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ABBREVIATIONS

AWY	average weighted yield
BCI	Business Conditions Index
BLS	Bank Lending Survey
CCI	construction cost index
COICOP	Classification of Individual Consumption by Purpose
COVID-19	coronavirus disease 2019
CGS	COVID-19 Guarantee Scheme
CPE	compensation per employee
CPI	consumer price index
DE	Germany
DFR	deposit facility rate
EA	Euro Area
ECB	European Central Bank
EEI	Employment Expectations Indicator
EER	Effective Exchange Rate
ES	Spain
ESA	European System of Accounts
ESI	Economic Sentiment Indicator
EU	European Union
EUI	Economic Uncertainty Indicator
EURIBOR	euro interbank offered rate
€STR	euro short-term rate
FC	financial corporation
FCI	Financial Conditions Index
Fed	Federal Reserve
FOMC	Federal Open Market Committee
FR	France
FTE	full-time equivalent
GDP	gross domestic product
GFCF	gross fixed capital formation
GHG	greenhouse gas
GNI	gross national income
GVA	gross value added
HICP	Harmonised Index of Consumer Prices
ILO	International Labour Organization
IT	Italy
LCR	liquidity coverage ratio
LFS	Labour Force Survey
LSGS	Liquidity Support Guarantee Scheme
MDB	Malta Development Bank
MFI	monetary financial institution
MGS	Malta Government Stocks
MGSB	Malta Government Savings Bond
MIA	Malta International Airport
MPC	Monetary Policy Committee
MRO	main refinancing operation
MSE	Malta Stock Exchange
MT	Malta
MTB	Malta Treasury Bills
NAIRU	non-accelerating inflation rate of unemployment
NEIG	non-energy industrial goods

NFC	non-financial corporation
NPISH	non-profit institutions serving households
NSFR	net stable funding ratio
NSO	National Statistics Office
OPEC	Organisation of the Petroleum Exporting Countries
OPEC+	OPEC and non-OPEC members
PEPP	pandemic emergency purchase programme
PPI	Property Price Index
RPI	Retail Price Index
SBS	Structural Business Statistics
SLS	Subsidised Loans Scheme
UCA	Urban Conservation Areas
ULC	unit labour cost
UK	United Kingdom
US	United States
VAT	value added tax
YTM	yield to maturity

FOREWORD

During the second quarter of 2024, annual real gross domestic product (GDP) growth rose by 4.4%, following a 7.6% increase in the preceding quarter. Growth was mainly driven by net exports, as the contribution of domestic demand, while still positive, was smaller. When adjusting for imports, exports remained the main driver of GDP growth.

Potential output growth is estimated to have stood at 5.4% in the second quarter of 2024, below that of 6.1% estimated for the first quarter. On a four-quarter moving average basis, the level increase in potential output relative to the previous quarter was stronger than that in GDP, resulting into a slightly smaller positive output gap. This implies a slight easing in the degree of over-utilisation of the economy's productive capacity.

The Bank's Business Conditions Index (BCI) edged down further in the second quarter and was in line with its historical average. This partly reflects GDP growth which was broadly in line with its long run average. At the same time, growth in other sub-components such as the issuance of development permits for residential buildings and the Economic Sentiment Indicator (ESI) was below average.

Developments in the labour market remained positive. The unemployment rate remained low from a historical perspective and was well below that in the euro area. Meanwhile, the job vacancy rate and the labour market tightness indicator while declining slightly, remained high in relation to recent outcomes.

Consumer price pressures eased further during the quarter under review. Annual inflation, as measured by the Harmonised Index of Consumer Prices (HICP), stood at 2.2% in June, down from 2.7% in March. This moderation stemmed from lower processed food inflation as all other main components retained the same contribution. Meanwhile, annual inflation based on the Retail Price Index (RPI), which only considers expenditure by Maltese residents, edged down to 1.3% in June, from 1.9% in March due to lower contributions from prices of food.

Annual growth in the industrial producer price index eased to 0.2% in the second quarter, down from 0.6% in the previous quarter. Other indicators such as the domestic producer price index, and the goods imports deflator also show some easing in cost pressures. On the other hand, the construction cost index (CCI) increased in annual terms, after it had declined in the previous quarter. Malta's unit labour cost (ULC) index, measured on a four-quarter moving average basis, rose at an annual rate of 1.4%, following a rise of 0.6% in the preceding quarter, largely reflecting an acceleration in compensation per employee (CPE).

In the second quarter of 2024, the current account surplus widened compared with a year earlier. This was due to higher net receipts from services, and to a lesser extent, a narrowing of the merchandise trade deficit. By contrast, net outflows on the primary income accounts increased and net inflows on the secondary income account decreased. On a four-quarter moving sum basis, the current account balance registered a surplus equivalent to 7.0% of GDP in the second quarter of 2024.

