

## BOX 2: BEYOND THE IMPACT ON EMPLOYMENT: THE FISCAL IMPLICATIONS OF MALTA'S TAPERING OF BENEFITS SCHEME<sup>1</sup>

This box provides a brief overview of a 2023 Working Paper which assessed the impact of Malta's Tapering of Benefits (TOB) scheme on employment.<sup>2</sup> The study employed survival analysis and cox proportional hazard models, based on high-quality anonymised national data on the whole population of beneficiaries and their employment history in Malta. This box expands on the original study by also analysing the fiscal implications of the scheme, focusing on the period 2014-2019.

### The impact of the scheme on employment

Since its independence, Malta has relied on a passive social welfare system, while developing a robust safety net. Following the European Commission's Europe 2020 goals,<sup>3</sup> the Maltese government committed to a paradigm shift and announced a number of Active Labour Market Policies (ALMPs) in 2014 aimed at 'Making Work Pay'. ALMPs are government initiatives aimed at assisting individuals find gainful employment, retain employment, enhance productivity and/or earnings, or improve the general functioning of the labour market. Their goal is to bring jobseekers closer to the labour market by eliminating or diluting the poverty trap, as well as helping individuals find stable employment in the longer term.

Example of such ALMPs introduced in Malta in recent years include free childcare for working parents, the creation of Breakfast Clubs, tax incentives to take up work and the TOB scheme. In line with the Employment Policy, and following Ireland's Back To Work Allowance (BTWA) scheme, the TOB scheme was targeted at unemployment assistance (UA), social assistance (SA) and SA for single unmarried parents (SUP) beneficiaries, that is, individuals judged to be considerably prone to fall into a poverty trap.

Support under the Maltese TOB scheme is granted for three years. Initially, in addition to the salary in their newly found job, individuals received 65% of their benefit in the first year, 45% of their benefits in the second year, and 25% of their benefit in the third year.<sup>4</sup> In the absence of such a scheme, individuals would have lost all their benefits upon finding a job. Hence, the TOB scheme works by increasing the opportunity cost of inactivity, making employment more enticing.

Shortly following the introduction of ALMPs, the number of UA, SA and SUP beneficiaries declined considerably (see Chart 1). However, these reforms coincided with a period of buoyant economic growth, an increasing labour force, and higher participation rates (driven by increases in female participation rate and inward migration). This confluence of factors makes it challenging to isolate the effect of the scheme.

<sup>1</sup> Prepared by Kurt Sant, Senior Economist within the Economic Analysis Department of the Bank. The views expressed in this article represent those of the author and should not be interpreted to reflect those of the Bank. Any errors are the author's own.

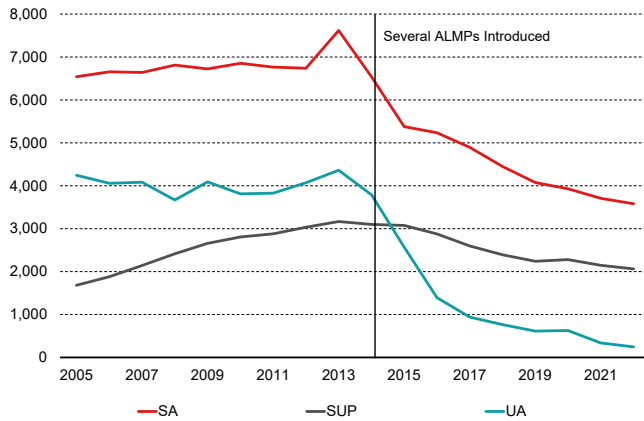
<sup>2</sup> Sant, K. (2023) "The Impact of Malta's Tapering of Benefits Scheme on Employment", [Working Paper 07/2023](#), Central Bank of Malta.

<sup>3</sup> The European Commission Europe 2020 goals include that the employment rate of the population aged 20-64 should increase from the current 69% to at least 75%, including through the greater involvement of women, older workers and that the number of Europeans living below the national poverty lines should be reduced by 25%, lifting over 20 million people out of poverty.

