Public and private-sector balance sheets remained broadly sound, with the government debt-to-gross domestic product (GDP) ratio comfortably below the Treaty reference value. Corporate indebtedness was below the euro area average, while aggregate household balance sheets remained supported by substantial financial wealth and savings. However, these household financial buffers may not be evenly distributed, leaving more highly indebted or financially constrained households more vulnerable to adverse shocks.

Housing market activity remained buoyant, with domestic house prices increasing further and mortgage lending continuing to grow strongly. The combination of such dynamics coupled with increasing household leverage warrants continued monitoring, particularly given banks' significant exposures to mortgages and property-related corporate lending. Borrower-based measures and prudent lending standards help mitigate borrower vulnerabilities, while the sectoral Systemic Risk Buffer (sSyRB) strengthens banks' loss-absorbing capacity. Nonetheless, the concentration of bank lending in property-related activities remains a structural vulnerability that could amplify the impact of a deterioration in domestic economic conditions or an adverse housing-market correction.

The banking sector continued to report strong capital and liquidity positions, sound asset quality and generally solid profitability. Core domestic banks expanded their balance sheets through higher customer lending and sovereign bond holdings, while non-performing loans (NPLs) declined further. Profitability remained broadly stable, although higher operating costs weighed on the banks' cost-efficiency. Non-core domestic banks' balance sheet continued to contract but retained comfortable capital and liquidity buffers and reported improved profitability. Some forward-looking credit-risk indicators for this category weakened, while investment portfolios shifted towards foreign corporate bonds and an increased share of speculative-grade and unrated securities. International banks expanded strongly and recorded improved asset quality and profitability, although some institutions remained exposed to concentrated sovereign holdings in their home jurisdictions and to higher-risk consumer lending segments.

Stress-test results continued to support the banking sector's overall resilience in terms of both solvency and liquidity. In particular, liquidity assessments indicated that, at the aggregate level, all three bank categories retained sufficient liquidity and stable funding buffers under the adverse scenarios considered, although a few individual institutions showed greater sensitivity to certain hypothetical shocks by scenario design. The interest-rate risk in the banking book (IRRBB) assessment, which seeks to quantify the impact of different interest-rate shock scenarios on banks' solvency, indicated that banks can absorb the materialisation of such shocks. This resilience continues to be supported by banks' relatively high share of instruments measured at amortised cost (AMC). Results vary across banks, reflecting the composition of their balance sheets.

The domestically relevant non-bank financial sector also remained broadly resilient. Domestically relevant insurance companies continued to expand and remained well capitalised, with broadly adequate liquidity across both life and non-life segments. Profitability developments were mixed, with life insurers reporting weaker profits despite improved underwriting performance, while non-life insurers benefited from stronger investment returns even as claims increased faster than premia. Domestically relevant investment funds

recorded only modest asset growth. These funds continued to be characterised by very low leverage, substantial holdings of liquid assets and robust aggregate redemption coverage, although liquidity buffers moderated and operating profitability weakened. Despite an improvement in the credit quality of their bond portfolios, increased equity exposures, material holdings of speculative-grade and unrated bonds leave the sector exposed to market repricing and redemption pressures, with links to domestic households and financial institutions providing possible channels of domestic contagion.

Looking ahead, Malta is expected to maintain robust economic growth, but risks to financial stability remain tilted to the downside. A further escalation of geopolitical tensions, a broadening of the recent energy and commodity-price shocks could weigh on import prices and foreign demand, as well as related disruptions to global trade could weaken economic activity and place pressure on sovereigns', corporates' and households' balance sheets. A further tightening of financial conditions and possible abrupt corrections in certain financial-market segments exhibiting stretched valuations represent additional sources of downside risk. These cyclical risks may be compounded by structural vulnerabilities arising from concentration and interconnectedness, reliance on critical third-party service providers, and growing operational, cyber, artificial intelligence (AI)-related and climate-related risks. Continued vigilance, together with sound risk management and adequate capital and liquidity buffers, therefore remains important to preserve the resilience of Malta's financial system.

The report is also complemented by five analytical boxes and two special features. Box 1 examines the extent to which residential property purchases in Malta are associated with mortgage financing from domestic banks, offering insights into how credit conditions, monetary policy and macroprudential measures may transmit to the housing market. Box 2 examines the relationship between cyclical systemic risk and downside risks to bank profitability, while Box 3 assesses the cost of equity (CoE) of Maltese banks and examines the extent to which it varies across institutions and over time. Box 4 assesses the significance of catastrophe risk for domestically relevant non-life insurers, focusing on its contribution to the Solvency Capital Requirement (SCR) under the Solvency II framework. Box 5 examines the role of stablecoins within Malta's licensed crypto-asset service providers (CASPs), assessing their relative importance, currency composition and concentration across reporting entities. Special Feature A uses TARGET2-Malta transaction data to quantify the potential liquidity effects of hypothetical cyber-related payment disruptions and their propagation through the payment network. Finally, Special Feature B presents a sensitivity analysis of the Redemption Coverage Ratio (RCR), providing a forward-looking assessment of the resilience of domestically relevant investment funds sector to redemption pressures at both fund and aggregate levels.

1. MACROPRUDENTIAL RISK ASSESSMENT AND POLICY RESPONSE

1.1 Macroprudential risk assessment

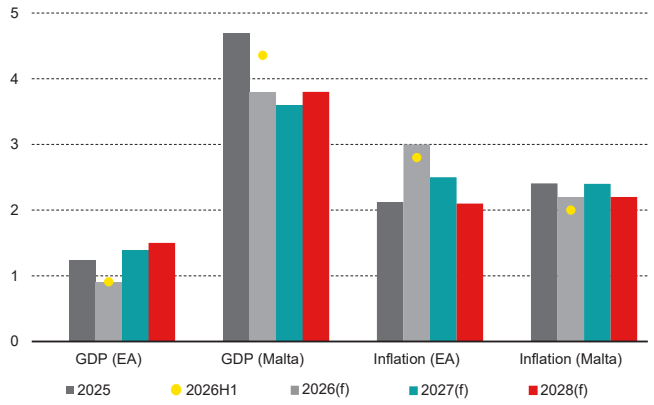
The external macro-financial risk environment remained characterised by elevated geopolitical tensions, heightened TPU and renewed volatility in energy and financial markets during the first half of the year. Against this backdrop, however, the global economy continued to display resilience, with economic activity holding up despite these shocks.[1] At the same time, these developments contributed to renewed inflationary pressures and uncertainty around the outlook and bouts of financial market volatility, while risks to global growth remained tilted to the downside. Although Malta, as a small and open economy, remains exposed to external shocks, the domestic financial system remained resilient. Nevertheless, the evolving external environment warrants continued vigilance, given the potential for external shocks to spill over into the domestic economy, potentially challenging financial stability.

1.1.1 Macroeconomic developments

Economic activity in the euro area remained subdued but stable in the first half of 2026, with real GDP expanding by 0.9% compared with the same period of 2025 (see Chart 1.1).[2] Growth was supported primarily by services and manufacturing, including technology and defence-related industries, as well as AI-related investment and inventory accumulation, the latter partly reflecting precautionary stock building amid supply-chain concerns.[3] Household consumption continued to support activity, benefiting from resilient labour market and wage growth, although consumption growth moderated amid higher energy prices and uncertainty. Public investment, including projects financed through the Recovery and Resilience Facility, also supported demand. By contrast, construction investment remained weak, while export growth and competitiveness challenges limited the contribution from external demand. Economic growth is expected to remain modest in the near term. The Middle East conflict and disruptions to energy supplies through the Strait of Hormuz contributed to upward inflationary pressures during the first six months of the year, driven mainly by energy prices. Services inflation made a more limited contribution, although it remained elevated amid persistent wage and domestic cost pressures. Against this background, the European Central Bank (ECB) raised its key interest rates by 25 basis points in both June and September of this year. These increases brought the deposit facility rate to 2.50% effective from 16 September 2026.

Economic activity in Malta remained robust in the first six months of the year. While real GDP growth moderated from 4.7% in the corresponding period of 2025 to around 4.4%, Malta continued to rank among the fastest-growing economies in the euro area. Domestic demand remained the main driver of growth, underpinned by strong consumption growth, favourable labour market conditions and continued government expenditure.[4] From a sectoral perspective, growth was driven by services, particularly wholesale and retail trade, transportation, accommodation and food services, as activity in the tourism industry remained buoyant. In contrast to the euro area, Harmonised Index of Consumer Prices (HICP) inflation in Malta fell to 2.0% in June 2026, and

Chart 1.1
ECONOMIC GROWTH AND INFLATION DEVELOPMENTS
(annual growth rate; per cent)

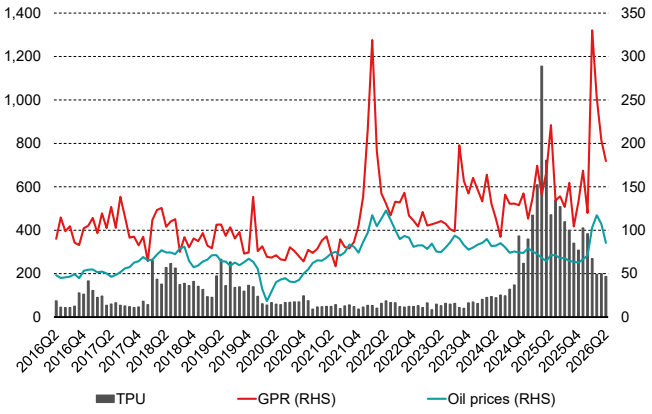


Sources: Eurostat; ECB; and Central Bank of Malta.
Note: Annual figures for 2026 onwards represent forecasts.

[1] Source: IMF World Economic Outlook, Resilience under strain, urgent choices, October 2026.
[2] Source: Eurostat.
[3] Source: *Economic Bulletin*, Issue 5/2026.
[4] Source: Central Bank of Malta, *Quarterly Review* 2026:3; *Economic Update* 7/2026 and *Outlook for the Maltese Economy* 2026:2.

stood below that of the euro area. Looking ahead, inflation is expected to rise modestly by year-end, with upward pressures stemming mainly from services and food. Services inflation is expected to remain elevated, reflecting continued strength in domestic demand and robust tourism activity.

Chart 1.2
GEOPOLITICAL RISK, TRADE UNCERTAINTY AND OIL PRICES



Source: "The Economic Effects of Trade Policy Uncertainty", Caldara et al. (2020) and "Measuring Geopolitical Risk", Caldara and Iacoviello (2022).
Note: Oil Price refers to the price of Brent crude oil in US dollars per barrel.

1.1.2 Geopolitical and trade-related uncertainty

Geopolitical risks remained elevated during the first half of 2026, with the escalation of conflict in the Middle East, the ongoing war in Ukraine and persistent trade frictions adding to uncertainty surrounding the euro area outlook. Concerns about disruptions to energy infrastructure and key shipping routes also contributed to higher and more volatile oil and gas prices, raising the prospect of renewed inflationary pressures. The Geopolitical Risk Index (GPR) rose sharply following the US–Israeli strikes on Iran at the end of February, surpassing the previous 2021 peak (see Chart 1.2). Although the index subsequently retreated, it remained elevated throughout the first half of the year, amid continued geopolitical tensions and heightened uncertainty surrounding the global economic outlook.

These tensions also affected global energy markets, particularly through concerns over disruptions to energy infrastructure and key shipping routes. Brent crude oil prices increased markedly, at times reaching their highest levels since 2022, before moderating on expectations of a gradual easing in supply constraints.[5] Similar pressures were evident across other energy markets, including natural gas and refined products, raising the risk that higher wholesale energy costs could feed through to electricity prices and broader inflationary pressures.

The TPU Index gradually receded from the exceptional levels recorded in 2025, as the parameters of the new US tariff regime became clearer. Nevertheless, geopolitical fragmentation and protectionist policies continued to weigh on global trade and investment, with potentially adverse implications for export-oriented euro area firms. From a financial stability perspective, these developments could weaken corporate earnings and debt-servicing capacity, particularly among trade-sensitive and energy-intensive firms, while increasing the risk of abrupt repricing in financial markets.

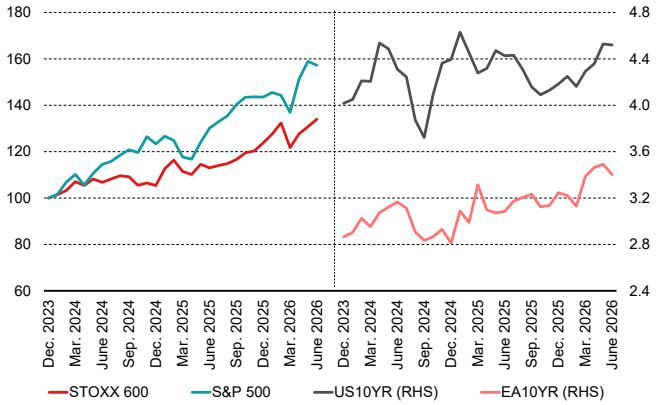
1.1.3 Financial market developments and asset valuations

Global financial markets experienced episodes of pronounced volatility during the first half of 2026, reflecting shifts in monetary policy expectations, geopolitical tensions and large swings in energy prices. Despite this volatility, equity markets recorded strong gains over the period. The S&P 500 rose by 9.6%, supported by resilient corporate earnings and continued investor optimism surrounding AI, which sustained demand for semiconductor and other technology stocks (see Chart 1.3). Gains were concentrated in the second quarter, despite episodes of heightened risk aversion linked to the Middle East conflict. Nevertheless, valuations remained elevated, with market capitalisation increasingly concentrated among a small number of large US technology firms.

[5] Oil prices surged once again especially in September 2026, mostly due to the Houthi forces attack on Saudi Arabia's East–West pipeline.

At the same time, the rapid expansion of AI-related infrastructure investment is increasingly reliant on debt financing as investment requirements outpace firms' internally generated cash flows.[6] This could extend AI-related vulnerabilities from equity into credit markets. Potential spillovers to the euro area could arise from investors' sizeable holdings of US technology equities and the growing issuance of euro-denominated bonds by major technology and cloud-computing firms. European equities also performed strongly, with the STOXX Europe 600 increasing by around 8.3% and reaching record highs, supported by improved risk sentiment, technology-related gains and expectations of resilient corporate earnings.

Chart 1.3
FINANCIAL MARKET DEVELOPMENTS
(Index; Dec.2023 = 100; per cent)



Sources: Investing.com; ECB.
Note: The equity indices and the EA 10-year bond yield represent end of month data observations, while the US 10-year bond yield represent the average of the month.

Government bond markets also experienced heightened volatility as investors reassessed the outlook for inflation and monetary policy. The escalation of the Middle East conflict and the associated energy-price shock contributed to higher inflation expectations and sovereign yields, alongside changing monetary-policy expectations. Elevated government financing needs and political uncertainty in key advanced economies put further pressure on government bond yields. By end-June 2026, benchmark ten-year sovereign yields rose to 3.4% in the euro area and 4.5% in the United States. Despite episodes of market volatility, the ten-year sovereign spreads remained broadly stable, following a slight widening earlier in the year.

1.1.4 Public debt sustainability

Concerns about euro area public debt sustainability remained a key source of financial stability risk amid modest growth, higher sovereign financing costs and mounting structural expenditure pressures. The euro area general government debt-to-GDP ratio rose to 88.8% as at the end of June, up from 87.3% as at end 2025. Debt ratios remained particularly elevated in Greece, Italy, France, Belgium and Spain, with all these countries except Greece recording further increases during the first half of the year. Higher defence and ageing-related expenditure, together with the refinancing of debt issued during the low-interest-rate period, are expected to raise fiscal and interest burdens. At the same time, high debt levels and rising issuance needs could increase sensitivity to shifts in investor sentiment, with an abrupt rise in sovereign yields potentially amplifying sovereign-bank nexus risks through valuation losses on banks' and non-bank financial intermediaries' sovereign bond holdings.[7]

Malta's public debt ratio remained comparatively low, although the persistent fiscal deficit and associated increase in nominal debt warrant continued monitoring. General government debt stood at 47.0% of GDP, at end-June 2026, up from 46.3% at end-2025, and well below both the euro-area average and the 60% Treaty reference value. While the favourable debt-to-GDP position continues to provide fiscal space, a further rise in energy prices could lead to a wider fiscal deficit unless compensating revenue or expenditure measures are implemented. In the absence of such compensating measures, debt and interest expenditure would rise, reducing fiscal space for future shocks.

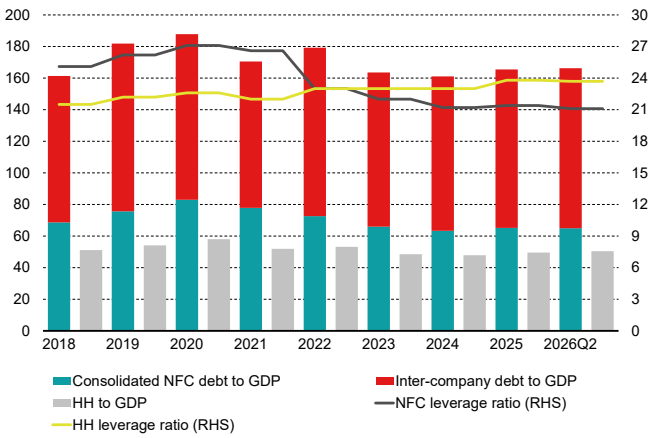
1.1.5 Private sector indebtedness

Private-sector balance sheets in the euro area remained broadly resilient during the first half of 2026, although the more challenging macro-financial environment increased downside risks. The consolidated debt-to-GDP

[6] Source: BIS: Financing the AI boom: from cash flows to debt.
[7] ECB – *Financial Stability Review*, May 2026.

ratio of euro area non-financial corporations (NFCs) remained broadly unchanged at 66.1% in the second quarter of 2026.[8] At the same time, corporate profitability weakened and financing conditions became less supportive as the year progressed. Banks tightened corporate credit standards, while lending conditions became less favourable amid higher interest rates.[9] Euro area household indebtedness remained contained and broadly stable, with household debt standing at 50.1% of GDP in the second quarter of 2026. The household debt-to-income ratio remained broadly unchanged at 80.3%, suggesting that aggregate household leverage remained stable.

Chart 1.4
HOUSEHOLD AND CORPORATE DEBT
(per cent)



Sources: Central Bank of Malta; NSO.

In Malta, comparatively contained private-sector indebtedness continued to provide a degree of resilience against external risks. NFC consolidated debt stood at 65.0% of GDP in June 2026, having decreased slightly since 2025, and remaining below the corresponding euro area ratio (see Chart 1.4). Despite edging up slightly since end 2025, the aggregate leverage ratio also remained comparatively low at 21.1%, below the euro area average.[10] Nonetheless, favourable aggregate indicators may conceal vulnerabilities among highly leveraged firms and sectors with significant bank borrowing, particularly where rising debt or refinancing needs coincide with weaker profitability. Maltese households' balance sheets also remained comparatively resilient during the first half of 2026, with the NPL ratio on resident household loans standing at just 1.2% in June 2026. Household debt rose marginally to 50.4% of GDP in June 2026, from 49.6% at end-2025 but remaining below that of the euro area. Meanwhile, the household leverage ratio increased to almost 24%, slightly exceeding the euro area average. Risks are mitigated by sizeable aggregate financial buffers, with net financial wealth amounting to around 153.9% of GDP and the savings rate standing at around 19% in 2025, exceeding the euro area average.[11] Nevertheless, these buffers may not be evenly distributed across indebted households. Against a backdrop of continued growth in housing credit and rising leverage, some households may become more vulnerable to adverse shocks, particularly in the event of a weakening labour market or a decline in real disposable income.

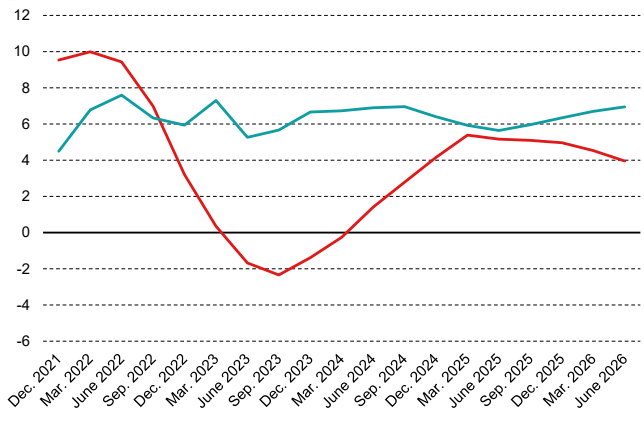
1.1.6 Real estate market developments

Euro area real estate markets continued their recovery into early 2026, although developments became increasingly heterogeneous and downside risks remained material. Residential real estate (RRE) prices increased by 4.0% year-on-year in the second quarter of 2026, down from 5.0% in December 2025 (see Chart 1.5). In the July 2026 Bank Lending Survey, banks reported a marked decline in net demand for housing loans in the second quarter of 2026, while credit standards tightened further, mainly because of higher risk perceptions and lower risk tolerance.[12] These developments point to a possible moderation in housing credit growth and indicate greater caution among banks amid a less favourable and more uncertain macro-financial environment.

[8] Source: ECB data.
[9] Source: Press release: *July 2026 euro area bank lending survey and Survey on the Access to Finance of Enterprises: lending conditions tightened*.
[10] The leverage ratio is calculated as the share of debt over financial assets.
[11] Sources: National Statistics Office (NSO); Eurostat.
[12] Source: Press release: *July 2026 euro area bank lending survey*.

After stabilising towards the end of 2025 and early 2026, sentiment in the Commercial Real Estate (CRE) market weakened during the second quarter, reflecting heightened geopolitical uncertainty and renewed inflation concerns. Investment activity remained subdued in the second quarter of 2026, and weaker demand for CRE lending weighed on investor appetite and investment enquiries flattened, with the net balance declining to 0% from +4% in the previous quarter.[13,14] Structural challenges remained particularly pronounced for office and non-prime commercial properties, where hybrid working, high vacancy rates and the costs of meeting higher energy-efficiency standards continued to weigh on valuations.

Chart 1.5
RRE PRICES
(per cent; year-on-year growth)



Source: Eurostat.

At the domestic level, housing market activity remained buoyant with RRE prices rising by 6.9% year-on-year in the second quarter of 2026, up from 6.3% as at end 2025. Transaction activity was similarly strong, with the number and value of final deeds of sale involving households increasing by 6.3% and 9.4%, respectively. The number of promises-of-sale agreements involving households rose by 4.8% over the same period. Indicators of prospective supply also strengthened, with building permit applications and the number of approved dwellings increasing by 4.9% and 18.7%, respectively, during the period under review.[15] While these developments partly reflected strong underlying housing demand and an expanding supply pipeline, the combination of strong increases in property prices, rapid mortgage credit growth and increasing household leverage warrants continued monitoring. Residential mortgage lending increased by 10.2% year-on-year in June 2026, outpacing nominal economic activity, while mortgages continued to account for a substantial share of banks' lending portfolios. Risks are partly mitigated by borrower-based measures and prevailing lending standards, with average loan-to-value (LTV) and loan-service-to-income (LSTI) ratios of around 76% and 25%, respectively. The Bank's house price misalignment indicator continues to suggest that house prices remained broadly in line with fundamentals, with the house-price-to-per-capita income ratio remaining below its historical average.

A comprehensive assessment of domestic CRE developments remains constrained by the limited and insufficiently granular price and transaction data. Nevertheless, risks associated with the banks' CRE exposures appear contained, supported by prudent lending standards. For CRE loans granted during the first half of 2026, the weighted average LTV and LSTI ratios stood at 53.5% and 25.1%, respectively, while the weighted average loan-to-income ratios were 2.7 times. These loans represented just 1.9% of the total number of loans granted by the banking sector during the period, and 5.5% of the corresponding credit volume.

1.1.7 Risk outlook and emerging risks

The outlook points to a gradual improvement in euro-area macroeconomic conditions and continued robust growth in Malta, although risks remain tilted to the downside. Euro area real GDP growth is projected to reach 1.4% in 2027 and 1.5% in 2028, supported by a gradual recovery in domestic demand and an improvement in external conditions, while inflation is projected to ease towards the ECB's 2% medium-term target by 2028.[16] In Malta, growth is projected to remain robust over the medium term at around 3.7% over

[13] Source: Europe Commercial Property Monitor – Q2 2026.
[14] ECB, *Financial Stability Review*, May 2026.
[15] Source: NSO.
[16] ECB staff macroeconomic projections for the euro area, September 2026.

the 2026–2028 projection horizon, supported mainly by private consumption, investment and net exports.[17] Following the decline in HICP inflation to 2.0% in June 2026, inflation is projected to rise moderately during the rest of the year, averaging 2.2% in 2026 and 2.4% in 2027, before moving close to 2% in 2028.

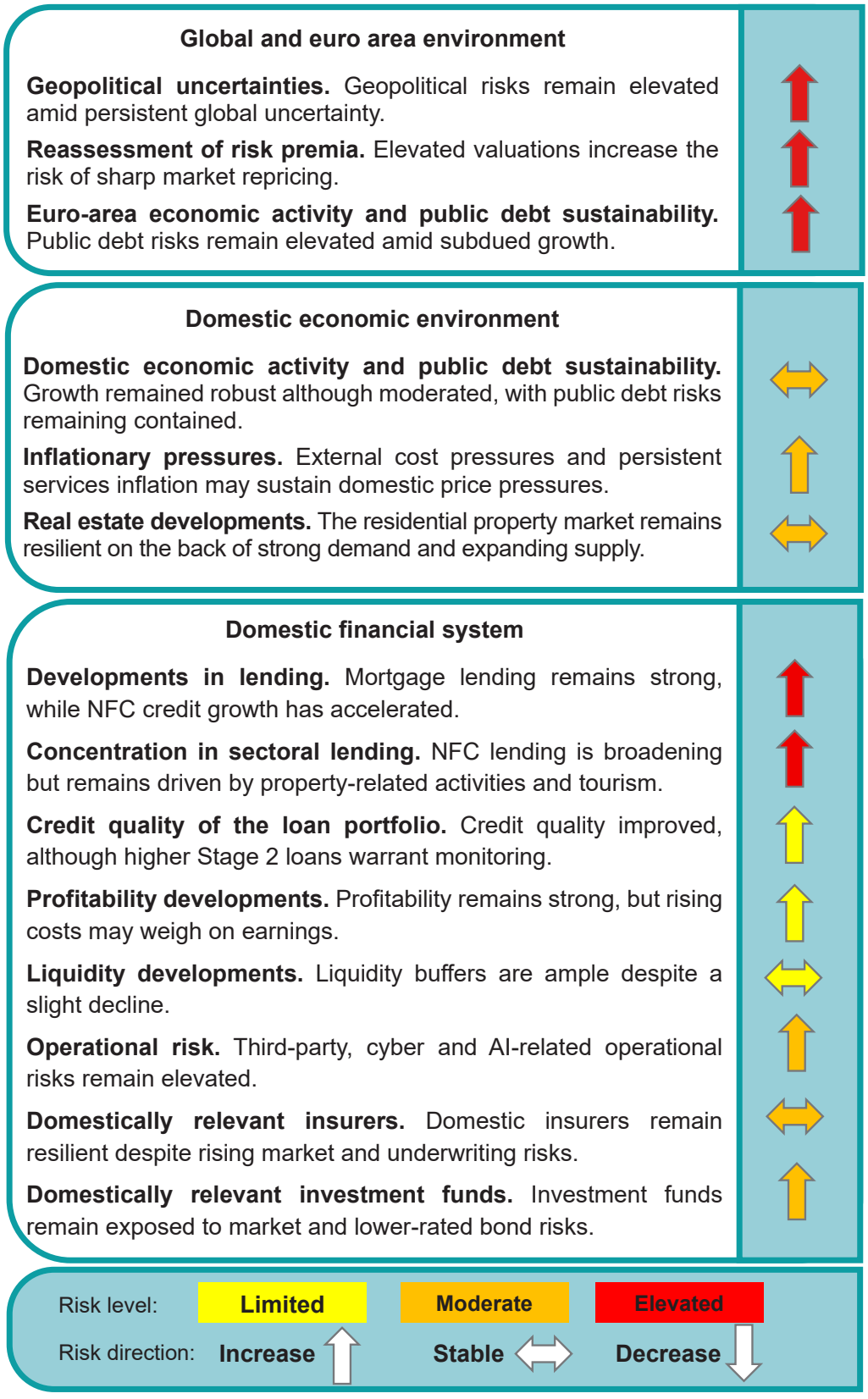
In the euro area, the principal downside risks arise from a further escalation of geopolitical tensions, renewed energy and commodity-price shocks, and disruption to global trade. Such developments could weaken growth, sustain inflationary pressures and lead to tighter-than-expected monetary and financial conditions. In this environment, rising sovereign yields and debt-servicing costs could intensify debt-sustainability concerns, particularly in highly indebted countries with limited fiscal space. Additional expenditure pressures related to defence, an ageing population and the green transition could further constrain public finances and contribute to wider sovereign spreads. Meanwhile, elevated financing costs could weaken corporate profitability and households' debt-servicing capacity. A simultaneous deterioration in corporates' and households' balance sheets could increase credit losses and reinforce adverse interactions between the real economy and the financial system.

Domestically, while data on GDP released after the cut-off date for projections point to some upside risks to the outlook in the near term, further out the risk assessment is more balanced. On the downside, prolonged geopolitical tensions and supply-chain disruptions could weaken external demand and raise imported cost pressures, with adverse repercussions for Malta's export-oriented sectors, investment and households' consumption. Renewed increases in international energy and commodity prices could also intensify inflationary pressures and raise the fiscal cost of maintaining stable domestic energy prices. Conversely, employment and wage growth could prove stronger than currently projected, supporting households' disposable income and private consumption. Moreover, faster adoption of AI and related technologies could generate productivity gains that are not fully captured in the baseline projections, supporting potential output and partly offsetting the expected moderation in labour-force growth.

Euro area banks, including Maltese banks, enter this period with strong aggregate capital and liquidity positions. Nevertheless, weaker economic conditions could increase credit losses, particularly among highly leveraged, trade-sensitive and energy-intensive firms and, at the wider euro-area level, through exposures to vulnerable CRE segments. A sustained rise in sovereign yields and wider risk premia could also generate valuation losses and increase wholesale funding costs. Within the wider financial system, interconnectedness between banks and non-bank financial institutions (NBFIs), liquidity mismatches in investment funds and continued expansion of private credit could amplify market corrections and transmit stress across sectors.[18,19] These cyclical risks may be compounded by growing reliance on digital infrastructure and critical third-party providers, which could increase operational vulnerabilities and concentration risks where key services are provided by a limited number of firms. The increasing use of AI may introduce additional model, governance and cyber risks, including those arising from model errors, data dependencies and common reliance on a limited number of technology providers. Climate-related risks could also affect the financial system through physical losses and transition-related adjustments, with implications for asset valuations and borrower creditworthiness. These vulnerabilities could become more systemic where they interact with geopolitical tensions, energy disruptions or abrupt asset-price corrections.

[17] Central Bank of Malta, *Outlook for the Maltese economy* 2026:3.
[18] ECB – Press release, *Financial stability vulnerabilities remain elevated as geoeconomic shock unfolds*, May 2026.
[19] ECB – Assessing the macroprudential impact of liquidity management tools for investment funds: a system-wide analysis, May 2026.

Figure 1.1
SUMMARY OF RISK OUTLOOK – 12-MONTH RISK OUTLOOK



BOX 1: MORTGAGE RELIANCE IN MALTA'S RESIDENTIAL PROPERTY MARKET[1]

Introduction

Residential mortgages represent a key link between the housing market, households and the domestic banking system. They constitute households' largest liability and an important component of banks' credit exposures. Understanding the extent to which property purchases rely on domestic bank mortgage credit is therefore relevant for assessing the transmission of monetary policy, credit conditions and macroprudential measures to the housing market.

This box measures estimated mortgage reliance on a transaction-count basis, as the ratio of new domestic bank mortgage contracts to registered property deeds between 2020Q4 and 2025Q4.[2] This ratio is calculated for different market segments, relying on administrative data on registered property deeds obtained from the NSO and new residential mortgage contracts granted by domestic banks, reported to the Central Bank of Malta through its Real Estate Reporting Return. The analysis finds that around 47% of all registered residential property transactions were associated with domestic bank mortgage credit, rising to around 64% for core housing transactions, indicating that reliance varies substantially across certain property types.[3] The analysis also shows considerable variation across locations. This heterogeneity is relevant for financial stability monitoring, since changes in interest rates, lending standards and borrower-based macroprudential measures are likely to affect different parts of the housing market unevenly.

Since individual mortgage contracts cannot be matched to specific property transactions, the estimates should be interpreted as indicators of financing patterns across groups defined by property types and locations, rather than as a classification of how each individual property purchase was financed. They do not capture household leverage, loan-to-value ratios, or banks' total property-secured exposures.

The analysis distinguishes between all residential property transactions and core housing transactions, defined as apartments, maisonettes, penthouses and houses. Garages and plots of land are treated separately because they exhibit distinct transaction characteristics and substantially lower mortgage reliance.

A grouped logit model is then used to estimate the mortgage-financed share within each market segment. This model approach accounts for differences in the number of transactions across market segments and enables comparisons after controlling for differences in property-type composition and common developments over time. The resulting model-adjusted estimates therefore facilitate comparisons of mortgage reliance across districts on a more comparable basis than the raw ratios alone. The robustness of these findings was also assessed using alternative modelling approaches, which yielded broadly consistent results. A complementary locality-level model examines how these financing patterns are associated with selected demographic, housing and household financial characteristics.

Mortgage financing is widespread, but not universal

Domestic bank mortgage credit plays an important role in Malta's residential property market, but it does not account for all transactions. Over the period under review, around 47% of all registered residential property transactions were associated with mortgage credit extended by domestic banks (see Chart 1a).

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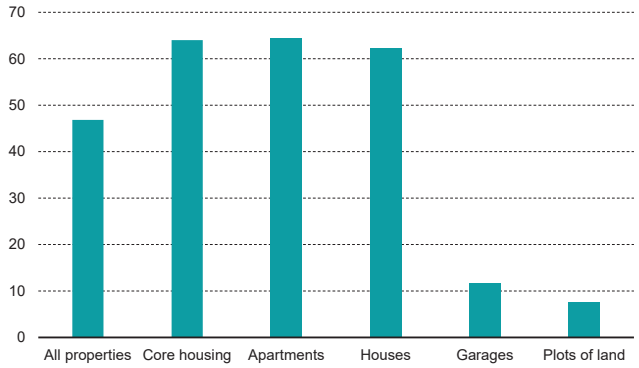
[1] Written by Mr Andrew Spiteri, Deputy Head within the Financial Stability Surveillance and Risk Assessment Department. The author would like to thank Ms Wendy Zammit, Mr Alan Cassar, Deputy Governors Oliver Bonello and Rita Schembri, and Governor Alexander Demarco for their valuable suggestions.

[2] This box draws on Spiteri, A. (2026), *Financing Residential Property Purchases in Malta: The Role of Domestic Bank Credit*, Central Bank of Malta *Working Paper* No. 11/2026. The working paper provides further details on the data, methodology, interpretation framework, and robustness checks.

[3] The underlying working paper also reports complementary value-based measures. Over the sample period, 59.5% of aggregate property value of core housing transactions is associated with a domestic bank mortgage, compared with mortgage reliance of 64.0% by transaction count.

When garages and plots of land are excluded, mortgage reliance rises to around 64% of core housing transactions. This increase largely reflects the very low mortgage reliance observed for garages and plots of land, while apartments and houses exhibit mortgage reliance of around 64% and 62%, respectively.

Chart 1a
MORTGAGE RELIANCE BY PROPERTY SEGMENT
(per cent)



Sources: Central Bank of Malta; NSO; Author's estimates.
Notes: Core housing includes apartments, maisonettes, penthouses and houses. Mortgage reliance is measured as new domestic bank mortgage contracts relative to registered deeds. Transactions classified as "other" are excluded.

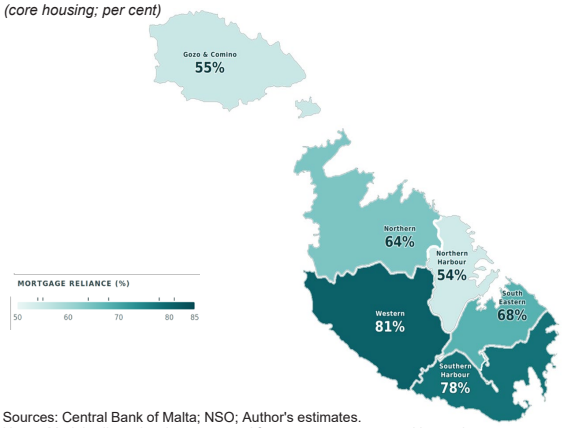
The presence of a sizeable share of transactions not associated with domestic bank mortgage credit indicates that housing market activity is only partly dependent on this channel. Such transactions may be financed through own funds, accumulated savings, housing equity, family financial assistance or other non-bank financing arrangements.

Mortgage reliance differs considerably across districts

The most prominent finding is the degree of spatial heterogeneity in mortgage reliance. Focusing on core housing transactions, the Western and South Eastern districts exhibit the highest reliance on domestic bank mortgage credit, while Northern Harbour and Gozo and Comino display the lowest reliance. To assess whether these differences persist after accounting for variations in transaction composition and developments over time, the grouped logit model described above is used to derive model-adjusted estimates. Property-type indicators control for differences in the mix of transactions across districts, while quarter indicators absorb developments common to the housing market in each period, including movements in financing conditions and the broader macroeconomic environment. The resulting probabilities therefore enable mortgage reliance to be compared across districts on a more consistent basis.

The model-adjusted estimates suggest that mortgage reliance for core housing is around 81% in the Western district and 78% in the South Eastern district. By contrast, the corresponding estimates are around 54% in Northern Harbour and 55% in Gozo and Comino. The Northern and Southern Harbour districts lie closer to the national average, with model-adjusted mortgage reliance of around 64% and 68%, respectively (see Figure 1a).

Figure 1a
MORTGAGE RELIANCE ACROSS ADMINISTRATIVE DISTRICTS OF MALTA AND GOZO
(core housing; per cent)



Sources: Central Bank of Malta; NSO; Author's estimates.
Notes: Model-adjusted estimates control for property-type composition and common quarter-specific effects. Core housing includes apartments, maisonettes, penthouses and houses.

These differences are economically meaningful. The model-adjusted mortgage-financed share in the Western district is around 26 percentage points higher than in Gozo and Comino, while the South Eastern district is around 23 percentage points higher. This suggests that the domestic bank mortgage credit channel is materially stronger in some parts of the housing market than in others.

The lower mortgage reliance in Northern Harbour and Gozo and Comino is consistent with differences in buyer composition and housing use. Northern Harbour has a comparatively high share of foreign residents and a relatively high concentration of apartments, while Gozo and Comino has a higher prevalence of properties used as non-main residences. These features may point to a greater role for rental-oriented, investment, second-home or equity-financed purchases. Conversely, the higher reliance observed in the Western and South Eastern districts is consistent with a stronger owner-occupied housing structure. Since individual buyer characteristics and purchase purposes are not observed, these interpretations should be treated as descriptive context rather than causal evidence.

Locality-level indicators provide supporting context

The complementary model examines whether differences in mortgage reliance across localities are associated with selected demographic, housing and household financial characteristics. The results indicate that localities with higher foreign population shares tend to exhibit lower mortgage reliance, while localities with higher owner-occupation tend to display higher reliance. Household Finance and Consumption Survey-based locality-level income and wealth proxies provide additional context: income is positively associated with estimated mortgage reliance, while wealth is negatively associated with it. These variables are area-level proxies and do not measure the characteristics of the actual buyers involved in the transactions. The results should therefore be interpreted as descriptive conditional associations rather than causal evidence.

Implications for financial stability and policy transmission

These findings have implications for the transmission of financial conditions and macroprudential policy to the housing market. In districts and localities where purchases are more commonly financed through domestic bank mortgage credit, housing demand is likely to respond more directly to changes in borrowing costs, credit availability and the Bank's borrower-based macroprudential measures. This applies particularly to higher-reliance districts such as the Western and South Eastern districts, where a larger share of transactions passes through the regulated mortgage-origination channel.

By contrast, in lower-mortgage-reliance locations, housing-market adjustment may occur less through new domestic mortgage origination and more through other channels, including rental demand, foreign demand, demographic developments, investment motives, accumulated wealth or housing equity. Lower mortgage reliance does not necessarily imply lower risk. Rather, it points to a different transmission mechanism and a potentially different sensitivity to credit-based policy measures.