When measured on a four-quarter moving sum basis, the general government deficit ratio narrowed by 0.4 percentage points, from 3.8% in the first quarter of 2024 to 3.4% in the second quarter. Meanwhile, the general government debt-to-GDP ratio declined by 0.5 percentage point to 46.7%, compared with 47.2% in the first quarter.

Over the 12 months to June, Maltese residents' deposits with monetary financial institutions (MFIs) in Malta increased, reflecting higher balances belonging to households and insurance companies. The annual rate of change exceeded that recorded in March. Credit to Maltese residents also expanded at a faster pace, as both credit to general government and credit to other residents picked up. According to the Bank's Financial Conditions Index (FCI), in the second quarter of 2024, financial conditions remained loose from a historical perspective, and also loosened further when compared with the previous quarter. As a result, financial conditions according to the FCI were the most accommodative since 2021. The recent improvement was driven by domestic factors, although foreign factors also contributed.

During the year to June, the weighted average interest rate offered to households and NFCs on their outstanding deposits stood above its year-ago level, increasing by 13 basis points, to reach 0.37%. This was largely driven by higher rates on time deposits belonging to NFCs and households, as well as by rates on household deposits redeemable at notice up to three months. Meanwhile, over the same period, the weighted average lending rate paid by households and NFCs to resident MFIs decreased by 7 basis points, to 3.51%, driven by lower rates charged to both households and NFCs.

Data on new business, which may be more indicative of the transmission of monetary policy impulses, show an increase in the weighted average deposit rate, and a decrease in the weighted average lending rate.

The primary market yield on Treasury bills increased between March and June. The secondary market yields on five-year and ten-year Malta Government Stocks (MGS) also rose over this period, while the MSE Equity Price Index declined.

After leaving its official rates unchanged for the preceding eight months, the Governing Council of the European Central Bank (ECB) lowered the three key policy rates by 25 basis points in June, since the inflation outlook had improved markedly, underlying inflation eased, and monetary policy kept financing conditions restrictive. Accordingly, the interest rates on the deposit facility, the main refinancing operations (MROs) and the marginal lending facility were decreased to 3.75%, 4.25% and 4.50%, respectively.

In light of persisting domestic price pressures, the Governing Council reiterated that it would keep policy rates sufficiently restrictive for as long as necessary to ensure that inflation would return to its 2% medium-term target in a timely manner. The Governing Council restated that it would continue to follow a data-dependent and meeting-by-meeting approach to determining the appropriate level and duration of restriction.

The Governing Council also confirmed that it would reduce the Eurosystem's holdings of securities under the pandemic emergency purchase programme (PEPP) by €7.5 billion per month, on average, over the second half of the year.

In September, the Governing Council decided to lower the deposit facility rate (DFR), by 25 basis points. Additionally, the spread between the MRO and the DFR was set at 15 basis points. By contrast, the spread between the rate on the marginal lending facility and the rate on the MROs was kept unchanged at 25 basis points. Accordingly, the DFR was decreased to 3.50% and the interest rates on the MROs and the marginal lending facility were decreased to 3.65% and 3.90%, respectively.

Furthermore, in October, the Governing Council decided to lower the three key ECB interest rates by 25 basis points as inflation continued to moderate. Accordingly, the interest rates on the deposit facility, the MROs and the marginal lending facility were decreased to 3.25%, 3.40% and 3.65%, respectively.

ECONOMIC SURVEY

1. THE EXTERNAL ENVIRONMENT AND THE EURO AREA

In the second quarter of 2024, real GDP expanded at a stronger pace in the United States and at a slower pace in the United Kingdom and in the euro area. During the quarter under review, the unemployment rate rose slightly in the United States, eased marginally in the United Kingdom and remained unchanged in the euro area.

Consumer price inflation eased in both the United States and the United Kingdom but rebounded slightly in the euro area. The increase in inflation in the euro area mainly reflected energy price dynamics and faster growth in the prices of unprocessed food and services. In the United States, inflation fell to 3.0% in June from 3.5% in March, while in the United Kingdom, inflation declined to 2.0% in June from 3.2% in March. By contrast, in the euro area, inflation edged up to 2.5% in June from 2.4% three months earlier. The Federal Reserve (Fed) and the Bank of England kept their key interest rates unchanged whereas the ECB cut its policy rates during the quarter under review.

Brent oil prices fell in the review period, mainly on account of lower growth in global oil demand amid a more abundant supply. By contrast, the price of European natural gas rebounded as demand increased in a tightening global market.