<sup>4</sup> The scheme was later improved by a ten-percentage point increase in the benefit due each year. The impact of this improvement is not studied in this box, as it was introduced in the Budget for 2023, while this box focuses on the period up to 2019.

A summary of the original Working Paper results can be found in Table 1. Results represent hazard ratios and should be interpreted as the risk of the event occurring when compared to the baseline category, keeping other variables constant. Deviations from the numeraire (1) represent changes in percentage probabilities of the events occurring.

**Chart 1**  
SA, SUP AND UA BENEFICIARIES IN MALTA  
(number of beneficiaries)



Source: Ministry for Social Policy and Children's Rights.

The first results show that the TOB doubles the job-finding probability, with SUP beneficiaries enjoying the scheme the most and SA beneficiaries experiencing it the least. The impact declines with age and has no gender effect. Meanwhile, in the second set of results, the negative (lower than one) estimated coefficient of the Qualification Dummy shows that those who qualify for the scheme have a lower probability of experiencing a return to unemployment. When assessing the difference between the TOB Effect and Qualification Dummy hazard ratios, the TOB scheme shows a powerful effect in terms of reducing the chance of the event occurring for those individuals who are eligible and able to benefit from the scheme. In fact, the chance of job termination drops by 11.8 percentage points for those individuals falling within the TOB regime.

**Table 1**  
**SUMMARY OF WORKING PAPER RESULTS**

Hazard rates

	Hazard rate <sup>(1)</sup>	Standard error <sup>(2)</sup>
<b>TOB impact on the job-finding rate of UA, SA and SUP beneficiaries</b>		
TOB effect (full sample)	1.996***	(0.065)
TOB effect (UA sample)	1.951***	(0.096)
TOB effect (SA sample)	1.673***	(0.139)
TOB Effect (SUP sample)	2.316***	(0.216)
<b>TOB impact on retaining employment once an individual finds a job</b>		
TOB effect	0.673***	(0.048)
Qualification dummy	0.791***	(0.036)
TOB long-term dummy	1.195	(0.212)

Source: Ministry for Social Policy and Children's Rights.

<sup>(1)</sup> Baseline (Hazard ratio = 1): No TOB in place.

<sup>(2)</sup> Standard errors in parentheses (\*  $p < 0.1$ , \*\*  $p < 0.05$ , \*\*\*  $p < 0.01$ ).

The “TOB Long-Term Dummy” hazard rate is statistically insignificant. This is a very reassuring finding, as it shows that once the scheme eligibility ends after 36 months, job-terminations of previously eligible individuals do not increase significantly. Thus, the scheme appears to be successful in not only helping individuals finding employment, but also to re-integrate them into the labour force in the longer term – even after benefit payments end.

### Tapering of benefits disbursements

Table 2 displays the total and average benefits tapering payments for each category from 2014 to 2019, offering insights into the efficacy and reach of this scheme. Across the three-year period during which individuals enjoy tapered benefit payments in addition to their employment income, an average individual receives €6,821.9 in tapered benefits. This means that over this three-year period, individuals on average earn up to 26% in additional income when compared to a situation without the TOB scheme.

Beneficiaries which enjoy the largest average TOB payments are aged 36 years and older. This is since individuals in these age categories are more likely to have additional dependents in their household, meaning that their original benefit is higher. On the other hand,

**Table 2**  
**TOTAL AND AVERAGE TOB PAYMENTS**

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	Total TOB payment	Average TOB payment
Total	38,455,242.4	6,821.9
<b>Age group</b>		
Under 26	5,703,224.8	5,575.0
Age 26-35	11,920,045.9	6,585.7
Age 36-45	11,594,275.6	7,305.8
Age 46-55	7,400,039.6	7,636.8
Age 56+	1,837,656.5	7,409.9
<b>Previous benefit</b>		
SA	12,649,870.9	7,110.7
SUP	13,878,987.1	6,008.2
UA	11,904,700.3	7,710.3
<b>Origin</b>		
Foreign	381,660.5	5,696.4
Gozitan	1,423,702.3	6,911.2
Maltese	36,649,879.7	6,832.6
<b>Gender</b>		
Female	26,713,253.0	6,455.6
Male	11,741,989.4	7,833.2
<b>TOB year</b>		
Tapered benefit year 1	15,967,637.3	3,086.1
Tapered benefit year 2	13,151,379.4	2,150.3
Tapered benefit year 3	9,336,225.8	1,553.4