Overall, the analysis suggests that Malta's housing market should not be viewed as a single homogeneous mortgage-sensitive market. Mortgage credit is important, particularly for core housing, but reliance on domestic bank mortgage credit differs substantially across locations and property segments. This heterogeneity matters for financial stability analysis, as changes in interest rates, lending standards and borrower-based measures are likely to transmit unevenly across the housing market.

1.2 Macroprudential regulatory developments

1.2.1 Capital-based macroprudential measures

As part of its macroprudential toolkit, the Central Bank of Malta applies a range of capital-based macroprudential measures aimed at safeguarding the stability and resilience of the Maltese financial system. These measures strengthen the capacity of financial institutions to absorb losses by addressing systemic vulnerabilities and mitigating the potential impact of adverse economic and financial shocks.

Other Systemically Important Institution Buffers

During the first half of 2026, the Bank conducted the Other Systemically Important Institution (O-SII) buffer exercise to assess whether the institutions previously identified as O-SIIs continued to meet the relevant criteria and to determine the corresponding buffer rates. The scores and applicable buffer rates for the identified O-SIIs are presented in Table 1.1. Compared with the previous exercise, no changes were observed other than in the institutions' respective scores. These changes, however, did not materially affect the O-SII rankings. Following discussions with the ECB and the European Systemic Risk Board (ESRB), the banks were informed of the outcome of the review on a bilateral basis. The results have been published in a CBM-MFSA Statement of Decision, with the buffer rates taking effect from January 2027.

Table 1.1
LIST OF IDENTIFIED O-SIIs AND CORRESPONDING O-SII BUFFER RATES FOR 2026

Institution	O-SII score (basis points)	2026 O-SII rate
Bank of Valletta plc	2,975	2.00%
HSBC Bank Malta plc	1,427	1.25%[1]
MDB Group Limited	1,298	1.00%
APS Bank plc	828	0.50%

Source: Central Bank of Malta.

[1] HSBC Bank Malta plc qualifies for the provisions of Article 131(8) of CRD, which results in the capping of its 1.50% O-SII buffer rate to 1.25%.

Sectoral Systemic Risk Buffer (sSyRB)

In January 2023, the Central Bank of Malta in collaboration with the Malta Financial Services Authority (MFSA) decided to set a sectoral SyRB of 1.5% applied on risk-weighted assets (RWAs) held against domestic mortgage exposures to natural persons secured by RRE. Following a phased-in approach, the buffer's fully loaded rate became applicable at end of March 2024. This buffer was then extended to cover all mortgages secured by immovable property in Malta after internal frameworks and risk assessments were pointing towards an increase in the broader real estate risk profile of MT banks. The buffer thus was extended to all risk-weighted assets secured by immovable property in Malta, whether residential or commercial in nature and covering both natural and legal persons. The revised framework became applicable as from June 2026. As a result of this extension, the releasable buffers have increased and now cover 0.81% of Total Risk Exposure Amount (TREA) for core banks. The financial system's loss absorption capacity has therefore become stronger with banks being more resilient to potential adverse macro-economic shocks.

Countercyclical Capital Buffer (CCyB)

The CCyB was adopted in 2016 and has remained at a rate of 0%, reflecting persistently negative Basel credit-to-GDP gaps alongside quarterly assessments that were indicating that vulnerabilities did not warrant the activation of a positive CCyB rate.

The Bank is currently reviewing its CCyB calibration framework, with a view to incorporate more tailored cyclical indicators and domestic risk metrics that go beyond the standard Basel indicators. The enhanced assessment is supported by a range of cyclical risk indicators such as the Cyclical Systemic Risk Indicator (cSRI) and the Bank's semi-structural credit gap.

The Bank will be consulting with the industry on the outcome of this ongoing review.

1.2.2 Borrower-based measures

As outlined in the Bank's *Financial Stability Report 2025*, the most recently amended CBM Directive No. 16 came into force on 26 March 2026. The main change was the replacement of the previous 40% stressed debt service-to-income (sDSTI) limit applicable to legal persons with a 1.3x stressed Debt Service Coverage Ratio requirement for legal persons engaged in RRE lending, including buy-to-let activities. The measure remains consistent with the sDSTI and considers a stressed interest rate of 1.5% over and above the prevailing applied rate, together with conservative haircuts to projected income streams to ensure prudent risk management. The aim is to align further the regulatory framework with prevailing best practices, while maintaining an appropriate balance between safeguarding financial stability and preserving adequate market flexibility.

Furthermore, during 2026, banks submitted the results of their internal audit reports to enable the Bank to assess banks' compliance with the Directive, referring to activities conducted during the 2025 financial year. This is in accordance with the requirements set out in Directive No. 16 as well as CBM Guidelines on Internal Audit Reports. Overall, these reports indicate that the banking sector generally continues to comply with the requirements of Directive No.16 as internal auditors consistently concluded that borrower-based limits relating to LTV-O, stressed DSTI-O, and loan maturity caps amongst others, were being applied appropriately, and that control frameworks remain broadly effective.

1.2.3 Other measures

Voluntary Reciprocation

During the first half of 2026, only one measure was proposed for reciprocation. This related to a sSyRB of 1%, increasing to 2% from 1 July 2026 to 30 June 2027 and to 3.5% from 1 July 2027. The buffer targets all relevant exposures to NFCs operating in the construction and real estate sector in Austria. Following its assessment, the Bank decided not to reciprocate this measure on the grounds that Maltese banks' exposures to the relevant sectors in Austria were immaterial. Moreover, the Central Bank of Malta maintained its existing stance of non-reciprocation with respect to previously identified measures eligible for reciprocation.

Other developments

European Commission Communication on the competitiveness of the EU banking sector

On 17 July 2026, the European Commission published a Communication on the competitiveness of the EU banking sector, outlining measures aimed at strengthening the Single Market for banking.

This Communication, a key pillar of the Commission's Savings and Investments Union Strategy, seeks to promote a more integrated, efficient and competitive banking sector capable of supporting Europe's economy by financing growth, innovation, and strategic priorities. The initiative is underpinned by a more balanced regulatory framework that enables banks to take prudent risks while maintaining resilience, improving services to households and businesses, preserving financial stability, and fostering sustainable economic growth.

The Communication follows a targeted consultation on EU banking competitiveness launched by the European Commission in February 2026.[20] The Central Bank of Malta actively contributed to these discussions both at the European level and domestically. At the national level, the Bank worked closely with the MFSA and the Ministry for Finance to prepare and submit a joint response to the consultation, reflecting the views of the Maltese authorities.

Beyond its contribution to the European Commission's targeted consultation, the Bank continues to play an active role in ongoing discussions at different international fora including at the ESRB, the ECB as well as the European Banking Authority (EBA), on measures to enhance the competitiveness and efficiency of the

[20] The ECB, the ESRB and the EBA submitted responses to the European Commission's consultation. Their respective responses are available on the websites of the ECB, ESRB and EBA.

European banking sector. The Bank also supports the Ministry for Finance on similar discussions taking place at Ecofin. Furthermore, the Bank is also engaged in the ongoing review of the European Banking regulatory framework. Specific attention is being given to recommendations concerning the capital buffer framework, including the interaction between microprudential, macroprudential and Minimum Requirement for Own Funds and Eligible Liabilities requirements. Looking ahead, the European Commission is expected to present a package of measures in the first quarter of 2027. The Central Bank of Malta maintains that the objective of these reforms should be better regulation with a simpler, more proportionate, and efficient framework that remains fully effective in safeguarding financial stability. Any proposed reforms should therefore be supported by robust impact assessments and result in a genuine reduction in regulatory complexity, rather than merely shifting complexity elsewhere within the framework or creating unintended consequences for supervisory effectiveness and financial stability.

BOX 2: BANK PROFITABILITY-AT-RISK: LINKING CYCLICAL SYSTEMIC RISK TO FUTURE BANK PROFITABILITY IN MALTA[1]

Introduction

The *at-risk* concept has become widely used as a forward-looking framework for quantifying the potential adverse impact of uncertain future events. This article applies it to bank profitability in Malta, measuring how weak profitability could become under adverse outcomes, given the prevailing level of cyclical systemic risk and other macro-financial conditions, thereby providing an input to the assessment of the capital banks may need to address the materialisation of such a scenario.

Cyclical systemic risk typically builds during periods of buoyant credit growth, rising leverage and stretched asset valuations. When these imbalances unwind, credit losses, weaker business volumes and asset repricing can reduce bank earnings and, in turn, capital. This can weaken banks' ability to absorb shocks and sustain credit supply at a time when the economy needs it most. Building on the Growth-at-Risk literature (Adrian et al., 2019), Lang and Forletta (2020) examine how cyclical systemic risk affects the lower tail of future bank profitability in a large panel of European banks, using quantile regressions that estimate this effect separately at different percentiles of the profitability distribution rather than only at its mean. The authors express low-end profitability outcomes in risk-weighted capital-ratio units through their Bank Capital-at-Risk (BCaR) measure, thereby linking cyclical-risk assessment to capital-buffer calibration.[2]

This article adapts the *at-risk* framework to Malta. Using data on core domestic banks, it estimates a location-scale panel quantile local projection (QLP) model (Koenker and Bassett, 1978; Jordà, 2005; Machado and Santos Silva, 2019) that relates banks' future pre-tax returns on assets (ROA) to the cSRI (Vella, 2024) which takes the place of the domestic cyclical systemic risk indicator (d-SRI) (Lang et al., 2019) used by Lang and Forletta (2020).[3] The cSRI is a summary indicator with forward-looking properties that provides information about the accumulation of cyclical systemic risk over time. It captures domestic credit, debt-servicing and housing-market developments and is already used within the Bank's broader risk-regime assessment.[4]

These quantile bank-level forecasts are aggregated into Bank Profitability-at-Risk (BPaR), which is a measure of downside bank profitability. Negative values indicate projected losses, whereas positive values indicate that profitability remains positive even in case of adverse outcomes. In other words, BPaR indicates how low the profitability of the core domestic banking sector could fall in case of unfavourable circumstances, given current macro-financial conditions. Unlike traditional regression models, which estimate the effect of cyclical systemic risk on average profitability, it captures the fact that this effect is stronger and more persistent for weak outcomes.

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[1] Written by Francesca Bozza, Senior Economist/Analyst, Pedro Pólvora, Deputy Head, and Francesco Ricciutelli, Senior Research Economist within the Macroprudential Policy, Stress Testing and Research Department of the Central Bank of Malta. The authors would like to thank Alexander Demarco, Rita Schembri, Oliver Bonello, Amy Camilleri, Alan Cassar, Christine Balzan, Mariah Azzopardi, Francesco Molteni, and Matteo Panfilo for their helpful inputs and suggestions. Any errors are the authors' sole responsibility.

[2] BCaR measures the change in banks' capital ratio implied by a low quantile of future profitability, given the prevailing level of cyclical systemic risk.

[3] The analysis focuses on core domestic banks, the main providers of credit to Maltese households and firms and whose business model centres on traditional intermediation with the domestic economy.

[4] The cSRI combines four sub-indicators using principal component weights estimated on Maltese data: two-year real bank credit growth, the four-quarter change in the debt-service-to-income ratio, the house-price-to-income-per-capita ratio and two-year real total debt growth. The indicator is available at quarterly frequency from 2006Q1, and its first principal component accounts for a large share of the common variation in the four sub-indicators. Vella (2024) shows that it is a suitable forward-looking gauge of cyclical systemic risk in Malta. Real GDP growth and the spread of government bond yields capture business-cycle conditions.

Estimating how cyclical systemic risk affects future bank profitability

The approach builds on a strand of research that models how cyclical systemic risk shapes future bank profitability in case of adverse events. This method was originally applied to the Growth-at-Risk concept, where systemic financial conditions are linked to the distribution of future GDP growth (Adrian et al., 2019) and has since been extended to BCaR (Lang and Forletta, 2020; Passinhas and Pereira, 2023; De Nora et al., 2025). In this latter framework, cyclical systemic risk is treated as a state variable that shifts the conditional distribution of future pretax ROA, with particular attention to downside profitability where losses erode capital and therefore threaten bank resilience.

Building on these contributions, the framework estimates a location-scale panel QLP model that links several quantiles of future bank profitability to the current level of cyclical systemic risk. The object of interest is the conditional quantile function of bank-level pre-tax ROA at a given horizon h, evaluated at quantiles τ. It is conditioned on the current value of the cSRI, bank characteristics, and macro-financial variables.

Bank profitability is projected on the basis of the current cSRI, while controlling for bank-specific and macro-financial factors. The QLP model is estimated based on a panel formed by considering six core domestic banks observed over 31 quarters (2018Q4–2026Q2). The dependent variable is pre-tax ROA for each quarter, while bank-specific controls, commonly found to influence profitability, include the logarithm of total assets (size), the net interest margin (business model), the cost-to-income ratio (efficiency), NPLs over total loans (asset quality), RWA over total assets (risk-taking), and the Tier 1 capital ratio (capitalisation).[5] The model also includes bank fixed effects, which absorb unobserved bank characteristics that are broadly stable over the sample period, such as business models, risk appetite and the quality of management and risk controls.

Furthermore, country-level macro-financial variables are included to capture aggregate drivers of bank profitability. Besides the cSRI (in real terms), which is the main variable of interest, the explanatory variables also include real GDP growth and the spread of government bond yields, measured as the difference between the three-month Euribor and the ten-year Maltese government bond yield. Relying on bank-level and macro-financial information together helps limit the extent to which losses arising from cyclical systemic risk are confounded with unrelated macroeconomic shocks or structural changes in the banking sector.

Over the estimation window, from 2018Q4 to 2026Q2, the cSRI completed approximately one full financial cycle (Chart 2a). It rose from around zero in late 2018 to approximately 1.9 in 2021Q1. It then declined steadily, reaching a trough of about -1.1 in 2024Q3, before rising again to around 0.5 in 2026Q1. The underlying drivers of the two increases differ. During the COVID-19 pandemic, the cSRI increase was initially driven by the house-price-to-income ratio component, and from 2021Q2 by stronger growth in total debt. The more recent increase is driven instead by strong bank credit and total debt growth, partly offset by a smaller contribution from the house-price-to-income ratio. This recent trend therefore suggests a more conventional and credit-driven build-up of vulnerabilities.

Chart 2b shows that developments in bank profitability have been far from uniform across institutions. During the COVID-19 pandemic, the median bank's quarterly pre-tax ROA decreased and turned marginally negative in late 2020. At the same time, the weakest banks recorded sizeable losses, pulling the lower end sharply into negative territory and turning the average profits negative. In other words, the shock did not weigh evenly on the system. Most banks remained profitable, while

[5] These variables separate the contribution of cyclical systemic risk from that arising from each bank's business model and other forms of idiosyncratic risk.

Chart 2a
cSRI OVER TIME
(index)

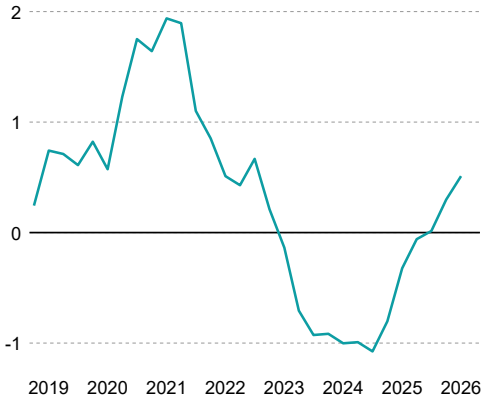
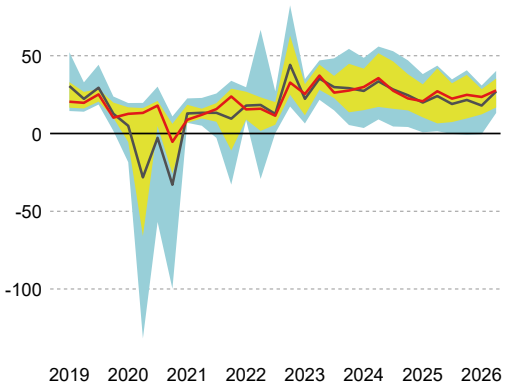


Chart 2b
ROA DISTRIBUTION OVER TIME
(basis points of quarterly pre-tax ROA)





Sources: Central Bank of Malta; ECB Statistical Data Warehouse; Eurostat; authors' calculations.
Notes: Chart 2a shows the real cSRI. Chart 2b shows the mean, median, 25th – 75th and 10th – 90th percentile ranges of quarterly pre-tax ROA across Maltese core domestic banks.

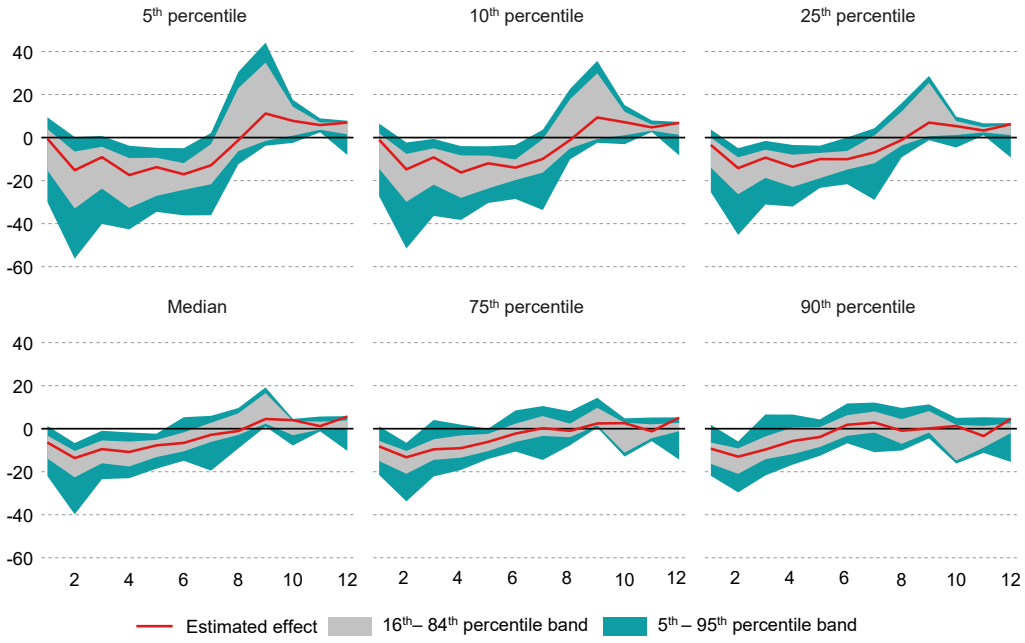
the deterioration was concentrated among a small number of institutions. Looking at the average alone would therefore give an incomplete picture, which is why this article models the full distribution of profitability, with particular attention to its lower end and expresses results in terms of quantiles. Profitability subsequently recovered, peaking in 2023–2024 as monetary policy tightening boosted net interest income (NII). It has since moderated, and estimated outcomes at the lower end of the distribution have moved closer to zero.

Chart 2c illustrates how future bank profitability responds when cyclical systemic risk rises, distinguishing between weak, typical and strong profitability outcomes. Specifically, it reports the effect of a one-unit increase in the cSRI on selected quantiles of future pre-tax ROA. The main insight is that higher cyclical risk does not affect all outcomes in the same manner. Whilst profitability initially falls across the board, the decline is larger and more persistent at the weak end of the distribution. This justifies the use of quantile techniques, as they capture the asymmetric nature of adverse or extreme impacts.

The response unfolds in three stages. In the short run, the decline is broadly uniform. Two quarters ahead, quarterly pre-tax ROA is about 13–15 basis points lower at each quantile considered. However, as the horizon lengthens, the responses start to diverge. Six quarters ahead, the estimated effect is around -17 basis points at the 5th percentile and -14 basis points at the 10th, compared with -6 basis points at the median and negligible effects at the 75th and 90th percentiles. In other words, while typical and strong outcomes are already recovering, weak outcomes remain depressed. By the end of the second year, the negative effects have disappeared, and the estimated responses turn positive, consistent with the subsequent recovery in profitability, although the estimates remain imprecise.

The key takeaway is that weak outcomes take longer to recover, with the largest lower-tail effects four to six quarters ahead. An analysis based only on average profitability would understate the losses that could arise in adverse outcomes. The timing is also relevant for policy considerations. Because these effects build over several quarters, the cSRI provides an early signal, leaving time to assess emerging vulnerabilities and, where warranted, to act before the effects on profitability materialise.

Chart 2c
MARGINAL EFFECT OF CYCLICAL SYSTEMIC RISK ON SELECTED QUANTILES OF THE DISTRIBUTION OF FUTURE BANK PROFITABILITY
(basis points of quarterly pre-tax ROA; horizon in quarters)



Sources: Central Bank of Malta; authors' calculations.
Notes: Panel QLP with bank fixed effects for the bank-level pre-tax ROA at horizon t+h on the cSRI, controlling for several other bank-specific and macro-financial variables at time t. Bands from a time-block bootstrap.

Some caveats apply when interpreting the results. First, the sample period does not include a domestic banking crisis. The estimates therefore reflect how profitability has responded to cyclical risk in the absence of such an event. This implies that losses in a systemic crisis, when shocks would be larger and spread across many banks at once, could be more severe than those captured in these results. Second, some of the weakest outcomes in the sample reflect bank-specific events, such as one-off impairments or provisions, which add to the variation in the lower end of the distribution without being directly related to systemic risk. Third, the relatively short time span also leaves fewer projection origins at longer horizons; thus, estimates beyond two years should be interpreted with greater caution. Finally, the results show that profitability tends to move together with the cSRI, which makes the analysis useful for anticipating risks, but it does not isolate the effect of systemic risk on its own. Although the model controls for bank-specific characteristics and macro-financial conditions, periods of rising cyclical risk tend to coincide with other developments that also affect bank profits, and such controls can only partly disentangle these effects. The results should therefore be read as indicating what typically happens to profitability when the cSRI rises, rather than as a precise measure of what an increase in systemic risk would cause in isolation.

Translating the estimates into a forward-looking measure of downside risk to banks' profitability

The second part of the framework turns the estimated model into a forward-looking measure of downside risk to bank profitability, which is called BPaR. While the previous section examined how profitability responds to a change in the cSRI, this section uses the same estimates to summarise, at the level of the core domestic banking sector, how weak bank profitability could become in adverse

outcomes, given the conditions observed today. Since the responses to cyclical risk differ across the distribution, the measure is built from the predicted lower quantiles of profitability rather than from its expected value, which would miss the asymmetry documented above.

BPaR at time t and horizon h is defined as the asset-weighted average of banks' predicted 5th percentiles for quarterly pre-tax ROA h quarters ahead:

$$BPaR_{t+h} = \sum_{i=1}^{N_t} \frac{a_{i,t}}{\sum_{k=1}^{N_t} a_{k,t}} \widehat{Q}_{\pi_{i,t+h}}\left(0.05 \,\middle|\, \Omega_{i,t}\right) \quad (1)$$

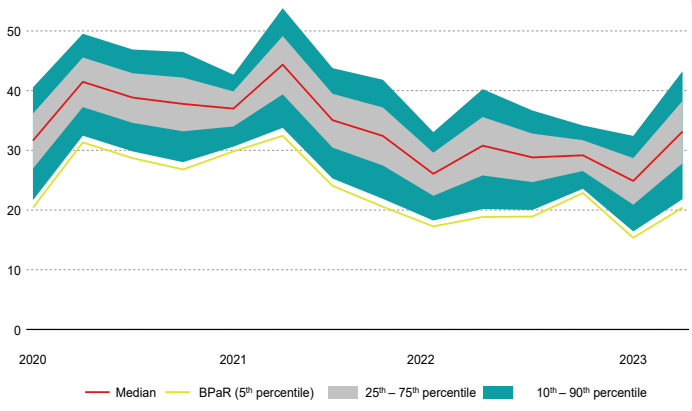
where $\pi_{i,t+h}$ denotes the quarterly pre-tax ROA of bank i in quarter $t + h$, $\widehat{Q}_{\pi_{i,t+h}}\left(0.05 \middle| \Omega_{i,t}\right)$ is its predicted 5th percentile, obtained from the QLP model estimated at horizon h. $\Omega_{i,t}$ is the information set available at t, comprising the cSRI, the bank-specific and macro-financial controls and bank fixed effects. N_t is the number of banks at t and $a_{i,t}$ denotes the total assets of bank i, so that each bank is weighted by its share of sector assets at each point in time. BPaR is a measure of conditional downside profitability. A negative value denotes a projected loss, whereas a positive value indicates that the model projects banks to remain profitable even at the adverse conditional quantile, that is, under severe scenarios.

Dividing each bank-level quantile by the bank's average risk weight (RWA over total assets), $\overline{rw}_{i,t}$, before aggregation, translates BPaR into percentage points of the risk-weighted capital ratio, giving the Malta-only equivalent of BCaR of Lang and Forletta.[6] Intuitively, a loss equal to 1% of total assets reduces capital by the same amount. For a bank whose RWA are half of its total assets, that loss lowers the capital ratio by 2 percentage points.

Chart 2d shows the 12-quarter-ahead BPaR for Malta between 2020Q1 and 2023Q2. It also shows the median, the 25th–75th and 10th–90th percentile ranges of the conditional distribution. For each origin quarter t, BPaR shows the asset-weighted average across banks of the predicted 5th percentile of quarterly pre-tax ROA twelve quarters ahead, conditional on the cSRI and the bank-level variables observed at t.

BPaR remained positive throughout the period. Even under an adverse outcome, the core domestic banking sector was projected to remain profitable three years ahead. Its level nonetheless varied considerably. BPaR peaked at about 31–33 basis points of total assets for origins in 2020Q2 and 2021Q2, then declined from mid-2021. It reached its lowest level, about 15 basis points, in 2023Q1, before recovering to around 20 basis points in 2023Q2. Notably, the highest readings coincide with the quarters when the cSRI peaked. At this horizon,

Chart 2d
THREE-YEAR-AHEAD BPaR OF CORE DOMESTIC BANKS
(basis points of total assets; quarterly pre-tax ROA, 12 quarters ahead)



Sources: Central Bank of Malta; authors' calculations.
Notes: Asset-weighted averages of the bank-level conditional quantiles of quarterly pre-tax ROA 12 quarters ahead, dated at the forecast origin. BPaR is the 5th percentile.

[6] BPaR describes downside risk to earnings, while BCaR expresses the same risk in capital-ratio units.

the estimated effect of the cSRI turns slightly positive, consistent with the recovery in profitability that follows the initial adverse impact (see Chart 2c). Over the period shown, the gap between typical and weak profitability outcomes remained broadly stable, at around 6 to 13 basis points. Movements in BPaR therefore mainly reflected changes in overall profitability rather than a disproportionate worsening of the weakest outcomes. In other words, downside risk to profitability rose and fell with the system as a whole, with no sign of weaker outcomes becoming detached from the rest.

Conclusions

This article examines whether Malta's cSRI provides early information on the distribution of future profitability of core domestic banks. It looks not only at typical outcomes, but also at the weakest ones, by considering the lower end of the profitability distribution of banks, thereby capturing the potential behaviour of bank profitability under adverse macro-financial conditions.

When cyclical systemic risk rises, profitability tends to fall across the board in the following quarters. Two quarters ahead, a one-unit increase in the cSRI is associated with quarterly pre-tax ROA roughly 13 to 15 basis points lower, in typical and weak outcomes alike. Over time, however, the picture changes. While typical and strong outcomes recover relatively quickly, weak outcomes remain depressed for longer. In practical terms, a build-up in cyclical risk does not simply dent profitability for a short while. It leaves banks exposed to poor results for an extended period, reducing the earnings they can rely on to absorb losses, thereby weakening their first line of defence.

The difference in scale is substantial. Six quarters ahead, the estimated decline at the 5th percentile is around 17 basis points, nearly three times the 6 basis points for the median, while in the upper part of the distribution, that is, in favourable outcomes, the effect is negligible. An assessment based only on average or typical profitability would therefore understate the risks stemming from cyclical vulnerabilities, which is why estimates across the whole distribution are particularly useful for financial stability analyses.

Bringing these estimates together, BPaR offers a simple gauge of how weak the profitability of the core domestic banking sector could become if conditions turned out to be unfavourable. Over the period examined, the measure remained positive: even in an adverse outcome, the sector was expected to stay profitable, rather than record losses that would erode its capital. Its movements also largely mirrored those of overall profitability, suggesting that the weakest outcomes have so far not drifted away from the rest of the system.

The timing of these effects is also informative. Since the strongest impacts on weak outcomes emerge four to six quarters ahead, current readings of the cSRI shed light on the resilience of bank profitability over the following one to two years. They thus provide an early indication of how today's cyclical risk could weigh on banks' capacity to absorb losses, before such a potential adverse outcome occurs. This analysis could accordingly serve as one of several inputs into macroprudential policy assessments, including assessments of the level of loss-absorbing capacity that may be appropriate to preserve financial-system resilience, though it should not be used mechanically or in isolation to determine a capital-buffer requirement.

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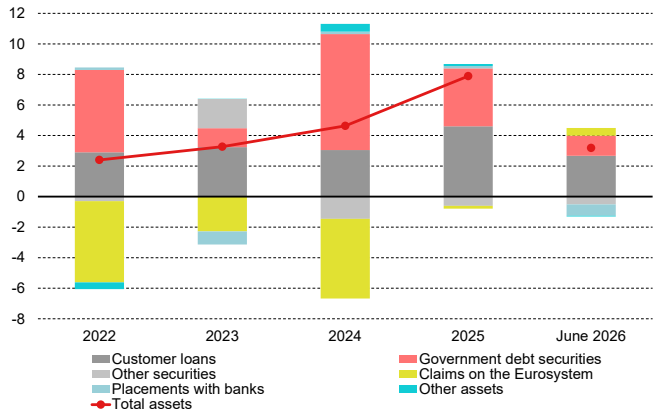
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2. DEVELOPMENTS IN THE BANKING SECTOR

2.1 Core domestic banks

The balance sheet of the core domestic banks continued to expand during the first half of 2026, with their total assets increasing by 3.2% and reaching the equivalent of almost 135% of GDP (see Chart 2.1). This category of banks continued to exhibit sound financial fundamentals, supported by sound asset quality, broadly stable profitability, and capital and liquidity buffers that remained well above regulatory requirements despite some moderation during the reviewed period.

Chart 2.1
CONTRIBUTION TO BALANCE SHEET GROWTH – CORE DOMESTIC BANKS
(percentage points)



Source: Central Bank of Malta.

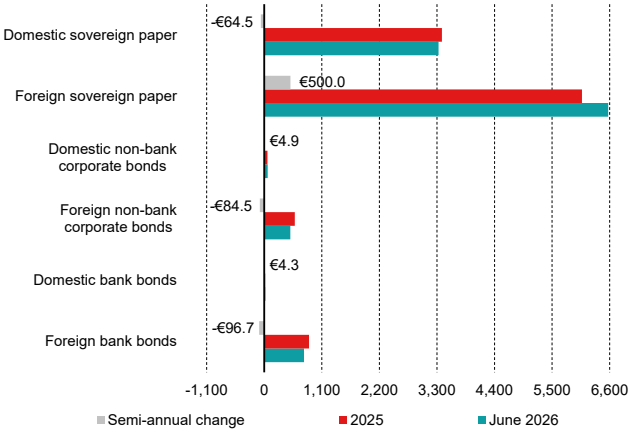
Asset growth was driven primarily by customer lending and higher sovereign bond holdings. In addition, claims on the Eurosystem increased by 7.0%, reversing the declining trend observed in recent years, although these remained limited in terms of their share of total assets. By contrast, interbank placements and non-sovereign debt securities decreased.

2.1.1 Securities portfolio

The core domestic banks' securities portfolio expanded by 2.3% during the first half of 2026, to account for 34.3% of total assets. Growth was driven primarily by debt securities, which increased further by 2.4%, while equity holdings remained relatively stable at a share of just 1.4% of these banks' balance sheets.

The increase in debt securities reflected higher holdings of foreign sovereign paper, which rose by 8.2%. These holdings accounted for 58.4% of overall debt securities (see Chart 2.2). Exposures remained concentrated in other European jurisdictions, with the increase mostly driven by exposures to France, Austria and the Netherlands, among others. By contrast, holdings of domestic sovereign paper declined by 1.9%, although these continued to account for almost 30% of total debt securities. Moreover, the latest decline reflects concentrated portfolio adjustments rather than a broad-based reduction across the banking sector. Collectively, sovereign securities increased their share from 86.2% to 88.0%. The continued preference for sovereign bonds may reflect their role in meeting liquidity management needs and regulatory requirements, as well as the relatively attractive risk-return characteristics of certain sovereign securities. Together, the bonds of foreign banks and corporates accounted for around 11% of total debt securities held by core domestic banks.

Chart 2.2
BOND PORTFOLIO – CORE DOMESTIC BANKS
(EUR millions)



Source: Central Bank of Malta.

Meanwhile, holdings of domestic bank and corporate bonds increased, although they continued to represent only a small share of the overall portfolio. Corporate bond exposures were concentrated in transportation firms, oil and gas producers and beverage companies.

The credit profile of the securities portfolio deteriorated slightly, although investment-grade assets continued to account for the large majority of holdings, consistent with the historical investment profile of core domestic banks. Low-rated debt securities rose by 27.8%, with their share increasing by 1.0 percentage point to 4.8% in June 2026.[1] Meanwhile, medium and high-rated bonds also increased, albeit to a lesser extent, up by 1.9% and 0.7%, respectively. Although the shares of medium and high-rated bonds declined slightly, these continued to account for the bulk of the bond portfolio, representing 56.1% and 37.9%, respectively. In addition, unrated and speculative bonds fell by 3.0% and represented only 1.2% of the bond portfolio.

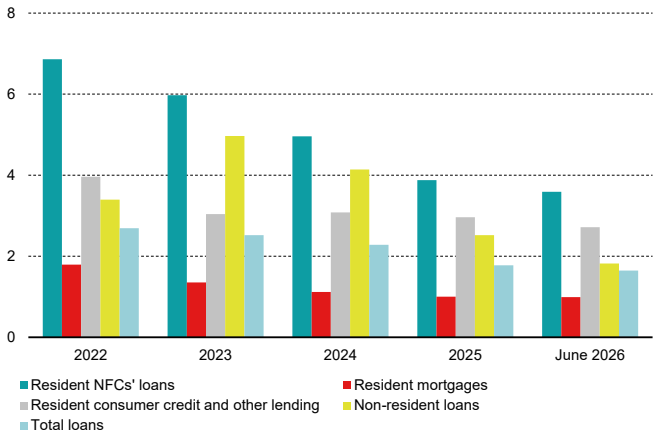
2.1.2 Loan portfolio

The customer loan book continued to expand during the first half of 2026, growing by 5.3% and accounting for just over half of these banks' balance sheets. Growth stemmed almost entirely from resident lending, which rose by 5.3% and represented around 97% of the customer loan book, while non-resident lending remained limited despite increasing by 5.5%.

The increase in resident lending extended beyond mortgage and property-related activities, although these remained the principal drivers of loan growth. Mortgages increased by 5.0% in the first half of the year, accounting for 56.4% of outstanding resident customer loans. Resident NFC lending also expanded strongly, up by 5.7%, with property-related activities accounting for just over three-quarters of this increase.[2] As a result, property-related NFC lending represented 54.8% of resident NFC loans by June 2026. Credit to other corporate sectors also strengthened, including wholesale and retail trade, as well as the non-bank financial sector. Resident consumer credit and other household lending likewise increased by 3.8%, largely reflecting loans granted to purchase goods and services.

Taken together, households and NFCs continued to underpin the expansion in core domestic banks' credit, accounting for over 93% of outstanding resident lending. The sustained pace and broader sectoral distribution of credit growth may contribute to a build-up of cyclical vulnerabilities over time. At the same time, the concentration of lending in mortgage and property-related NFC lending warrants continued monitoring as it could amplify the impact of adverse developments in the property market or a broader deterioration in domestic economic conditions.

Chart 2.3
NPL RATIOS – CORE DOMESTIC BANKS
(per cent)



Source: Central Bank of Malta.

2.1.3 Credit quality

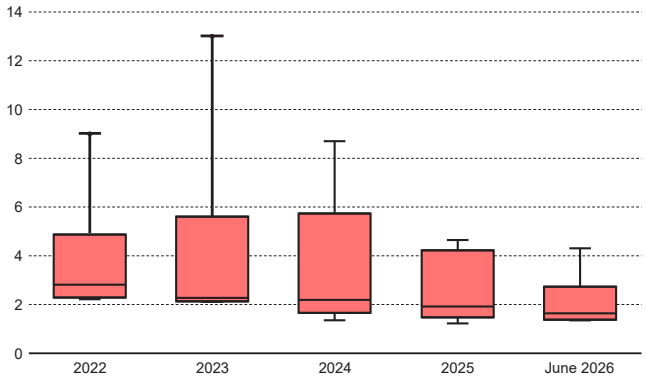
Asset quality continued to improve during the first half of 2026, with the overall NPL ratio edging further downwards by 0.1 percentage point to 1.6%. This reflected both a continued expansion in lending and a 3.7% reduction in the stock of NPLs (see Chart 2.3). The improvement was also evident across institutions, with the median NPL ratio declining

[1] Investment-grade bonds rated AA- or higher are classified as high-rated, those rated A- to A+ as medium-rated, while those rated BBB- to BBB+ as low-rated.

[2] Property-related NFC sectors refer to firms operating in construction and real estate activities, as well as accommodation and food services activities.

further and the interquartile range narrowing slightly, indicating greater convergence among banks at comparatively low NPL ratios (see Chart 2.4). Excluding Eurosystem placements, the NPL ratio also decreased by 0.2 percentage points to 1.9%.

Chart 2.4
OVERALL NPL RATIO – CORE DOMESTIC BANKS
(per cent)



Source: Central Bank of Malta.
Note: The central line within each box represents the median NPL ratio, while the lower and upper edges of the box correspond to the 25th and 75th percentiles, respectively. The whiskers extend to the minimum and maximum values observed in the distribution.

The decline in NPLs was observed across most borrower segments, although the largest contribution stemmed from non-resident exposures. Non-residents' NPLs declined by more than one third, lowering the corresponding NPL ratio from 2.5% in 2025 to 1.8% in June 2026. This mainly reflected the absence of NPLs among non-bank financial entities, together with an improvement in household NPLs, particularly within the mortgage segment.

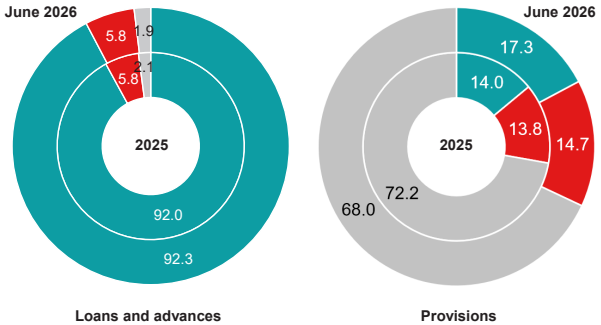
The resident NPL ratio declined marginally to 1.6%, reflecting improvements across all major loan categories. The most pronounced reduction was again recorded among non-bank financial entities, with their NPL ratio declining from 0.5% in 2025 to 0.2% following a substantial reduction in NPLs. Resident NFC NPLs also declined, resulting in a 0.3 percentage point reduction in the corresponding NPL ratio, to 3.6%. This improvement was driven primarily by firms operating in the construction and real estate sectors, followed by the health and social work sector. Nevertheless, non-performing corporate exposures remained concentrated in the construction and real estate sectors, and the accommodation and food services sector, reflecting their significant share within the overall NFC loan portfolio. Collectively, the NPL ratio of these sectors declined by 0.6 percentage points to 3.7%.

Asset quality also improved within the resident household segment. Consumer credit NPLs declined, reducing the corresponding NPL ratio by 0.2 percentage points to 2.7%. Although mortgage NPLs increased by 3.5%, growth in mortgage lending was faster, and reduced the corresponding NPL ratio to just 1.0%.

The reduction in NPLs was mirrored by a decline in Stage 3 loans. By contrast, Stage 2 loans increased by 4.2%, reflecting developments within the NFC portfolio. However, their share in total lending remained unchanged at 5.8%, as Stage 1 loans also expanded (see Chart 2.5).

Overall provisions declined by 2.7%, reflecting lower Stage 3 provisioning, partly offset by higher provisions for Stage 1 and Stage 2 loans. Nevertheless, the coverage ratio improved slightly, increasing by 0.5 percentage points to 46.8%, supported by the substantial reduction in NPLs.