Key advanced economies

US economic activity expands at a faster pace

In the United States, real GDP grew at a quarterly rate of 0.7% in the second quarter, up from 0.4% in the preceding quarter, driven by stronger growth in domestic demand (see Table 1.1). Higher personal consumption expenditure was the main contributor to growth during the quarter under review, followed by a marked increase in private inventory investment. Government consumption and investment spending contributed to a lesser degree. By contrast, net exports contributed negatively to economic growth, as imports outpaced exports.

Meanwhile, labour market conditions showed some signs of easing. Non-farm payroll data show that employment grew by 0.4% on average during the quarter, compared to 0.5% in the previous quarter. These data suggest that the increase in employment was driven by private services. In turn, within private services, employment growth was most pronounced in education and health, followed by trade, transportation and utilities. Government employment increased mildly when

Table 1.1
REAL GDP GROWTH IN SELECTED ADVANCED ECONOMIES
Quarter-on-quarter percentage changes; seasonally and working day adjusted

	2022			2023				2024	
	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
United States	0.1	0.7	0.8	0.7	0.6	1.1	0.8	0.4	0.7
Euro area	0.9	0.5	-0.1	0.0	0.1	0.0	0.1	0.3	0.2
United Kingdom	0.3	0.1	0.3	0.1	0.0	-0.1	-0.3	0.7	0.5

Sources: Bureau of Economic Analysis, US; Eurostat; Office for National Statistics, UK.

compared to private services. The participation rate remained unchanged at 62.6% during the review period. On average, the unemployment rate rose slightly to 4.0% in the second quarter, compared to 3.8% in the previous quarter (see Chart 1.1).

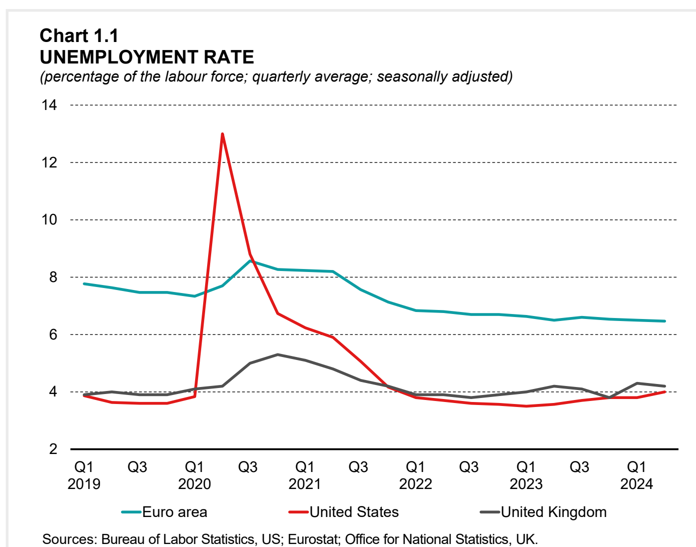


Chart 1.1
UNEMPLOYMENT RATE
(percentage of the labour force; quarterly average; seasonally adjusted)

Sources: Bureau of Labor Statistics, US; Eurostat; Office for National Statistics, UK.

Inflationary pressures eased in the quarter under review, largely reflecting a drop in prices of goods (less food and energy) as well as lower energy and services inflation. Thus, the annual inflation rate based on the consumer price index (CPI) stood at 3.0% in June, compared to 3.5% three months earlier (see Chart 1.2). The annual rate of change of prices of goods excluding food and energy, became even more negative, falling to -1.8% in June, compared to -0.7% in March, partly reflecting a steeper decline in the prices of durables. Annual energy inflation declined to 1.0% in June, compared to 2.1% in March, while services inflation eased to 5.0% in June, from 5.3% three months earlier. On the other hand, food inflation (including beverages) stood at 2.2% in June, unchanged from March. Inflation excluding food and energy eased to 3.3% in June, from 3.8% in March.

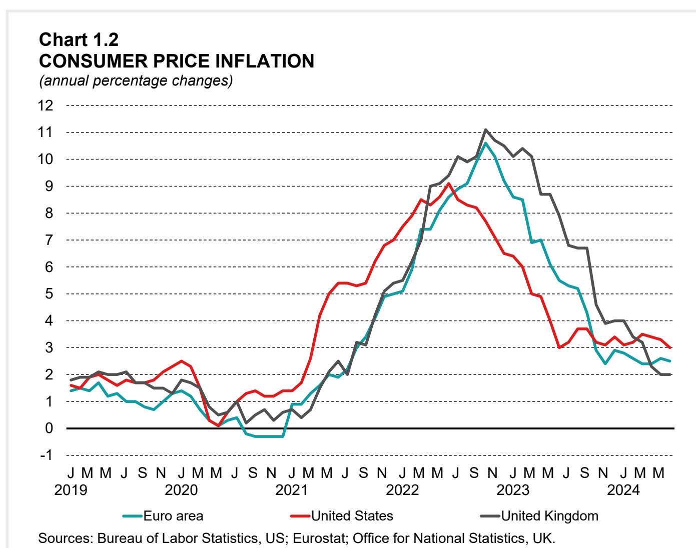


Chart 1.2
CONSUMER PRICE INFLATION
(annual percentage changes)

Sources: Bureau of Labor Statistics, US; Eurostat; Office for National Statistics, UK.