Source: Ministry for Social Policy and Children's Rights.

beneficiaries with age categories of less than 36 years have the lowest average TOB payment, even though they are responsible for the largest absolute TOB payments.

The monetary boost which the TOB scheme provides towards females is evident. In fact, when analysing payments according to the previous benefit, the largest amount of TOB payments is disbursed towards the single parent category, which almost wholly consists of females. Furthermore, the gender analysis shows that 70% of all TOB payments were disbursed towards females.

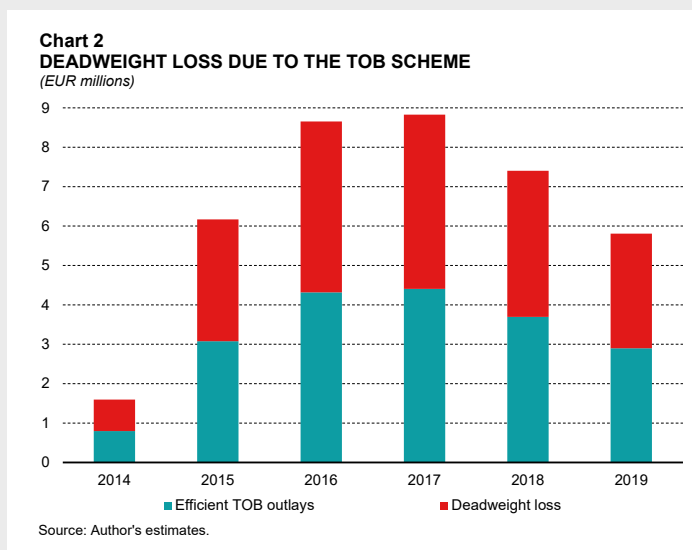
However, the average TOB payment towards SUP and female beneficiaries was lower than those for UA, SA and male beneficiaries, respectively. This is also due to the fact that the tapered amount is linked to the previous benefit levels.

### The fiscal implications of the Tapering of Benefits Scheme

ALMPs have the potential to be extremely costly, especially if not designed and implemented correctly.

The costliest aspect in the TOB scheme is by far the deadweight loss which is inherently created through its design. This deadweight loss arises since any individuals who would have moved into employment even in absence of the TOB scheme, will still enjoy the monetary gains from the scheme. Using the probability results obtained in the Working Paper, the TOB scheme gives rise to €19.4 million in deadweight losses in the period between 2014 and 2019, i.e. in the period preceding the outbreak of COVID-19 (see red bar in Chart 2). Such deadweight loss peaks at €4.4 million in 2017. The remaining outlays reflect the cost of the benefit working as intended. The bar labelled 'efficient TOB outlays' in Chart 2 represents those tapered benefits transferred to individuals who would not have moved into employment in absence of the TOB scheme.

At the same time, Government made savings on expenditure on other social benefits. TOB beneficiaries would have continued to rely on UA, SA or SUP benefits should the scheme had not been in place. To estimate savings made in this counterfactual scenario, the above-mentioned probabilities are once again used. Furthermore, it is assumed that individuals would still be eligible for benefits under the same



criteria as before – without any additional family members, changes in dependency (such as children reaching 18), or variations in means-tested conditions. In this scenario, the benefits are inclusive of the cost-of-living adjustment (COLA) increments that would have been disbursed to recipients.