Chart 2.5
STAGE ALLOCATION OF LOANS AND ADVANCES AND PROVISIONS – CORE DOMESTIC BANKS
(per cent)



Source: Central Bank of Malta.

Forborne loans contracted further, down by 4.9% in the first six months of 2026. This reflected lower non-performing exposures subject to forbearance measures. As a result, the overall forbearance ratio declined by 0.2 percentage point to just 1.8% in June 2026, consistent with the generally sound asset quality observed across this segment of banks.

2.1.4 Funding and liquidity

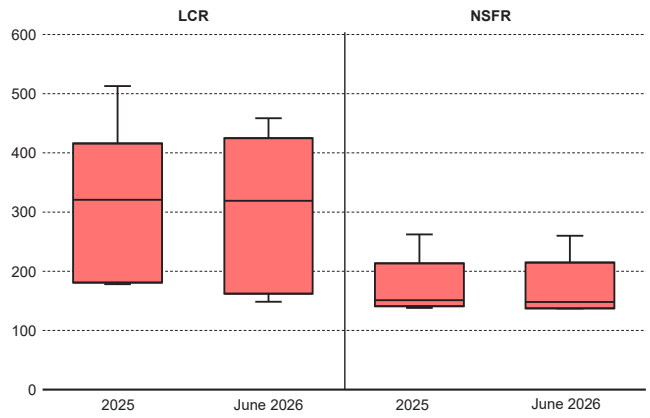
Customer deposits, which financed over 80% of these banks' balance sheets, expanded by 2.2%. The increase was entirely attributable to resident customers, whose deposits grew by 2.4% compared with December 2025, while non-resident deposits contracted by 1.0%. Within the resident segment, households continued to account for the largest share of deposit growth, increasing by 3.5% and representing almost three-quarters of total resident customer deposits. Resident NFC deposits also increased, albeit modestly, rising by 0.5%, largely driven by firms operating in the wholesale and retail trade, and construction and real estate sectors. As customer lending grew faster than deposits, the customer loans-to-deposits ratio increased by 1.8 percentage points to 62.1%. Nevertheless, it remained substantially below the euro area average of 106.3%, highlighting these banks' continued reliance on customer deposits as their primary source of funding.[3]

The decline in the remuneration offered on time deposits may have reduced their relative attractiveness, with the weighted average interest rate (WAIR) falling from 1.9% in December 2025 to 1.7% in June 2026. Consequently, time deposits fell by 2.5%, driven mainly by household deposits with maturities of up to six months, while demand and savings deposits increased by 2.9%. These developments suggest some reallocation in depositors' preferences towards more liquid deposit products amid lower returns on time deposits. Consequently, demand and savings deposits represented 87.3% of total deposits by mid-2026.

Alternative funding sources, including wholesale and Eurosystem funding, continued to represent only a marginal share of total liabilities. During the first half of 2026, the liquidity coverage ratio (LCR) declined by 5.9 percentage points to 369%, while remaining comfortably above the regulatory minimum. The drop primarily reflected a more pronounced rise in net liquidity outflows than in high-quality liquid assets (HQLA). At the same time, HQLA rose by 3.1%, mainly driven by higher sovereign bond holdings and central bank reserves. The net stable funding ratio (NSFR) also continued to signal a robust long-term funding position, standing at 186.8%, marginally below the 188.3% recorded in December 2025.

The distribution of liquidity ratios across banks continued to point to a comfortable liquidity position. The LCR remained characterised by a high median level but a relatively wide interquartile range, indicating some variation in liquidity buffers across individual banks, despite all banks remaining above the regulatory threshold (see Chart 2.6). By contrast, the NSFR displayed lower dispersion, suggesting broadly similar funding structures and stable funding positions across these banks.

Chart 2.6
LIQUIDITY RATIOS – CORE DOMESTIC BANKS
(per cent)



Source: Central Bank of Malta.
Note: The minimum requirement of LCR and NSFR ratios is 100%.

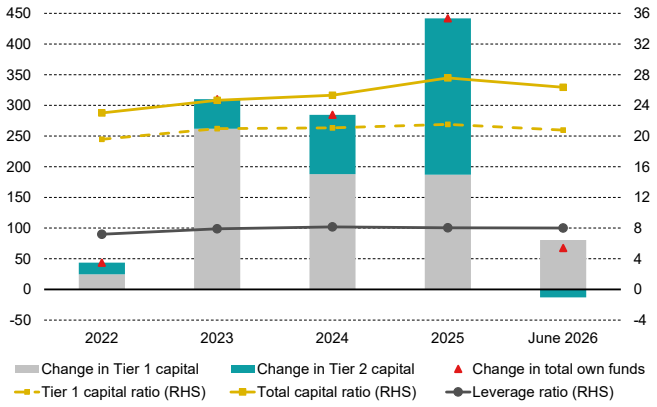
2.1.5 Capital and leverage

The capital position of core domestic banks remained strong, with the total capital ratio standing at

[3] Source: EBA Risk Dashboard 2026Q2.

26.3%, despite decreasing by 1.3 percentage points compared with end-2025 (see Chart 2.7). This decline reflected growth in RWA, which outpaced the increase in own funds. RWA increased by 6.7%, driven primarily by credit risk exposures, which accounted for 90.5% of total RWA. This partly reflected continued growth in customer lending, including to NFCs operating in property-related activities. Market risk exposures also increased, although they continued to account for only 0.1% of total RWA, while operational risk exposures declined slightly. Consequently, the ratio of RWA to total assets increased by 1.3 percentage points to 40.1% in June 2026, indicating a modest rise in the overall risk intensity of the banks' balance sheets.

Chart 2.7
CHANGE IN TOTAL OWN FUNDS, CAPITAL AND LEVERAGE RATIO – CORE DOMESTIC BANKS
(EUR millions; per cent)



Source: Central Bank of Malta.

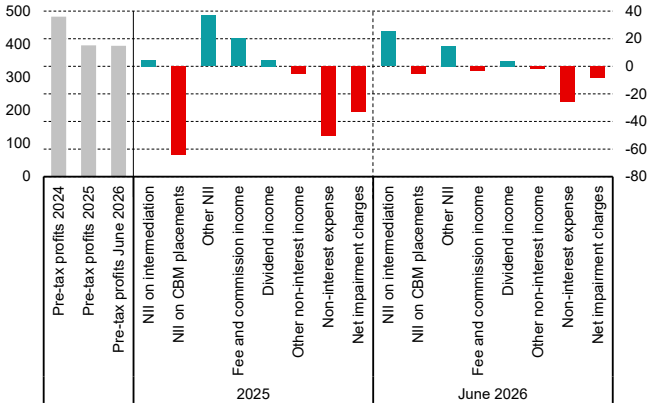
Meanwhile, own funds increased by 1.9%, supported mainly by higher retained earnings, although this was partly offset by a decline in Tier 2 capital. Concurrently, the leverage ratio remained stable at 8.0%, comfortably above the minimum regulatory requirement, providing additional comfort regarding the banks' capacity to absorb potential losses.

2.1.6 Profitability

Profitability remained broadly stable in the first half of the year, as a modest increase in NII was largely offset by higher operating costs, resulting in a marginal 0.3% decline in pre-tax profits.[4] Post-tax return on equity (ROE) dropped slightly to 8.7% whilst ROA remained broadly unchanged at 0.8% in June 2026. While ROE remained below the euro area average of 11.3%, the ROA was in line with that of other euro area banks.[5]

NII increased by 4.9% and continued to account for more than three-quarters of gross income. Growth was largely driven by higher NII from intermediation activities, which increased by around 5%, supported by continued expansion in mortgage lending volumes as the related WAIR remained unchanged at 2.4%. NII from other components also increased by about 8%, reflecting higher sovereign bond holdings and the still elevated yield environment (see Chart 2.8). By contrast, NII from Eurosystem placements declined by 11.3%, driven

Chart 2.8
MAIN CONTRIBUTORS TO PROFITS – CORE DOMESTIC BANKS
(EUR millions)



Source: Central Bank of Malta.
Note: Grey bars indicate pre-tax profits in absolute amounts. Teal (positive) and red (negative) bars indicate annual and semi-annual changes in profit components.

[4] Pre-tax profits refer to a four-quarter moving sum of the reported quarterly flows.
[5] See footnote 3.

by the lower average deposit facility rate in the first half of 2026 compared with the corresponding period of 2025.

Meanwhile, operating expenses increased by 4.8%, largely reflecting higher staff and other administrative costs, particularly those related to information technology, advertising, marketing and communication. In addition, reversals of net impairment charges were lower than those recorded at end-2025. Non-interest income declined marginally by 0.5%, as lower fee and commission income, weaker trading income, non-trading losses, and reduced foreign exchange income exceeded the increase in dividend income.

As operating costs grew slightly faster than gross income, cost efficiency weakened during the review period. Consequently, the operating cost-to-income ratio increased by 0.7 percentage points to 58.9% in June 2026, remaining above the euro area average of 51.5%.[6]

2.1.7 Risk outlook

Looking ahead, core domestic banks' profitability is expected to remain supported by balance sheet growth and income from intermediation activities, particularly if lending growth continues to be underpinned by favourable property market conditions. However, rising operating expenses may weigh on earnings and partly offset these positive developments.

While asset quality remains sound, the increase in Stage 2 loans warrants continued monitoring, particularly in an environment characterised by heightened geopolitical uncertainty, trade tensions and energy market volatility. These developments could affect external demand, supply chains and firms' operating costs, with possible implications for debt-servicing capacity and banks' credit risk.

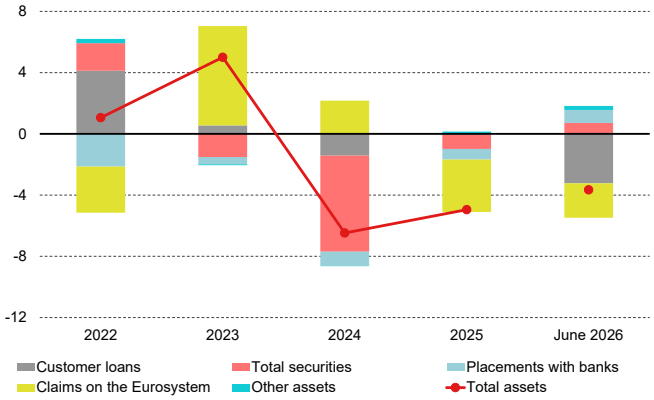
At the same time, the strong pace of credit growth, together with the continued broadening of lending across sectors warrants close monitoring. While asset-quality indicators remained sound, these developments could contribute to the emergence of cyclical vulnerabilities over time. The sector's continued concentration in mortgage and property-related lending remains another structural feature requiring continued attention.

Nevertheless, stress-test exercises conducted by the Bank indicate that core domestic banks have adequate capacity to absorb the shocks considered under the respective scenarios, supported by strong capital buffers, ample liquidity and sound asset quality.

2.2 Non-core domestic banks

The balance sheet of the non-core domestic banks, which has been contracting for the past three years, fell by 3.7% during the first half of 2026, with total assets standing at €3.1 billion, equivalent to around 12% of GDP. This reduction reflected lower customer lending and reduced placements with the Eurosystem, partly offset by increases in inter-bank claims, securities holdings and other assets (see Chart 2.9).[7] Notwithstanding the contraction in business volumes, this category of banks maintained strong capital and liquidity buffers, while profitability strengthened and asset quality remained broadly stable.

Chart 2.9
CONTRIBUTION TO ASSETS GROWTH – NON-CORE DOMESTIC BANKS
(percentage points)



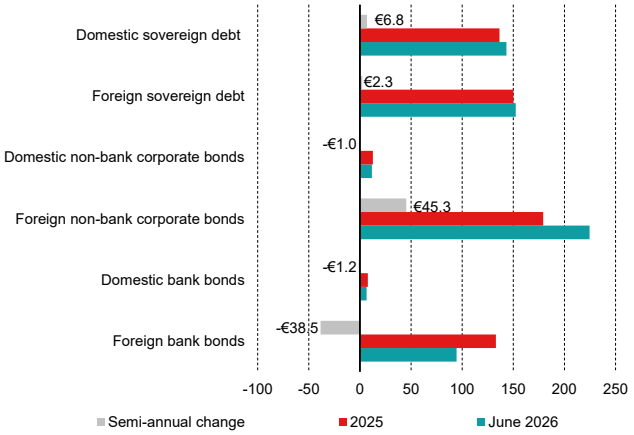
Source: Central Bank of Malta.
Note: June 2026 figures refer to growth over end 2025.

[6] See footnote 3.
[7] Increase in other assets mainly reflected cash in transit, receivables and customer suspense accounts, although these continued to represent a relatively small share of the overall balance sheet.

2.2.1 Securities portfolio

Non-core domestic banks' total securities portfolio grew by 2.9% during the first half of 2026, accounting for 26.4% of total assets. Growth was driven by increases in both debt securities and equities. Debt securities increased by 2.2% and continued to represent the largest component of these banks' securities portfolio, accounting for almost 78% of holdings. The increase in debt securities was primarily driven by a 25% rise in foreign corporate bond holdings, mainly comprising securities issued by investment companies (see Chart 2.10). As a result, the share of non-bank corporate bonds in the debt securities portfolio rose by 6.3 percentage points to 37.3%. Holdings of sovereign paper also contributed positively, increasing by 3.2%, and remained the largest component of the debt securities portfolio. By contrast, holdings of bank bonds, predominantly issued by foreign institutions, declined by around 28%, reducing their share of total debt securities by 6.8 percentage points to 16.0%.

Chart 2.10
BOND PORTFOLIO – NON-CORE DOMESTIC BANKS
(EUR millions)



Source: Central Bank of Malta.

These changes in the bond portfolio composition were accompanied by some weakening in the credit quality profile of their debt securities holdings. High-rated debt securities contracted by almost a fifth, largely reflecting a reduction in foreign government bond holdings, with the decline concentrated in a single bank. As a result, the share of highly rated securities in total debt securities fell from 27.5% in December 2025 to 21.9% in June 2026. Medium-rated bonds rose modestly by 1.7%, with high and medium-rated bonds together continuing to account for almost three-quarters of the portfolio. In contrast, the share of low-rated bonds declined to 4.6% of the overall debt securities portfolio, while the combined share of speculative-grade and unrated securities increased from 16.2% to 22.4%. Taken together, the increase in foreign corporate bond holdings, particularly speculative-grade and unrated instruments, alongside lower Eurosystem placements, is consistent with a reallocation towards higher-yielding assets during the review period.

Equity holdings increased by 5.3%, bringing their share of the overall securities portfolio to around 22%. This growth was mainly driven by one bank's direct equity investments in subsidiaries, with such investments accounting for around 96% of the total equity exposures.

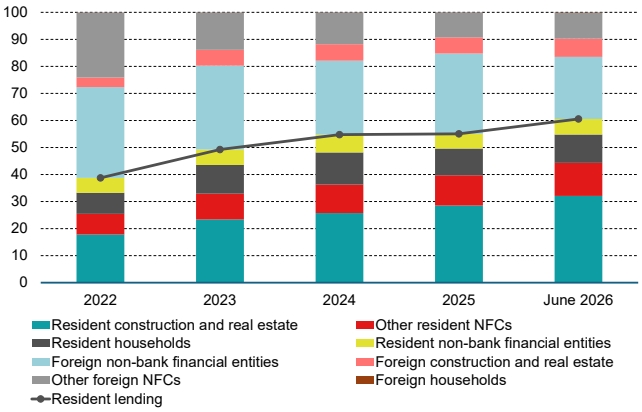
2.2.2 Loan portfolio

The customer loan portfolio of these banks contracted further in the first half of the year, driven entirely by a 19.1% decline in non-resident lending. This decline was driven by one bank, while the remaining banks collectively reported an increase. This primarily reflected a 28.8% reduction in lending extended to foreign non-bank financial entities. Lending to foreign NFCs also edged down mainly owing to lower exposures to the public administration and defence sector and, to a lesser extent, the manufacturing sector and the professional, scientific and technical activities sector. The drop was partly offset by higher loans for the wholesale and retail trade sector.

By contrast, resident customer loans increased by 1.3%, raising their share of total customer loans by 5.5 percentage points to 60.6% (see Chart 2.11). Nevertheless, these banks continued to have a limited presence in the domestic retail market, with their lending to residents accounting for just 4.0% of total resident customer

loans. The increase was entirely driven by lending to NFCs, particularly those operating in the construction and real estate sectors, which together accounted for more than half of total resident lending by these banks. This highlights the continued importance of property-related sectors within these banks' domestic lending portfolios, while also contributing to concentration risk in their loan portfolios. Meanwhile, lending to resident households and non-bank financial entities declined by 2.9% and 2.2%, respectively.

Chart 2.11
DISTRIBUTION OF RESIDENT LOANS AND NON-RESIDENT LOANS – NON-CORE DOMESTIC BANKS
(per cent)



Source: Central Bank of Malta.

2.2.3 Credit quality

The quality of these banks' loan portfolio remained broadly sound, with the NPL ratio unchanged at 1.3% in June 2026. Excluding Eurosystem placements, however, the NPL ratio edged up to 2.2% from 2.1% in December 2025, reflecting a sharper decline in loans and advances than in NPLs, which fell by 3.4% over the period.

Developments across borrower segments were mixed. The household NPL ratio rose by 0.4 percentage points to 1.1%, reflecting weaker credit performance within the mortgage portfolio. More specifically, the overall mortgage NPL ratio increased from 1.4% in December 2025 to 2.7% in June 2026, driven mainly by developments in the resident mortgage portfolio of one bank. While resident mortgages declined by 3.3%, the associated NPLs rose substantially, partly reflecting the relatively small size of the underlying portfolio. By contrast, the overall NFC NPL ratio improved by 0.2 percentage points to 3.5%. This reflected strong lending growth to NFCs, which more than offset the rise in NPLs among resident NFCs, notably those operating in real estate activities. In contrast, NPLs among NBFIs fell by more than half, contributing to the overall decline in NPLs.

The reduction in NPLs translated into a decline in Stage 3 loans, which fell by 3.5% to account for just 2.1% of total loans. By contrast, Stage 2 loans increased by more than a third, particularly from NFC exposures, raising their share to 6.4%. This points to some deterioration in forward-looking credit risk assessments despite the continued low level of NPLs.

In line with lower NPLs, provisions declined by almost 10% in the first half of the year, largely reflecting lower Stage 3 provisioning. Consequently, the share of Stage 3 provisions in overall provisions fell by 2.4 percentage points to 64.4%. Stage 2 provisions also declined, accounting for 16.4% of total provisions, while Stage 1 provisions increased by 6.9%, raising their share to 19.2%. As provisions fell more rapidly than NPLs, the coverage ratio declined by 5.5 percentage points to 76.1% in June 2026.

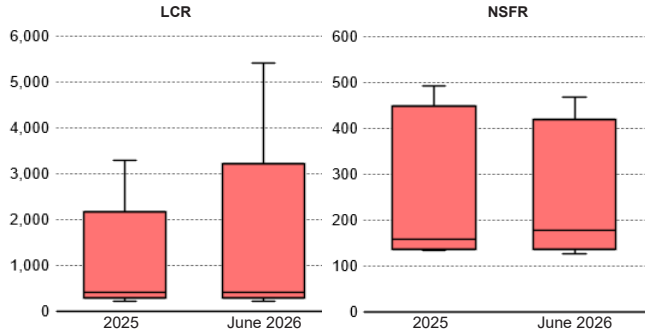
The forbearance ratio increased from 1.9% in December 2025 to 2.2% in June 2026. This rise was entirely attributable to higher performing exposures subject to forbearance measures, which accounted for 70.1% of all forborne loans.

2.2.4 Funding and liquidity

In line with the contraction in the non-core domestic banks' balance sheets, customer deposits declined by almost 6%, albeit still financing just over three-quarters of total assets. This drop was driven mainly by a 9.1% decline in non-resident deposits, partially reflecting lower deposits sourced through online platforms. The overall decline stemmed primarily from lower savings deposits, although term deposits also declined, albeit to a much lower extent.

Resident customer deposits also edged down by 0.9%, largely reflecting lower deposits held by private NFCs. This was partly offset by a 5.7% increase in household deposits, which accounted for around 54% of resident customer deposits. The decrease in resident deposits was driven by time deposits, as withdrawable on-demand deposits increased. Although interest rates on deposits declined, they remained above those offered by core domestic banks. Despite the contraction in resident deposits, their share in total customer deposits increased by 2.1 percentage points to almost 42%, reflecting the larger drop in non-resident deposits. Nevertheless, resident deposits held with non-core banks accounted for only 3.5% of the total resident customer deposits across the domestic banking system.

Chart 2.12
LIQUIDITY RATIOS – NON-CORE DOMESTIC BANKS
(per cent)



Source: Central Bank of Malta.
Note: The minimum requirement of LCR and NSFR ratios is 100%. Merkanti Bank Ltd was excluded from the LCR chart, as it is currently in the process of surrendering its licence.The central line within each box represents the median LCR and NSFR ratios, while the lower and upper edges of the box correspond to the 25th and 75th percentiles, respectively. The whiskers extend to the minimum and maximum values observed in the distribution.

Interbank funding declined by 4.8%, with its share of total assets standing at just 2.9%. By contrast, Eurosystem funding rose by 1.6%, reflecting higher participation in MROs, and three-month longer-term refinancing operations (LTROs), although it remained limited at 2.3% of total assets by end-June 2026.

The liquidity position strengthened during the first half of 2026, with the LCR increasing to 402.4%. The ratio remained substantially above the regulatory minimum, with even the lowest reported ratio standing at a comfortable level of around 220%, despite considerable variation across institutions (see Chart 2.12). This improvement was primarily driven by lower net liquidity outflows, partly offset by a 7.1% decline in HQLA, reflecting lower holdings of withdrawable central bank reserves and other central bank assets. Meanwhile, the NSFR declined by 3.0 percentage points to 169.4%. Despite this moderation, all institutions remained comfortably above regulatory requirements, with ratios ranging between 125.4% and 466.9%.

2.2.5 Capital and leverage

Total own funds decreased by 1.3%, reflecting a reduction in Tier 1 capital primarily due to lower accumulated other comprehensive income, and lower retained earnings. Meanwhile, RWAs fell by 0.2%, in part reflecting the winding down of operations at one bank. The drop in RWA mainly reflected lower operational risk exposures, which accounted for 8.3% of total RWA in June 2026. Credit risk exposures also fell marginally by 0.1%, although they continued to represent the vast majority of RWA at 89.5%.

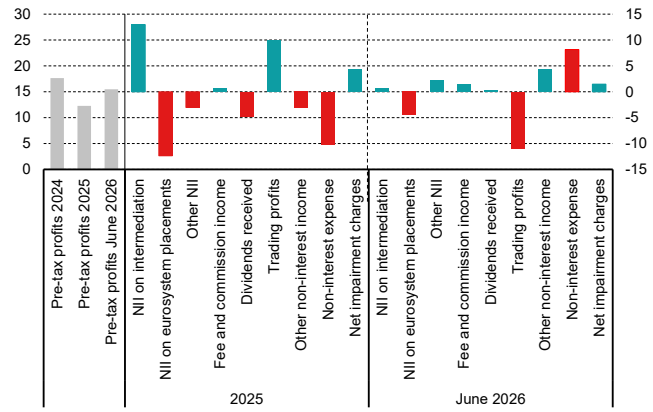
As a result of the decline in own funds, both the total capital ratio and the Tier 1 capital ratio edged down, while remaining at comfortable levels of 22.2% and 19.9%, respectively. Meanwhile, the ratio of RWA to total assets increased by 2.0 percentage points to 60.9%, mainly reflecting the contraction in overall assets. The leverage ratio improved to 11.6%, well above regulatory requirements and indicating substantial capacity to absorb potential losses.

2.2.6 Profitability

On a four-quarter moving-sum basis, pre-tax profits increased by more than a quarter between December 2025 and June 2026. As a result, post-tax ROE and ROA stood at 1.7% and 0.2%, respectively. This improvement was driven primarily by a 10.7% drop in non-interest expenses, particularly operating expenses, following

one-off currency revaluation losses reported in 2025 (see Chart 2.13). In addition, net impairment charges declined considerably during the review period.

Chart 2.13
MAIN CONTRIBUTORS TO PROFITS – NON-CORE DOMESTIC BANKS
(EUR millions)



Source: Central Bank of Malta.
Note: Grey bars indicate pre-tax profits in absolute amounts. Teal (positive) and red (negative) bars indicate annual and semi-annual changes in profit components.

These favourable developments were partly offset by a 7.1% decline in gross income. This mainly reflected a 16.9% reduction in non-interest income, driven by trading losses. NII also contracted by 2.6%, although its share of total gross income rose by 3.4 percentage points to 71.6%. The decline in NII was entirely driven by lower income earned on Eurosystem placements, which fell by 22.3%, owing to a reduction in such holdings. By contrast, income from other interest-generating activities increased. NII from intermediation activities increased by 2.1%, as interest expenses on customer deposits, particularly those held by households and NFCs, declined at a faster pace than interest income on loans. This largely reflected lower deposit volumes and liability repricing at lower interest rates, which reduced funding costs more than the decline in interest income associated with lower non-resident lending. Other NII also increased by 30.5%, supported by higher debt securities holdings and still elevated bond yields, with part of the increase associated with unrated instruments.

Against this backdrop, operating costs declined more rapidly than income, resulting in improved cost efficiency. Consequently, the cost-to-income ratio fell by 3.3 percentage points to 81.0% in June 2026.

2.2.7 Risk outlook

The outlook for non-core domestic banks remains challenging, reflecting elevated global economic uncertainty and the characteristics of their specific business models. The continued contraction in balance sheets, alongside lower customer lending, deposits and Eurosystem placements, suggests that pressures on business volumes may persist over the period ahead.

While credit quality indicators remain broadly favourable, developments in some indicators warrant continued monitoring. In particular, the increase in Stage 2 loans, the decline in the coverage ratio and the higher forbearance ratio point to some weakening in selected credit risk metrics, despite the NPL ratio remaining low. In addition, the growing exposure to resident borrowers within the construction and real estate sectors could increase impairment risks should economic conditions weaken or borrowers' repayment capacity come under pressure.

Market and concentration risks may have risen, reflecting the shift towards foreign corporate bonds and the greater share of speculative and unrated securities within investment portfolios. These developments occurred against a backdrop of heightened market volatility and increased uncertainty surrounding the global economic outlook, which could increase the sensitivity of lower-rated and unrated debt securities to adverse market repricing.

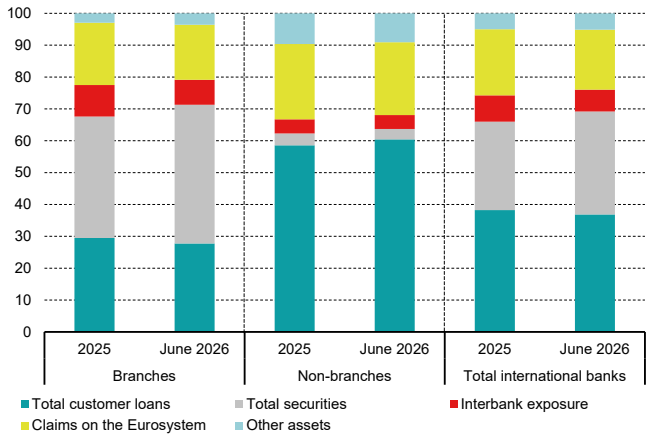
Overall, the non-core domestic banks remain resilient, supported by sound capital and liquidity positions. However, while profitability improved, earnings remain relatively modest and continue to be supported partly by lower operating costs and impairment charges. Looking ahead, profitability may face headwinds from lower gross income and potentially volatile trading income. Consequently, the sector's outlook remains subject to

downside risks, particularly if economic conditions deteriorate or geopolitical uncertainty intensifies.

2.3. International banks

International banks' balance sheets expanded by 10.6% in the first half of 2026, reversing the contraction recorded in the previous year. As a result, these banks' total assets increased to about 49.4% of GDP. Growth was mainly driven by the branches of foreign banks, which recorded a 14.2% increase in total assets, compared to a more modest growth rate of 2.1% among the non-branches. Despite this expansion, the sector continued to exhibit strong capital and liquidity positions, supported by improving profitability and sound asset quality.

Chart 2.14
COMPOSITION OF ASSETS – INTERNATIONAL BANKS
(per cent)



Source: Central Bank of Malta.

The increase in assets stemmed predominantly from higher debt securities holdings, particularly Turkish sovereign bonds held by the branches, which continued to offer attractive yields amid Turkey's elevated inflation and interest rates. Customer loans also rose, albeit at a more moderate pace than total assets, resulting in a lower share (see Chart 2.14). At the same time, placements with the Eurosystem remained broadly stable, while interbank exposures declined, reflecting lower holdings by branches.

2.3.1 The securities portfolio

The securities portfolio of international banks increased by more than a quarter over the first six months of 2026, raising its share of total assets to almost one-third. This growth remained largely driven by branches, whose securities holdings increased to 43.5% of total assets, up by 5.4 percentage points from end 2025. By contrast, the share held by non-branches declined to just 3.3%, mainly reflecting lower investment in debt securities, and, to lower extent, equity holdings.

Foreign government bonds remained the dominant asset class in the securities portfolio, accounting for 86.7% of total securities holdings, compared with 85.5% in 2025. This mainly reflected further investments in Turkish sovereign bonds by branches, which continued to offer comparatively high returns. Holdings of bonds issued by foreign non-bank corporates also rose markedly, up by more than three-quarters, with the expansion exclusively driven by branches. These securities were primarily issued by diversified financial companies and, to a lesser extent, investment companies.[8] By contrast, holdings of MFI bonds grew by a more moderate 3.9%, accounting for 8.5% of the overall securities portfolio. Meanwhile, holdings of Malta Government Stocks (MGSs), which were held exclusively by non-branches, remained broadly unchanged and continued to represent only a marginal share of the portfolio.

The bond portfolio remained heavily concentrated in unrated and speculative-grade investments, largely reflecting the branches' sizable exposure to Turkish sovereign securities. The remainder was invested in medium-rated bonds, held exclusively by the non-branches. The non-performing securities ratio stood at 0.8%, marginally lower than the 0.9% six months earlier.

2.3.2 Loan portfolio

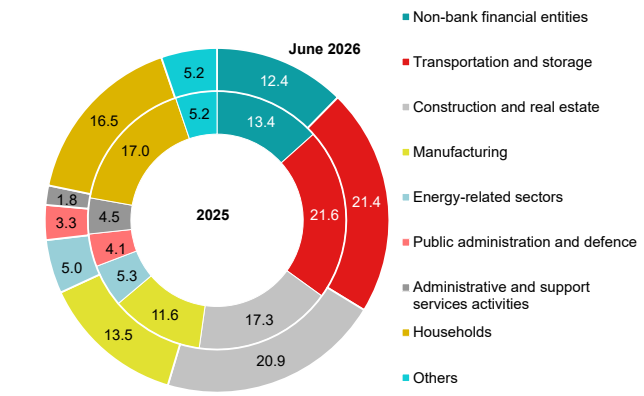
In the six months to June 2026, the customer loan portfolio of international banks expanded by 6.6%, to account for 36.9% of their total assets. Growth was recorded across both the branches and non-branches,

[8] Diversified financial companies refer to NBFIs engaged in a range of financial activities, such as investment management, financing, leasing and other financial services.

with lending increasing by 7.6% and 5.4%, respectively.

NFC lending remained the main driver of customer loan growth, accounting for almost 95% of the overall increase in customer loans. Lending to NFCs grew by 8.9%, raising their share in total customer loans to 71.1%. Growth was concentrated in the construction and real estate, manufacturing, as well as the transportation and storage sectors. Higher loans in these sectors offset declines in others, particularly in the sector comprising administrative and support service activities (see Chart 2.15). Consumer credit rose by 3.4% on the back of higher lending by the non-branches and accounted for 16.5% of total customer loans. By contrast, lending to non-bank financial entities declined by 1.6%, as lower lending by branches outweighed the increase recorded by the non-branches.

Chart 2.15
CUSTOMER LOANS BY SECTOR – INTERNATIONAL BANKS
(per cent)



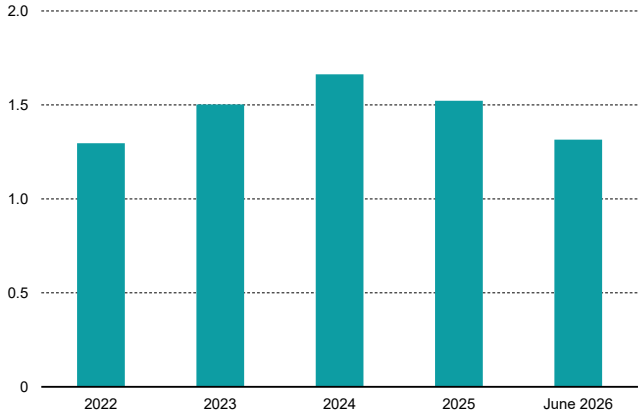
Source: Central Bank of Malta.

Interbank placements contracted by 7.8%, reducing their share to 6.9% of total assets in June 2026. This decline was exclusively attributable to branches and mainly reflected a sharp reduction in placements with related banks, which fell by almost two-thirds. Consequently, the share of related bank exposures in overall interbank placements declined to 19.1%. This was partly offset by higher placements with unrelated banks, whose share increased to 80.9%, pointing to a notable shift in the composition of interbank exposures.

2.3.3 Credit quality

Asset quality strengthened further during the first six months of 2026, with the NPL ratio declining by 0.2 percentage points to 1.3% (see Chart 2.16). This was largely driven by an 8.3% drop in NPLs, mainly reflecting positive developments in the consumer credit portfolio, with write-offs by one bank making only a marginal contribution. As a result, the household NPL ratio fell from 13.6% to 11.8%. Nevertheless, the ratio remained elevated, solely reflecting the specialised payday lending activities undertaken by a small number of institutions. NPLs within the NFC portfolio also declined, with the corresponding NPL ratio remaining low at just 0.3%. In line with the overall improvement, the dispersion of NPL ratios across international banks narrowed somewhat but remained relatively wide. Excluding Eurosystem placements, the NPL ratio declined further by 0.5 percentage points to 1.9%, reflecting the faster growth in loans and advances excluding Eurosystem placements.

Chart 2.16
OVERALL NPL RATIO – INTERNATIONAL BANKS
(per cent)

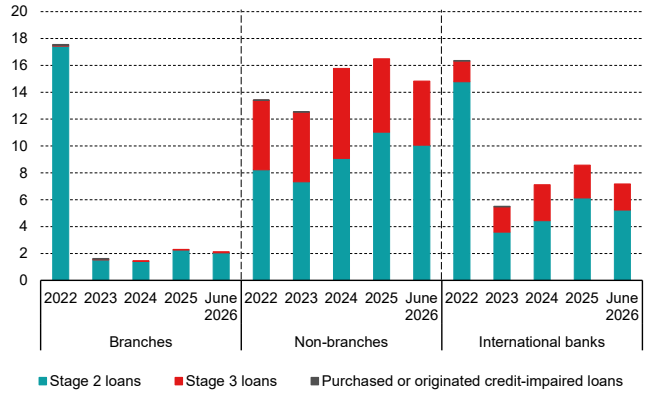


Source: Central Bank of Malta.

The strengthening in asset quality was also reflected in lower Stage

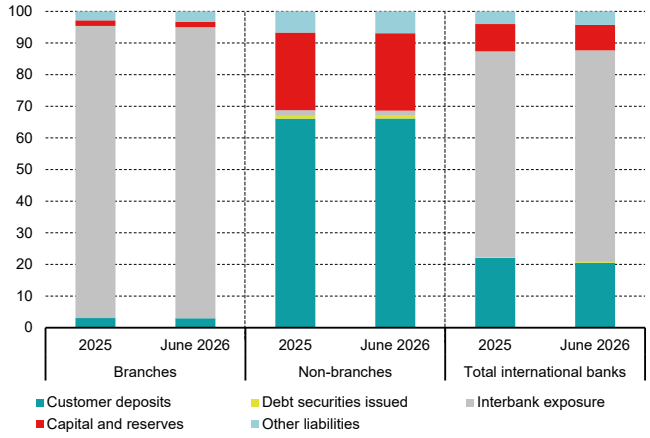
2 and Stage 3 exposures (see Chart 2.17). Provisions associated with these stages fell accordingly, although higher Stage 1 provisions resulted in overall provisions remaining broadly unchanged. Consequently, the coverage ratio strengthened from 101.2% in 2025 to 110.2% in June 2026, indicating that NPLs remained fully covered at the aggregate level. Meanwhile, the forbearance ratio improved slightly, declining from 2.3% to 2.1% during the first six months of 2026. This improvement was exclusively driven by a reduction in performing loans with forbearance measures, which nevertheless continued to account for most of the forborne loans. By contrast, non-performing forborne loans rose, albeit from a low base.

Chart 2.17
SHARES OF HIGHER CREDIT RISK LOANS – INTERNATIONAL BANKS
(per cent)



Source: Central Bank of Malta.
Note: Shares are calculated on the total portfolio of loans excluding placements. When considering Stage 1 loans, the shares would add up to 100%.

Chart 2.18
SOURCES OF FUNDING – INTERNATIONAL BANKS
(per cent)



Source: Central Bank of Malta.

2.3.4 Funding and liquidity

International banks continued to rely heavily on interbank funding, which accounted for around two-thirds of assets in June 2026 (see Chart 2.18). This largely reflected the business model of branches, whose balance sheet growth was mainly financed through increased intragroup funding and, to a much lesser extent, through foreign customer deposits. By contrast, non-branches remained predominantly funded through customer deposits, mainly sourced from non-resident non-bank financial entities and households, with growth in these deposits underpinning their balance sheet expansion.

Customer deposits for the whole segment increased by 3.1% during the first half of 2026. Growth was driven primarily by deposits from households and, to a lower extent, private NFCs, which rose by 8.0% and 9.2%, respectively. These accounted for 50.2% and 16.7% of the deposit base, respectively. Meanwhile, deposits from non-bank financial entities fell by 6.2%, accounting for around a third of customer deposits. The overall increase reflected growth in both withdrawable-on-demand and term deposits, with the latter accounting for 54.4% of total customer deposits.

Other funding sources also increased during the period under review, reflecting higher profits earned in the current financial year by one of the branches, as well as a rise in capital and reserves of non-branches. Debt securities issued by non-branches also increased, though they remained a negligible source of funding, accounting for just 0.2% of total assets.

The liquidity position of the non-branches strengthened during the first half of 2026. The LCR increased to 324.9% in June 2026, standing comfortably above the regulatory threshold. Similarly, the NSFR rose from 129.7% in 2025 to 132.4% in June 2026, pointing to a sustained surplus of stable funding.

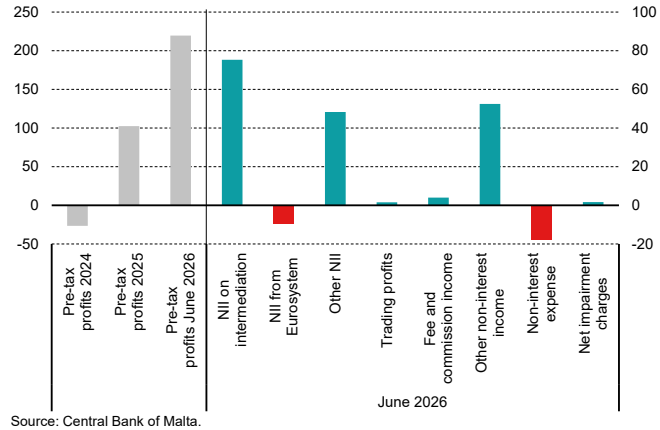
2.3.5 Capital and leverage

International banks maintained a strong capital position during the first half of 2026. The total capital ratio increased by 0.5 percentage points to 35.2% as own funds rose by 2.3%, supported by higher Tier 1 capital. RWA rose by 1.1%, reflecting higher credit and operational risk exposures. This was partly offset by a decline in market risk exposures following a reduction in net long commodity positions. Consequently, the ratio of risk-weighted assets to total assets edged down by 0.3 percentage points to 75.6%, suggesting a marginal improvement in the sector's overall risk profile. The leverage ratio for the non-branches remained broadly unchanged at a comfortable 24.1%, well above the regulatory minimum.

2.3.6 Profitability

The profitability of international banks strengthened markedly during the four-quarter to June 2026, with pre-tax profits more than doubling compared to 2025 (see Chart 2.19). As a result, the post-tax ROA increased from 0.9% in 2025 to 2.0% six months later. The improvement was driven primarily by the branches, although subsidiaries and stand-alone banks also reported stronger results, reflecting higher operating income.