During the second quarter of 2024, the Federal Open Market Committee (FOMC) kept the target range for the federal funds rate unchanged at between 5.25% and 5.50% as it awaited firmer signs that inflation is moving sustainably towards 2%. In considering any adjustments to the target range for the federal funds rate, the FOMC reiterated that it would carefully assess incoming data, the evolving outlook and the balance of risks. In May, the Committee announced that, beginning in June, it would slow the pace of quantitative tightening by reducing the monthly redemption cap on Treasury securities from USD 60 billion to USD 25 billion. The Committee would maintain the monthly redemption cap on agency mortgage-backed securities at USD 35 billion and would reinvest any principal payments above this cap into Treasury securities. In June, the FOMC restated

that it would continue reducing its holdings of Treasury securities and agency debt and agency mortgage-backed securities.[1]

UK economy expands at a slower pace

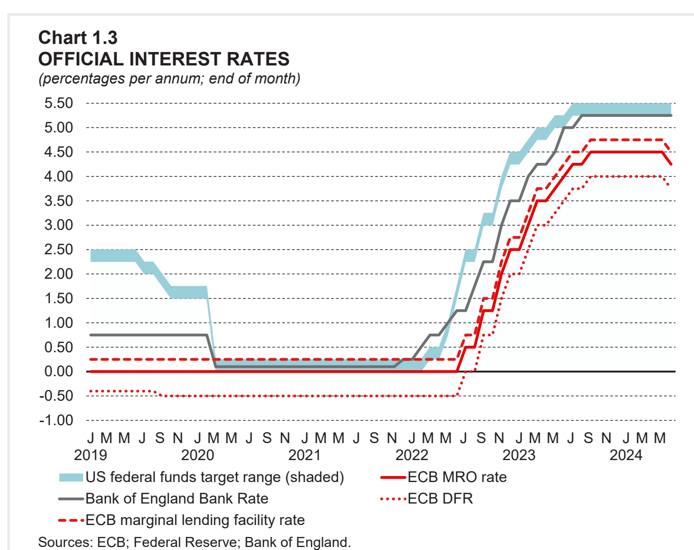
Real GDP in the United Kingdom grew at a quarterly rate of 0.5% in the review period, compared to 0.7% recorded in the first quarter (see Table 1.1). An expansion in inventories, increases in government and household consumption as well as higher business investment outweighed a more negative international trade balance, reflecting higher imports and lower exports.

Labour market conditions were largely stable during the quarter reviewed. The employment rate remained unchanged at 74.5%, on a quarterly-average basis, while the unemployment rate averaged 4.2% during the review period, compared to 4.3% in the previous quarter (see Chart 1.1).

Consumer price inflation in the United Kingdom continued to decline during the review period, with the annual rate falling from 3.2% in March to hit the Bank of England's 2.0% medium-term target in May. Inflation remained unchanged at 2.0% in June (see Chart 1.2). Inflation fell across the major components. Energy prices fell further during the quarter and did so at a faster pace than that recorded in the previous quarter. Thus, the annual rate of energy price inflation fell to -16.0% in June, compared to -12.7% three months before. The annual rate of change of prices of non-energy industrial products turned negative during the quarter, falling to -0.1% in June, compared to 1.5% in March. Although both food and services inflation continued to ease, falling to 3.0% and 5.7%, respectively in June, services inflation in particular remained high. The annual rate of inflation based on the CPI excluding energy, food, alcohol and tobacco fell to 3.5% in June, from 4.2% in March.

During the quarter under review, the Bank of England's Monetary Policy Committee (MPC) kept the Bank Rate unchanged at 5.25% (see Chart 1.3). The MPC considered that although the restrictive monetary policy stance was dampening inflationary pressures and key indicators of inflation persistence continued to moderate, they remained elevated.[2]

Chart 1.3
OFFICIAL INTEREST RATES
(percentages per annum; end of month)



Sources: ECB; Federal Reserve; Bank of England.

[1] On 18 September, the FOMC decided to lower the target range for the federal funds rate by 50 basis points to 4.75%-5.00% as inflation moved closer to target. The FOMC also reaffirmed that it would continue reducing its holdings of Treasury securities and agency debt and agency mortgage-backed securities.