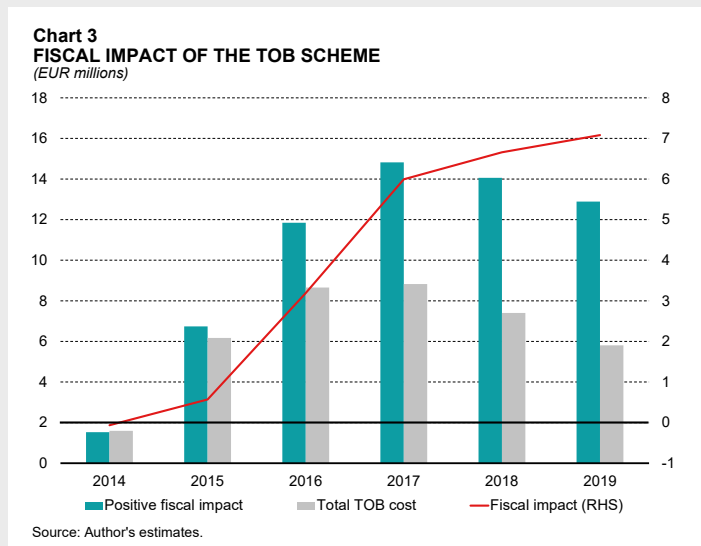
On the basis of these assumptions, it is estimated that the TOB scheme enabled the Government to save approximately €46.1 million, equivalent to around 0.3% of GDP, that would have otherwise been disbursed as UA, SA, or SUP benefits.

Government also earned additional tax revenue from the entry of TOB beneficiaries into the labour market. Even if one assumes that all individuals who entered employment earned a minimum wage, thereby making them ineligible for income tax, they would still pay social contributions. Between 2014 and 2019, Government is estimated to have earned at least €15.0 million (around 0.1% of GDP) in additional revenue from social contributions.

When comparing the complete TOB cost (not solely the deadweight loss) with the cost savings and additional tax revenue, the scheme appeared to exhibit a negligible negative fiscal impact during the first year of operation (see Chart 3). However, over the next five years, the scheme makes a positive contribution to the budget balance. The cumulative estimated impact amounts to around €7.0 million by 2019.

Overall, the TOB scheme added around 5,600 persons in employment, and is estimated to have raised the country’s labour supply by 1.3%. The cumulative impact on the potential level of economic activity amounts to around 0.9%.<sup>5</sup>

The estimates presented in Chart 3 only take into account the direct, first-round fiscal impact of having more people in employment. The full fiscal impact of this scheme is gauged in a counterfactual scenario in which the TOB scheme was not implemented, and the above mentioned 5,600 persons remained among the ranks of long-term unemployed. In turn, this lowered the potential output of the economy. If one were to exclude the positive impact of this policy on potential output, on average the structural



<sup>5</sup> Grech (2022) estimated the impact of an additional 5,500 workers in 2021 to boost potential output by 1.2% (see Grech, A.G. (2022), The impact of COVID-19 longer careers – an initial assessment for Malta, Central Bank of Malta *Policy Paper*). In this study, the impact on potential output is somewhat smaller, and likely reflects revisions to the labour force dataset.

fiscal balance would have worsened by around 0.3% of GDP each year between 2014 and 2019.<sup>6</sup>

### Conclusion

This analysis shows that the TOB scheme has been an effective instrument to address the poverty trap. It has also shown that the scheme's positive fiscal impact extends well beyond the immediate savings, suggesting that it holds considerable promise for fiscal sustainability over time.

However, recent inflation surges have dampened real wage growth and reduced disposable income, posing new challenges for those at risk of poverty. This intensifies the need for policymakers to adequately complement existing schemes to ensure that such individuals do not relapse into benefit dependency once the tapering period ends. Additional government measures, beyond the scope of the TOB scheme, were thus necessary to protect the more vulnerable in society. To this end, in recent years Government increased a number of social benefits and introduced new schemes, notably the additional COLA payment which varies according to the size and income level of households.

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<sup>6</sup> The structural government balance shows the underlying fiscal stance after correcting for the impact of the economic cycle and net of temporary government measures. The impact of the cycle is estimated by the output gap, i.e. the difference between the potential and actual level of output.