Chart 2.19
MAIN CONTRIBUTORS TO PROFITS – INTERNATIONAL BANKS
(EUR millions)



Source: Central Bank of Malta.
Note: Grey bars indicate pre-tax profits in absolute amounts. Teal (positive) and red (negative) bars indicate yearly contribution to the change in profits.

The increase in profitability was mainly underpinned by higher NII. Income generated from non-intermediation activities rose by more than three-fifths, driven mainly by returns on branches' holdings of high-yield Turkish government bonds. At the same time, income from intermediation activities increased by almost one-fifth, more than offsetting a 7.2% decline in income from Eurosystem placements. Non-interest income also increased significantly, rising by 57.9% as favourable movements in foreign exchange valuations reported by the branches led to valuation gains compared with losses recorded in 2025. Higher net fees and commission income, together with stronger trading profits among non-branches, further supported overall earnings.

Non-interest expenses rose by 10.9%, reflecting higher staff and administrative costs, particularly among non-branches. Nevertheless, revenue growth outpaced the increase in expenses, resulting in an improvement in operational efficiency. As a result, the cost-to-income ratio declined from 52.4% in 2025 to 36.6% in June 2026. Profitability was further supported by a 1.7% reduction in net impairment charges during the period under review.

2.3.7 Risk outlook

The risk outlook for international banks remains broadly stable, underpinned by strong capital and liquidity buffers, improving profitability, and continued strengthening in asset quality. The overall decline in NPLs further supports the sector's resilience, although heightened geopolitical and macroeconomic uncertainty continues to pose downside risks.

Branches remain particularly exposed to developments in their respective home jurisdictions through their concentrated holdings of sovereign securities. While these exposures have benefitted from the relatively high yields and have supported profitability in recent periods, they expose a subset of institutions to shifts in economic conditions, sovereign risk perceptions, and financial market developments in those jurisdictions. In addition, a small number of institutions remain exposed to consumer lending segments that may be more sensitive to adverse economic conditions, labour market developments and borrower repayment capacity, warranting continued monitoring despite the recent improvement in asset quality.

Going forward, maintaining diversified earnings streams and prudent risk management practices will remain important in safeguarding the sector's resilience to external shocks.

BOX 3: MEASURING THE COST OF EQUITY OF MALTESE BANKS[1]

Introduction

The CoE reflects the return that shareholders require to hold a bank's equity. From a financial stability perspective, a persistently elevated CoE may increase the cost of raising capital. This can potentially constrain banks' capacity to expand lending or rebuild capital buffers following periods of stress. However, the CoE is not directly observable, and its estimation is particularly challenging in Malta's small and relatively illiquid equity market.

This box presents market-based CoE estimates for domestic banks listed on the Malta Stock Exchange (MSE) using a range of capital asset pricing models (CAPMs). The analysis considers three listed core-banks and one non-core bank. It then examines the relationship between these estimates and bank-specific characteristics, including asset quality, capitalisation, funding structure and bank size, to derive indicative CoE measures for other non-listed domestic banks. Since the CoE of banks is not directly observable, the resulting measures are sensitive to the model specification adopted. Hence, the results presented should be interpreted as indicative model-based estimates rather than as precise measure of banks' actual required ROE.

Market-based cost of equity estimates

The market-based analysis uses monthly equity returns for listed core and non-core banks from January 2018 to May 2026. Estimating the CoE of Maltese banks is particularly challenging owing to the small and less liquid domestic equity market, in which individual bank share prices may not always closely reflect broader market developments. Hence, changes in share prices do not always reflect closely with broader market developments, making estimates based on any single model potentially unreliable. To address this limitation, the analysis considers several alternative capital asset pricing approaches rather than relying on one model.

Capital asset-pricing frameworks

The starting point of this analysis is the standard CAPM, estimated from excess bank returns:

$$R_{i,t} - R_{f,t} = \alpha_i + \beta_i(R_{m,t} - R_{f,t}) + \varepsilon_{i,t} \quad (1)$$

where $R_{i,t}$ is the monthly ROE of bank i, $R_{m,t}$ is the market return and $R_{f,t}$ is the risk-free rate. The estimated beta measures the sensitivity of the bank's equity return to market movements.

The corresponding CoE is constructed as:

$$k_{i,t} = R_{f,t} + CRP_{(MT,t)} + \beta_{i,t} \times ERP \quad (2)$$

where $k_{i,t}$ denotes the estimated CoE, $R_{f,t}$ is proxied by the German Bund ten-year yield and $CRP_{(MT,t)}$ is Malta's country-risk premium measured using the Malta–Germany sovereign yield spread. The ERP denotes Malta's mature-market equity risk premium (ERP), derived according to Damodaran (2013).[2] This decomposition allows the headline estimate to vary with the risk-free rate, country risk (as measured by the sovereign yield spread) and the bank's exposure to systematic equity-market risk.

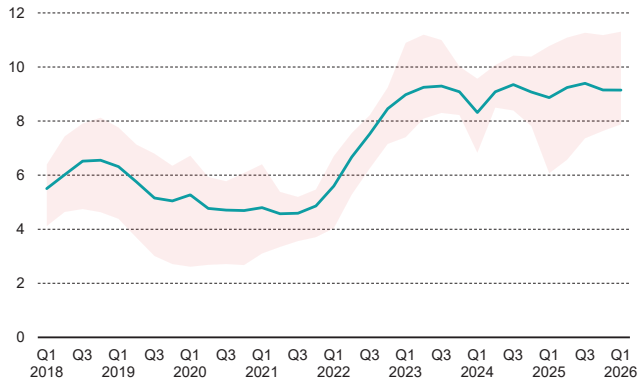
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[1] Written by Ms Sarah Vella, Principal Research Economist within the Macroprudential Policy, Stress Testing and Research Department and Doctoral Researcher at Universitat de Barcelona and University of St Andrews. The author would like to thank Governor Alexander Demarco, Deputy Governors Rita Schembri and Oliver Bonello, Ms Amy Camilleri, Mr Alan Cassar, Dr Aaron G. Grech, Ms Christine Balzan and Mr Pedro Polvora for their helpful inputs and valuable suggestions.

[2] Damodaran, Aswath (2013), "Equity risk premiums (ERP): Determinants, estimation and implications — the 2012 edition."*In Managing and measuring risk: Emerging global standards and regulations after the financial crisis*, pp. 343–455, World Scientific.

After estimating the baseline CAPM, a range of alternative CAPMs are estimated separately for each bank to allow for time variation in market sensitivity, additional sources of systematic risk and to cater for banks' different business models. These include rolling and shrunk rolling CAPM models, Constant Conditional Correlation and Dynamic Conditional Correlation (DCC) models, as well as richer Fama–French (1993) and sovereign-credit specifications.[3] Each model is then evaluated for each bank based on statistical performance, economic plausibility and stability.[4] The three highest-ranked models for each bank are then combined to obtain a more robust headline estimate. This approach follows the principle that there is considerable volatility surrounding any individual estimate of the CoE.

Chart 3a
MARKET-BASED AVERAGE CoE ESTIMATES
(percentage)



Source: Central Bank of Malta calculations.
Notes: The series represents the average of the three highest CoE estimates implied by the various asset-pricing models for each selected banks. The shaded region represents the minimum-to-maximum range of these three bank-level models across the selected banks.

Across banks and time, the resulting estimates based on the three best performing models per bank, range from approximately 4% to 9% (see Chart 3a). More recently, CoE has increased across listed banks, reaching an average of around 9% by March 2026, above the respective historical averages. These developments appear to be largely driven primarily by changes in the risk-free rate and the market risk premium. During 2019–2021, declining risk-free rates and lower estimated market betas contributed to lower required returns. The sharp increase during 2022–2023 is mainly associated with higher risk-free rates amid rising inflation expectations and tighter monetary conditions in key advanced economies. Overall, the results indicate that interest-rate developments are particularly important in driving the initial post-2022 increase in CoE, while greater estimated exposure to systematic equity-market risk subsequently helped sustain model-implied elevated required returns. During 2024–2025, for example, higher estimated market betas partly offset the downward impact of declining risk-free rates and country-risk premia.

Extending the analysis to unlisted banks

Following Altavilla et al. (2021), the analysis is extended to three unlisted banks because the absence of share-price data prevents direct market-based estimation.[5] However, their CoE remains relevant for loan pricing and shareholders' required returns. Regressing listed banks' estimates on their fundamentals provides a basis for inferring this otherwise unobservable funding cost for unlisted banks. In Malta, unlisted banks operate within both the core and non-core domestic

[3] Fama, Eugene F. and Kenneth R. French (1993), "Common risk factors in the returns on stocks and bonds."*Journal of Financial Economics*, 33, pp. 3–56.

[4] Model selection follows a four-step procedure. First, specifications are screened for economic plausibility, requiring an economically meaningful market beta and limited incidence of CoE floor binding. Second, model stability is assessed based on the stability of parameter estimates. For DCC models, conditional-correlation dynamics are considered. Third, eligible models are ranked according to the correlation between realised and fitted bank returns, with higher correlations indicating better statistical fit. Finally, the three highest-ranked specifications are retained for each bank. The headline CoE is calculated as their equal-weighted average.

[5] Altavilla, Carlo, Paul Bochmann, Jeroen De Ryck, Ana-Maria Dumitru, Maciej Grodzicki, Heinrich Kick, Cecilia Melo Fernandes, Jonas Mosthaf, Charles O'Donnell, and Spyros Palligkinis (2021), "*Measuring the cost of equity of euro area banks.*" ECB Occasional Paper.

banking groups, but still play a role in credit provision and deposit-taking.[6] Their inclusion therefore provides a broader and more comprehensive assessment of the CoE underpinning domestic financial intermediation activities.

A comparison of customer deposits-to-non-interbank loan ratios helps to assess the similarity of the funding structures of both listed and unlisted banks. This comparison informs and supports the application of the fundamentals-CoE relationship estimated for listed banks to unlisted banks. Customer deposits are substantial when compared to non-interbank lending both for unlisted banks and listed banks. Over 2018Q1–2026Q1, the average customer deposits-to-non-interbank loans ratio of unlisted banks is 109.5%, compared with 144.3% for listed banks. Although the average ratio is lower for unlisted banks, the difference is not statistically significant.[7] These averages indicate that customer deposits exceed non-interbank loans on average for both listed and unlisted banks in the sample. This common feature provides further support for applying the fundamentals-CoE relationship estimated for listed banks to unlisted banks.

To extend the analysis to the unlisted domestic banks, the market-based estimates derived for listed banks are regressed against their fundamentals as shown in equation (3).

$$CoE_{i,t} = \alpha + \beta_1 NPL_{i,t} + \beta_2 CET1_{i,t} + \beta_3 (Deposits/Loans)_{i,t} + \beta_4 \ln(Assets)_{i,t} + \tau_t + \varepsilon_{i,t} \quad (3)$$

The dependent variable is the quarterly average of the top-three headline market-based cost of equity ($CoE_{i,t}$) for listed banks.[8] The explanatory variables capture asset quality (the NPL ratio), common equity tier 1 (CET1) ratio, funding structure (customer deposits relative to loans) and bank size (the logarithm of total assets). The specification also includes time fixed effects (τ_t) to capture common developments across banks.

Overall, the estimates identify asset quality and funding structure as the balance-sheet characteristics most clearly associated with banks' CoE. A higher NPL ratio is associated with a higher estimated CoE, consistent with investors requiring greater compensation when asset quality is weaker. Moreover, a higher customer-deposits-to-loans ratio is associated with a lower CoE, suggesting that a more deposit-based funding structure, which tends to be stable, may be viewed favourably by investors. The coefficient on the CET1 is negative, as expected, but is not statistically significant in the preferred specification, consistent with the range of results by Altavilla et al. (2021). Bank size enters positively and significantly in this baseline regression. However, given the small number of listed banks and the sensitivity of the results to the size measures used, the coefficient should be interpreted with caution. Bank size should be interpreted primarily as a control variable and should not be viewed as a structural determinant of the CoE.[9]

Model-implied estimates for unlisted banks broadly mirror the trend observed for listed banks, although asset quality and stable deposit funding help contain differences across institutions. Applying the coefficients reported in Table 3a to the balance-sheet characteristics of unlisted banks produces estimated costs of equity ranging from approximately 4% to 10% over the sample period

[6] See Central Bank of Malta, *Financial Stability Report 2025*, Chapter 2: "Developments in the banking sector".

[7] A two-sided t-test does not reject equal mean ratios for listed and unlisted banks at the 5% significance level so there is no strong evidence of difference between the groups ($p = 0.08$).

[8] This approach is inspired by the model-averaging framework of Altavilla et al. (2021). The authors average ten models including five factor models and five implied CoE models requiring analysts' earnings and profitability forecasts. Given the smaller set of factor models available for each bank, the headline CoE per bank is calculated as the equal-weighted average of the three highest-ranked eligible models.

[9] The results reported in the Table 3a are robust to alternative specifications of bank size, including the use of a relative-size measure based on banks' assets. Robustness checks also include retained earnings relative to loans and an extended 2014–2026 sample allowing for a structural break in 2018 due to a break in the data series. The extended specification retains the variables in the main model and additionally includes retained earnings relative to loans and ROA.

Table 3a
BANK-FUNDAMENTALS DETERMINANTS OF CoE

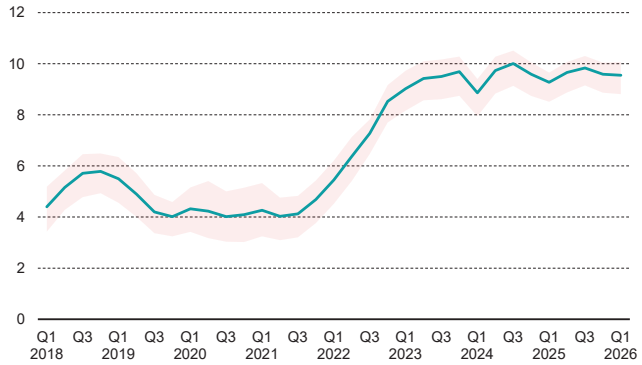
Percentage points

Economic group	Variable	Coefficient	Statistical significance
Asset quality	NPL ratio	+0.1030***	p < 0.01
Capitalisation	CET1 ratio	−0.0450	Not statistically significant
Funding structure	Customer deposits / loans	−0.0133***	p < 0.01
Bank size	Log assets	+1.2285***	p < 0.01

Source: Central Bank of Malta calculations.
Note: Pooled OLS with quarter fixed effects, 2018Q1–2026Q1; Driscoll–Kraay standard errors with four quarterly lags (to allow for heteroskedasticity, serial correlation and cross-sectional dependence);
*** denotes p < 0.01.

(see Chart 3b). The estimated cost of equity range for unlisted banks is broadly comparable to that of listed banks. This similarity may partly reflect the composition of the unlisted bank sample, which includes banks with business models broadly comparable to those of the studied listed banks. The average estimated CoE increased markedly during 2022-2023, reflecting the common upward trend observed for listed banks and captured by the time fixed effects in equation (3). Changes in bank fundamentals help explain differences across institutions. Declining NPL ratios generally exerted downward pressure during 2022–2024, while subsequent increases contributed positively for some banks. Changes in customer deposits relative to loans also moderated the estimated CoE in several periods, particularly towards the end of the sample. However, this contribution was not uniform across all banks. Capitalisation effects were generally smaller, while changes in bank size mostly contributed positively. Overall, these patterns are consistent with business models in which sound asset quality and substantial reliance on customer deposits may help to contain credit and refinancing risks. This moderated the estimated CoE for both listed and unlisted banks where the funding structure is broadly similar. Stronger CET1 ratios may provide an additional mitigating influence, although their contribution in the decompositions is generally smaller.

Chart 3b
UNLISTED BANKS: AVERAGE CoE ESTIMATES BASED ON BANK FUNDAMENTALS
(percentage)



Source: Central Bank of Malta calculations.
Notes: The series represents the average of the three highest CoE estimates implied by the various asset-pricing models for each selected banks. The shaded region shows the minimum-to-maximum range of the bank-level cost-of-equity average estimates.

Among listed banks, asset quality and funding composition are the main bank-specific contributors to year-on-year movements in the estimated CoE. Over 2019Q1–2026Q1, the NPL ratio accounts for 42.5% of average absolute contributions, followed by the customer deposits-to-loans ratio at 35.2%. Bank size and CET1 play smaller roles, accounting for 12.5% and 9.8%, respectively.

Among unlisted banks, changes in bank size and asset quality make the largest bank-specific contributions to year-on-year movements in the estimated CoE. Over the same period, log assets account for

35.4% of average absolute contributions, followed by the NPL ratio at 30.5%. The customer deposits-to-loans ratio contributes a further 21.9%, while CET1 accounts for the smallest share, at 12.2%.[10]

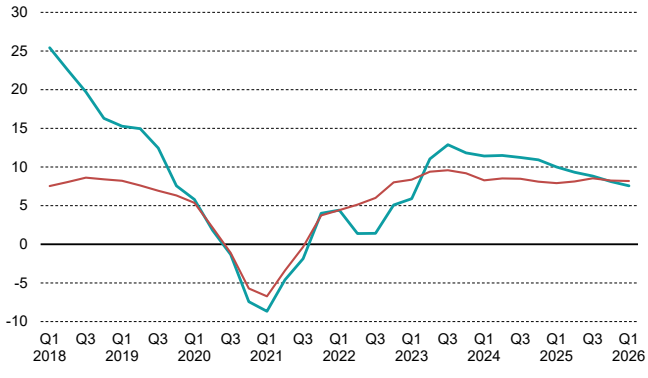
By 2026Q1, the increase moderated, with the average estimated CoE stabilising around 9% when all seven banks are weighted equally. This level falls within the range reported by many European banks. The EBA's June 2026 Risk Assessment Report indicates that approximately one-third of surveyed banks estimated their CoE at between 8% and 10%, while around 40% reported estimates between 10% and 12%.[11] The model-based estimate for Maltese banks therefore appears broadly comparable with European benchmarks, although differences in methodology, reference periods and bank characteristics make this comparison indicative.[12]

These results should not be interpreted as the actual CoE faced by unlisted banks. Rather, these represent model-implied estimates of the CoE on the assumption that unlisted banks would behave the same as listed banks, if such banks were publicly listed on the MSE. The estimates are therefore conditional on the model specification and should be interpreted with appropriate caution.

Bank profitability

For most banks in the sample, average profitability exceeded the estimated return required by shareholders, although the results varied across institutions and over time. Comparing each bank's ROE with its respective estimated CoE provides an indication of whether it generated returns sufficient to meet shareholders' required return.[13] Over 2018–2026, average ROE of approximately 8.02% exceeded the corresponding average CoE at 5.76% for the six core banks (see Chart 3c).[14] Five of the six core banks registered higher ROE than their respective CoE average over 2018–2026. Indeed, this does not imply that these banks maintained a positive gap throughout the period, as some experienced episodes in which ROE fell below their estimated CoE. Assessing the results at bank level therefore provides a more representative picture than comparing aggregate sample averages, which would be disproportionately affected by these negative observations.

Chart 3c
CORE BANKS: FUNDAMENTAL-BASED CoE VS PROFITABILITY
(percentage)



Source: Central Bank of Malta calculations.
Note: The sample contains the six Maltese core banks. Average RoE and CoE are calculated as asset-weighted averages of the corresponding bank-level measures.

Conclusion

Overall, the results point to a marked increase in Maltese banks' CoE after 2021, followed by stabilisation in early 2026. At the same time, the analysis emphasises that no single asset-pricing specification is sufficient to estimate the

[10] For each fundamental, the average size of its contribution to the year-on-year change in CoE across common time quarters and banks in each group is averaged, treating increases and decreases equally. This average is expressed as a percentage of the combined averages for all four fundamentals. Banks receive equal weight and the common time effect is excluded.
[11] European Banking Authority (2026), *Risk Assessment Report – June 2026*, Section 5, "Profitability".
[12] Only two banks are similar across this study's sample and the EBA report.
[13] ROE is calculated as the sum of quarterly profits over the latest four quarters divided by the simple average of total equity at the current quarter-end and the previous December year-end, multiplied by 100. The December balance provides a consistent calendar-year reference point. Alternative denominator averaging conventions yield very similar ratios.
[14] Average ROE and CoE are calculated as asset-weighted averages of the corresponding bank-level measures.

CoE of Maltese banks in a small and relatively illiquid market. Combining the best-performing asset-pricing specifications provides a more robust market-based measure. This approach shows that CoE increased but stabilised towards the start of 2026. The analysis further suggests that asset quality and funding structure are important correlates of the market-based estimated CoE for Maltese banks.

Against this backdrop, future work could extend the analyses to the cost of debt. This would provide a more comprehensive understanding of the factors influencing banks' funding cost and capital structures, while also capturing the role of creditors' risk perceptions and broader funding conditions.

3. STRESS TESTS

The Central Bank of Malta conducts solvency and liquidity stress tests to assess banks' resilience to severe but plausible adverse scenarios. These frameworks are regularly updated to reflect emerging risks and regulatory developments.

This chapter reviews the results of the stress-testing exercises presented in the FSR 2025 and assesses how these have evolved in light of developments during the first half of 2026. Given that the Macro Stress Test is run at annual frequency, this chapter examines the liquidity and the IRRBB frameworks exclusively.

The chapter also presents the results of the newly introduced cyber stress-testing framework in a dedicated Special Feature A. Given the increasing digitalisation and interconnectedness of the financial sector, cyber incidents can have implications beyond operational disruptions, potentially affecting liquidity conditions and financial stability. The cyber stress-testing framework applies transaction-level T2 data to examine how payment disruptions affect banks' liquidity and propagate through the banking system.

3.1 Liquidity stress test

The liquidity stress test results continue to indicate the banking sector's strong capacity to withstand short- and longer-term liquidity shocks. The assessment is based on three liquidity frameworks: the Persistent Deposit Withdrawals (PDW), LCR and the NSFR. The PDW framework assesses banks' capacity to withstand a four-week deposit run scenario, the LCR framework captures short-term resilience over 30 days, and the NSFR framework assesses the stability of banks' funding structures over one year. The scenarios are hypothetical and are intended to identify potential vulnerabilities at the individual-bank and system-wide levels rather than to forecast liquidity levels.

Table 3.1 compares the results of the above-mentioned tests as at June 2026 with those reported in the FSR 2025, which were based on December 2025 data. The table provides a snapshot of the key outcomes and underlying drivers while further details and developments are discussed in the sections that follow. For each bank category, the table presents the results under the baseline scenario and the hypothetical adverse scenario that generates the largest impact within each framework, for the individual bank categories.[1] The coloured circles indicate whether the banking category, on aggregate, breaches the relevant threshold considered. The arrows illustrate whether the overall assessment improved, deteriorated, or remained broadly unchanged relative to the previous vintage. A brief description highlights the main driver of the observed outcome.

As illustrated in Table 3.1, the results point to a generally favourable aggregate liquidity position across all three bank categories. The PDW framework suggests that banks are able to absorb significant outflows through existing counterbalancing capacity (CBC), thereby meeting liquidity needs under the extreme but plausible conditions considered in the test.

Similarly, the LCR results indicate that credit institutions, at the aggregate level, maintain sufficient HQLAs to withstand the severe short-term funding shocks considered, although individual bank results vary.

The NSFR framework indicates resilience in banks' aggregate longer-term funding structures, although international banks exhibit relatively greater sensitivity under the most severe stress assumptions, as reflected by the yellow grading. Nonetheless, the aggregate stressed NSFR remains within the 110%–119% range, comfortably above the regulatory minimum requirement of 100%. Consequently, the deterioration observed under a stress scenario does not signal a funding vulnerability, but rather a relative reduction in available stable buffers, reflecting a sensitivity to the assumed shocks.

[1] The baseline for the LCR and NSFR frameworks reflects the regulatory assumptions and haircuts prescribed in the applicable regulations. In contrast, the PDW framework uses internally calibrated assumptions and haircuts as a complementary short-term liquidity assessment. Further details on the baseline and adverse scenarios are available in FSR 2023, FSR 2021 and FSR 2018, together with a more concise description of the assumptions underlying each scenario presented throughout the current report.

Table 3.1
SUMMARY OF LIQUIDITY STRESS TESTING RESULTS

Framework	Core domestic banks	Non-core domestic banks	International banks	Change[1]	Main driver
PDW	●	●	●	↔	Retail deposits are more prominent among core domestic banks, while non-core domestic and international banks exhibit a more balanced distribution of deposits across retail, corporate, and other customer sectors.
	●	●	●	↔	The CBC is primarily driven by debt securities in core domestic banks, while overnight deposits are the main contributor for non-core domestic and international banks.
LCR:					
Baseline	●	●	●	↓ ↑	Negligible changes for core domestic banks Reduction in net liquidity outflows for non-core domestic and international banks
Adv. Scenarios (largest impact)	●	●	●	↑	Adv. Scenarios (largest impact) Committed facilities for core domestic banks (AS3)
NSFR:					
Baseline	●	●	●	↔ ↑	Negligible variations for core domestic and international banks Strong available stable funding (ASF) for non-core domestic banks
Adv. Scenarios (largest impact)	●	●	●	↓ ↓	Higher run-off for retail and wholesale deposits, the deterioration of some loans into non-performing exposures, and market pressures for non-core domestic and international banks (AS2). Committed facilities for core domestic banks (AS4)

[1] Change refers to the overall assessment relative to the previous stress-testing exercise: ↑ improving; ↔ broadly unchanged; ↓ deteriorating.

● (>120%): Threshold comfortably exceeded.

● (110%-119%): Vulnerabilities identified, but adequate buffer remains.

PDW classification: ● indicates banks can withstand the full four-week withdrawal horizon;
● indicates failure to withstand the full horizon.

Abbreviations: AS1 = Adverse Scenario 1; AS2 = Adverse Scenario 2; AS3 = Adverse Scenario 3; AS4 = Adverse Scenario 4.

Overall, the three liquidity frameworks indicate aggregate resilience to the shocks considered, with existing liquidity buffers remaining sufficient to absorb the losses generated under stressed conditions. Taken all together, the predominance of green indicators highlights the banking sector's capacity to withstand severe, but plausible liquidity shocks, thereby preserving financial stability.

3.1.1 Persistent deposit withdrawals

The PDW framework tests banks' ability to withstand PDW, over a four-week horizon, by comparing the assumed 100% run-off of outflows with each bank category's CBC. The CBC is determined according to the predefined hierarchy of liquid assets, ranging from cash, central bank placements, and eligible securi-

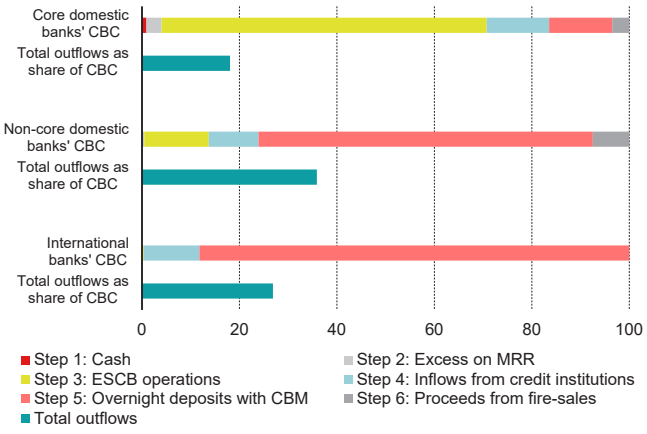
Figure 3.1
ASSUMED HIERARCHY FOR CBC



Source: Central Bank of Malta.

ties that may be used as a source of additional liquidity in a fire sale scenario (see Figure 3.1).[2,3]

Chart 3.1
COMPOSITION OF CBC AND TOTAL OUTFLOWS AS SHARE OF CBC
(per cent)



Source: Central Bank of Malta calculations.

In the first half of 2026, the CBC for core and non-core domestic banks remained broadly unchanged, with core domestic banks' CBC composition heavily concentrated in instruments eligible for Standard Monetary Policy Operations. This share, however, contrasts with non-core domestic and international banks, which relied more on Central Bank of Malta placements, particularly overnight deposits. Compared with December 2025, the most notable changes were among international banks, whose share of total CBC held in overnight deposits rose by 19 percentage points to 88%, accompanied by a reduction in cash and MMR holdings.

The assumed high deposit withdrawals under the adverse scenario would absorb 27%, 37% and 18% of the available CBC for core, non-core and international banks, respectively. This would result in still ample liquidity buffers and is a comparable outcome with the preceding vintage (see Chart 3.1).

At the individual bank level, most banks would manage to sustain the assumed deposit outflows over the four-week horizon. Some institutions would also need to draw on overnight deposits held with the Central Bank of Malta within the defined CBC hierarchy. Nevertheless, the majority of banks would continue to meet the assumed liquidity outflows over the four-week horizon, retaining, on average, an excess of CBC of at least 14% to absorb further withdrawals beyond the tested horizon.

3.1.2 Liquidity coverage ratio

The LCR stress test assesses banks' capacity to absorb short-term liquidity outflows over a 30-day period. The baseline follows the regulatory assumptions applicable to the LCR, while the three adverse scenarios

[2] For more details on the framework's methodology and the setting of the assumed hierarchy for the CBC, refer to Section 3.2.1 of the FSR 2023.

[3] Following the adoption by the Governing council of the ECB of Decision (EU) 2026/812 under which excess reserves by eligible counterparties that meet the relevant access conditions will be remunerated at the deposit facility rate (DFR) as from 17 June 2026, the CBC hierarchy will be updated accordingly as from the next vintage.

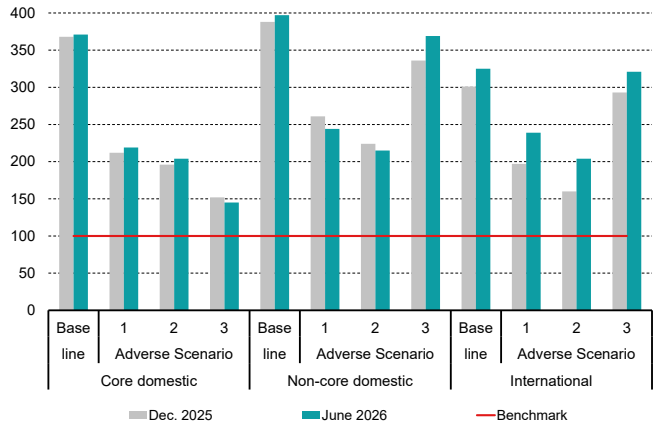
Table 3.2
DESCRIPTION OF LCR FRAMEWORK'S BASELINE AND ADVERSE SCENARIOS

Scenario	Description
Baseline	Haircuts and outflow/inflow rates set out in the (EU) 2015/61
Adverse:	
Scenario 1	Higher outflows compared to the LCR Delegated Regulation
Scenario 2	Scenario 1 with additional withdrawals from both resident and non-resident time deposits
Scenario 3	Baseline scenario with full withdrawal of committed facilities to NFCs and households

Source: Central Bank of Malta.

progressively test higher deposit outflows, withdrawals from resident and non-resident term deposits, and full withdrawal of committed facilities (see Table 3.2).

Chart 3.2
STRESS TEST RESULTS – LCR RESULTS FOR ALL BANKS
(per cent)



Source: Central Bank of Malta calculations.

Under the baseline, the aggregate LCR stood at 370%, 397% and 325% for core domestic, non-core domestic and international banks, respectively. Compared with December 2025, the ratios increased by 2.6, 9.4 and 24.6 percentage points, respectively. For non-core domestic and international banks, the increases mainly reflected lower net liquidity outflows, while HQLA holdings remained broadly stable. In contrast, both the numerator and denominator increased marginally for core domestic banks (see Chart 3.2).

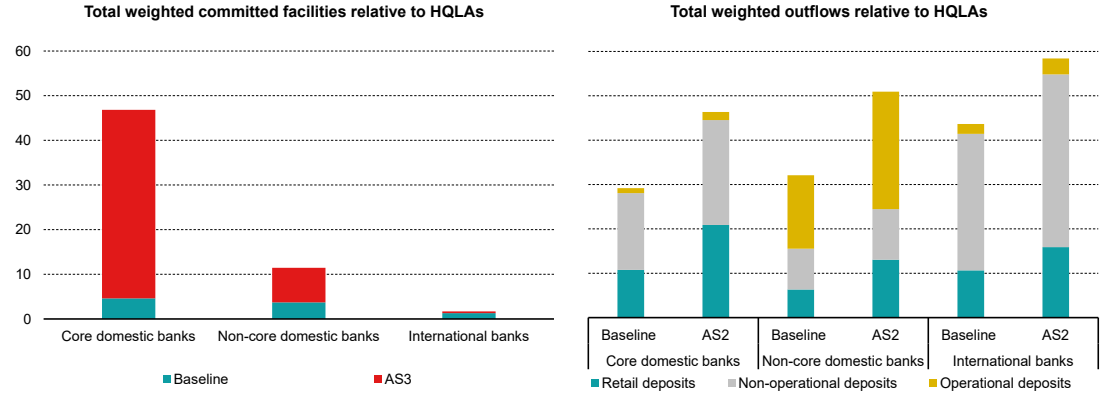
Core domestic banks were most affected by adverse scenario 3, with the LCR falling to 144%, primarily reflecting their sensitivity to the assumed full drawdown of committed facilities. Non-core domestic and international banks recorded their lowest ratios under scenario 2 (214% and 204%, respectively), consistent with their higher reliance on non-resident deposits. These results are similar to those observed at end-2025, continuing to show a greater sensitivity to this scenario.

Scenario 3 has the largest impact for core domestic banks as facilities amount to 42% of their HQLA amplifying the deterioration in their liquidity position. By contrast, these facilities amount to only 7.75% and 0.38% for non-core domestic and international banks, respectively, such that the assumption of a 100% drawdown of committed facilities has a limited impact (see Chart 3.3 on the left). A larger impact is not necessarily driven by higher exposure alone but may reflect differences in the portfolio composition and the relative size of HQLA buffers.[4]

The greater sensitivity for non-core and international banks to scenario 2 reflects their deposit funding composition, with operational and non-operational deposits accounting for the largest share of total outflows, respectively. After applying the stressed outflow rates, combined outflows from retail, operational,

[4] Due to data limitations, it is not possible to have a distinction between revokable and non-revokable committed facilities. Therefore, a conservative approach is adopted assuming that all commitments are withdrawn.

Chart 3.3
IMPACT OF BANKS UNDER EXTREME LIQUIDITY CONDITIONS RELATIVE TO HQLA HOLDINGS – 2026 Q2
(per cent)



Source: Central Bank of Malta.
Note: Adverse scenario 2 (AS2) included higher outflows and additional withdrawals from both resident and non-residents. Adverse scenario 3 (AS3) included full withdrawal of committed facilities.

and non-operational deposits rise to 46%, 51%, and 58% for core domestic, non-core domestic, and international banks, respectively (see Chart 3.3 on the right).[5]

Despite these declines, aggregate LCRs remained comfortably above the 100% regulatory requirement across all bank categories. At the individual bank level, however, a few banks would record stressed LCRs below this benchmark under the hypothetical adverse scenarios. This mainly reflects their lower starting LCRs, which leave less headroom to absorb the assumed liquidity shocks. These modelled outcomes should be distinguished from banks' reported baseline positions.

3.1.3 Net stable funding ratio

The NSFR framework complements the short-term liquidity assessment by examining whether banks maintain sufficient stable funding to support their assets and off-balance sheet exposures over a longer-term horizon. Similar to the LCR framework, the baseline follows the regulatory assumptions applicable to the NSFR, with four adverse scenarios assessing higher run-off rates for retail and wholesale deposits, the migration of some loans to non-performing status, market pressures, and the full withdrawal of committed facilities (see Table 3.3).

As at June 2026, NSFR changes were negligible for core domestic and international banks, rising by less than 0.3 percentage points to 188.7% and 136.9%, respectively. However, non-core domestic banks experienced a more pronounced and positive increase of 13 percentage points to reach 202.8% compared to December 2025. The improvement for non-core domestic banks was mainly attributable to higher ASF, particularly from other non-financial customers and operational deposits, which increased by 15% and 19%, respectively, compared with December 2025.

The NSFR of non-core domestic banks reflects differences in their funding profile, alongside a 5% decrease in loans relative to ASF.

In a stress context, the largest estimated decline in the NSFR was observed under adverse scenario 4 for core domestic banks and adverse scenario 3 for non-core domestic banks and international banks. Under these scenarios, the NSFR declined by 61, 51, and 22 percentage points to reach 128%, 152% and 115%, respectively. These results mainly reflect greater reliance on committed facilities and the assumed full drawdown of those facilities for core domestic banks. Non-core domestic banks and international banks showed more sensitivity to the combined effects of higher run-off rates for retail and wholesale deposits, some loans

[5] Retail deposits are deposits from individual consumers generally considered more stable funding sources. Meanwhile, operational and non-operational deposits are deposits placed to support day-to-day business operations and investment purposes by non-financial customers, corporates or financial institutions, which generally are more prone to withdrawals under stress.

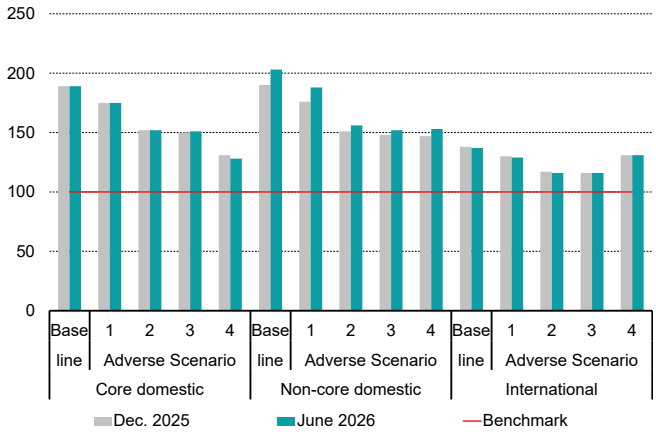
Table 3.3
DESCRIPTION OF NSFR FRAMEWORK'S BASELINE AND ADVERSE SCENARIOS

Scenario	Description
Baseline	ASF and RSF factors as prescribed by the Regulation (EU) 2019/876
Adverse:	
Scenario 1	A higher run-off for retail and wholesale deposits impacting the availability of stable funding
Scenario 2	Adverse scenario 1 with some loans becoming non-performing requiring more stable funding to support them impacting the RSF
Scenario 3	Adverse scenario 2 with pressure in the market reducing the value of bonds and equities (level 1, 2A and 2B HQLA and other securities) implying the need for further stable funding
Scenario 4	Baseline with full withdrawal of committed facilities to NFCs and households (similar to LCR adverse scenario 3).

Source: Central Bank of Malta.

becoming non-performing exposures, and market pressures (see Chart 3.4).

Chart 3.4
STRESS TEST RESULTS – NSFR RESULTS FOR ALL BANKS
(per cent)



Source: Central Bank of Malta calculations.

At the individual bank level, all banks' baseline NSFR remained above the 100% minimum requirement. However, a few banks recorded stressed NSFRs slightly below 100% under adverse scenarios 2, 3 and 4. Shortfalls across most scenarios were concentrated in one small institution, mainly reflecting a significant decline in its starting NSFR compared with December 2025. Overall, the three liquidity frameworks indicate that the banking sector continues to maintain substantial aggregate liquidity and stable funding buffers, although some banks exhibit vulnerabilities under the hypothetical adverse scenarios. The results reflect both the severity of the assumed shocks and differences in banks' starting buffers and business model structures rather than a broad-based deterioration in liquidity conditions.

3.2 Interest rate risk in the banking book

The IRRBB framework assesses banks' exposure to changes in interest rates arising from shifts in the slope and shape of the yield curve. The assessment captures the immediate impact of such movements on banks' profitability through their NII, as well as the impact of the revaluation of instruments held at fair value (FV).

The analysis is conducted under the six interest rate shock scenarios set out in Annex 2 of the 2016 Basel Committee on Banking Supervision standards.[6] These capture a parallel upward and downward shift, an increase and decrease in the short rate end of the curve, and two composite shifts in short and long-term rates represented by the steepener and flattener scenarios. All six scenarios affect the term structure of the yield curve, with the shocks differing by currency denomination of the instruments. The analysis focuses on EUR, GBP and USD, which represent the material currencies in the banking book, with GBP and USD remaining the most relevant non-EUR currencies across all three banking categories as of June 2026.

[6] https://www.bis.org/publications/201604-standards-interest-rate-risk-banking-book.pdf

Table 3.4 presents the resulting impact of changes in NII and bond revaluations on the Tier 1 capital ratios of the three banking categories under the different scenarios.