[2] On 31 July 2024, the MPC reduced the Bank Rate by 25 basis points, to 5.0%. The MPC stated that the impact from past external shocks had abated and some progress was registered in moderating risks of persistence in inflation, while the restrictive stance of monetary policy was bearing down on inflationary pressures. However, the Committee reiterated that monetary policy needed to continue to remain restrictive for sufficiently long until the risks to inflation returning sustainably to the 2% target in the medium term would have dissipated further. Indeed, on 18 September, the MPC kept the Bank Rate unchanged.

The euro area

GDP in the euro area grows moderately

Economic activity in the euro area continued to recover modestly in the second quarter of 2024. In real terms, GDP rose by 0.2% on a quarter-on-quarter basis, compared to 0.3% recorded in the previous quarter (see Table 1.2). Growth was driven by the services sector, as activity in manufacturing and construction decreased, and occurred in the context of a continued improvement in global trade. Consumer confidence increased further but remained short of its long-term average despite unemployment being at historic lows and headline inflation having fallen significantly. Meanwhile, business sentiment indicators moved broadly sideways, with sentiment in industry below the long-term average.

In the second quarter, net exports contributed 0.5 percentage point to economic growth, as a rise in exports outweighed an increase in imports. In contrast, domestic demand deducted 0.3 percentage point from GDP growth. Investment fell sharply, leading to a negative contribution to GDP growth. This reflected a marked fall in Irish non-construction investment, but also a further decline in housing investment. Excluding developments in Irish non-construction investment, it is estimated that the contribution from domestic demand would be practically neutral. Private consumption expenditure and business inventories remained almost unchanged, while government consumption contributed 0.1 percentage point to GDP growth.

Table 1.2
CONTRIBUTIONS TO QUARTERLY REAL GDP GROWTH IN THE EURO AREA[(1)]
Percentage points; quarter-on-quarter percentage change

	2022			2023				2024	
	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
Private consumption	0.6	0.6	-0.5	0.1	0.2	0.1	0.0	0.2	0.0
Government consumption	0.0	-0.1	0.1	0.1	0.0	0.2	0.2	0.0	0.1
GFCF	0.0	0.2	0.0	0.1	0.0	0.0	0.2	-0.4	-0.5
Changes in inventories[(2)]	0.1	0.1	-0.1	-0.6	0.3	-0.4	-0.3	-0.3	0.0
Exports	1.0	0.7	0.2	-0.2	-0.6	-0.6	0.2	0.6	0.7
Imports	-0.8	-1.0	0.2	0.5	0.2	0.8	-0.2	0.3	-0.2
GDP	**0.9**	**0.5**	**-0.1**	**0.0**	**0.1**	**0.0**	**0.1**	**0.3**	**0.2**

Source: Eurostat.

(1) Data are seasonally and working day adjusted. Figures may not add up due to rounding.

(2) Including acquisitions less disposals of valuables.

Labour market remains strong

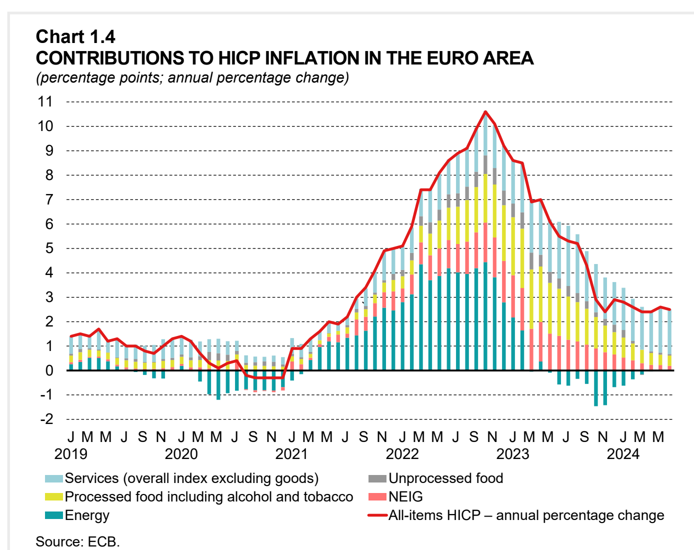
The labour market in the euro area remained robust during the second quarter. Indeed, employment continued to expand, growing at a quarterly rate of 0.2% during the review period, compared to 0.3% in the preceding quarter.[3] Meanwhile, the seasonally adjusted unemployment rate stood at 6.5% in June, the same as three months before, also averaging 6.5% in the quarter under review (see Chart 1.1).