Instruments held by banks measured at FV remained broadly unchanged when compared to December 2025, except for non-core domestic banks. For core domestic banks, these instruments accounted for 21% of their total bond holdings, while for non-core domestic banks the share increased by 24 percentage points to 41%. By contrast, the investment portfolios of international banks are accounted for at AMC. This reflects the banks' preference to insulate these holdings from market movements and to retain these instruments until maturity.

Consistent with previous test vintages, the three scenarios featuring an increase in interest rates show positive results for all three bank categories, given a predominantly loan-based asset portfolio and an investment portfolio that is largely accounted for at AMC. The most adverse impact is observed for core domestic and international banks under the short-rate down scenario. In this scenario, and under the assumption that both interest-sensitive assets and liabilities re-price immediately, the decline in interest income from loans is the main driver for the overall negative impact, reflecting the differences in the composition of these banks' balance sheets. Overall, revaluation gains offset only a limited portion of the decline in interest income.

Given the importance of the investment portfolio structures in shaping these results, an examination of their sectoral composition and the associated accounting treatment provides further insight into the interpretation of the results. As of June 2026, the aggregate banks' bond portfolios maintain significant exposures to sovereign debt securities, followed by financial corporations, and NFCs, representing 72.2%, 25.2% and 2.6% of total bond holdings, respectively. Sovereign securities represented the largest asset class across all three bank categories, accounting for 80.8%, 66.5%, and 100% of total bond holdings for core domestic,

Table 3.4
STRESS TEST RESULTS – IRRBB FRAMEWORK – RELATIVE IMPACT OF CHANGES IN INTEREST RATES ON THE TIER 1 CAPITAL RATIO
Per cent

		Core domestic banks	Non-core domestic banks	International banks
Initial Tier 1 capital ratio		20.77	19.94	33.01
Parallel up	*NII*	*2.08*	*1.66*	*0.70*
	Revaluations	*-0.80*	*-1.33*	*0.00*
	Post-shock Tier 1 capital ratio	22.04	20.27	33.71
Parallel down	*NII*	*-1.65*	*-1.56*	*-0.59*
	Revaluations	*1.04*	*3.11*	*0.00*
	Post-shock Tier 1 capital ratio	20.16	21.49	32.42
Flattener	*NII*	*1.97*	*1.46*	*0.66*
	Revaluations	*-0.13*	*0.25*	*0.00*
	Post-shock Tier 1 capital ratio	22.61	21.65	33.67
Steepener	*NII*	*-1.25*	*-1.12*	*-0.45*
	Revaluations	*0.01*	*-0.35*	*0.00*
	Post-shock Tier 1 capital ratio	19.53	18.47	32.56
Short rate up	*NII*	*2.47*	*1.83*	*0.83*
	Revaluations	*-0.39*	*-0.32*	*0.00*
	Post-shock Tier 1 capital ratio	22.85	21.46	33.84
Short rate down	*NII*	*-1.95*	*-1.73*	*-0.70*
	Revaluations	*0.41*	*0.33*	*0.00*
	Post-shock Tier 1 capital ratio	19.23	18.54	32.31

Source: Central Bank of Malta calculations.

non-core domestic, and international banks, respectively. These exposures were concentrated in a relatively limited number of sovereign issuers, with particularly high concentrations in the banks' countries of operation. Maltese sovereign bonds accounted for 30.4% and 32.1% of total bond holdings of core and non-core domestic banks, respectively, while international banks' sovereign bond holdings were entirely concentrated in Maltese government securities.

The significance of sovereign exposures makes their accounting classification and geographical distribution particularly relevant to the assessment of potential market shocks. As of June 2026, sovereign bonds measured at AMC accounted for 78.6% of the total sovereign bond portfolio, while the remaining 21.4% were classified at FV. In terms of geographical distribution, Malta represented the largest sovereign exposure, accounting for 29.6% of the total bond portfolio, followed by France (8.1%), Belgium (4.9%), Italy (2.9%) and Austria (2.4%). Together, these five geographical exposures amount to 47.9% of the total bond portfolio, while a further 28.9% was invested across 27 other European countries. The remaining 3.4% exposure to sovereigns is spread across nine non-European countries, with the United Kingdom and the United States accounting for 0.22% and 0.23%, respectively. Lastly, most of the sovereign exposures are EUR-denominated (98.9%), with USD and GBP representing, respectively, 0.4% and 0.5% of the total sovereign portfolio.

This information is relevant in the context of fiscal debt sustainability concerns and sovereign bond-market conditions across a number of European jurisdictions, including some of the countries to which banks have material exposures.[7] Adverse developments in sovereign and non-sovereign bond markets could affect banks through both solvency and liquidity channels. From an accounting perspective, the predominance of AMC-classified securities limits the immediate recognition of unrealized FV changes. However, from a liquidity perspective, European System of Central Banks eligible collateral holdings in sovereign (and non-sovereign) bonds could adversely affect the availability of liquidity under open market operations when the increase in sovereign bond yields transmits into lower bond prices. The extent of the impact would also depend on other factors such as the applicable valuation haircuts. Consequently, in addition to the accounting treatment that influences banks' solvency position as tested above, another important dimension to consider when assuming rising yields is their impact on banks' liquidity stance.

[7] Financial Stability Review, May 2026; EBA Risk Assessment Report - June 2026.

4. INSURANCE COMPANIES AND INVESTMENT FUNDS

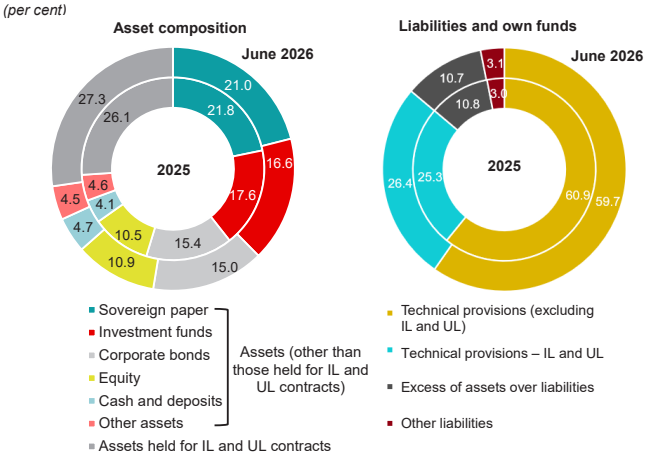
4.1 Domestic insurance companies

The number of active licensed insurance undertakings operating in Malta increased by two to 71 by June 2026, following the licensing of three new entities and the surrender of one licence during the review period. Of these, ten were considered as domestically relevant, and recorded a 3.5% increase in their aggregate balance sheet, with assets standing at €4.1 billion equivalent to 16.2% of GDP.[1] This growth was observed across both life and non-life insurers, with both segments remaining well capitalised and maintaining broadly adequate liquidity levels. Non-life insurers reported an improvement in profitability, whereas life insurers recorded lower profits and a comparatively weaker ROA.

4.1.1 Domestically relevant life insurance companies

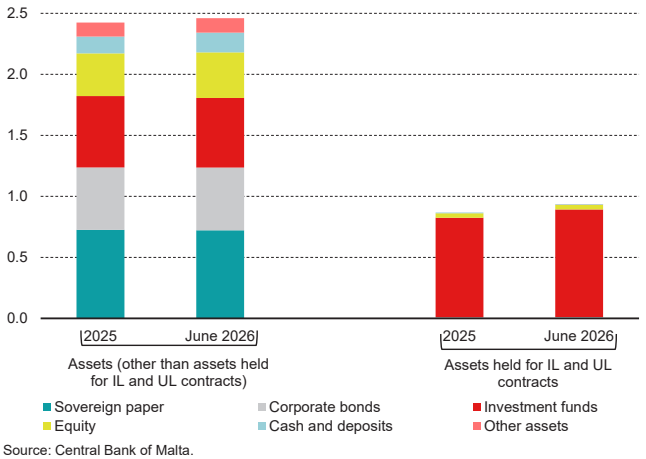
The life insurance sector's assets grew by 3.2% to €3.4 billion, representing 13.3% of GDP. The expansion was mainly driven by assets associated with unit-linked (UL) and index-linked (IL) contracts, which increased by 8.0% to €937 million and accounted for more than one-quarter of the life insurers' balance sheet by June 2026.[2] The increase in this share reflects a greater proportion of life insurers' business being associated with products under which policyholders bear the investment risk and may benefit from investment gains or incur investment losses (see Chart 4.1). Assets excluding UL and IL business also increased, although at a more subdued rate of 1.4%, to €2.5 billion.

Chart 4.1
LIFE SECTOR BALANCE SHEET
(per cent)



Source: Central Bank of Malta.

Chart 4.2
LIFE INSURANCE SECTOR ASSET COMPOSITION
(EUR billions)



Source: Central Bank of Malta.

Asset composition – IL and UL policies

Participations in investment funds remained the principal assets backing IL and UL contracts, accounting for 94% of the portfolio and reflecting the market-linked nature of these products (see Chart 4.2). These holdings consisted mainly of equity, bonds and asset allocation funds. Overall claims on investment funds increased by 7.9%, mainly reflecting higher exposures

[1] Of the ten domestically relevant insurers, four specialise in life insurance and six in non-life insurance. Three non-life insurers also underwrite a small proportion of life business. As this represents only 3.8% of their total gross written premia, these undertakings are included within the non-life segment for analytical purposes.

[2] The performance of IL and UL contracts depends on the underlying investments, with the associated investment risks borne primarily by policyholders. By contrast, other life insurance products may provide guarantees that expose insurers to a greater share of market and balance-sheet risk. IL and UL contracts are therefore assessed separately to reflect their distinct risk profiles and implications for the insurers' financial positions.

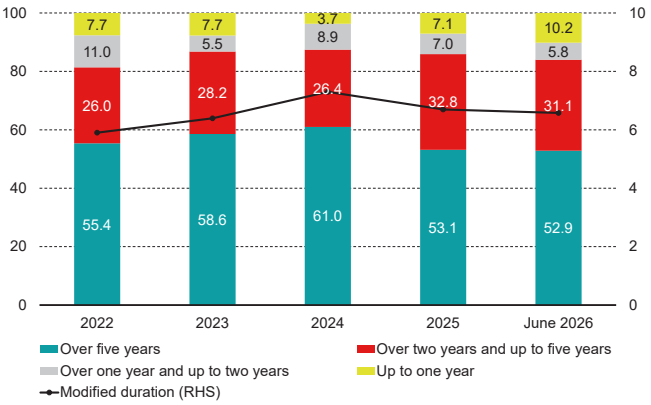
to euro area asset allocation and equity funds. In contrast, investments in bond funds contracted by 6.3%, mainly owing to lower participations in domestically-focused funds. The remainder of IL and UL assets was held predominantly in equities, with only a limited allocation to bonds.

Asset composition – excluding IL and UL policies

Assets excluding IL and UL contracts, which mainly comprise investments backing other life insurance products and insurers' own-account holdings, remained concentrated in fixed-income securities, which accounted for 50.2% of such assets. Sovereign debt remained the largest component of the portfolio, reflecting insurers' preference for relatively lower-risk assets (see Chart 4.2). However, holdings of sovereign securities declined marginally during the first half of the year, mainly reflecting lower exposures to euro area government bonds. In contrast, corporate bond holdings increased by 0.5%, largely due to higher exposures to securities issued by US financial institutions, and NFCs in the US and the euro area. NFC exposures remained concentrated in the manufacturing and energy supply sectors, both of which registered further increases by June 2026.

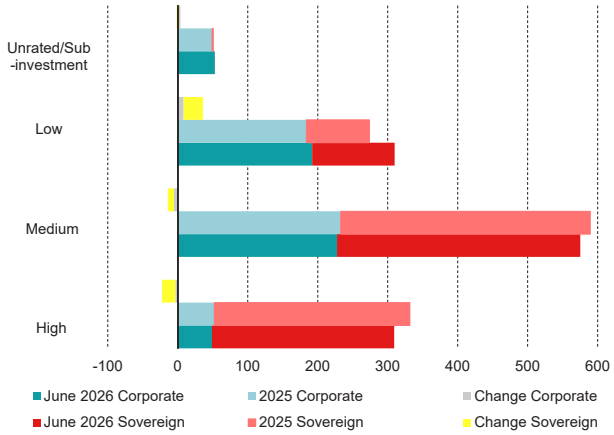
The maturity profile of life insurers' bond portfolios remained broadly stable. Bonds with residual maturities exceeding five years continued to represent the largest segment, accounting for 52.9% of holdings (see Chart 4.3). While the share of bonds maturing within one year increased to 10.2%, the shares of bonds in the one-to-two-year and two-to-five-year maturity buckets declined. These movements had only a limited impact on the portfolio's interest rate risk sensitivity, with modified duration declining marginally to 6.6%. Yields-to-maturity increased across most maturity buckets, particularly for bonds with residual maturities of more than one year, reflecting the rise in bond yields observed during the first half of 2026. While higher yields may weigh on the market value of existing bond holdings, they could support insurers' investment income over time, if maturing assets are reinvested at more favourable rates.

Chart 4.3
LIFE – MATURITY STRUCTURE AND MODIFIED DURATION OF DEBT SECURITIES
(per cent of total debt securities holdings; per cent)



Source: Central Bank of Malta.

Chart 4.4
LIFE – DEBT SECURITIES PORTFOLIO – INVESTMENT RATINGS
(EUR millions)



Source: Central Bank of Malta.

The credit quality of the life insurers' debt portfolios remained broadly sound. Despite a 3.7% decline, medium and high-rated securities accounted for around 70% of holdings (see Chart 4.4). Meanwhile, holdings of lower-rated debt increased by 7.5%, indicating some reallocation towards higher-yielding securities. The overall

credit quality of the portfolio was supported by sovereign bonds, of which more than 80% were rated medium or high investment grade. Corporate bond holdings had a comparatively weaker credit profile, with slightly more than half invested in lower-rated and sub-investment-grade securities.

Investment funds' units other than those backing IL and UL contracts declined by 2.7%, mainly owing to lower exposures to euro area money market funds (MMFs). This could indicate a reallocation towards longer-duration fixed-income instruments amid the higher bond yields observed during the first half of 2026. Direct equity holdings, by contrast, increased by 6.9%, with growth recorded across domestic, euro area and other international exposures, mainly driven by equities issued by NFCs. US equities remained the largest geographical exposure, reflecting the international presence of the underlying companies. Domestic equities accounted for around one-fifth of total equity holdings, with exposures to monetary financial institutions (MFIs) and NFCs collectively representing most of the domestic portfolio.

Cash and cash-equivalents increased by 17.2%, reaching 6.5% of total assets in June 2026. Exposures to other asset classes, including collateralised securities, property, mortgages and loans, as well as recoverables and receivables, remained limited, collectively accounting for around 4.8% of total assets. Overall, assets remained concentrated in fixed-income securities and investment funds, while exposures to less liquid and non-traditional assets remained modest.

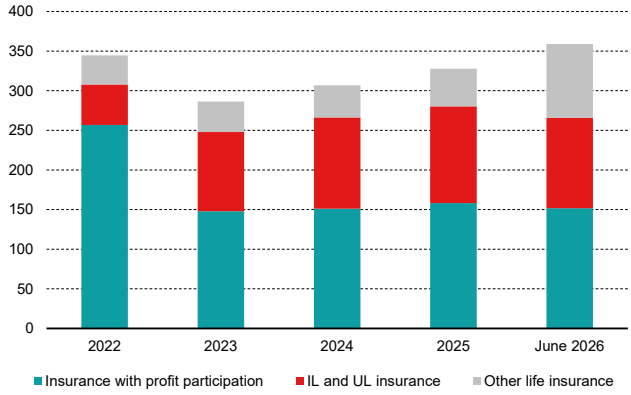
Liabilities and own funds

Liabilities associated with IL and UL contracts rose by 7.9%, in line with the expansion in market-linked business (see Chart 4.1). Technical provisions for other life insurance products remained the largest liability component, but grew more moderately, by 1.2%. Overall, technical provisions increased by 3.2%, broadly mirroring the expansion on the assets side of the balance sheet. The excess of assets over liabilities rose by 2.3% and accounted for 10.7% of total assets. This supported insurers' loss-absorbing capacity, although the adequacy of their solvency position is more directly assessed below.[3]

Gross written premia and claims

Gross written premia (GWP) increased by 9.5% during the first half of 2026, driven by the 'other life' insurance category, where premia almost doubled, partly reflecting the introduction of a new guaranteed savings-type product (see Chart 4.5).[4] Consequently, the share of 'other life' premia rose by 11.2 percentage points to 26.0% of total GWP. By contrast, premia for 'insurance with profit participation' and IL and UL business declined by 4.1% and 6.6%, respectively. Their shares of total GWP consequently fell by 4.8 percentage points to 42.3%, and by 6.4 percentage points to 31.8%, respectively.

Chart 4.5
GWP OF THE DOMESTIC LIFE INSURANCE SECTOR BY LINE OF BUSINESS
(EUR millions)



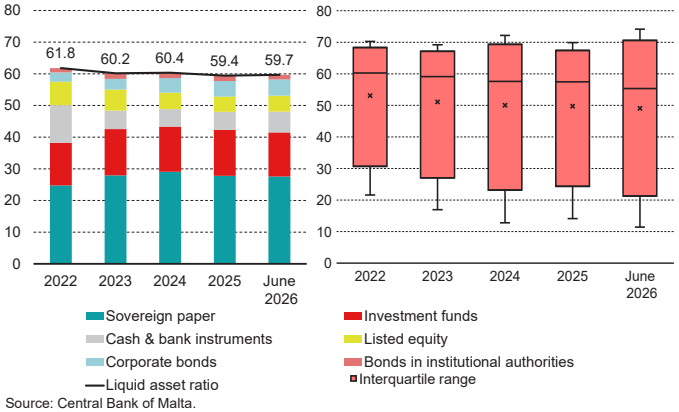
Source: Central Bank of Malta.

Gross claims incurred increased by 5.8%, mainly reflecting higher claims associated with IL and UL products. Claims under the 'other

[3] Under the Solvency II framework, eligible own funds comprise the excess of assets over liabilities determined under regulatory valuation rules, together with eligible subordinated items classified as Tier 1, Tier 2 or Tier 3 capital.
[4] Around 0.7% of total GWP was underwritten outside Malta, mainly elsewhere in the euro area, and were related to IL and UL contracts and other life insurance business.

life' insurance line also increased, albeit to a lesser extent, while claims relating to 'insurance with profit participation' declined slightly.

Chart 4.6
LIQUID ASSETS RATIO OF THE LIFE INSURANCE SECTOR
(per cent)



Source: Central Bank of Malta.
Note: The left panel shows the composition of liquid assets; the right shows the distribution of the indicator, where the box, horizontal line, and × denote the interquartile range, median and unweighted mean, respectively.

Liquidity and capital

The life insurance sector's liquidity position remained broadly stable, with the aggregate liquid assets ratio increasing by 0.2 percentage points to 59.7% (see Chart 4.6). The increase was supported primarily by higher cash holdings, together with increased exposure to listed equities and corporate bonds. These developments more than offset declines in exposures to collective investment undertakings and bonds issued by institutional and supranational entities. Sovereign securities, however, continued to account for the largest share of liquid assets. Liquidity positions nevertheless continued to vary across insurers, reflecting differences in business models and investment strategies. Most insurers continued to maintain sizeable liquidity buffers, with the median liquid assets ratio remaining above 50%.

Life insurers remained well capitalised, with the aggregate SCR coverage ratio standing at 247.7% in June 2026. The ratio declined by 23.8 percentage points from end-2025, mainly reflecting the faster growth in the SCR relative to eligible own funds. Nevertheless, the sector's solvency position remained comfortably above regulatory minimum requirements, indicating a sizeable aggregate buffer to absorb losses arising from market, underwriting and operational risks. The quality of eligible own funds also remained high, consisting mostly of Tier 1 capital.

Profitability

Life insurers' profitability weakened during the period, with profit before tax declining by 14.9% and pre-tax ROA falling to 0.7%. The deterioration reflected weaker financial performance, as the increase in financial expenses, particularly expenses associated with insurance contract liabilities, exceeded the gains from higher investment returns. This was partly offset by stronger underwriting performance, with the insurance service result increasing by 7.6% on the back of higher insurance revenue.

Operational efficiency also improved, as the growth in net premia earned outpaced that of operating expenses. Accordingly, the expense ratio declined by 0.8 percentage points to 16.8%.[5] Nevertheless, it remained above the ten-year average of 13.3%.

4.1.2 Domestically relevant non-life insurance companies

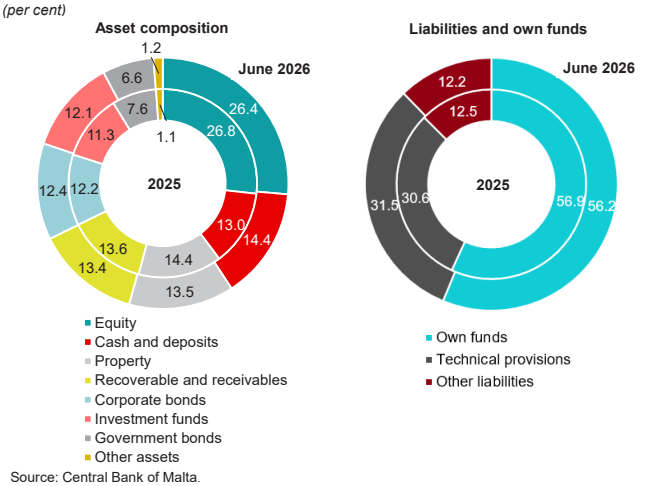
The non-life insurance sector recorded stronger balance sheet growth than the life insurance segment, with total assets increasing by 5.2% during the first half of 2026 and reaching the equivalent of 2.9% of GDP.[6]

[5] The expense ratio is defined as operating expenses, excluding claims, divided by net premia earned.
[6] The June 2026 data for one undertaking were not available by the reporting cut-off date. The latest available data for that undertaking, related to March 2026, were therefore used to ensure full sector coverage.

Asset composition

Growth was recorded across most asset classes. Direct equity holdings remained the largest asset class, accounting for more than one-quarter of total assets and increasing by 3.8% (see Chart 4.7). A substantial share of just over a fourth of these investments consisted of equity participations in affiliated insurance undertakings, reflecting intra-group ownership links within the sector.

Chart 4.7
NON-LIFE SECTOR BALANCE SHEET
(per cent)



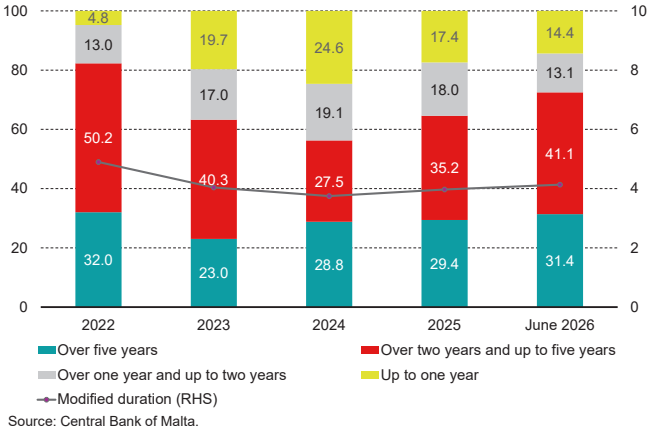
Source: Central Bank of Malta.

Fixed-income securities remained the second-largest asset class, accounting for 19.0% of overall assets. Developments within the bond portfolio, though, were mixed. Government bond holdings declined by 8.5%, mainly reflecting lower exposures to euro-area sovereign issuers. In contrast, corporate bond exposures increased by 7.0%, supported by higher holdings of debt securities issued by euro-area NFCs and by MFIs outside the euro area. NFC bond holdings were primarily concentrated in manufacturing, energy, and information and communication activities, with the latter recording the strongest growth.

The maturity profile of non-life insurers' bond portfolios shifted moderately towards longer-dated securities by June 2026 (see Chart 4.8). Bonds with residual maturities of between two and five years increased by 11.2%, and accounted for 41.1% of total bond holdings, thereby remaining the largest maturity bucket. Exposures to bonds maturing in over five years also rose slightly, reaching 31.4% of the bond portfolio. By contrast, holdings of debt securities maturing within one year, and those maturing between one and two years declined by 21.4% and 30.7%, respectively. These developments resulted in a marginal increase in modified duration to 4.1%, indicating a slight rise in the portfolio's sensitivity to interest rate movements. Higher yields were also recorded across all maturity buckets.

The credit quality of non-life insurers' bond portfolios remained broadly sound during the first half of 2026. High and medium-rated securities continued to represent the majority of holdings, accounting for around 73% of the portfolio in June 2026. Although the share of high-rated securities declined slightly, this was more than offset by an increase in medium-rated exposures. At the same time, holdings of sub-investment-grade debt contracted, reducing their share of the portfolio to 8.8%. Overall, these developments point to a modest improvement in the portfolio's credit profile.

Chart 4.8
NON-LIFE – MATURITY STRUCTURE AND MODIFIED DURATION OF DEBT SECURITIES PORTFOLIO
(per cent of total bond holdings; per cent)



Source: Central Bank of Malta.

Credit quality remained particularly strong within the sovereign bond portfolio, with more than 97% of holdings rated either high or medium-investment grade. The rating distribution of corporate bonds was more mixed. Medium-rated securities represented the largest category, while lower-rated and sub-investment-grade instruments collectively accounted for around 41% of corporate bond holdings.

Cash and deposits increased by 16.3%, making them the third-largest asset class held by the non-life sector. Property holdings remained broadly stable, declining marginally by 0.7%, with property held for own use continuing to account for just over half of the sector's property portfolio. Recoverables and receivables rose by 3.6%, reflecting higher amounts due from policyholders, intermediaries and reinsurers. Investment funds' holdings increased by 12.5%, supported by broad-based growth across all regions, particularly euro-area equity funds.

Liabilities and own funds

Technical provisions increased by 8.5%, accounting for 31.5% of the balance sheet by June 2026, while other liabilities rose by 2.5% to 12.2% of the balance sheet (see Chart 4.7). Nevertheless, the excess of assets over liabilities remained the largest balance-sheet component, increasing by 4.1% and representing more than half of total assets. This surplus is broadly related to, but does not necessarily correspond exactly to, eligible own funds calculated under the Solvency II framework.

Gross written premia and claims

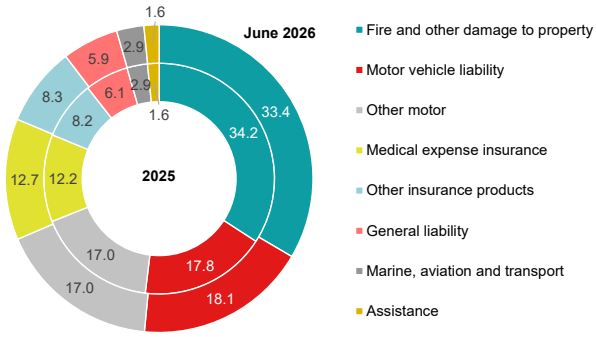
GWP in the non-life insurance sector increased by 2.8%, driven primarily by the health insurance segment, where premia rose by 6.9% and accounted for almost 13% of the total GWP (see Chart 4.9). Motor and property insurance remained the principal lines of business, collectively representing more than two-thirds of total premia. Motor insurance premia increased by 3.7%, while activity within the property segment remained broadly stable.[7]

The increase in GWP was driven entirely by domestic activity, as underwriting abroad contracted marginally. Nevertheless, foreign business remained significant, accounting for 27.4% of overall premia. Such activity remained concentrated among a small number of undertakings and was predominantly written in euro-area markets. Property insurance generated more than 65% of premia written outside Malta, indicating concentration across both undertakings and lines of business.

Gross claims incurred increased by 11.9%, substantially outpacing premium growth. The increase was broad-based across most lines of business, but was driven mainly by property insurance, followed by miscellaneous financial loss and motor vehicle liability business. Higher property claims partly reflected several loss events during the period, including Storm Harry in January and a fireworks factory explosion in June.

Reinsurance continued to play a central role in non-life insurers' risk management strategies, with 39.2% of GWP ceded to reinsurers. Dependence on reinsurance was especially prominent in the property line of business, where more than three-quarters of written business

Chart 4.9
GROSS WRITTEN PREMIUM OF THE DOMESTIC NON-LIFE INSURANCE SECTOR BY LINE OF BUSINESS
(per cent)

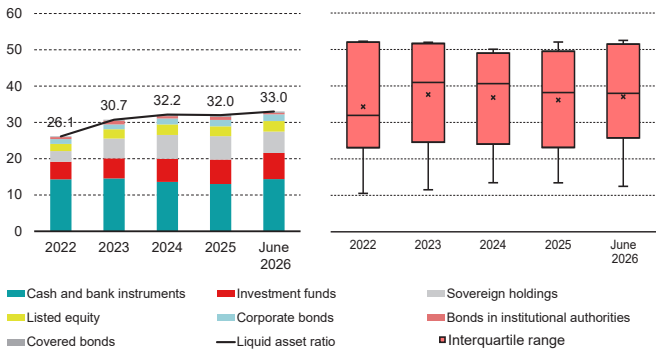


Source: Central Bank of Malta.
Note: Solvency II Reporting. Other insurance products include workers' compensation, income protection, miscellaneous, other life insurance and profit participation, IL and UL insurance.

[7] Motor vehicle liability insurance covers liabilities to third parties from accidents, including bodily injury and property damage. Other motor insurance covers damage to or loss of the insured vehicle but does not cover third-party liabilities.

was reinsured. While this reduced net exposure to large losses, it also left underwriting capacity and profitability more sensitive to changes in reinsurance pricing, availability and counterparty performance.

Chart 4.10
LIQUID ASSETS RATIO OF THE NON-LIFE INSURANCE SECTOR
(per cent)



Source: Central Bank of Malta.
Note: The left panel shows the composition of liquid assets; the right shows the distribution of the indicator, where the box, horizontal line, and × denote the interquartile range, median and unweighted mean, respectively.

Liquidity and capital

The liquid assets ratio increased to 33.0% by June 2026, reflecting an improvement in the sector's overall liquidity position. Higher holdings of cash and investment funds were the main contributors to the increase in liquid assets (see Chart 4.10). Significant differences nevertheless persisted across insurers, reflecting heterogeneity in asset allocation, business models and funding structures. While most undertakings maintained liquidity ratios above the euro area median, some continued to fall below this level, highlighting the importance of monitoring firm-specific liquidity positions.[8]

The non-life insurance sector remained strongly capitalised, with the aggregate SCR coverage ratio standing at 231.6% as at June 2026, despite a decline of 6.9 percentage points from end-2025. The decrease reflected stronger growth in the SCR than in eligible own funds. Solvency positions varied across undertakings, but all insurers remained comfortably above the regulatory minimum, with firm-level ratios ranging from 191.2% to 292.5%. The quality of eligible own funds also remained high, with capital consisting predominantly of Tier 1 own funds.

Profitability

The non-life insurance sector remained profitable during the first half of 2026, with profit before tax increasing by 8.1% and pre-tax ROA standing at 12.1%. Profitability nevertheless varied across insurers, with firm-level pre-tax ROA ranging from 2.9% to 17.9%. The improvement in overall profitability was driven by stronger investment performance, with investment returns increasing by 44.8% and contributing to a 48.4% rise in the net financial result.

This increase was partly offset by a weaker underwriting performance. Underwriting profitability deteriorated moderately, as insurance service expenses increased at a faster pace than insurance revenue, largely reflecting the rise in claims incurred discussed earlier. The increase in claims-related expenses was only partially offset by a decline in net expenses from reinsurance contracts, primarily reflecting a larger amount recoverable from reinsurers. As a result, the underwriting result declined by 2.6%.

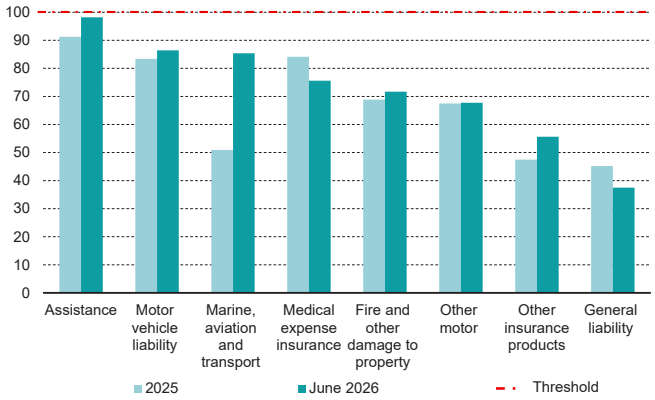
The weaker underwriting performance was also reflected in the combined ratio, which increased by 1.6 percentage points to 73.2%, indicating that claims and expenses accounted for a larger share of premia earned. The increase was driven mainly by developments in the marine, aviation and transport, and motor vehicle liability segments (see Chart 4.11). Nevertheless, the ratio remained comfortably below the 100% threshold, indicating that the sector continued to generate a technical profit from its underwriting activities.

[8] See the EIOPA Insurance Risk Dashboard, July 2026.

4.1.3 Risk outlook

Both the life and non-life insurance sectors entered the second half of 2026 with sound capital positions and continued balance-sheet growth. Nevertheless, the outlook remains uncertain amid persistent geopolitical tensions, volatile commodity prices and an elevated risk of abrupt corrections in financial markets, including in market segments with relatively high valuations. In particular, uncertainty surrounding global energy markets remained elevated, increasing the risk of renewed inflationary pressures and adverse second-round effects. More persistent inflation could raise claims and operating costs, weaken household demand for insurance and savings products, and tighten financial conditions. Financial market volatility could also weigh on insurers' investment performance and, if sufficiently severe, reduce their capital headroom.

Chart 4.11
NET COMBINED RATIO BY LINE OF BUSINESS
(per cent)



Source: Central Bank of Malta.
Note: Solvency II reporting. Other products include income protection, miscellaneous financial loss and workers' compensation insurance. Bars are ranked by June 2026 net combined ratio, from highest to lowest.

Risks differ across the two insurance segments. For life insurers, premium growth was supported primarily by a new guaranteed savings product, while premia from 'insurance with profit participation' and IL and UL business declined. Demand could therefore weaken if uncertainty surrounding household incomes, interest rates and financial market performance persists. Life insurers also remain exposed to movements in interest rates and credit spreads, through their fixed-income portfolios. While higher reinvestment yields may support returns on new investments, further increases in market yields could reduce the value of existing bond holdings. The net effect on capital and profitability would depend on the accounting and regulatory treatment of these assets. The increase in lower-rated debt and the recent deterioration in net financial result warrant continued monitoring.

For non-life insurers, the principal risk arises from claims outpacing premia, particularly if recent increases in claims frequency were to become a persistent feature. Although underwriting remained profitable, sustained claims inflation or further catastrophe-related losses could place additional pressure on margins. Extensive reinsurance coverage limits insurers' net exposure to large losses but also increases sensitivity to changes in reinsurance pricing and capacity, and to reinsurer counterparty risk, particularly in the property business. These risks are more pronounced given the concentration of foreign property underwriting among a small number of undertakings.

Operational and cyber risks also remain important across both segments. The emergence of increasingly capable frontier AI models may facilitate more sophisticated and scalable cyber-attacks, exposing insurers to potential business disruption, data losses, higher operating costs and cyber-underwriting losses. Reliance on external information and communications technology and other critical service providers further reinforces the need for effective third-party risk management and business-continuity planning. Regulatory changes and the transition towards more climate-resilient business models may create adjustment costs. Continued investment in operational resilience and effective risk management will therefore remain important in preserving the sector's capacity to absorb future shocks.

Private credit exposure in the domestically relevant insurance companies

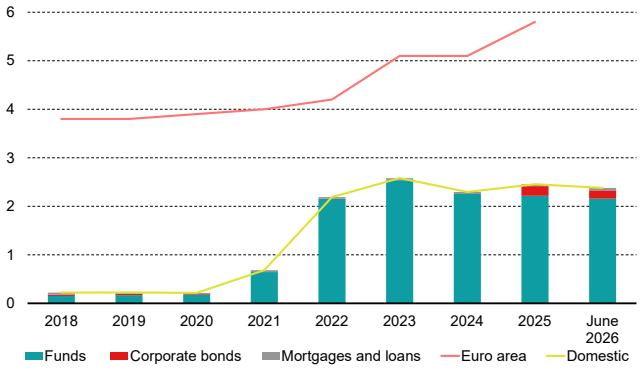
Private credit generally refers to financing provided outside the traditional banking system and public debt markets. Globally, this form of financing has expanded as businesses seek alternative sources of funding and institutional investors pursue higher returns and greater portfolio diversification. For insurers, private credit may offer a liquidity premium and broaden exposure beyond traditional fixed-income securities. However, it can also entail heightened credit and liquidity risks, less frequent and potentially less transparent valuations, and greater complexity than publicly-traded instruments. These features may make exposures more difficult to assess and monitor, particularly during periods of market stress. Moreover, the absence of a universally accepted definition complicates comparisons across jurisdictions and institutions.

Against this background, the European Insurance and Occupational Pensions Authority (EIOPA) examined insurers' private credit exposures in its December 2025 *Financial Stability Report* using a broad classification based on Solvency II reporting.[9] Under this approach, private credit includes selected non-listed or non-tradable debt instruments, mortgages and loans, structured notes and collateralised credit securities subject to credit risk, as well as relevant indirect holdings through investment funds.[10] Lending to banks and intra-group transactions are excluded. Consequently, investments that otherwise exhibit characteristics of private credit, such as loans or non-listed corporate bonds, are not included where the counterparty is a bank or another entity within the same group.

Using this definition, private credit exposures held by European insurers increased from 3.9% of total assets in Q4 2016 to 5.8% in Q2 2025, with the most significant increase taking place since 2023. In absolute terms, related exposures rose by around 80% over the period assessed, underscoring the growing importance of private credit.

Domestically relevant insurers followed a similar trajectory, with exposures increasing more noticeably from 2022 onwards (see Chart 4.12). Following a period of very limited exposures between 2018 and 2020, the share of private credit increased steadily, reaching 2.4% by June 2026, while remaining below the European average. Exposures were concentrated in the life insurance sector, where private credit represented 2.7% of total assets, compared with 0.8% for non-life insurers.

Chart 4.12
PRIVATE CREDIT EXPOSURES AND COMPOSITION OF DOMESTIC INSURERS' PORTFOLIOS
(per cent of total assets)



Sources: EIOPA; Central Bank of Malta.
Note: Euro area data for 2025 refer to June 2025, the latest available observation, while domestic insurers' data refer to December 2025.

[9] European Insurance and Occupational Pensions Authority (EIOPA), (2025), Financial Stability Report 2025, Topical Focus: *Private Credit Investments by EEA Insurers and IORPs: Exposures, Trends and Vulnerabilities*.

[10] Following EIOPA's methodology, private credit comprises selected direct and indirect credit exposures identified through Solvency II CIC classifications. Direct exposures include non-listed or non-tradable corporate debt (CIC 21, 22, 25, 28 and 29), mortgages and loans (CIC 8), structured notes subject to credit risk (CIC 54), and collateralised securities subject to credit risk (CIC 64). Indirect exposures include relevant holdings through investment funds (CIC 4), including alternative investment funds (CIC 46), private equity funds (CIC 47) and infrastructure funds (CIC 48).

The composition of domestic insurers' exposures also differed from the broader European pattern. Whereas mortgages and loans constituted the largest component of private credit exposures across European insurers, domestic exposures were held predominantly through investment funds, particularly infrastructure and alternative investment funds. This comparatively limited contribution from direct loans partly reflected the exclusion of intra-group lending, which represented a significant share of domestic loan exposures.

Private credit exposures varied considerably across insurers. While some insurers reported no private credit exposure, others exhibited higher concentrations, with the highest share standing at 4.7% of total assets. Although the sector-wide exposure remains contained, firm-level concentrations may create vulnerabilities through credit losses, illiquidity and valuation uncertainty. Indirect exposures through investment funds may also increase interconnectedness with the broader non-bank financial sector and make the ultimate counterparties and underlying risks more difficult to identify. These developments highlight the importance of continued monitoring, particularly in relation to concentrated exposures, valuation practices and the underlying composition of investment-fund holdings.

BOX 4: HOW SIGNIFICANT IS CATASTROPHE RISK FOR MALTESE NON-LIFE INSURERS' SOLVENCY CAPITAL REQUIREMENT?[1]

Introduction

Catastrophe events are typically low-frequency but high-impact events that can give rise to severe and concentrated losses, posing significant risks to the financial resilience of insurance undertakings. The Solvency II framework therefore requires insurers to hold capital against catastrophe exposures as part of the SCR. This helps to ensure that sufficient financial resources are available to absorb unexpected losses and continue meeting policyholder obligations following a major catastrophic event.[2] Catastrophe risk has also attracted increasing attention at European level, reflecting concerns about the financial impact of natural catastrophe events, insurance protection gaps and the resilience of the insurance sector to severe losses.

This article examines the significance of catastrophe risk within the SCR of domestically relevant non-life insurers over the period 2016–2025.[3] To establish the regulatory context for the subsequent analysis, it first explains how catastrophe risk enters the SCR calculation. It then assesses the contribution of catastrophe risk to insurers' capital requirements and its evolution over time. The analysis focuses on changes in the composition of catastrophe risk across categories and perils, the geographical distribution of underlying exposures, including exposures located outside Malta, and the effects of risk mitigation and diversification. Particular attention is paid to observed gaps in the Malta-specific calibration of the Solvency II Standard Formula at present, and their implications for the interpretation of reported natural catastrophe capital requirements. Consequently, the findings should be interpreted in the context of the existing calibration and should not be taken as a comprehensive assessment of Malta's underlying catastrophe risk profile.

Catastrophe risk under the Solvency II Standard Formula

Under Solvency II, insurers are required to hold eligible own funds to cover the SCR, which is calibrated to a 99.5% confidence level over a one-year horizon. Under the standard formula, the SCR covers a range of risks, including non-life underwriting risk. This module comprises premium and reserve risk, lapse risk, and catastrophe risk, with the latter capturing potential losses arising from extreme or exceptional events.

The relative importance of catastrophe risk within the total SCR increased over the period under review, rising from around 10% in 2016 to more than 13% in 2025. However, the contribution of catastrophe risk to total SCR varied considerably across undertakings, ranging from 4% to 19% in 2025, reflecting differences in underwriting profiles and risk exposures.

Unlike claims arising from more typical loss experience, catastrophe risks are calibrated using low-frequency, high-severity scenarios that may generate exceptionally large and concentrated losses. They may arise from a natural catastrophe affecting numerous policyholders simultaneously or from a major man-made event, such as a large-scale marine or aviation accident, a significant fire, or an event generating multiple motor or liability claims.

Catastrophe risk comprises three broad categories of exposures: natural catastrophe risk, man-made catastrophe risk, and other non-life catastrophe risk. Natural and man-made catastrophe risks are further subdivided into individual perils. Natural catastrophe risk encompasses windstorm,

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[1] Written by Ms Luana Camilleri, Senior Expert within the Financial Stability Surveillance and Risk Assessment Department. The author would like to thank Mr Andrew Spiteri, Ms Wendy Zammit, Mr Alan Cassar, Deputy Governors Oliver Bonello and Rita Schembri, and Governor Alexander Demarco for their valuable suggestions.

[2] Directive 2009/138/EC of the European Parliament and of the Council of 25 November 2009 on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II) (recast) (Text with EEA relevance).

[3] Argus Insurance (Europe) Limited is included in the sample from 2024 onwards.

earthquake, flood, hail and subsidence, while man-made catastrophe risk comprises motor vehicle liability, marine, aviation, fire, general liability, and credit and suretyship risks.[4,5]

Other non-life catastrophe risk is reported as a separate category and primarily relates to certain marine, transport, casualty, and miscellaneous financial loss exposures not captured within the dedicated natural and man-made catastrophe risk sub-modules.

For the natural and man-made catastrophe perils considered here, the calculation starts with the undertaking's underlying exposures. The relevant parameters or stress scenarios prescribed under the Solvency II standard formula are then applied to determine the capital requirement before risk mitigation. For natural catastrophe risk, the calculation relies on country-specific factors and prescribed scenarios intended to reflect the severity of natural hazards across jurisdictions. These calibrations are periodically reviewed by EIOPA to reflect available evidence and modelling developments.

The coverage of Malta-specific factors in the natural catastrophe calibration is relevant to interpreting the results. Earthquake is currently the only natural catastrophe peril with a Malta-specific country factor in that calibration. Although flood risk for Malta was considered during EIOPA's 2023–2024 reassessment of natural catastrophe perils and country factors, no Malta-specific flood factor was proposed owing to the absence of a suitable model, with Malta identified for reconsideration in a future review.[6,7] Hail, windstorm and subsidence were not assessed for Malta and therefore remain outside the Malta-specific calibration of the standard formula. The absence of country-specific factors does not imply that these hazards are absent or immaterial, but rather that the current standard formula does not quantify the associated capital requirements for exposures located in Malta.

Once the pre-mitigation capital requirements are estimated, recognised risk-mitigation techniques, principally reinsurance, are applied to determine the corresponding post-mitigation capital requirements. These are then aggregated using the prescribed Solvency II methodology, which recognises diversification effects arising from the fact that different catastrophe risks are unlikely to materialise simultaneously at their stressed levels.

Composition of catastrophe risk by category and peril

In 2025, the aggregate pre-mitigation peril-level capital requirements of domestically relevant undertakings amounted to approximately €1.2 billion for man-made catastrophe risk and €464 million for natural catastrophe risk. Following reinsurance, the corresponding requirements declined to around €18.9 million and €14 million, respectively. An additional €2.2 million relates to other non-life catastrophe risk. Post-mitigation capital requirements were therefore equivalent to approximately 1.5% and 3.0% of the corresponding pre-mitigation requirements for man-made and natural catastrophe risk, respectively.

The impact of risk mitigation varied across catastrophe perils. Fire and earthquake recorded the largest proportionate reductions, consistent with the extensive use of reinsurance arrangements for

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4 Subsidence refers to damage caused by the sinking or settlement of the ground beneath a property. Liability catastrophe risk captures the possibility that a single event could give rise to a large number of third-party compensation claims, resulting in a significant accumulation of losses for insurers.

5 Wildfire is not currently included as a separate natural catastrophe peril under the Solvency II standard formula. While EIOPA is considering its potential inclusion, fire damage is already captured under the fire risk sub-module of the man-made catastrophe risk module, giving rise to potential double-counting concerns.

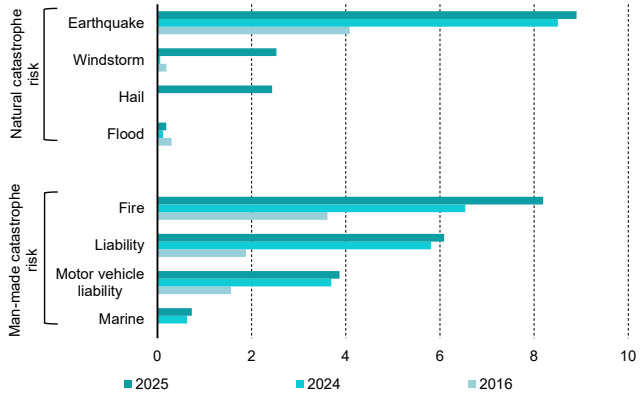
6 European Insurance and Occupational Pensions Authority (EIOPA), (2025, January 30), *Opinion on the 2023/2024 Reassessment of the Nat Cat Standard Formula*.

7 Recent experience illustrates the potential relevance of flood-related losses in Malta. Claims associated with Storm Harry in 2026 amounted to around €12 million, with flooding and other water damage accounting for approximately two-thirds of the total claims cost. While a single event is insufficient to support a regulatory calibration, it highlights the value of systematically collecting granular claims and exposure data to inform future Malta-specific flood-risk assessment and modelling.

these risks. Among the main perils, liability risk remained comparatively less affected by risk mitigation.

After risk mitigation but before peril-level diversification, man-made catastrophe risk remained the largest component throughout the period under review, driven by fire and liability risk (see Chart 4a). While the capital requirement for liability risk rose only marginally between 2024 and 2025, the increase in fire risk reinforced the contribution of man-made catastrophe risk.

Chart 4a
AGGREGATE CATASTROPHE RISK BY PERIL (2016, 2024 and 2025)
(EUR millions)



Source: Central Bank of Malta.
Note: Figures represent catastrophe capital requirements after recognised risk-mitigation arrangements and before the recognition of diversification benefits.

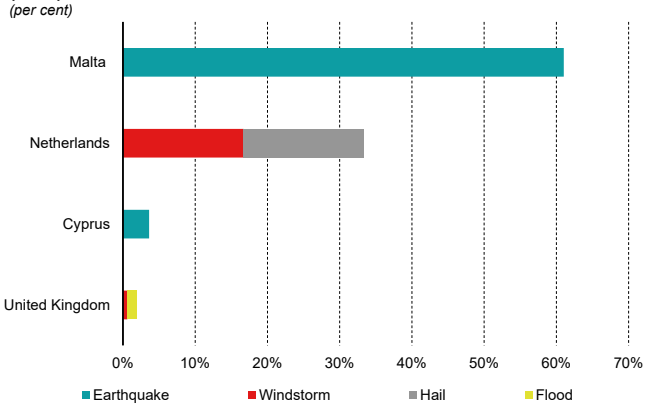
The capital requirement for natural catastrophe risk increased markedly in 2025, driven primarily by higher capital requirements for windstorm and hail. However, these increases were associated with a limited set of foreign exposures and did not reflect a broad-based increase across the insurers analysed. Despite these developments, earthquake remained the largest natural catastrophe peril by capital requirement and was broadly stable relative to the previous year. Its continued prominence is consistent with the standard formula calibration applicable to the reporting period, under which earthquake is the only natural catastrophe peril subject to a Malta-specific country factor. This should not be interpreted as evidence of dedicated earthquake products but rather reflects the insurers' exposure to the earthquake scenario prescribed under the standard formula.

Geographical distribution of natural catastrophe risk

Although the analysis covers domestically relevant insurers, their underlying exposures are not confined to Malta. Since natural catastrophe scenarios are calibrated according to the location of the insured risk, the geographical distribution of these exposures provides important context for interpreting the reported capital requirements (see Chart 4b).

At aggregate level, exposures located in Malta accounted for just under 60% of post-mitigation natural catastrophe capital

Chart 4b
GEOGRAPHICAL DISTRIBUTION OF NATURAL CATASTROPHE RISK (2025)
(per cent)



Source: Central Bank of Malta.
Note: Figures represent catastrophe capital requirements after recognised risk-mitigation arrangements and before the recognition of diversification benefits.

requirements in 2025, making Malta the largest geographical contributor. The remaining requirements arose from risks located in foreign jurisdictions, with the Netherlands representing the largest foreign component. Malta's predominance reflects the orientation of insurers' portfolios towards domestic risks, while the composition of its natural catastrophe capital requirement is also influenced by earthquake being the only peril with a Malta-specific country factor in the calibration examined. These shares relate to calculated capital requirements, rather than shares of total insured exposure. A comparable geographical breakdown is not available for man-made catastrophe risk.

At peril level, capital requirements for windstorm risk were primarily associated with exposures in the Netherlands, with a smaller share relating to the United Kingdom, while those for hail risk related to exposures in the Netherlands. Capital requirements for earthquake risk were primarily linked to exposures in Malta and, to a lesser extent, Cyprus, while those for flood risk were driven by exposures in the United Kingdom.

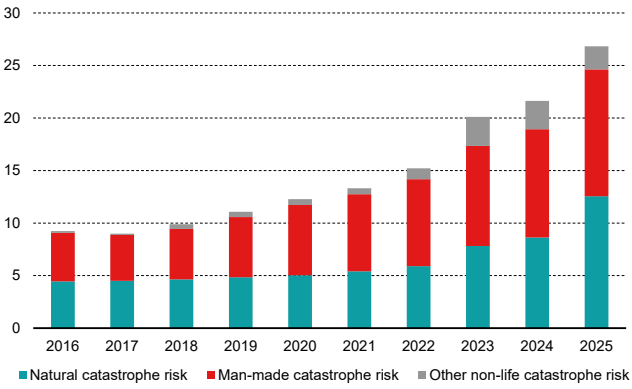
Diversification effects

Diversification reduces catastrophe-related capital requirements. In 2025, the sum of post-mitigation peril-level capital requirements for man-made, natural, and other non-life catastrophe risk, before diversification, amounted to approximately €35.1 million. After recognising diversification within and across the catastrophe risk sub-modules, the overall capital requirement for non-life catastrophe risk declined to €20.5 million, representing a reduction of around 41.6%. This percentage reduction remained broadly stable throughout the period under review.

This reduction can be assessed in two stages. First, diversification among the individual perils within the natural and man-made catastrophe risk sub-modules reduces the combined capital requirement by approximately €8.3 million, to €26.8 million. The diversification benefit is greater for man-made catastrophe risk than for natural catastrophe risk. Consequently, following peril-level diversification, natural catastrophe risk becomes marginally larger, with a capital requirement of approximately €12.6 million, compared with €12.1 million for man-made catastrophe risk (see Chart 4c). Other non-life catastrophe risk remains comparatively small, at €2.2 million, and therefore does not materially affect the overall composition of catastrophe risk.

Second, diversification across natural, man-made and other non-life catastrophe risks at undertaking level achieves a further reduction of approximately €6.3 million, bringing the overall capital requirement for the non-life catastrophe risk sub-module to €20.5 million.

Chart 4c
COMPOSITION OF AGGREGATE CATASTROPHE RISK BY TYPE
(EUR millions)



Source: Central Bank of Malta.
Note: Figures reflect capital requirements after the application of risk mitigation techniques and diversification within each catastrophe risk category, but before diversification across catastrophe risk categories.

Conclusion

The analysis shows that catastrophe risk is becoming an increasingly important component of non-life insurers' capital requirements within the context of the current Solvency II standard-formula calibration. For exposures located in Malta, earthquake is currently the only natural catastrophe peril subject to a country-specific factor. Consequently, the prominence of earthquake within the results reflects the risks explicitly captured by the framework and should not be interpreted as a comprehensive assessment of Malta's natural catastrophe risk profile.

The findings therefore point to a gap between the risks captured by regulatory capital requirements and the broader range of natural catastrophe risks that may be relevant to the Maltese insurance market. Addressing the significance of this gap would benefit from further development of the underlying exposure and claims data, together with suitable hazard assessments and catastrophe models. Continued engagement between national supervisory authorities and EIOPA would support future assessments of whether additional Malta-specific calibrations are warranted and whether the prudential framework adequately reflects catastrophe risks relevant to the Maltese market. It should be noted, however, that the absence of a dedicated country factor does not, by itself, establish that insurers' overall capital is inadequate.

The analysis also highlights the substantial but distinct roles of risk-transfer arrangements and diversification in determining the final catastrophe capital requirement reflected in insurers' solvency positions. Reinsurance reduces insurers' direct exposure to catastrophe losses by transferring part of the risk to reinsurers, while diversification lowers aggregate capital requirements by recognising that different catastrophe risks are unlikely to materialise simultaneously at their stressed levels. Together, these effects materially reduce the capital impact of catastrophe exposures. However, reliance on reinsurance also creates counterparty exposures that require appropriate risk management.

From a prudential and financial stability perspective, the assessment of catastrophe risk should extend beyond the resulting capital requirement and consider the broader range of natural hazards potentially relevant to Malta, the nature and geographical concentration of underlying exposures, and the distribution of these exposures across insurers. Continued monitoring of these dimensions remains important for assessing the sector's resilience to severe catastrophe events and identifying emerging changes in the nature, concentration, and transmission of catastrophe risk over time.

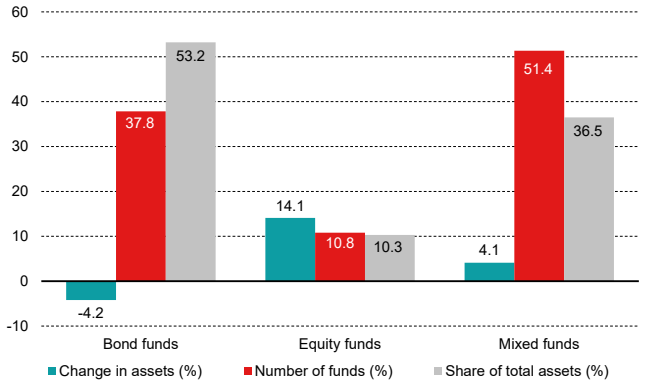
4.2 Domestically relevant investment funds

At the end of June 2026, 37 subfunds were identified as domestically relevant, one fewer than that reported in the *FSR 2025*.[11] Their combined assets grew marginally by 0.4% to €1.73 billion, equivalent to 6.8% of GDP. Exposures to equities and investment fund units rose, reflecting both increased portfolio allocations and a favourable market performance, while bond holdings declined. Maltese households remained the largest investor group and increased their net asset value (NAV). Overall, resilience continued to be supported by very low leverage and strong reported redemption coverage. Although the HQLA ratio declined, largely reflected changes in portfolio composition, it remained at a relatively strong level.

Developments by fund strategy

Investment funds are classified according to their predominant investment strategy. Mixed funds accounted for just over half of the number of domestically relevant sub-funds at the end of June 2026. However, in terms of assets under management (AUM), bond funds remained the dominant category, accounting for 53.2% of the sector's assets, compared with mixed funds at 36.5% and equity funds at 10.3% (see Chart 4.13).

Chart 4.13
DOMESTICALLY RELEVANT SUB-FUNDS BY MAIN STRATEGY
(per cent)



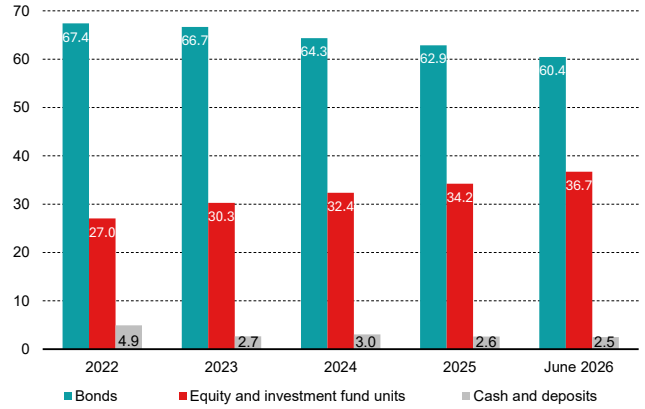
Source: Central Bank of Malta.
Note: Teal indicates the change in assets compared with 2025. Red represents the share by number of funds, while grey denotes the share of total assets.

4.2.1 Asset composition and investment strategies

Holdings of equities and investment funds' units increased by 11.7%, reflecting both higher portfolio allocations and favourable market performance. Consequently, their share in total assets rose by 2.5 percentage points to 36.7% (see Chart 4.14). The increased allocation raised the funds' sensitivity to equity-market corrections and broader changes in investor risk sentiment, in an environment of heightened volatility and geopolitical uncertainty.

By contrast, the share of debt securities declined by 2.4 percentage points, although these remained the dominant asset class, accounting for 60.4% of total assets. As a result, developments affecting bond markets are likely to have a proportionately larger impact on the domestic funds sector. Cash and deposits remained broadly stable at 2.5% of the overall portfolio and continued to stand below their historical levels following a gradual decline in recent years. While this indicates that only a small share of assets was held in cash, the overall liquidity position

Chart 4.14
ASSETS COMPOSITION OF THE DOMESTICALLY RELEVANT INVESTMENT FUNDS
(per cent)



Source: Central Bank of Malta.

[11] The BOV Capital Guaranteed Fund 2026 matured in April 2026 and was therefore discontinued in accordance with its prospectus.

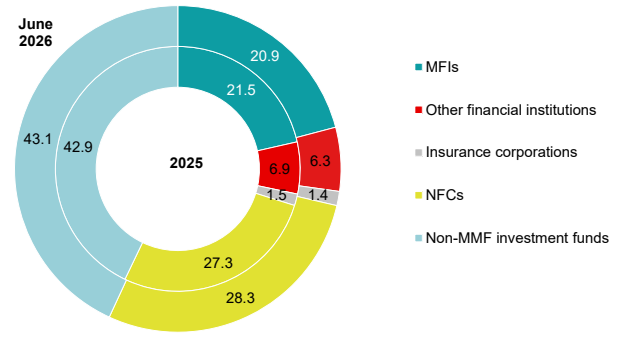
also depends on the market liquidity of the remaining assets (see Section 4.2.3). Other assets remained marginal at 0.4%.

Equities and participations in investment funds

The increase in the sector's holdings of equities and investment fund units was driven primarily by higher direct equity exposures. Holdings of equities issued by NFCs increased by 11.2%, making them a key contributor to the overall growth in equities and investment funds, accounting for just above 28% of the overall increase in this asset category. Although holdings of bank equities rose by 4.5%, their share fell to about 21%, reflecting stronger growth in other components (see Chart 4.15). By contrast, holdings of equities issued by other financial institutions and insurance corporations declined slightly.

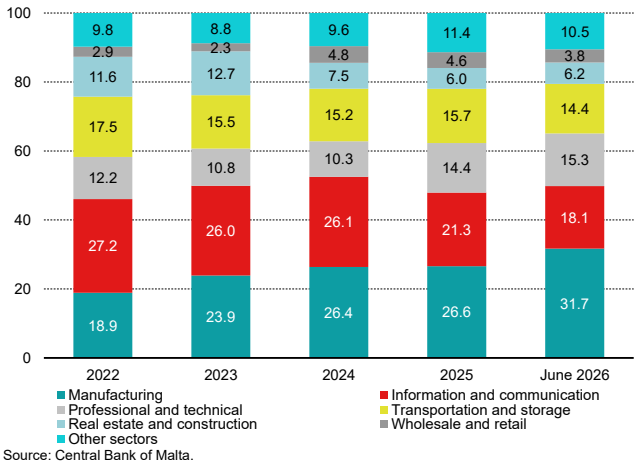
Holdings of investment fund units also increased substantially in absolute terms, although their share of the combined category remained broadly unchanged. Exchange-traded funds (ETFs) accounted for 62.9% of investment funds' unit holdings, representing a slight increase from December 2025. Most of the ETFs were held by mixed funds, with exposures concentrated mainly in broad market indices and complemented by allocations to sector-specific and fixed-income ETFs. Their prominence may reflect the diversification, tradability, cost and transparency benefits commonly associated with these instruments. The continued importance of index-tracking ETFs is also consistent with the broader shift towards passive investment strategies observed internationally.[12]

Chart 4.15
EQUITY HOLDINGS COMPOSITION OF DOMESTICALLY RELEVANT INVESTMENT FUNDS
(per cent)



Source: Central Bank of Malta.
Note: Other financial institutions includes other financial intermediaries (OFIs), financial auxiliaries and captive financial institutions and money lenders.

Chart 4.16
SECTORIAL DISTRIBUTION OF NFC HOLDINGS



Source: Central Bank of Malta.

Equity exposures increased across all geographical categories during the first half of 2026. The euro area accounted for the largest increase in absolute terms and remained the largest geographical allocation, accounting for 44.9% of total equity holdings. US equities registered the strongest percentage growth and the largest increase in portfolio share, rising to 14.1%. Domestic holdings also rose, although their share declined to 35.9% as they grew more slowly than the overall equity portfolio. Exposures to the rest of the world increased only marginally, while emerging-market holdings grew more strongly but remained negligible.

NFC equity exposures remained moderately concentrated across economic sectors, with manufacturing accounting for almost a third of holdings (see Chart 4.16). This broad sector also includes

[12] See ECB (2024), "Passive investing and its impact on return co-movement, market concentration and liquidity in euro area equity markets", *Financial Stability Review*, November; and European Fund and Asset Management Association (2025), "The rise of active ETFs in Europe: A short overview".

the manufacturing of electronic components, computers and peripheral equipment. Information and communication represented the second-largest exposure accounting for around 18% of holdings. Within the latter sector, exposures were concentrated mainly in the wired telecommunications activities. As a result, these holdings may be sensitive to broader digitalisation trends, including shifts in demand for connectivity services, evolving technological requirements, infrastructure investment needs and competitive pressures within the telecommunications industry. Given the concentration of exposures, developments affecting these activities warrant continued monitoring. Overall, sectoral distribution of NFC equity holdings has remained broadly stable throughout the past five years.

Bond holdings

Bond holdings declined by 3.6% during the first half of 2026, driven by an 8.0% fall in sovereign bonds, whose share of the overall bond portfolio declined to 33.4% (see Chart 4.17). Holdings also declined across several non-sovereign bond categories. Bank bonds fell by 5.5%, while NFC bonds declined by a more modest 0.8%. As a result, the share of NFC bonds increased to 22.6% of overall bond holdings. Holdings of bonds issued by OFIs rose marginally by 0.9%, while units in bond funds increased sharply from a very low base and remained negligible. Overall, bonds issued by financial corporations accounted for 43.9% of bond holdings.

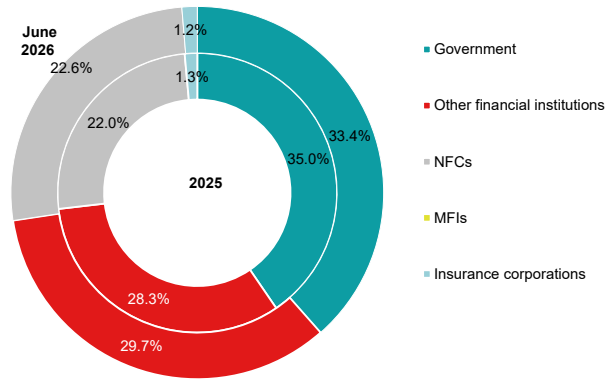
NFC bond exposures were concentrated in some economic sectors, with information and communication representing the largest exposure at 20.1%, followed by professional, scientific and technical activities at 18.9%. Together, these exposures indicate a notable concentration in knowledge-intensive and technology-related activities, warranting continued monitoring of sector-specific developments.

Despite this decline, the portfolio remained strongly domestically oriented. MGSs and Treasury bills accounted for nearly 77% of sovereign bond holdings, while domestic issuers represented 53.2% of the overall bond portfolio, broadly unchanged from December 2025. From a broader geographical perspective, bonds issued in other euro area countries represented the second-largest allocation, with their share increasing marginally to 21.4%, followed by issuers from the rest of the world at 13.6%. Exposures to the United States and emerging markets remained limited.

During the first half of 2026, the maturity profile of bond portfolios shifted towards shorter maturities. The share of long-dated bonds[13] declined by 4.3 percentage points but remained the largest component of bond portfolios, at 48.7% (see Chart 4.18). Meanwhile, the share of medium-term bonds increased to 41.9%, while short-term bonds rose to 9.5%. Consequently, the portfolio's estimated modified duration declined slightly to 5.3%. Overall, these developments suggest a modest reduction in the portfolio's sensitivity to changes in interest rates.

The credit quality of the bond portfolios improved modestly during the first half of the year, with the share of investment-grade fixed-income securities increasing by 4.8 percentage points to almost 64% of the bond holdings. Within

Chart 4.17
BOND HOLDINGS COMPOSITION OF DOMESTICALLY RELEVANT INVESTMENT FUNDS
(per cent)

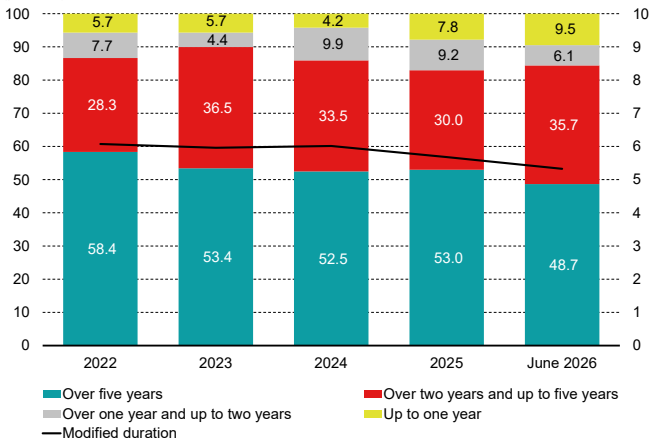


Source: Central Bank of Malta.
Note: Other financial institutions includes other OFIs, financial auxiliaries and CFIML.

[13] Short-dated bonds are defined as those with maturities of up to one year; medium-term bonds as those with maturities between one and five years; and long-term bonds as those with maturities exceeding five years.

this category, the shares of high and medium-rated bonds rose to 8.7% and to 39.4%, respectively, while that of lower-rated investment-grade securities declined to 15.7%. However, the share of speculative-grade securities edged up by 0.5 percentage points to 16.1%. Unrated bonds continued to represent a material share of the portfolio, at around 20%, although this was down from 25.5% in 2025. While unrated status does not necessarily imply weaker credit quality, the sizeable share of such securities limits the extent to which overall credit quality can be assessed solely based on external ratings. Overall, the shift towards high-rated investment-grade securities points to a moderate improvement in the portfolio's credit quality. Nevertheless, the concurrent increase in speculative-grade and the continued material exposure to unrated securities remain relevant.

Chart 4.18
OUTSTANDING MATURITY STRUCTURE AND MODIFIED DURATION
(per cent)



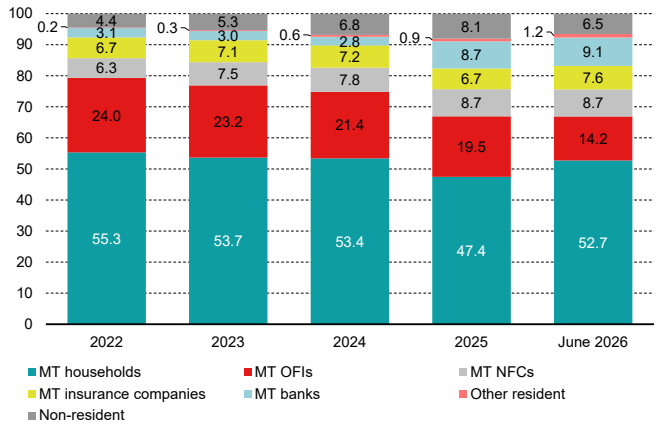
Source: Central Bank of Malta.

4.2.2 Investors

Maltese households remained the largest investors in domestically relevant sub-funds, increasing their share of NAV by 5.3 percentage points to 52.7% in June 2026 (see Chart 4.19). OFIs remained the second-largest investor group, accounting for 14.2% of NAV, notably lower than in December 2025. Insurance corporations also increased their share to 7.6%. By contrast, the shares held by NFCs and local domestic banks declined to 8.7% and 9.1%, respectively, while the share held by other residents remained marginal at 1.2%.

In line with the domestic relevance of these funds, the investor base remained predominantly domestic, with resident investors collectively accounting for 93.5% of NAV. Valuation losses could affect households' financial wealth, although the potential impact is largely mitigated by the relatively limited share of financial assets invested in these funds relative to households' substantial holdings of cash and deposits. In fact, holdings in these funds represented around 16% of households' financial assets. Furthermore, around half of the households' financial wealth is in cash and deposits providing further cushioning. Nevertheless, their prominence in the investor base increases the relevance of retail investor behaviour for fund liquidity, particularly if deteriorating market conditions or investment performance were to lead to more widespread redemption activity.

Chart 4.19
DOMESTIC INVESTMENT FUNDS' NAV BY COUNTERPART
(per cent)



Source: Central Bank of Malta.

Moreover, the participation of OFIs and insurance corporations provides a potential channel through which market stress affecting investment funds could be transmitted to other

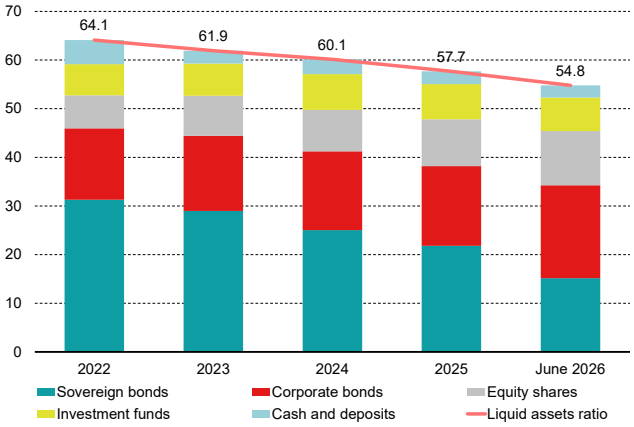
parts of the domestic financial system. The importance of these channels would, however, depend on the materiality of such exposures relative to the investors' overall balance sheets.

Foreign participation declined during the review period. The share held by euro area investors fell from 5.6% to 4.7% of NAV, while that of investors from the rest of the world declined from 2.5% to 1.8%. Consequently, the overall non-resident shares fell by 1.5 percentage points to 6.5%, further reinforcing the domestic orientation of the investor base.

4.2.3 Liquidity and leverage

The HQLA ratio declined by 2.9 percentage points during the first half of 2026 to 54.8% in June 2026 (see Chart 4.20). This mainly reflected the reduction in sovereign bond holdings, which generally carry higher liquidity weights under the applied methodology, together with the increased allocation of equities, which receive lower weights. Cash and deposits also retained a limited share of total assets. Although the ratio continued to indicate a substantial stock of liquid assets, its decline points to some moderation in the sector's aggregate liquidity buffer, albeit from a relatively strong level.

Chart 4.20
LIQUIDITY RATIO
(per cent)



Source: Central Bank of Malta.

The RCR, assessed against the most severe quarterly outflows observed since 2016, decreased slightly to 5.6 times from 6.1 in December 2025.[14] This decrease reflected both a reduction in HQLA and a notable increase in the estimated outflows. Nevertheless, aggregate liquid assets remained well above the estimated quarterly redemption requirement, indicating that redemption coverage remained robust. The aggregate ratio should, however, be considered alongside differences across individual sub-funds (see Special Feature B).

Leverage remained very low. The aggregate AUM-to-NAV ratio increased from 100.3% as at end 2025 to 100.6% by June 2026. This indicates limited reliance on borrowed funds at sector level, consistent with the regulatory framework, as most of these funds are licensed and supervised under the Undertakings for the Collective Investment in Transferable Securities (UCITS) Directive.[15]

4.2.4 Interconnectedness

Domestically relevant investment funds maintained direct links with other parts of the domestic financial system. On the assets side, holdings of bonds and equities issued by key domestic financial institutions accounted for 13.2% of total funds' assets in June 2026, marginally higher than in December 2025, with exposures to domestic banks representing the largest component. Investment funds also continued to support domestic market-based financing, holding around 8.1% of the outstanding value of corporate bonds listed on the MSE.

[14] The RCR is calculated as the ratio of HQLA to the estimated worst-case quarterly redemptions observed since 2016. Closed-ended funds are excluded from the analysis because their structure generally limits investors' ability to redeem their holdings.
[15] Article 83 of the UCITS Directive restricts borrowing by retail funds to up to 10% of their assets and only on a temporary basis (as found in Directive 2009/65/EC).

On the liability side, domestic financial institutions collectively remained an important investor group, accounting for 17.9% of NAV, with banks representing approximately half of these holdings.

While direct exposures appear contained at aggregate level, they may provide channels through which developments affecting investment funds could be transmitted to other parts of the domestic financial system and vice versa. Additional indirect links may arise where funds have ownership, management, branding or distribution arrangements with domestic banking groups. Such affiliations may give rise to reputational or operational interdependencies under stressed conditions, notwithstanding the separate legal status of the entities concerned. The relevance of these linkages depends on the scale of the respective exposures and the extent of common asset holdings.

4.2.5 Profitability

Aggregate operating profitability weakened during the first half of 2026 with the operating profit margin declining by 2.0 percentage points to 69.2%.[16] The deterioration was driven by a 2.2% fall in income, largely reflecting lower dividend income, while operating expenses increased by 4.7%. The rise in expenses was mainly driven by higher management and legal and professional fees and commission expenses. Despite this deterioration, the sector continued to report a positive aggregate operating result. If sustained, lower income and higher operating costs could weigh on fund performance and, indirectly, influence investor sentiment. Across fund categories, operating profitability improved slightly among bond funds, but declined within mixed funds and equity funds.

4.2.6 Risk outlook

Looking ahead, domestically relevant investment funds will remain influenced by global financial market developments, including geopolitical uncertainty, changing interest-rate expectations and shifts in investor risk sentiment. The increase in equity exposures has raised the sector's sensitivity to market movements, particularly in international market segments where valuations remain elevated, including segments associated with strong investor interest in AI-related themes. This could potentially raise the risk of a sharper repricing if macro-financial conditions deteriorate or if the gains from AI do not match the market's expectations. Bond portfolios also remain exposed to changes in yields and credit spreads, while higher financing and refinancing costs could weaken corporate credit quality. However, the shift towards shorter maturities and the decline in estimated modified duration have moderately reduced sensitivity to interest rate movements.

The sector enters the outlook period with very low leverage, substantial holdings of liquid assets and an improved credit quality profile within its bond portfolio. Despite a moderately lower HQLA ratio, liquidity remains relatively strong, while aggregate redemption coverage remained robust. Speculative-grade and unrated bonds continued to represent a material share of fixed-income portfolios. Under less favourable market conditions, individual sub-funds' resilience would depend, among other factors, on their liquidity profiles, redemption activity and ability to realise assets without material valuation effects. In addition, elevated asset valuations in international equity markets may increase the risk of abrupt price corrections and portfolio repricing should investor sentiment deteriorate.

Persistent concentration in domestic issuers and links with domestic financial institutions may limit diversification and provide channels through which market developments could be transmitted within the financial system. The predominance of households in the investor base further increases the relevance of retail investor behaviour. At the same time, as in other parts of the financial sector, operational dependencies on technology and increasing reliance on third-party service providers remain relevant from a resilience perspective as related disruptions could have implications for business continuity, investor confidence and market functioning. Overall, while the sector remains exposed to market, liquidity and concentration risks, these are mitigated at aggregate level by its low leverage, substantial liquidity holdings and strong reported redemption coverage.

[16] The margin is calculated as the difference between total income and expenses, excluding other income, other expenses, and capital gains or losses, expressed as a percentage of total income.

BOX 5: STABLECOIN ACTIVITY AMONG LICENSED CRYPTO-ASSET SERVICE PROVIDERS[1]

The Markets in Crypto-Assets Regulation (MiCA) provides a harmonised European Union (EU) framework for issuers of asset-referenced tokens and e-money tokens, the two categories generally associated with stablecoins, as well as for CASPs. The provisions relating to asset-referenced and e-money tokens have applied since 30 June 2024, while the broader MiCA framework, including the provisions governing CASPs, has applied since 30 December 2024.[2] Stablecoins are crypto-assets designed to maintain a stable value by referencing one or more official currencies or other assets. At end-June 2026, stablecoins in circulation worldwide were valued at around USD 311 billion.[3] Tokens referenced to the US dollar accounted for 99.5% of the total, while euro-referenced tokens accounted for only 0.2%. The two largest tokens, Tether (USDT) and USD Coin (USDC), together accounted for around 83% of the global market. This high degree of concentration means that the de-pegging of a major token or disruption affecting one of the leading issuers could have broader effects across the stablecoin market. Within crypto-asset markets, stablecoins serve mainly as a bridge between trades and a temporary store of value, and they provide a significant share of the liquidity in decentralised finance applications.[4] As issuers back their tokens with reserve assets such as bank deposits and government bonds, large redemptions may give rise to asset sales and could transmit stress to parts of the banking system and sovereign bond markets.[5]

This box draws from the regulatory returns submitted by CASPs licensed by the MFSA to assess the materiality, currency composition and concentration of reported stablecoin activity within Malta's licensed CASP population, using end June 2026 as the reference date. After providing context on the size, business models and overall client base of the sector, the box examines the importance of stablecoins within crypto-assets reported as held for sale, their currency composition, their concentration across reporting entities and how stablecoins held in custody for clients are stored. It does not assess stablecoin issuance in Malta, the overall crypto-asset holdings of Malta residents, part of which may be held with CASPs authorised in other Member States, or the potential transmission of risks from Malta-licensed CASPs to other European jurisdictions, as the returns submitted by CASPs do not cover stablecoin issuance or provide a breakdown of stablecoin positions by the client's residence.

The licensed CASP population

Ten CASPs submitted returns for end June 2026, with combined total assets of €5.2 billion.[6] This sector is highly concentrated in terms of total assets, as reflected in a Herfindahl-Hirschman Index (HHI) well above 1,800, a threshold commonly associated with a highly concentrated market.[7] Crypto-assets dominate the aggregate balance sheet, with those reported as held for sale accounting for 81.0% of total assets. As discussed below, however, this category also includes crypto-assets held on

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[1] Written by Mr Mohamed Yagob, Senior Analyst within the Financial Stability Surveillance and Risk Assessment Department. The author would like to thank Mr Andrew Spiteri, Deputy Head, and Ms Wendy Zammit, Head, within the same Department and Mr Alan Cassar, Chief Officer Financial Stability and Statistics Division, for their valuable suggestions.