Inflation rises marginally

After having abated notably since around mid-2023, inflation in the euro area picked up again in the second quarter. The annual rate of inflation based on the HICP stood at 2.5% in June, up

[3] Employment data refer to the national accounts, total employment domestic concept. Data are seasonally and calendar adjusted.

from 2.4% three months before (see Chart 1.4). The increase in overall inflation reflected a rebound in energy prices and in the prices of unprocessed food, coupled with slightly faster growth in services prices. On the other hand, slower growth in the prices of processed food and in non-energy industrial goods (NEIG) inflation mitigated the increase in overall inflation.



Turning to the major HICP components in more detail, energy prices rose at an annual rate of 0.2% in June 2024, as against a drop of 1.8% in March. Similarly, unprocessed food prices increased at an annual rate of 1.3% in June, in contrast to a decrease of 0.5% in March. The annual rate of change of services prices edged up to 4.1% in June, from 4.0% three months earlier. On the other hand, processed food inflation (including alcohol and tobacco) eased to 2.7% over the review period, compared to 3.5% in March. Also, the annual rate of NEIG inflation slowed down to 0.7% in June, compared to 1.1% three months earlier.

Underlying inflationary pressures stabilised during the review period. HICP inflation excluding energy and food eased in April but intensified in the following month so that the annual rate stood at 2.9% in June, the same as in March.

Real GDP expected to expand further, inflation projected to continue easing

According to the ECB staff macroeconomic projections, published in September 2024, real GDP growth in the euro area is estimated to increase to 0.8% in 2024. Real GDP is then expected to expand further by 1.3% and 1.5% in 2025 and 2026, respectively (see Table 1.3). Although the

Table 1.3
MACROECONOMIC PROJECTIONS FOR THE EURO AREA[(1)]
Annual percentage changes

	2023	2024	2025	2026
GDP	**0.5**	**0.8**	**1.3**	**1.5**
Private consumption	0.7	0.8	1.4	1.5
Government consumption	1.0	1.2	1.1	1.1
GFCF	1.2	-0.5	1.2	2.1
Exports	-0.3	1.2	2.6	3.0
Imports	-1.1	0.0	2.8	3.3
HICP	**5.4**	**2.5**	**2.2**	**1.9**
HICP excluding energy and food	4.9	2.9	2.3	2.0

Source: ECB.
[(1)] ECB staff macroeconomic projections (September 2024).

latest economic indicators suggest below-expectations growth in the euro area in the short term, ECB staff foresee a consumption-driven economic recovery. A continued rise in real disposable income and a gradual increase in confidence are expected to support this recovery. Over the medium term, the recovery would also be underpinned by the gradual dissipation of the impact from the ECB's monetary policy tightening, a likely continued easing of financial conditions and an expected rise in foreign demand. Meanwhile, the labour market is expected to remain resilient, while the unemployment rate will likely stay at historically low levels. Against this background, real GDP is expected to expand at rates similar to historical averages.

Compared to the June 2024 projections, the latest projections are conditioned on lower commodity prices (though some energy prices are higher), a stronger euro as well as slightly lower short-term interest rates and long-term sovereign bond yields. Real GDP growth is revised downwards by 0.1 percentage point for 2024, 2025 and 2026, respectively. The downward revision to the 2024 forecast mainly reflects lower private consumption and investment as well as slower export growth in light of ongoing competitiveness issues. The downward revision for 2025 reflects the effects of the revisions to the growth profile in the second half of 2024, which carry over into the following year. For 2026, the change mainly reflects downward revisions to both private consumption growth and the contribution from net trade.

Turning to the outlook for prices, ECB staff foresee HICP inflation to decline from 5.4% in 2023 to an average of 2.5% in 2024 and to ease further to 2.2% and 1.9% in 2025 and 2026, respectively. Following its recent moderation, HICP inflation is expected to rebound somewhat in the fourth quarter of 2024, before declining further to the ECB's 2% target by the end of 2025, in line with the June 2024 projections. The expected rebound in the near term largely reflects energy base effects. Over the medium term, however, energy inflation is expected to settle at low positive rates in the context of market expectations for energy prices as well as planned climate-change related fiscal measures. After progressively declining until July 2024, food inflation is expected to remain largely unchanged in the near term. It is then expected to fall modestly, reflecting moderate developments in input costs.

HICP inflation excluding energy and food is expected to remain above headline inflation for almost the entire projection horizon. Nevertheless, it is also expected to continue moderating gradually from an average of 4.9% in 2023 to 2.9% in 2024 and further to 2.3% and 2.0% in 2025 and 2026, respectively. Although services inflation has remained persistently high over recent months, a gradual decline is still expected later in the horizon as wage growth and other cost pressures will likely ease, while past monetary policy tightening measures continue to exert downward pressure on consumer prices.

Compared to the June 2024 projections, the outlook for HICP inflation remains unchanged. For 2024, an upward revision to underlying inflation is offset by a downward revision for energy and food. Underlying inflation projections are revised upwards by 0.1 percentage point for both 2024 and 2025, mainly on account of higher data outturns for services inflation. As from the second half of 2025, however, underlying inflation has been revised slightly downwards, mainly reflecting the downward revision of real GDP and wages as well as the downward impact from the appreciation of the euro. The underlying inflation projection for 2026 is unrevised.

ECB cuts interest rates

On 6 June, the Governing Council lowered the three key policy rates by 25 basis points since the inflation outlook had improved markedly, underlying inflation eased and monetary policy kept financing conditions restrictive. Accordingly, the interest rates on the deposit facility, the MROs and the marginal lending facility were decreased to 3.75%, 4.25% and 4.50%, respectively. This was the first adjustment in official interest rates since September 2023.

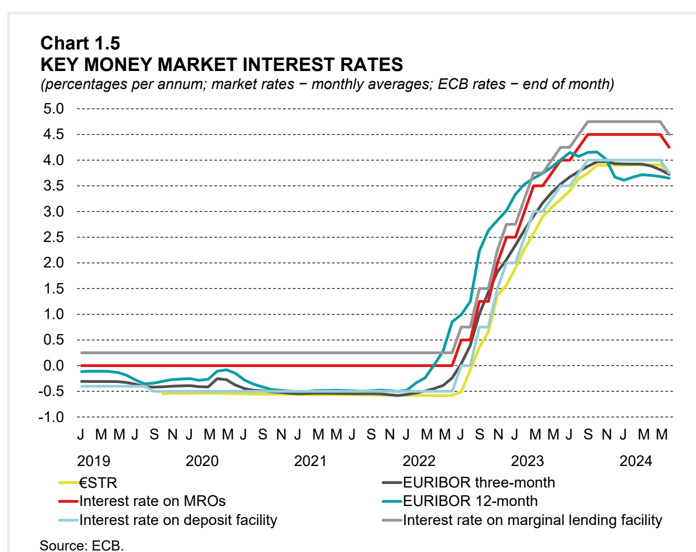
In light of persisting domestic price pressures, the Governing Council reiterated that it would keep policy rates sufficiently restrictive for as long as necessary to ensure that inflation would return to its 2% medium-term target in a timely manner. The Governing Council restated that it would continue to follow a data-dependent and meeting-by-meeting approach to determining the appropriate level and duration of restriction.

The Governing Council also confirmed that it would reduce the Eurosystem's holdings of securities under the PEPP by €7.5 billion per month, on average, over the second half of the year.[4]

Money market rates drop

Money market interest rates in the euro area tended to fall during the review period, reflecting market expectations of lower official interest rates. Hence, the euro short-term rate (€STR) averaged 3.75% in June, compared to 3.91% in March (see Chart 1.5).[5] The three-month euro interbank offered rate (EURIBOR) averaged 3.72% in June, as against 3.92% three months earlier. The 12-month EURIBOR averaged 3.65% in June, compared to 3.72% in March.[6] The 12-month EURIBOR thus remained below the DFR, indicating market players' expectations of further lowering of interest rates.

Chart 1.5
KEY MONEY MARKET INTEREST RATES
(percentages per annum; market rates − monthly averages; ECB rates − end of month)



Source: ECB.

Euro area government bond yields rise further

The euro area ten-year benchmark government bond yield rose further to 3.17% in June, compared to 2.95% three months earlier. This was mainly because market participants reassessed

[4] On 12 September, the Governing Council decided to lower the DFR – the rate through which it steers the monetary policy stance – by 25 basis points. Additionally, the spread between the DFR and the interest rate on the MROs was set at 15 basis points. By contrast, the spread between the rate on the marginal lending facility and the rate on the MROs was kept unchanged at 25 basis points. Accordingly, the DFR was decreased to 3.50% and the interest rates on the MROs and the marginal lending facility were decreased to 3.65% and 3.90%, respectively.

[5] The €STR is a reference rate based on money market data collected by the Eurosystem, reflecting the wholesale euro unsecured overnight borrowing costs of banks located in the euro area. The €STR is published on each T2 business day based on transactions conducted and settled on the previous T2 business day.

[6] The EURIBOR is an interest rate benchmark indicating the average rate at which principal European banks lend unsecured funds on the interbank market in euro for a given period.

their expectations about the timing and extent of official interest rate cuts in the United States, which spilled over to the euro area.