[2] Article 149 of Regulation (EU) 2023/1114.

[3] Source: DefiLlama, Stablecoins dashboard, data downloaded on 8 October 2026.

[4] Adachi, M. et al. (2022), Stablecoins' role in crypto and beyond: functions, risks and policy, *Macroprudential Bulletin*, Issue 18, Frankfurt: European Central Bank.

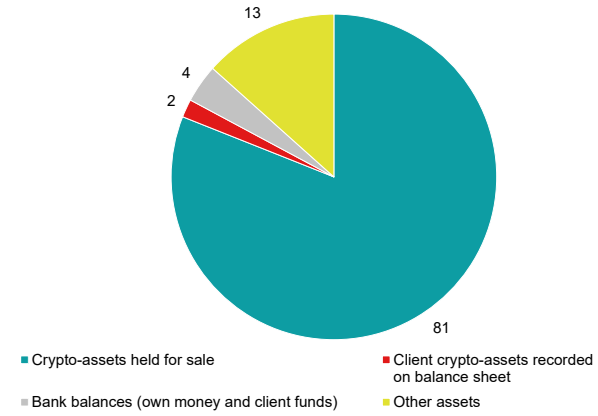
[5] Born, A. et al. (2026), Euro stablecoins and their potential effect on sovereign bond markets, *Macroprudential Bulletin*, Issue 33, Frankfurt: European Central Bank.

[6] Of the 22 CASPs authorised by the MFSA at end-June 2026, 10 submitted returns for the reference period and are included in the analysis. The remainder mainly comprised CASPs authorised towards the end of June, for which a return was not yet available. Entities operating solely under a Virtual Financial Assets Act licence were also excluded, as the transitional period expired on 30 June 2026.

[7] The HHI is the sum of the squared market shares of all firms, where market shares are expressed as percentages. It ranges from close to 0, in a market with many small firms, to 10,000 in a pure monopoly. The threshold of 1,800 follows the 2023 Merger Guidelines issued by the US Department of Justice and Federal Trade Commission.

behalf of clients (see Chart 5a). Client crypto-assets recorded separately on the balance sheet accounted for a further 1.8%. Bank balances held for the CASPs' own purposes or on behalf of clients represented 3.8%, while other assets, mainly 'amounts receivable from' and 'loans to group entities', accounted for the remaining 13.4%.

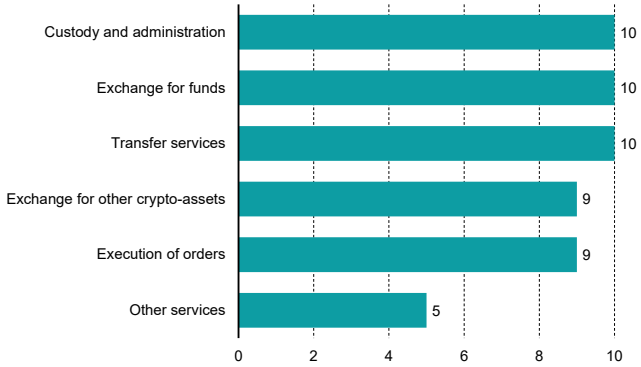
Chart 5a
BALANCE-SHEET COMPOSITION OF REPORTING CASPs
(per cent of total assets; end-June 2026)



Source: Central Bank of Malta.

In terms of business models, all ten CASPs reported providing the exchange of crypto-assets for funds, as well as custody and transfer services. Most also reported exchanging crypto-assets for other crypto-assets and executing client orders, while fewer reported providing other services, such as operating a trading platform or placing crypto-assets (see Chart 5b). At end June 2026, CASPs held €3.9 billion of client crypto-assets in custody and reported 9.7 million client relationships, of which 1.3 million were classified as active, having undertaken at least one trade during the preceding 12 months.[8] Retail clients accounted for almost all active client relationships at sector level, with fewer than 1,000 active corporate clients reported. However, four of the ten CASPs primarily served corporate clients, highlighting differences in business models across the sector.[9] Almost all client crypto-assets held in custody were recorded on the CASPs' balance sheets, mainly within crypto-assets held for sale. This category therefore includes assets held on behalf of clients and should not be interpreted as representing crypto-assets owned by the CASPs.

Chart 5b
SERVICES PROVIDED BY REPORTING CASPs
(number of CASPs; end-June 2026)



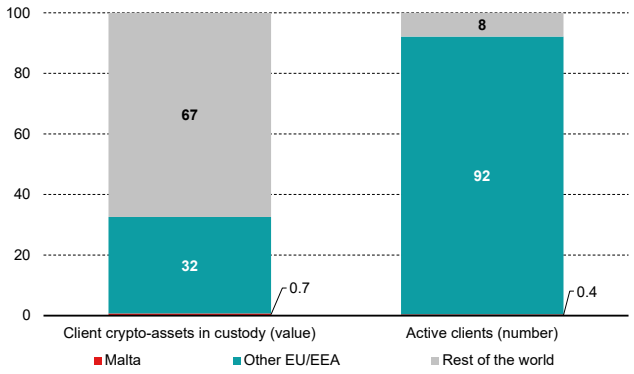
Source: Central Bank of Malta.
Note: Services reported as being provided by each CASP in the June 2026 return. Other services comprise operating a trading platform, placing of crypto-assets, and receiving and transmitting orders. A CASP providing more than one of these services is counted only once in this category.

The sector's business is largely cross-border. Across the ten reporting CASPs, the median number of jurisdictions served was more than 40. Residents of Malta accounted for 0.7% of the value

[8] Client numbers are reported by each CASP and may count the same person more than once where a client uses more than one CASP.
[9] Active clients by client type. Business-to-business clients are corporate clients and business-to-consumer clients are non-corporate clients. See MFSA, *Guidance Notes on the Compilation of Crypto-Asset Service Providers' Return*, version 2.0, August 2025.

of client crypto-assets held in custody by the reporting CASPs, or around €27.5 million, and for 0.4% of their active clients (see Chart 5c).[10] Most active clients were resident in EU/EEA countries, while around 8% were resident in the rest of the world. The geographical distribution differed when measured by the value of crypto-assets held in custody, with around two-thirds of that value belonging to clients resident in the rest of the world. However, the two measures are not directly comparable. The client count covers only active clients, whereas the custody measure covers crypto-assets held for all clients, irrespective of their activity status. Identifiable links with the domestic banking system are also limited. CASPs' own balances with domestic banks amounted to €6.2 million, or less than 5% of their own bank balances.[11] These indicators describe the general business profile of the CASP sector and are not specific to stablecoin activity.

Chart 5c
CLIENTS AND CUSTODY ASSETS BY RESIDENCY
(per cent of total; end-June 2026)

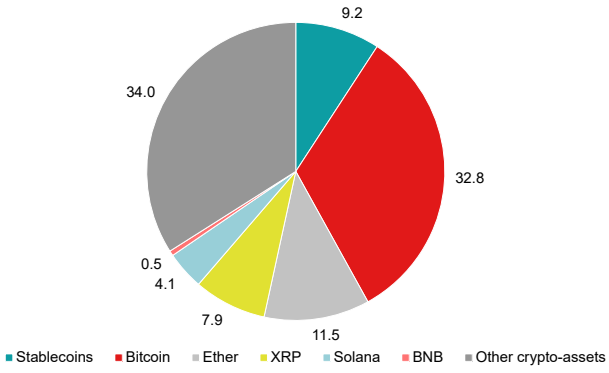


Source: Central Bank of Malta.
Note: Custody covers the value of crypto-assets held for all clients, whatever their activity status. Residency by number is reported only for active clients, who made at least one trade in the preceding 12 months and accounted for 13% of all clients. Malta-resident shares are below 1% in both cases.

Size and currency composition of reported stablecoins

A breakdown by crypto-asset category is only available for assets reported as held for sale. The return distinguishes between Bitcoin, Ether, USD and EUR-denominated stablecoins, BNB, Solana, XRP and a residual category of other crypto-assets.[12] Stablecoins reported within the held-for-sale category amounted to around €385 million as at end-June 2026, equivalent to 9.2% of that category (see Chart 5d). This was equivalent to 7.4% of the sector's total assets, although the ratio should not

Chart 5d
COMPOSITION OF CRYPTO-ASSETS HELD FOR SALE
(per cent; end-June 2026)



Source: Central Bank of Malta.
Note: Crypto-assets reported as held for sale, converted to euro at end-June 2026 exchange rates. The category includes crypto-assets held on behalf of clients and should not be interpreted as comprising only CASPs' own-account holdings. Stablecoins comprise the dedicated USD and EUR-denominated stablecoin lines and exclude any stablecoins within the residual category.

[10] These figures cover only Malta residents who are clients of the ten reporting CASPs. They do not include holdings with CASPs providing services in Malta on a cross-border basis under Article 65 of Regulation (EU) 2023/1114, providers established outside the EU, or in self-hosted wallets. Accordingly, they do not provide a comprehensive measure of total crypto-asset holdings or users among Malta residents.

[11] Residency refers to the institution with which the account is held and follows the centre of economic interest, not the licence of the institution. CASPs report balances as resident in Malta where a split is not possible. See footnote 9.

[12] Source: MFSA, *Crypto-Asset Service Providers' Return*, template version 25-03.

be interpreted as a measure of CASPs' own stablecoin exposure. Among the identified categories, stablecoins were the third largest, after Bitcoin and Ether, and exceeded the reported amounts of XRP, Solana and BNB. The residual category of other crypto-assets, which groups a wide range of tokens, was the largest single item. As the held-for-sale category includes crypto-assets held on behalf of clients, the returns do not permit reported stablecoins to be reliably separated into CASPs' own-account positions and assets associated with client balances.

Reported stablecoins were almost entirely denominated in US dollars, accounting for 99.9% of the total. EUR-denominated stablecoins were reported by four CASPs, amounting to only €0.2 million.[13] Stablecoins denominated in other currencies, such as the pound sterling or the Brazilian real, are not reflected separately in dedicated return lines and instead are included within the residual category.

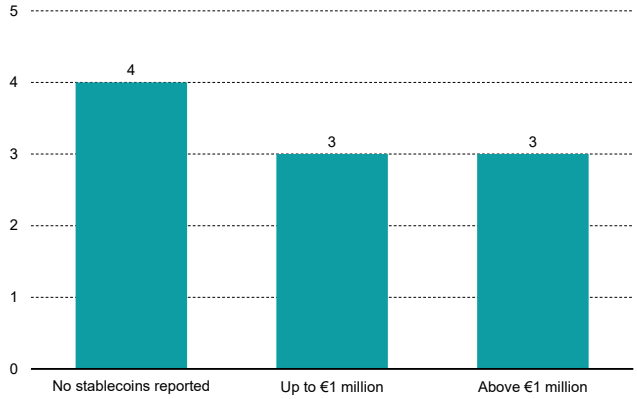
Concentration of reported stablecoins

As holdings are not valued by individual token, the return does not permit an assessment of token- or issuer-level concentration. However, reported stablecoins are almost entirely denominated in USD, broadly mirroring the global currency composition of the stablecoin market. The return does not reveal, however, whether the reported positions are similarly concentrated in the two largest global tokens. The custody data discussed below provide a partial indication.

Reported stablecoins were also highly concentrated across entities. Six of the ten CASPs reported stablecoins, although only three reported amounts exceeding €1 million (see Chart 5e). The findings therefore point to concentration both in terms of currency denomination and across reporting entities (see Table 5a).

Qualitative information on the five largest crypto-assets held in custody for clients provides some indication of the tokens used by the sector.[14] Seven of the ten CASPs listed a USD-denominated stablecoin among these assets, all of them naming USDC, while none listed a EUR-denominated stablecoin.[15] As values by token are not available, this information cannot be used to measure token-level concentration. It nevertheless supports the broader finding that the stablecoin activity reported by these CASPs is predominantly linked to USD-referenced tokens.

Chart 5e
CASPs BY SIZE OF REPORTED STABLECOINS
(number of CASPs; end-June 2026)



Source: Central Bank of Malta.
Note: Stablecoins reported within crypto-assets held for sale, converted to euro at end-June 2026 exchange rates.

[13] The denomination of a stablecoin is distinct from the currency in which a CASP compiles its return. Both USD and EUR-denominated stablecoins are expressed in euro before they are added together. Figures were converted to euro at the ECB euro foreign exchange reference rate for 30 June 2026, which was USD 1.1394 per euro (EUR 0.878 per US dollar).
[14] The return reports the overall top five crypto-assets held in custody and the share of each held in hot, warm and cold wallets. The box uses the split reported for the stablecoins among these assets.
[15] The custody information covers crypto-assets held for clients, including those not recorded on CASPs' balance sheets, whereas the number of CASPs reporting stablecoins refers only to the dedicated USD and EUR-denominated lines within crypto-assets held for sale. The two counts are therefore not directly comparable, and stablecoins reported within the residual category of other crypto-assets are not included in the latter.

Table 5a
STABLECOIN MONITORING INDICATORS, JUNE 2026

(per cent; unless otherwise stated)

	June 2026
Stablecoins reported within crypto-assets held for sale (EUR millions)	384.6
Stablecoins as a share of crypto-assets held for sale	9.2
Stablecoins as a share of total assets	7.4
USD-denominated share of stablecoins	99.9
CASPs reporting stablecoins (number)	6
CASPs reporting stablecoins above €1 million (number)	3

Source: Central Bank of Malta.

Note: Stablecoins comprise USD and EUR-denominated tokens reported within crypto-assets held for sale, converted into euro using the ECB euro foreign exchange reference rates applicable on 30 June 2026. As crypto-assets held for sale also include assets held on behalf of clients, the ratio of reported stablecoins to the sector's total assets is a scale comparison and should not be interpreted as a measure of CASPs' own stablecoin exposure. Stablecoins included within the residual crypto-asset category are excluded. The €1 million cut-off is an indicative analytical threshold used to distinguish small residual positions from larger holdings and has no regulatory meaning.

The custody information also indicates how these stablecoins are stored, as the split between hot, warm and cold wallets is available for each listed stablecoin. Hot wallets are connected to the internet and allow more immediate access and transfer but are generally more exposed to cyber and operational risks. Cold wallets are kept offline, providing greater protection from online threats, while warm wallets combine features of both arrangements.[16] All seven CASPs that listed a stablecoin held at least part of it in hot or warm wallets. Three held the majority in cold storage, while the remaining four held their listed stablecoins entirely in hot or warm wallets.

Financial stability considerations

The available data do not provide evidence of significant direct links between reported stablecoin activity and the wider domestic financial system. At end-June 2026, stablecoins accounted for 9.2% of crypto-assets reported as held for sale and were concentrated in a small number of CASPs. The entities' overall business is predominantly cross-border and retail: almost all of their active clients are retail clients, and only a small share are resident in Malta. This reflects the client base of Malta-licensed CASPs and does not capture crypto-asset activity by Malta residents through providers authorised in other jurisdictions. The observable links with domestic banks are also limited. These indicators relate to CASPs' broader activities, however, and are not specific to stablecoins.

The predominance of USD-referenced stablecoins is the main common feature across reporting entities. All six CASPs reporting stablecoins held USD-denominated positions, indicating common sensitivity to developments in this segment of the global market. However, the regulatory reporting does not identify the individual tokens held and therefore cannot establish whether the entities share material exposure to the same issuers. The custody data nevertheless suggest that USDC is the most commonly held stablecoin in client custody.

The information currently available does not allow stablecoins held on CASPs' own account to be distinguished from those held on behalf of clients. It is therefore not possible to gauge whether the effects of a de-pegging or an issuer disruption would fall mainly on the CASPs or on their clients. Similarly, the purpose for which stablecoins are held and their distribution by client type and residence cannot yet be determined from the available returns. Even where the economic risk rests with clients, safeguarding client assets may expose CASPs to operational, conduct and reputational risks,

[16] US Securities and Exchange Commission (2025), Crypto Asset Custody Basics for Retail Investors, *Investor Bulletin*, Investor.gov.

particularly as all CASPs that listed a stablecoin among their largest custody assets held at least part of it in hot or warm wallets.

Notwithstanding improvements in regulatory reporting under MiCA, data limitations remain an important challenge for crypto-asset monitoring, particularly when assessing exposures and potential channels of transmission to the wider financial system.[17] Continued monitoring, especially of the concentration of reported stablecoins within a small number of entities and the overwhelmingly USD-denominated composition, together with greater reporting granularity where feasible, could support a more comprehensive assessment of potential financial stability implications. More granular data could also support scenario analysis of the possible impact of an issuer's failure on the system as well as modelling market-wide stress. Greater consistency in stablecoin-related reporting across EU jurisdictions would also improve comparability and facilitate the assessment of cross-border activity and common exposures.

[17] Kochanska, U. (coord.) (2026), Crypto-Asset Monitoring Expert Group (CAMEG) 2025 Conference – Book of abstracts, ECB *Occasional Paper Series* No. 382, Sections 2.1.1 and 2.5, Frankfurt: European Central Bank.

SPECIAL FEATURE A: CYBER-RELATED PAYMENT DISRUPTIONS: ASSESSING BANKS' LIQUIDITY RESILIENCE THROUGH T2[1]

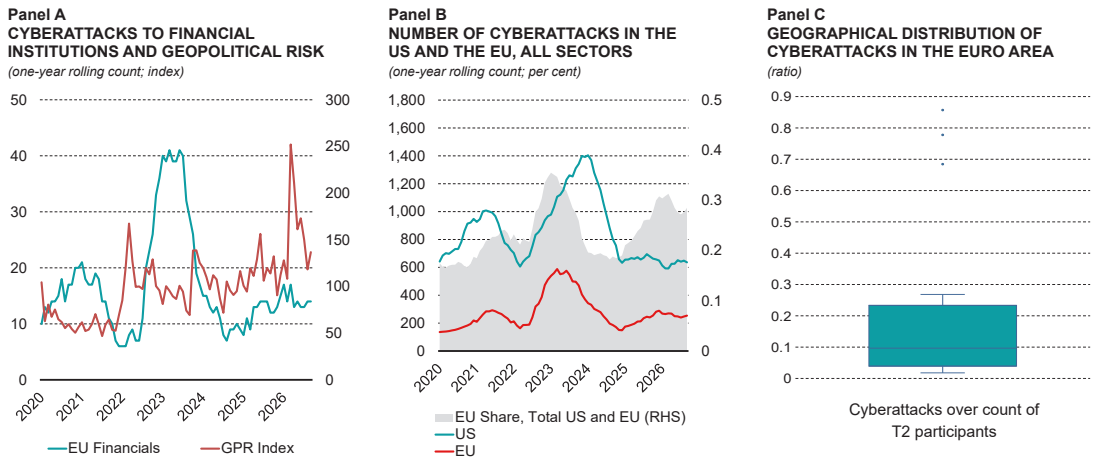
An evolving financial landscape

The rapid digitalisation of financial services has increased banks' dependence on interconnected payment infrastructures, core banking systems and third-party technology providers, making cyber risk increasingly relevant from a financial stability perspective. A severe cyber incident can extend beyond the immediate operational disruption and generate broader financial consequences.

Understanding and quantifying how liquidity stress propagates through payment and settlement systems is essential for assessing how a cyber incident can evolve from an operational disruption into a broader financial stability risk. Disruptions to critical banking services or uncertainty about the scope of an attack may undermine confidence in the affected institution, potentially triggering deposit outflows and increasing funding pressures. Meeting unexpected liquidity needs may require the sale of assets, potentially at a discount, thereby generating losses that could adversely affect a bank's solvency position and, in extreme circumstances, its viability (or going concern). As payment and settlement systems are highly interconnected, liquidity shortages can also spread to other institutions through delayed or missed payments, amplifying stress across the banking sector.[2]

Given the evolving financial landscape, cyber risks have attracted increasing regulatory and supervisory attention. As shown in Chart A.1, cyberattacks targeting the EU financial and insurance corporations have rebounded since 2024 lows but remain below their 2023 peak, while the number of cyberattacks per institution varies markedly across EU countries. The available data also indicates that reported cyberattack exposure is unevenly distributed across EU countries. This heterogeneity is particularly relevant when

Chart A.1
PUBLICLY DISCLOSED CYBER EVENTS AND GEOPOLITICAL RISK



Sources: University of Maryland Cyber Event Database; ECB; Authors' calculations.

Notes: Panel A illustrates the 12-month rolling count of publicly disclosed cyberattacks to financial and insurance corporations and the GPR Index by Caldara, D., & Iacoviello, M. (2022); Panel B depicts the 12-month rolling count of all the publicly disclosed cyberattacks to US and EU across all sectors, and showing the share of EU cyberattacks on the right-hand axis; Panel C presents the distribution across euro area countries of the number of cyberattacks targeting financial and insurance corporations from 2020 per credit institution that is a direct participant in the national T2 component system (calculated using observations following the migration from TARGET2 to T2 in 2023).

[1] Written by Matteo Panfilo and Francesco Ricciutelli, Senior Research Economists, and Kanan Musayev, Senior Economist within the Stress Testing and Research Office of the Central Bank of Malta. The authors would like to thank Mr Alan Cassar, Ms Christine Balzan, Mr Pedro Polvora for their helpful comments as well as Mr Edward Magro, Ms Tiziana Grech, Mr Shaun Vella, Mr Paul Azzopardi and Ms Abela Ritlen, for technical assistance on T2.

[2] A special feature published in FSR 2025 applies transaction-level data from T2 to map the topology of payment flows and identify key interlinkages, critical nodes and connections within Malta's payment system.

assessing exposures to foreign financial institutions that are significant net senders of payments. In this context, the ECB's 2024 cyber resilience stress test assessed banks' ability to respond to and recover from a severe cyber incident. In parallel, the Digital Operational Resilience Act has strengthened the EU framework for ICT risk management, incident management and reporting, and resilience testing.

Against this background, this study assesses the Maltese banking system's resilience to a cyber-induced liquidity disruption, focusing on how the shock may be transmitted through the payment network. By applying the Bank of Finland Payment and Settlement System Simulator (BoF-PSS3), and based on Eisenbach (2020), this exercise simulates a liquidity-sink scenario in which a selected institution is unable to execute outgoing payments while continuing to receive incoming funds. The resulting interruption to liquidity flows may affect counterparties that normally rely on the disrupted flows to fund their own obligations, creating potential second-round effects across the network. The tool allows payment and liquidity outcomes under the stressed scenario to be compared to a baseline simulation that represents normal payment activity.

The analysis quantifies the effects of liquidity being temporarily removed from circulation by identifying the banks most exposed to the resulting suspension or delay of incoming payments, and by assessing the potential direct and second-round effects on payment settlement and liquidity positions. The exercise employs T2-Malta transactions for the fourth quarter of 2025. It simulates one-day and three-day liquidity-sink scenarios involving the largest domestic direct participants and the largest foreign senders of payments to Maltese banks. The resulting liquidity deterioration is subsequently translated into changes in banks' Liquidity Coverage Ratios (LCRs) to assess the extent to which regulatory liquidity buffers may come under pressure. In doing so, the exercise moves beyond the operational impact on the initially affected institution and provides a quantitative assessment of how a cyber-related payment disruption could translate into broader financial stability effects.

The Bank of Finland Payment and Settlement System Simulator: its application to a liquidity disruption

BoF-PSS3 is an analytical simulation tool developed by the Bank of Finland to study liquidity needs and risks in payment and settlement systems. The simulator is widely used by central banks and the research community for payment-system analyses, scenario analyses and stress testing.[3,4]

The tool supports a wide range of payment and securities settlement structures, including real-time gross settlement (RTGS), deferred net settlement, continuous net settlement, hybrid, retail and large-value payment systems, as well as securities settlement systems. At a minimum, BoF-PSS3 requires transaction data only, but simulations can also incorporate account balances, intraday credit limits, bilateral and multilateral limits, system events and reservations. The resulting outputs support the analysis of liquidity consumption, settlement volumes, queuing and gridlock, counterparty risk and the role of critical participants.

An important feature of BoF-PSS3 is its application to scenario analyses and stress testing. Financial distress scenarios are generated by modifying the underlying input data or system configuration.[5] The framework can represent a range of disruptions, including participant defaults, cyber-attacks, and other operational incidents, by allowing stressed outcomes to be compared with the normal functioning of a system. The study focuses on a one-day cyber event and, subsequently, calculates average daily impacts in Q4 2025. It also considers a three-day disruption, as described below. PSS3 establishes a

[3] Its application in recent research further illustrates its relevance for stress-testing exercises. Khiaonarong et al. (2025) use BoF-PSS3 as a cyber stress-testing framework, applying it to transaction-level TARGET Services data to simulate cyber disruptions and assess their impact on payment settlement and liquidity risk. Similarly, Laine and Korpinen (2021) employ the PSS3 to analyse the resilience of the Finnish payment system to liquidity-sink shocks and resulting contagion effects.

[4] Bank of Finland Payment and Settlement System Simulator.

[5] Depending on the shock applied, a scenario can involve cancelling, delaying or reordering transactions, changing beginning-of-day balances or credit limits, modifying bilateral or multilateral limits, or altering system setups, algorithms and account structures.

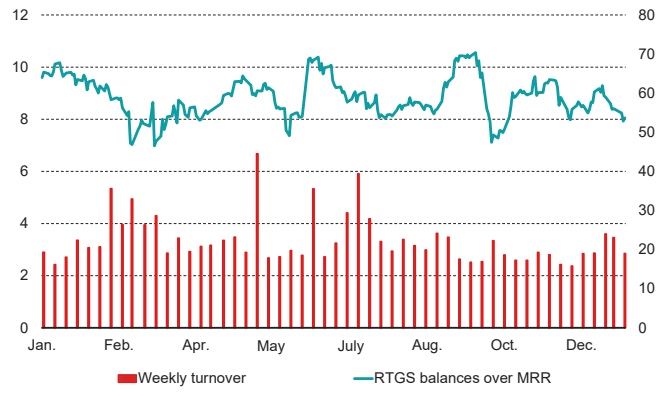
baseline of payment activity calibrated using T2 transactions and subsequently imposes a liquidity-sink scenario. This simulates an interruption of ICT services, preventing T2 Direct Participants (both foreign and domestic participants, determined on the basis of T2-Malta activity and their relevance to domestic banks) from forwarding orders through the RTGS to other domestic participants. Following Eisenbach et. al (2020), the shock is introduced by preventing the affected bank from executing outgoing payments. The liquidity impact is estimated by comparing the stressed simulation with the baseline scenario. This comparison enables the calculation of counterfactual end-of-day balances and the quantification of unsettled transactions.

An environment characterised by a strong level of reserves

Malta's current ample-reserves environment reflects a prolonged process of liquidity accumulation, originating in the aftermath of the Global Financial Crisis and subsequently reinforced by the ECB's implementation of non-standard monetary policy measures.

In 2009, the introduction of fixed-rate full-allotment refinancing operations, together with significant disruptions in interbank markets, generated substantial excess liquidity within the Maltese banking system. Banks obtained approximately €1.2 billion through LTROs.[6] This liquidity-rich position, coupled with high levels of wholesale and retail deposits, remains a structural feature of the banking system. By 2018, core domestic banks reported an aggregate LCR exceeding 184%, while non-core and international banks reported an average LCR of 415.5%, with liquid assets largely comprising central bank reserves and sovereign securities.[7] The expansionary monetary policy measures adopted during the COVID-19 pandemic further strengthened this position: between early 2021 and February 2022, excess liquidity in the Maltese banking system increased from approximately €5.5 billion to €6.6 billion,[8] predominantly in the form of excess reserves held with the central bank. Throughout 2025, available RTGS balances remained broadly equivalent to around eight to ten times regulatory reserve requirements, while average weekly payment turnover accounted for only about 20% of available balances (see Chart A.2). Overall, the structurally abundant level of excess liquidity – relative both to regulatory requirements and to ordinary payment and settlement needs – provides an important buffer against liquidity disruptions. The analysis, therefore, focuses on the structure of transaction flows, systemically relevant institutions and the geographical concentration of payment senders.

Chart A.2
RTGS BALANCES AND TURNOVER IN 2025
(ratio; per cent (RHS))



Sources: T2; Authors' calculations.
Notes: RTGS Balance divided MRR (LHS); weekly turnover is calculated by averaging the absolute value of inflow and outflows, to then divide by the amount available for RTGS transactions (RHS).

Simulating the liquidity impact of cyber disruptions in T2-Malta

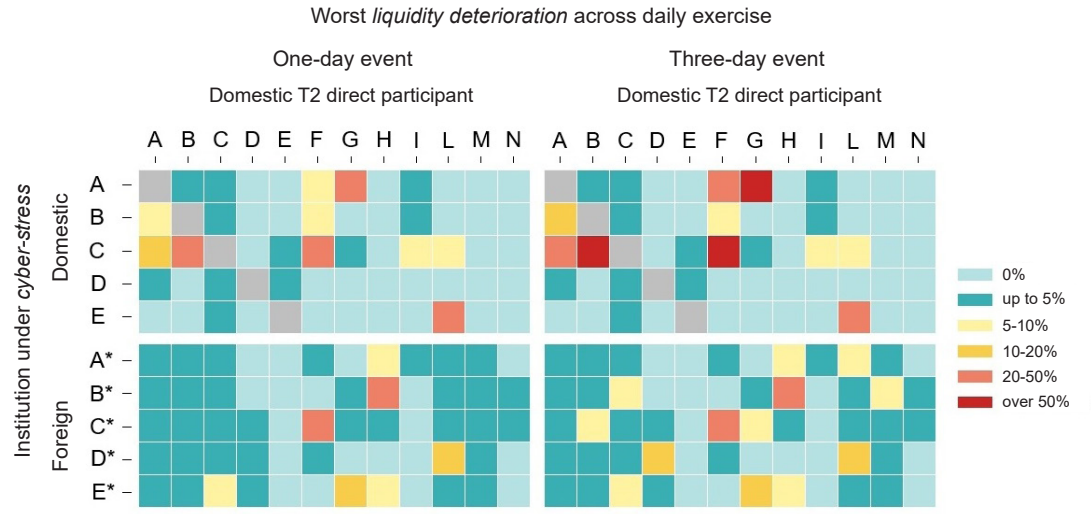
A simulation exercise was conducted using BoF-PSS3 and T2-Malta payment system data to quantify the liquidity implications of a hypothetical cyber event. This exercise stresses the top five most active T2 domestic direct participants[9] and the top five foreign

[6] Central Bank of Malta (2009), *Annual Report* 2009.
[7] Central Bank of Malta (2018), *Interim Financial Stability Report* 2018.
[8] Central Bank of Malta (2022), Central Bank of Malta *Quarterly Review* 2022.
[9] Those involved in higher exchanged value for the quarter.

senders (from Germany, Austria and France)[10] to domestic direct participants, by imposing an independent liquidity-sink behaviour. For each liquidity-sink of interest (i.e., the bank under cyber pressure), the exercise runs a separate simulation for each operational day in the fourth quarter of 2025, assuming the target bank cannot send payments for the entire day,[11] but continues to receive funds from other T2 participants. In this framework, each liquidity sink represents a single scenario, composed of a set of independent simulations involving each day in the quarter. This approach allows the estimation of scenario-specific statistics by averaging the indicators across days, or by picking the worst-case liquidity deterioration for the stressed quarter. The exercise is then repeated by prolonging the simulation to a three-day event starting on each day of 2025Q4 to study more severe scenarios through a rolling window.[12]

Figure A.1 shows the simulated cyber-stress scenarios for one-day, and prolonged to three-days, by distinguishing between T2-Malta direct participants and foreign banks. Each row identifies the liquidity-sink of five domestic and five foreign banks, while the columns represent the 12 Maltese T2 Direct Participants. Cell colours indicate the magnitude of the liquidity deterioration, showing how the simulated reductions vary with both the origination and duration of the cyber event. The results indicate that some domestic banks appear closely linked to specific network participants, with multi-day disruptions causing liquidity deterioration to accumulate to potentially severe levels. A number of institutions could be affected simultaneously. This highlights the degree of dependency among domestic banks and the most active T2-Malta direct participants. When foreign participants drive cyber-incidents, liquidity shocks tend to affect a broader set of domestic banks, although the resulting magnitude of impacts generally remains more contained.

Figure A.1
LIQUIDITY DETERIORATION MATRIX, DAILY EXERCISES FOR Q4 2025

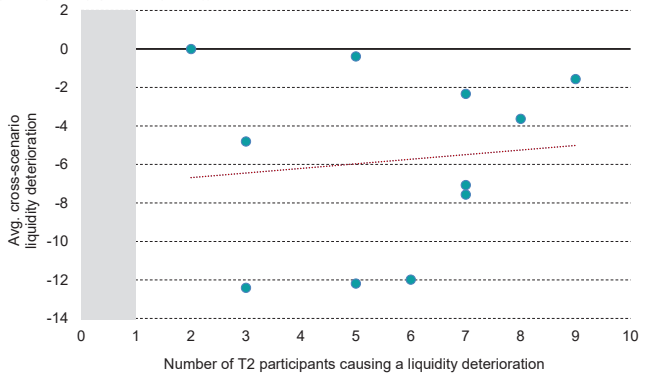


Sources: T2; Authors' calculations.
Notes: Cells represent the maximum liquidity deterioration of T2-Malta Direct Participants (x-axis) which other T2 participants (y-axis) might potentially cause if unable to send payments on any day of Q4 2025. Liquidity deterioration is measured as the percentage end-of-day deviation from baseline RTGS balances due to the missing inflow related to the cyber-event.

[10] For more information on geographical breakdown and domestic network, please see "Special Feature: Using T2 to assess payment-system flows relevant for cyber stress testing in Malta" (*Financial Stability Report* 2025).
[11] For the purposes of this study, direct debits and analogous payments directed to ancillary systems are excluded from the sample of payment orders processed by the simulator, thereby restricting the analysis to payer-initiated payment instructions.
[12] In this framework, the impacts originated by a three-day event are the result of cumulating one-day impacts and assumes that the affected bank still continues to provide liquidity even though it is not receiving any from the liquidity sink. This can underestimate the quantification of second-round effects whereby banks would react to the liquidity sink behaviour to preserve their liquidity stance and this impact is not being captured.

Chart A.3 shows, for any bank, the number of T2 participants that may cause a positive deterioration in its liquidity position when acting as a liquidity sink,[13] and the bank's average worst-case liquidity deterioration across those liquidity sinks.[14] The first measure, shown on the x-axis, captures the number of potential sources from which cyber-induced liquidity stress can propagate through the payment network. The second measure, shown on the y-axis, captures the average severity of their impact, calculated by averaging the largest liquidity decline caused by each impactful liquidity-sink across the simulated days. Together, these measures allow banks to be compared in terms of both the breadth and severity of their simulated payment-network exposure.

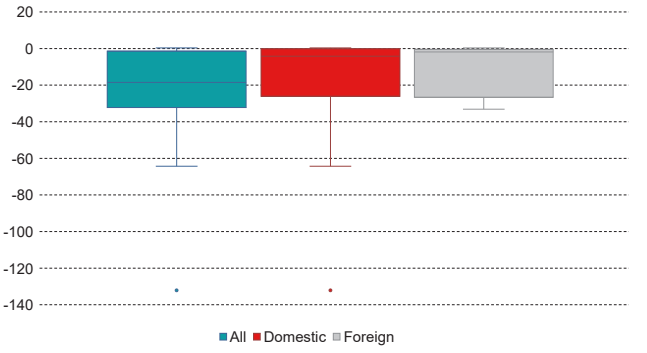
Chart A.3
COUNT OF CONNECTIONS CAUSING LIQUIDITY PRESSURE VERSUS AVERAGE WORST-CASE LIQUIDITY DETERIORATION
(count (x-axis); per cent (y-axis))



Sources: T2; Authors' calculations.
Notes: Each point represents a bank; the y-axis shows the average of maximum liquidity deterioration (across liquidity sinks); the x-axis the number of T2 participants that cause such liquidity erosion (i.e. the count of x-axis average components); quadrants are identified by median values.

The two measures are weakly positively correlated, although individual banks show different patterns of simulated exposure. Some banks record substantial liquidity deterioration in the simulations despite being exposed to relatively few problematic connections. By contrast, another small group is exposed to more participants causing liquidity deterioration but records smaller average maximum liquidity declines, although these remain above the sample median. These differences indicate that exposure to more sources of stress within the simulated network does not necessarily coincide with more severe liquidity deterioration.

Chart A.4
DISTRIBUTION OF WORST-LCR SHIFTS
(per cent)



Sources: T2; Authors' calculations.
Notes: counterfactual LCR shifts are calculated by differencing actual LCR and the one obtained after adjusting the LCR using the worst-case liquidity deterioration produced by the simulations; for any impacted bank, the amount of Q4 2025 HQLA is adjusted by subtracting the cross-scenario maximum liquidity deterioration (i.e. the worst liquidity deterioration observed across days and liquidity sinks). Such an adjustment term is firstly picked from the pool of domestic scenarios; secondly, from the pool of scenarios that involves foreign banks and then includes all domestic and foreign.

Impact on liquidity coverage

The analysis investigates further the potential for severe liquidity deterioration in terms of the regulatory threshold of 100% for the LCR.[15] Chart A.4 shows that cyber-stress scenarios generally deteriorate banks' LCR, with negative shifts across all scenario groups.

[13] Given the business model of certain Maltese banks, as well as their transactional structure as T2 participants, a subsample of banks cannot be impaired when the liquidity-sink is applied to specific domestic or foreign banks.

[14] The y-axis reports the average worst-case liquidity deterioration across scenarios, where each scenario corresponds to a T2 participant acting as a liquidity sink and involves multiple daily simulations over Q4 2025. For each scenario, the maximum daily liquidity deterioration is first identified. These worst-case values are then averaged across scenarios to obtain the value reported on the y-axis.

[15] Defined as per *Commission Delegated Regulation (EU) 2015/61*. The RTGS balance is part of Level 1 HQLA, therefore the reduction is assumed to affect the numerator of the LCR, while net liquidity outflows over the 30-day stress horizon are kept unchanged. The resulting decline in the LCR, measured in percentage points, equals the balance shortfall expressed as a percentage of net liquidity outflows. The scenarios are deliberately mechanical, whereby affected banks do not seek alternative liquidity in the money market or through Eurosystem facilities, counterparties do not stop paying the sink, and no contingency arrangements are activated. The results therefore measure liquidity at risk before any mitigating or amplifying response, rather than forecasts of actual outcomes.

Scenarios involving domestic participants show a more pronounced tail of larger LCR reductions, while those involving foreign participants are more concentrated around relatively modest LCR reductions.

With an average LCR of 478% in Q4 2025, the banks included in the exercise entered the simulated scenarios with substantial liquidity buffers. Although the worst-case shocks cause a significant liquidity deterioration, LCRs remain well above the 100% regulatory minimum. The results therefore suggest that these ample reserves provide a strong buffer against cyber-induced liquidity stress. Disruptions originating at some domestic participants generate sizeable liquidity reduction, while those originating from foreign participants affect a broader set of domestic banks but generally have a more limited impact. Nevertheless, some banks record substantial simulated liquidity deterioration following disruptions to a small number of counterparties on particular days. These findings illustrate how payment-network analysis can complement traditional liquidity indicators by identifying concentrated payment-flow dependencies that may leave individual banks vulnerable despite ample overall liquidity buffers.

Concluding remarks

This article assesses how a cyber incident that prevents a domestic or foreign bank from sending payments through T2, could affect the liquidity position of other banks operating in Malta. Using the BoF-PSS3 and T2-Malta transaction data for the fourth quarter of 2025, it simulates one-day and three-day liquidity-sink scenarios for the five largest domestic direct participants and the five largest foreign senders of payments to Maltese banks. The resulting liquidity reductions are expressed as percentage changes in affected banks' liquidity balances as well as in terms of changes to their LCR.

The results suggest that the ample reserves held by Maltese banks help to absorb cyber-induced liquidity stress transmitted through T2 under the simulated scenarios. Within this framework, the results highlight the importance of payment-flow concentration alongside the aggregate level of liquidity. A small number of domestic T2 participants act as critical sources of incoming payments for specific banks, and a liquidity sink at one of them can generate sizeable liquidity reductions, particularly if the disruption lasts several days or coincides with days of unusually large flows. Larger simulated reductions arise when a disruption at a relevant participant coincides with days of high transactional concentration, so the timing of an incident matters as much as the institution it hits. Foreign participants transmit disruptions more widely across the system, but with smaller effects on individual banks.

These findings suggest that monitoring of payment-network dependencies, including the concentration of each bank's incoming payments by counterparty and by country of origin, could complement traditional liquidity indicators, which capture the size of buffers but not their exposure to the failure of specific participants. Banks' liquidity contingency plans and digital operational resilience testing could benefit from scenarios in which a key counterparty stops paying for several days, alongside the disruption of the bank's own systems; arrangements that allow an affected participant to continue settling its most critical payments would also limit the liquidity withdrawn from the system (Kosse and Lu, 2022).

Going forward, the framework could be extended to help define a systemic cyber tolerance threshold, based on the severity and duration of participant-specific disruptions and their potential system-wide effects. This analysis could also inform escalation criteria within contingency and crisis management frameworks. The scenario design could also move beyond single-participant disruptions to include simultaneous disruptions in groups of smaller banks, disruptions propagated through common third-party providers, and more widespread or prolonged interruptions to cross-border payment inflows. Test scenarios can also comprise simulations of malicious insider knowledge of single entities or system wide peak vulnerability patterns to maximise a harmful impact. Furthermore, the analysis could be expanded to incorporate banks' reserves and portfolio management responses to assess how adverse liquidity scenarios could impact their solvency positions. In particular, this extension could examine whether heightened liquidity pressures trigger forced asset liquidations and whether the resulting losses materially weaken banks' capital positions.

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SPECIAL FEATURE B: INVESTMENT FUNDS' LIQUIDITY HEADROOM UNDER HIGHER REDEMPTIONS[1]

Motivation and financial stability relevance

Open-ended investment funds may face liquidity pressures when investor redemptions exceed the liquid assets available to meet them. In such circumstances, funds may need to sell less-liquid assets, particularly when redemption requests are large or persistent.[2] Such asset sales could amplify market stress through valuation and liquidity spillovers to other market participants. Assessing the relationship between funds' liquid-asset buffers and redemption pressures is therefore an important element of financial stability monitoring.

The Central Bank of Malta currently monitors this liquidity risk through its HQLA framework[3] and the RCR, which assesses whether funds' liquid asset buffers are sufficient to cover historical redemption pressures. An HQLA shortfall indicates that redemption pressures exceed the liquid assets buffer captured by the Bank's methodology. It does not necessarily imply that a fund would be unable to meet redemptions since the exercise does not model additional asset sales, borrowing, liquidity management tools or other management actions.

This box extends the existing analysis by estimating how much redemptions would need to increase before individual funds experience an HQLA shortfall and before such shortfalls affect a material share of aggregate sample NAV. It considers both fund-specific historical redemption rates and a common redemption benchmark. It also helps distinguish whether positions with limited modelled liquidity headroom reflect lower liquid asset buffers, more severe historical redemptions or greater reliance on the assumed liquidity of marketable securities.

Methodology

The analysis focuses on 35 domestically relevant open-ended investment funds, with an aggregate NAV of €1.7 billion as at June 2026. Closed-ended funds are excluded because their units are generally not redeemable directly from the fund at investors' request and they are therefore not exposed to the same redemption-driven liquidity risk.

For each fund i, the liquid assets buffer ratio is measured using the Bank's existing HQLA estimates and expressed as a share of NAV:

$$h_i = \frac{HQLA_i}{NAV_i}$$

The HQLA ratio h_i can also be interpreted as the gross redemption rate, expressed as a share of NAV, that would fully exhaust the modelled liquidity asset-buffer, assuming there are no liquidity sources or management actions beyond those captured by the HQLA methodology.

Two complementary approaches are applied.

Approach 1: Own historical redemptions

The first compares each fund's current HQLA ratio with its own highest observed historical redemption rate. For each fund, the historical redemption rate r_i^{hist} is calculated as the highest cumulative gross redemptions recorded over any rolling four-quarter period from December 2016 to June 2026, expressed as a share of NAV at the beginning of the relevant window.

$$r_i^{hist} = max_t\left(\frac{Gross\ Redemption_{i,t}^{4Q}}{NAV_{i,t-4}}\right)$$

[1] Authored by Mr Jake Muscat, Economist/Analyst within the Financial Stability Surveillance and Risk Assessment Department and Mr Andrew Spiteri, Deputy Head within the same department. The authors would like to thank Ms Wendy Zammit, Mr Alan Cassar, Deputy Governors Oliver Bonello and Rita Schembri, and Governor Alexander Demarco for their valuable suggestions.

[2] When faced with elevated redemptions, a fund may have several options besides selling less liquid assets. These may include drawing on cash inflows, using liquidity management tools, borrowing temporarily if permitted by its mandate, or in severe circumstances, applying exceptional measures such as redemption gates or suspensions. These responses are not modelled in the exercise.

[3] Camilleri, L., & Dos Santos Carinha, R. (2023). Box 4: Methodological update on the calculation of the liquid assets ratio for insurances and investment funds, *Financial Stability Report* 2023 (pp. 87–93), Central Bank of Malta.

This measure captures the highest cumulative four-quarter redemption pressure observed for each fund during the sample period. Since the episode may occur at different points in time, the historical redemption rate is fund-specific and need not refer to the same period across funds.

Each fund's historical rate is then progressively increased using a common scaling factor, λ:

$$r_i^{scaled} = \lambda\, r_i^{hist}$$

An HQLA shortfall arises when the scaled redemption rate exceeds the fund's HQLA ratio:

$$\lambda\, r_i^{hist} > h_i$$

The fund-specific critical multiplier is therefore:

$$\lambda_i^* = \frac{h_i}{r_i^{hist}}$$

A critical multiplier below one indicates that the fund's June 2026 HQLA ratio is already lower than its worst historical rolling four-quarter redemption rate. A multiplier above one indicates how many times the historical rate could be scaled before the modelled HQLA buffer is exhausted.

Fund-level results are also aggregated by NAV. At any multiplier λ, the share of aggregate NAV experiencing an HQLA shortfall is:

$$S(\lambda) = \frac{\sum_i NAV_i\, I\left(\lambda\, r_i^{hist} > h_i\right)}{\sum_i NAV_i}$$

where $I(\cdot)$equals one when a fund experiences an HQLA shortfall and zero otherwise. The analysis then estimates the minimum scaling factor required for HQLA shortfalls to affect funds representing at least 20% and 30% of the overall NAV.

Approach 2: Common redemption benchmark

The second approach applies the same redemption rate to all funds. Each fund's HQLA ratio is compared with the median historical redemption rate across the sample, which stands at 18.6%. This provides a common benchmark and helps distinguish between shortfalls driven by severe fund-specific historical redemption rates and those reflecting comparatively low HQLA buffers. Taken together, the two approaches separate the effect of funds' historical redemption experience from the strength of their current liquid assets buffers.

Sensitivity analysis: alternative asset-liquidity assumptions

The sensitivity of the results to alternative asset-liquidity assumptions is also assessed. This sensitivity simulates a deterioration in the liquidity profile of the marketable securities held by funds, whereby bonds and equities may need to be sold at larger discounts to their market value.

The Bank's existing HQLA factors are retained as the baseline, while the factors assigned to bonds and/or equities are reduced by one quarter of their baseline value. Accordingly, a baseline factor of 100% falls to 75%, a baseline factor of 85% is reduced to 63.8%, while a baseline factor of 50% falls to 37.5% (see Table B.1).

Three sensitivities are considered: a combined bond and equity adjustment, a bond-only adjustment and an equity-only adjustment. Under the bond-only adjustment, only the contribution of bond holdings is reduced; under the equity-only adjustment, only the contribution of equity holdings is reduced; and under the combined adjustment, both are lowered. Cash and deposits remain unchanged.

These adjustments test whether the baseline results depend materially on the liquidity attributed to marketable securities.

Table B.1

HQLA FACTORS UNDER THE BASELINE AND ALTERNATIVE ASSET-LIQUIDITY ASSUMPTIONS

Per cent

Instrument	Issuer	Rating bands	Baseline factor	Equities-only adjustment factor	Bonds-only adjustment factor	Combined adjustment factor
Cash and deposits			100.0	100.0	100.0	100.0
Bonds	Government	BBB- to AAA	100.0	100.0	75.0	75.0
	Banks	AA- to AAA	85.0	85.0	63.8	63.8
		BBB- to A+	50.0	50.0	37.5	37.5
	NFCs & NBFIs	AA- to AAA	85.0	85.0	63.8	63.8
		BBB- to A+	50.0	50.0	37.5	37.5
Equities	All issuers	BBB- to AAA	50.0	37.5	50.0	37.5
Other financial assets (incl. loans, derivatives and fixed assets)	All issuers	n.a.	0.0	0.0	0.0	0.0

Note: Under the alternative assumptions, the baseline HQLA contribution of the affected asset classes is reduced by 25%. For example, a baseline factor of 85% falls to 63.8%, while a baseline factor of 50% falls to 37.5%. The adjustments are illustrative and do not represent alternative regulatory HQLA requirements.

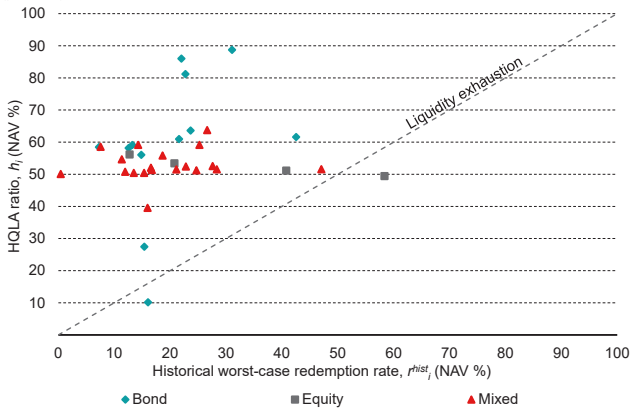
Results

Resilience relative to funds' own historical redemptions

Fund-level results

Chart B.1 compares each fund's HQLA ratio as at June 2026 with the highest rolling four-quarter gross redemption rate observed since December 2016. Funds above the 45-degree line hold sufficient HQLA to cover their highest observed 12-month redemptions, whereas funds below the line would face an HQLA shortfall under such a scenario.

Chart B.1
HQLA RATIOS AND HIGHEST OBSERVED ROLLING FOUR-QUARTER REDEMPTION RATES
(per cent)



Source: Central Bank of Malta.

Overall, only two of the 35 funds fall below the line. The underlying drivers differ across the two funds. In one case, the shortfall is driven by a relatively low HQLA ratio of around 10%, reflecting a portfolio composition heavily concentrated in assets that receive a zero weight under the Bank's HQLA methodology. The second case relates to an equity fund whose highest observed rolling four-quarter redemption rate of 58% exceeded its HQLA ratio of around 50%.

A further fund has limited headroom, with a critical multiplier of 1.10. This means that a modest increase of around 10% relative to its historical redemption rate would be sufficient to deplete its modelled HQLA buffer. Across the full sample, however, the median critical multiplier stands at 2.9, implying that the historical redemption rate of the median fund would need to increase by around 190% before the fund's HQLA buffer is exhausted.

The factors driving the critical multipliers differ across fund types. Among bond funds, differences in liquidity buffers are the main source of variation, with HQLA ratios ranging from almost 10% to almost 90% of NAV. By contrast, HQLA ratios are relatively similar across equity and mixed funds, mostly falling within the 50% to 60% range. As a result, differences in historical redemption patterns play a larger role in explaining variations in their critical multipliers.

The timing of the highest rolling four-quarter redemption rates also varies across fund types. Peaks among bond funds were mainly split between windows ending in 2017–2019 and 2025–2026, while those of mixed and equity funds were more concentrated in the recent period. Indeed, 15 of the 23 mixed and equity funds recorded their highest rate from December 2024 onwards. Equity funds recorded the highest median historical redemption rate, at around 31%, compared with 17% for mixed funds and 19% for bond funds, although the equity-fund sample consists of only four funds. Only four funds recorded peaks in windows overlapping either the COVID-19 market turmoil in 2020 or the 2022 interest-rate increases and bond-market repricing, and these temporal overlaps should not be interpreted as evidence of causality. Overall, the concentration of peaks in 2025–2026 suggests that the historical benchmarks used for many mixed and equity funds largely reflect relatively recent redemption experience rather than earlier market-wide stress episodes.

Aggregate sector results

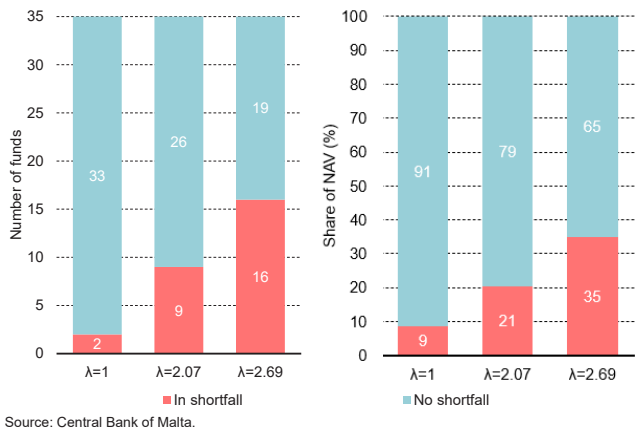
The fund-level results are aggregated by NAV to assess how liquidity vulnerabilities evolve as redemption pressures increase across the funds (see Chart B.2). At λ = 1, corresponding to the application of each fund's own highest observed rolling four-quarter redemption rate, the two funds identified earlier record an HQLA shortfall, which together represent less than 10% of aggregate sample NAV.

For HQLA shortfalls to affect funds representing more than 20% of aggregated NAV a multiplier of 2.07 is needed. This corresponds to a 107% increase relative to each fund's own historical redemption benchmark. Under this scenario, nine funds, accounting for 20.5% of aggregate sample NAV, would experience an HQLA shortfall.

More severe redemption pressures are required before liquidity strains become more widespread. A multiplier of 2.69, equivalent to a 169% increase relative to each fund's own historical redemption benchmark, is needed for funds accounting for over 30% of aggregate NAV to experience an HQLA shortfall. At this point 16 funds representing 35.1% of aggregate sample NAV would record an HQLA shortfall.

Overall, these results suggest that under the initial historical benchmark HQLA shortfalls are initially concentrated in a small number of funds. However, the share of aggregate NAV affected increases progressively as the scaling factor rises, while the liquidity headroom of funds not yet in shortfall also narrows. Nevertheless, a substantial share of the sampled funds maintains positive liquidity headroom under the most severe redemption assumptions.

Chart B.2
DISTRIBUTION OF FUNDS BY HQLA COVERAGE UNDER SELECTED REDEMPTION MULTIPLIERS
(number of funds; per cent)



Source: Central Bank of Malta.

Resilience under a common redemption assumption

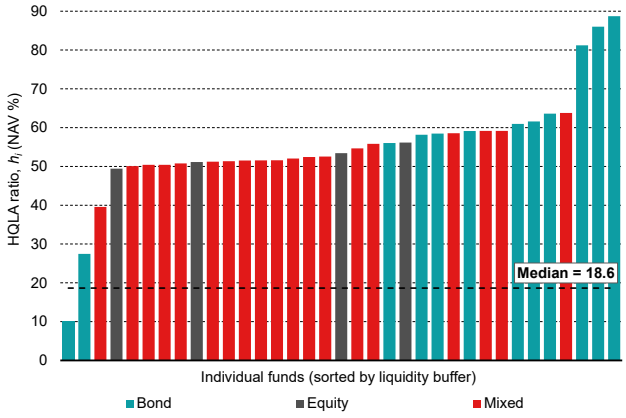
Fund-level results

To provide a common benchmark across funds, Chart B.3 compares each fund's HQLA ratio with the median of the fund-specific highest observed rolling four-quarter redemption rates, which stands

at 18.6%. This is shown by the dashed line.

Under this assumption, only one fund records an HQLA shortfall. This is the same fund identified in the previous section as having a comparatively low HQLA ratio of around 10%. The fact that the second fund identified under the fund-specific approach remains above the common benchmark confirms that its shortfall is driven by its exceptionally high historical redemption rate, rather than by an HQLA ratio that is low relative to the rest of the sample. Meanwhile, one additional fund lies relatively close to the benchmark, with an HQLA ratio of around 27%. By contrast, the remaining funds hold substantially larger HQLA buffers, with most ratios ranging between 50% and 65% of NAV, more than double the median redemption rate.

Chart B.3
HQLA RATIOS RELATIVE TO THE COMMON REDEMPTION BENCHMARK
(per cent of NAV)



Source: Central Bank of Malta.

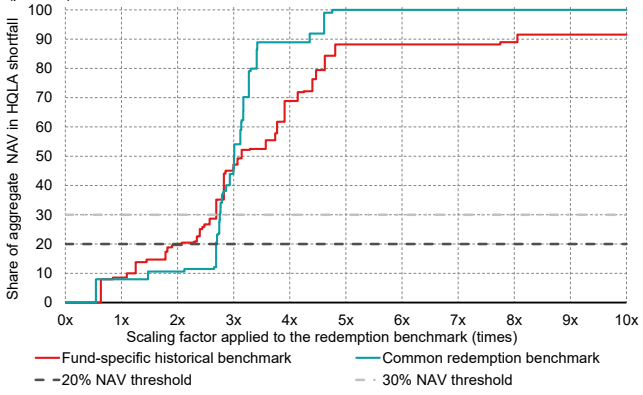
Aggregate sector results

The common redemption rate is then progressively increased to assess how much redemption pressure would be needed for the HQLA shortfalls to affect larger shares of the sector. At the initial redemption rate of 18.6%, only one fund records a shortfall.

The common redemption rate would need to rise to 50.1%, equivalent to 2.69 times the initial median rate, before funds representing more than 20% of aggregate sample NAV, experience a shortfall in their HQLA. Under this scenario, five funds representing 20.8% of aggregate sample NAV record an HQLA shortfall. A relatively small increase in the common redemption rate to 51.3%, or 2.75 times the initial median rate, raises the share of affected NAV to 30.3%. At this point, eleven funds record an HQLA shortfall. The sharp increase in the number of affected funds over this narrow range reflects the clustering of several HQLA ratios around the 50% mark.

Compared with the fund-specific approach, a larger increase in redemption pressure is required under the common assumption for HQLA shortfalls to affect funds representing more than 20% of aggregate NAV (see Chart B.4). This indicates that the lower fund-specific threshold is partly driven by a limited number of funds with particularly elevated historical redemption rates. However, the results converge at the 30% threshold, suggesting that funds' HQLA ratios become more influential as redemption pressures increase across the sample. Since several funds have HQLA ratios at similar

Chart B.4
SHARE OF AGGREGATE NAV IN HQLA SHORTFALL
(per cent)



Source: Central Bank of Malta.
Note: The chart compares the fund-specific historical benchmark with the common redemption benchmark. Both curves are shown as step functions because funds enter HQLA shortfall at discrete scaling factors. The x-axis is limited to 10x.

levels, a relatively small increase in the common redemption rate causes several funds to exhaust their modelled liquidity buffers in close succession, resulting in a rapid increase in the share of aggregate NAV affected.

Sensitivity to alternative asset-liquidity assumptions

Fund-level results

The baseline results are compared with three alternative asset-liquidity assumptions: a 25% reduction in the HQLA contribution of both bonds and equities, bonds only, and equities only. Cash and deposits remain unchanged.

The bonds-only adjustment does not bring any additional funds into shortfall when compared with the baseline. By contrast, both the equities-only and the combined adjustments increase the number of funds in shortfall to four, together representing around 14% of aggregate sample NAV.

The two additional funds, operating as mixed and equity funds, held critical multipliers of 1.10 and 1.25, respectively, under the baseline scenario. Equities account for more than 75% of their HQLA. Reducing the equity contribution by 25% consequently lowers their HQLA buffers by around one-fifth to one-quarter and moves both funds into shortfall. These additional shortfalls therefore reflect the combination of high reliance on equities within the funds' recognised HQLA buffers and historical redemption rates of around 47% and 41%, which were already close to their baseline HQLA ratios.

Aggregate sector results

At the aggregate level, all three adjustments lower the scaling factor at which HQLA shortfalls affect a material share of sample NAV. First, the adjustments reduce the HQLA contribution of bonds and/or equities, thereby lowering funds' estimated HQLA buffers. With a smaller HQLA buffer available to cover redemptions, a smaller increase in the critical multiplier is required for funds to experience an HQLA shortfall. Under the baseline calibration, the 20% NAV threshold is reached at a scaling factor of 2.07, consistent with the baseline results reported in Chart B.2. This falls to 1.90 under the bond-only adjustment, 1.77 under the equity-only adjustment and 1.56 under the combined adjustment. For the 30% NAV threshold, the multiplier falls from 2.69 under the baseline calibration to 2.03, 2.40 and 2.02, respectively (see Table B.2).

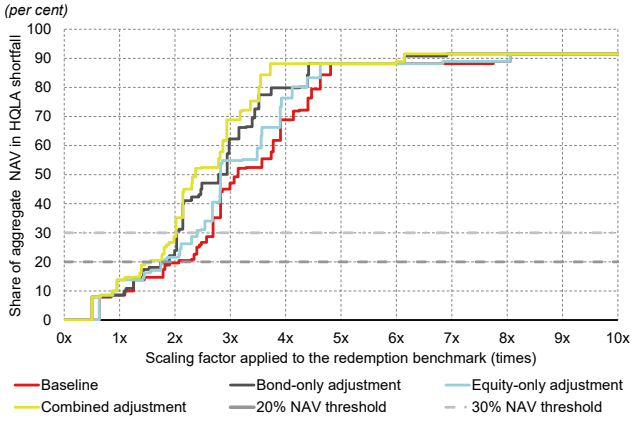
Table B.2
HQLA SHORTFALLS AND CRITICAL SCALING FACTORS UNDER ALTERNATIVE ASSET-LIQUIDITY ASSUMPTIONS

HQLA calibration	Funds in shortfall at λ =1	NAV in shortfall at λ =1	Multiplier for 20% NAV	Multiplier for 30% NAV
Baseline	2	<10%	2.07	2.69
Bond-only adjustment	2	<10%	1.90	2.03
Equity-only adjustment	4	13.90%	1.77	2.40
Combined adjustment	4	13.90%	1.56	2.02

Note: The table shows the scaling factors at which funds representing at least 20% and 30% of aggregate sample NAV experience an HQLA shortfall. Under the alternative assumptions, the HQLA contribution of bonds and/or equities is reduced by 25% relative to the baseline calibration. Cash and deposits remain unchanged.

The relative effects of the bond and equity adjustments vary across the two thresholds (see Chart B.5). The equity adjustment has a larger effect at the 20% NAV threshold, while the bond adjustment has a larger effect at the 30% NAV threshold. This reflects differences in the portfolio composition and size of funds closest to the NAV thresholds. The combined adjustment consistently produces the largest decline in the critical scaling factors.

Chart B.5
SHARE OF AGGREGATE NAV IN HQLA SHORTFALL
(per cent)



Source: Central Bank of Malta.
Notes: The curves are shown as step functions because funds enter HQLA shortfall at discrete scaling factors. The x-axis is limited to 10x.

Main findings and conclusion

The analysis indicates that most of the domestically relevant open-ended funds in the sample have positive modelled liquidity headroom relative to their historical redemption experience. Thirty-three of the 35 funds hold HQLA buffers above their own highest observed rolling four-quarter redemption rates. For the median fund, the historical redemption rate would need to rise to 2.9 times its observed level, before its HQLA buffer is exhausted. This broad pattern is observed across fund types, although the extent and drivers of liquidity headroom vary considerably across individual funds. Overall, the results indicate that most of the funds considered could accommodate materially higher redemption pressures before exhausting their modelled HQLA buffers. From a financial stability perspective, this is relevant since liquid assets provide a first line of defence against forced sales of less-liquid assets and associated valuation effects.

Two funds, one bond fund and one equity fund, would nevertheless record an HQLA shortfall if their respective historical redemption benchmarks were applied to their June 2026 liquidity positions. The shortfalls reflect different underlying factors. The bond fund has a comparatively low HQLA ratio, as a large share of its portfolio is invested in assets assigned a zero weight under the Bank's HQLA methodology. In contrast, the equity fund recorded a relatively high historical redemption rate relative to its HQLA buffer.

Under the fund-specific approach, each fund's historical redemption rate would need to increase by 107% for HQLA shortfalls to affect funds representing more than 20% of aggregate NAV. For funds representing 30% of aggregate NAV, the required increase is 169%. Under the common redemption benchmark, which applies the same redemption rate across all funds, the common rate would need to rise by 169% and 175% for HQLA shortfalls to affect more than 20% and 30%, respectively, of aggregate NAV. The higher increase under the common assumption indicates that the fund-specific results are initially influenced by a limited number of funds whose own historical redemption rates are already high relative to the HQLA buffers. At the 30% NAV threshold, the two approaches produce broadly comparable results. This suggests that the level and distribution of HQLA buffers play a greater role as redemption pressures broaden across the sample.

The results are also sensitive to a deterioration in the assumed liquidity profile of marketable securities. Reducing the recognised HQLA contribution of bonds and equities by a further 25% increases the number of funds in shortfall at their historical redemption rates from two to four. The combined adjustment also reduces the increase in historical redemption rates required for HQLA shortfalls to affect 20% of aggregate NAV from 107% to 56%, and the increase required for shortfalls to affect 30% of NAV from 169% to 102%. The funds closest to shortfall are particularly sensitive to the equity adjustment, as equities account for a large share of their recognised HQLA buffers. At the aggregate level, the relative effects of the bond and equity adjustments depend on which funds experience a shortfall at each NAV threshold, as well as on their size and portfolio composition.

Overall, the positions with the lowest modelled liquidity headroom are concentrated in a limited number of funds but arise through different channels, including comparatively low HQLA ratios, unusually high historical redemptions, and a strong reliance on equities within the HQLA buffer. These findings remain conditional on the methodology and assumptions applied and should not be interpreted as predictions of redemption behaviour or fund distress. Future work could incorporate changes in market liquidity as redemptions rise, as well as common asset holdings and spillovers from simultaneous asset sales.

APPENDICES

Appendix A – Table 1
FINANCIAL SOUNDNESS INDICATORS – BANKING SECTOR

	Core Domestic Banks					Non-Core Domestic Banks					International Banks					Total Banks				
	2022	2023	2024	2025	June 2026	2022	2023	2024	2025	June 2026	2022	2023	2024	2025	June 2026	2022	2023	2024	2025	June 2026
Capital[1]																				
Regulatory capital to RWAs	23.0	24.7	25.3	27.6	26.3	18.7	20.8	23.2	22.4	22.2	41.1	38.7	37.6	34.7	35.2	24.6	26.0	26.7	28.1	27.2
Regulatory Tier 1 capital to RWAs	19.6	21.0	21.1	21.5	20.7	17.6	19.7	22.1	20.2	19.9	40.7	38.5	36.3	32.3	32.8	21.9	23.0	23.2	23.0	22.4
Leverage ratio	7.2	7.9	8.2	8.0	8.0	8.9	9.5	10.6	10.9	11.6	32.3	28.8	28.9	24.1	24.1	8.9	9.5	9.8	9.6	9.6
Large exposures to total own funds	83.3	60.6	58.3	57.6	54.1	194.4	133.5	104.2	96.1	102.6	75.6	65.4	64.6	79.7	89.5	91.8	68.3	63.8	64.9	64.6
RWAs to total assets	38.0	38.8	39.8	38.8	40.1	51.7	49.5	52.9	58.9	60.9	70.8	67.3	71.9	76.0	75.6	41.6	42.1	43.5	43.5	44.6
Profitability																				
ROA[2]	0.4	1.0	1.1	0.8	0.8	-0.4	0.6	0.4	0.1	0.2	2.6	2.5	-0.3	0.9	2.0	0.9	1.3	0.7	0.8	1.0
ROE[1,2]	5.4	12.0	11.6	8.9	8.7	-3.4	5.7	4.2	0.9	1.7	6.0	11.3	8.7	8.6	9.7	4.5	11.2	10.3	8.1	8.2
Operational cost-to-income ratio	82.3	51.0	52.4	58.1	58.9	81.0	66.6	73.3	84.3	81.0	44.5	55.8	80.0	52.4	36.6	62.9	53.9	60.4	58.1	52.8
Interest margin to gross income	71.8	78.8	78.8	76.7	77.6	54.0	66.2	71.2	68.2	71.6	49.2	36.0	46.3	63.0	68.3	59.3	60.0	70.7	72.1	74.3
Non-interest expense to gross income	83.2	51.5	52.8	58.4	59.1	81.3	67.4	73.8	84.7	81.5	44.5	55.8	80.0	52.4	36.6	63.3	54.2	60.7	58.3	53.0
Personnel expenses to non-interest expenses	36.4	46.6	47.5	46.5	47.0	47.3	49.1	49.8	43.4	47.0	10.0	9.2	9.0	16.1	20.8	27.6	30.4	29.9	38.2	41.4
Non-interest income to gross income	28.2	21.3	21.2	23.3	22.4	46.0	33.8	28.8	31.8	28.4	50.8	64.0	53.7	37.1	31.7	40.7	40.0	29.4	27.9	25.7
Net impairment charges to gross income	-11.5	0.4	-4.8	-1.3	-0.4	35.2	5.8	6.6	1.7	0.0	14.5	5.5	29.1	23.4	19.5	4.2	2.9	3.9	6.1	6.1
Asset Quality																				
NPLs to total own funds[1]	21.5	17.9	14.2	10.4	9.8	30.0	8.0	6.8	7.0	6.8	11.5	11.8	15.2	13.5	12.1	20.3	15.8	13.7	10.7	10.0
NPLs to total gross loans	2.7	2.5	2.3	1.8	1.6	4.3	1.2	1.1	1.3	1.3	1.3	1.5	1.7	1.5	1.3	2.5	2.2	2.0	1.7	1.5
Overall NPL Ratio excluding CBM placements	3.7	3.3	2.7	2.1	1.9	6.4	2.0	2.0	2.1	2.2	1.6	1.9	2.7	2.4	1.9	3.4	2.9	2.7	2.2	1.9
Non-performing exposures to total gross exposures	2.0	1.8	1.5	1.2	1.1	3.1	0.9	0.9	1.0	1.0	0.9	0.9	0.9	1.3	1.2	1.8	1.5	1.3	1.2	1.1
Total coverage ratio	46.5	43.5	39.5	46.3	46.8	72.7	60.1	71.2	81.6	76.1	189.6	125.3	107.4	101.2	110.2	66.1	55.7	54.8	61.0	62.5
Unsecured loans to total lending	18.7	18.0	17.4	17.1	23.7	55.3	47.5	49.6	51.7	45.6	23.6	27.9	33.1	39.0	38.5	22.4	22.1	22.5	23.5	27.8
Share of Stage 3 provisions to total provisions	69.6	67.3	70.8	72.2	68.0	88.4	56.6	54.8	66.8	64.4	26.5	45.3	55.1	49.6	47.0	58.5	59.9	63.6	63.1	59.5
Forborne loans to gross loans	3.5	2.5	2.3	2.0	1.8	0.6	1.1	1.4	1.9	2.2	7.4	1.3	1.4	2.3	2.1	4.1	2.2	2.0	2.1	1.9
Liquidity																				
LCR[1]	380.0	366.4	362.0	374.9	369.0	316.0	405.2	438.3	399.4	402.4	383.7	566.9	422.6	296.3	324.9	373.8	379.4	371.9	371.3	368.5
Liquid assets to total assets[1,3]	36.3	35.0	36.7	39.1	38.9	31.1	36.1	41.3	37.3	36.1	26.9	30.5	30.6	24.1	23.5	35.1	34.7	36.6	37.7	37.4
Customer loans to customer deposits	56.0	58.9	59.1	60.2	62.1	54.4	49.5	49.0	51.5	50.2	230.6	184.6	179.3	173.4	179.3	67.2	67.0	66.9	68.3	70.4
CBC on net cash outflows	251.0	287.2	331.0	337.4	326.8	240.7	272.0	315.7	310.7	313.2	58.6	189.1	131.0	138.4	190.7	239.8	281.2	318.0	321.8	317.7
NSFR[1]	187.1	175.8	183.9	188.3	186.8	172.9	191.3	180.9	172.4	169.4	118.4	137.7	144.5	129.7	132.4	180.3	173.8	180.3	181.0	180.0
Balance Sheet																				
Assets-to-GDP	157.8	140.4	133.2	134.4	134.3	19.0	17.2	14.6	12.9	12.1	56.0	47.5	56.3	46.2	49.4	232.8	205.1	204.0	193.5	195.7
Domestic debt securities to total assets	9.4	8.9	10.3	10.5	10.0	7.9	6.0	5.2	4.9	5.3	0.2	0.0	0.0	0.0	0.0	7.1	6.6	7.1	7.6	7.2
Foreign debt securities to total assets	16.5	19.2	22.4	22.7	22.9	18.0	17.0	13.6	14.5	15.3	29.8	35.9	39.5	27.5	32.1	19.8	22.9	26.5	23.3	24.7
Customer loans to total assets	47.2	48.8	49.6	50.2	51.3	38.2	36.9	37.9	39.9	38.0	41.7	38.4	30.4	38.3	36.9	45.1	45.4	43.5	46.7	46.8
Interbank exposures to total assets	4.9	3.9	3.9	3.8	2.9	7.2	6.4	5.9	5.5	6.5	10.0	7.7	4.7	8.3	6.9	6.3	5.0	4.3	5.0	4.2

Note: All figures are expressed as percentages. Annual observations refer to end-December; Jun-26 refers to end-June 2026. All ratios are calculated on a solo basis. Profitability indicators, balance-sheet indicators and the customer loans-to-customer deposits ratio are calculated using BR06 statutory returns. All other indicators are based on FINREP/COREP returns.

[1] Data for international banks excludes the branches of foreign banks.

[2] Profitability ratios use a four-quarter moving sum of profits after tax.

[3] Liquid assets defined in line with the EBA Liquidity Coverage Ratio (LCR DA) Methodology.

Appendix A – Table 2
FINANCIAL SOUNDNESS INDICATORS – NON-BANK FINANCIAL INSTITUTIONS

Domestically relevant Insurance Companies	Life Insurance Firms					Non-life Insurance Firms					Overall Insurance Firms				
	2022	2023	2024	2025	June 2026	2022	2023	2024	2025	June 2026	2022	2023	2024	2025	June 2026
SCR coverage ratio	180.2	219.7	249.5	271.5	247.7	233.6	242.9	246.5	238.6	231.6	200.2	230.1	248.0	253.8	239.2
Excess of assets over liabilities as a share of total assets[1]	10.1	10.1	10.1	10.8	10.7	44.3	53.1	54.6	56.9	56.2	15.4	16.6	17.4	18.8	18.8
Technical provisions as a share of net written premia	788.5	983.2	954.6	907.8	852.1	124.7	86.2	79.6	75.9	78.0	541.4	573.7	547.6	514.9	494.2
Liquid assets ratio[2]	61.8	60.2	60.4	59.4	59.7	26.1	30.7	32.2	32.0	33.0	55.4	54.8	54.6	53.3	53.6
Modified duration	5.9	6.4	7.3	6.7	6.6	4.9	4.0	3.7	4.0	4.1	5.8	6.2	7.0	6.4	6.3
ROA[3]	1.0	0.8	0.9	0.9	0.7	2.5	10.0	10.5	11.8	12.1	1.3	2.2	2.5	2.7	2.7
Assets-to-GDP	17.2	15.0	14.0	13.3	13.3	3.1	2.7	2.7	2.8	2.9	20.3	17.7	16.7	16.2	16.2
Growth in premia[4]	-17.7	-16.9	7.2	6.8	9.5	15.2	16.6	13.8	17.8	2.8	-5.0	-1.3	10.8	13.0	5.5
Growth in claims[4]	-10.7	-8.5	-0.5	-8.8	5.8	38.9	-24.7	37.2	32.2	11.9	-0.8	-13.0	8.6	3.8	8.2
Bond holdings as a share of total assets	33.7	37.5	38.9	37.4	36.3	12.9	16.8	18.9	19.8	19.0	30.5	34.4	35.7	34.4	33.3
Equity holdings as a share of total assets	16.8	14.7	11.9	11.6	12.0	24.1	27.9	27.7	26.8	26.4	17.9	16.7	14.4	14.2	14.5
Investment fund units as a share of total assets	34.5	38.1	40.2	42.1	42.3	8.2	9.4	10.8	11.3	12.1	30.4	33.7	35.4	36.8	37.0

	Bond Funds					Equity Funds					Mixed Funds					Overall Funds				
	2022	2023	2024	2025	June 2026	2022	2023	2024	2025	June 2026	2022	2023	2024	2025	June 2026	2022	2023	2024	2025	June 2026
Leverage ratio	100.3	100.2	100.6	100.4	100.8	100.2	100.2	100.5	100.1	100.1	100.2	100.4	100.6	100.2	100.6	100.3	100.3	100.6	100.3	100.6
Liquid assets ratio[2]	69.2	66.8	64.2	61.0	56.2	55.3	52.5	52.6	53.1	53.5	55.3	54.9	54.8	53.6	53.1	64.1	61.9	60.1	57.7	54.8
RCR[5]	14.4	12.6	7.4	7.9	7.2	4.0	3.8	3.8	3.8	4.0	41.7	36.5	35.3	35.2	33.3	7.0	6.8	6.4	6.1	5.6
Modified duration	5.8	5.8	5.7	5.4	5.1	5.4	2.6	2.7	2.0	1.5	7.3	6.9	7.5	6.9	6.5	6.1	6.0	6.0	5.7	5.3
Operating profit margin[6]	65.9	68.2	68.8	68.2	69.6	2.6	21.5	25.8	18.1	9.9	56.2	65.7	73.3	79.7	74.8	63.4	65.8	68.7	71.2	69.2
Assets-to-GDP	5.3	4.5	4.3	3.9	3.6	0.5	0.5	0.6	0.6	0.7	2.6	2.5	2.4	2.5	2.5	8.3	7.5	7.3	7.0	6.8
Growth in NAV	-21.9	0.2	4.9	-3.4	-4.6	-3.1	25.8	32.2	15.9	14.1	-10.4	11.3	6.5	9.2	3.7	-18.0	5.1	7.5	2.0	1.2
Share of NAV by resident households	56.8	56.2	56.2	50.6	57.0	39.4	41.5	44.5	43.1	46.0	55.3	53.5	51.5	44.6	48.2	55.4	54.3	53.7	47.8	52.7
Share of NAV by other resident sectors	37.6	38.2	34.6	38.1	34.8	54.4	53.0	49.7	51.2	47.9	42.9	44.4	45.6	51.8	47.6	40.2	41.3	39.4	44.0	40.8
Bond holdings as a share of total assets	89.3	91.5	90.4	92.8	93.3	1.9	5.4	4.2	2.9	2.3	34.6	33.6	32.4	30.9	28.9	67.4	66.7	64.3	62.9	60.4
Equity holdings as a share of total assets	0.4	0.4	0.4	0.4	0.5	49.2	60.8	59.3	59.2	57.4	34.5	37.4	37.5	39.7	40.2	13.7	16.6	17.3	19.6	20.8
Investment fund units as a share of total assets	4.5	4.6	5.8	4.1	3.8	37.6	29.4	31.8	32.1	33.6	26.3	26.7	27.3	27.0	28.3	13.1	13.5	15.0	14.7	15.8

[1] The excess of assets over liabilities is the difference between total assets and liabilities, representing the solvency margin under Solvency II.
[2] For info on the methodology refer to FSR 2023 Box 4 (https://www.centralbankmalta.org/site/Reports-Articles/2024/FSR-2023-Box-4.pdf).
[3] Based on profit before tax. Figures from 2023 onwards are based on IFRS 17. Earlier data reflect IFRS 4 and are not directly comparable.
[4] Figures for June 2026 reflect the difference relative to December 2025.
[5] The RCR compares the stock of HQLA to the largest quarterly outflow recorded since the inception of the time series in December 2016.
[6] Defined as the funds' net profit as a share of total revenue.

Appendix B
FINANCIAL STABILITY HEATMAP



Note: For the financial sector, the framework evaluates key indicators for core domestic banks, domestically relevant insurance companies, and domestically relevant investment funds (see Table 1a in Box 1: Monitoring Financial Stability Risks: A Heatmap Approach for the list of indicators). As each category comprises multiple indicators, variables are first standardised using z-scores to ensure comparability and then aggregated within each category using equal weights. The resulting category-level measures are subsequently weighted by the relative size of the respective financial institutions. Where necessary, indicators are transformed so that higher values consistently correspond to higher levels of risk, ensuring a coherent interpretation across indicators and categories. Indicators are assessed relative to their historical distributions. Values in the lowest quintile of the historical distribution are shown in dark green, indicating levels that are significantly below their historical range, while values in the highest quintile are shown in red, indicating relatively elevated levels within the historical distribution.