Individual sovereign bond yields rose to varying degrees in almost all euro area countries. In Germany, ten-year sovereign bond yields increased by 13 basis points to 2.48%. Yields went up by 33 basis points, to 3.15%, in France, while in Italy yields rebounded by 24 basis points, to 3.94%. Moreover, in Spain they rose by 16 basis points, to 3.35%. In all the remaining euro area jurisdictions (except Lithuania), yields were up, with increases ranging from 28 basis points in Estonia and Greece to just 4 basis points in Latvia.

Spreads between yields on the ten-year German bonds and those on the bonds issued by most of the other euro area jurisdictions widened. This applies particularly to spreads between German benchmark yields and those on French government bonds, which increased by 20 basis points to 67 basis points during the quarter, reflecting increased political uncertainty (see Chart 1.6).

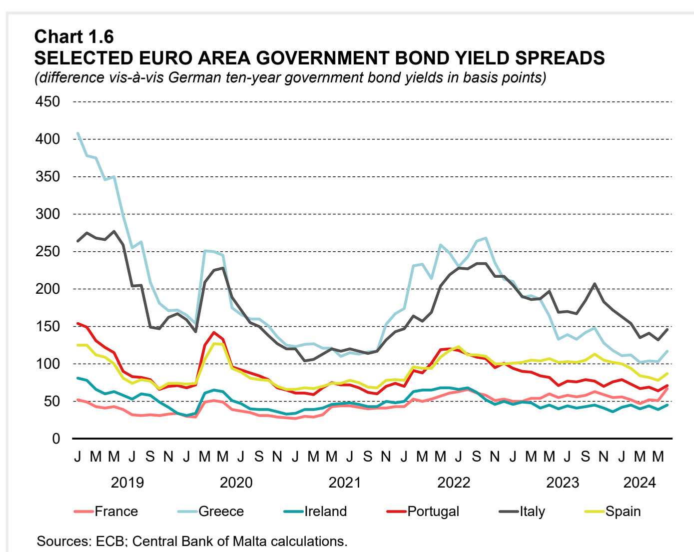


Chart 1.6
SELECTED EURO AREA GOVERNMENT BOND YIELD SPREADS
(difference vis-à-vis German ten-year government bond yields in basis points)

Sources: ECB; Central Bank of Malta calculations.

The euro falls versus the US dollar and in effective terms

During the second quarter of 2024, the euro depreciated by 1.0% against the US dollar, extending the losses recorded in the previous quarter (see Chart 1.7). Divergent economic fundamentals between the United States and the euro area, elevated geopolitical tensions as well as market expectations of a later start of monetary policy easing in the United States, supported the dollar. The single currency also depreciated by 1.0% versus the British pound mainly on account of economic-growth and interest-rate differentials between the United Kingdom and the euro area.

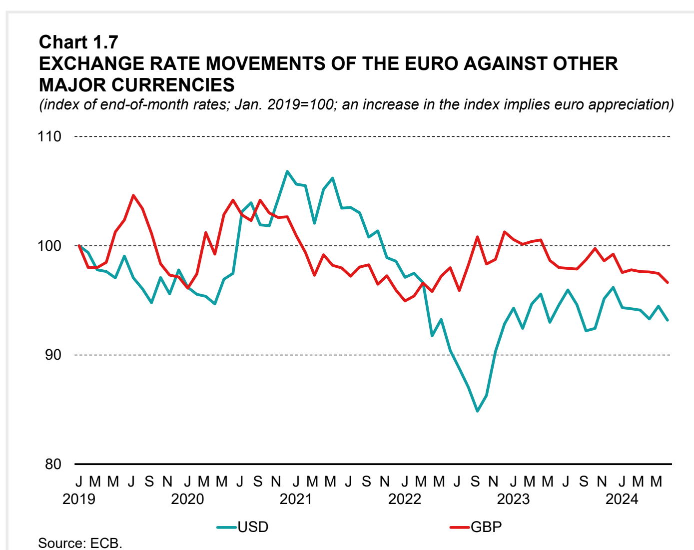


Chart 1.7
EXCHANGE RATE MOVEMENTS OF THE EURO AGAINST OTHER MAJOR CURRENCIES
(index of end-of-month rates; Jan. 2019=100; an increase in the index implies euro appreciation)

Source: ECB.

Furthermore, the euro also registered losses against the Australian dollar, the Czech koruna,

the Hong Kong dollar and the Norwegian krone. To a lesser degree, it also weakened against the Swiss franc and the Chinese renminbi.

On the other hand, the euro appreciated further against the Japanese yen as very low interest rates in Japan compared to other major jurisdictions continued to exert downward pressure on the Japanese unit. The euro was up also against the Korean won and rose slightly versus some other currencies such as the Polish zloty and the Canadian dollar.

Overall, the nominal effective exchange rate (EER) of the euro against the EER-18 group of countries declined by 0.5% between the end of March and the end of June 2024.[7]

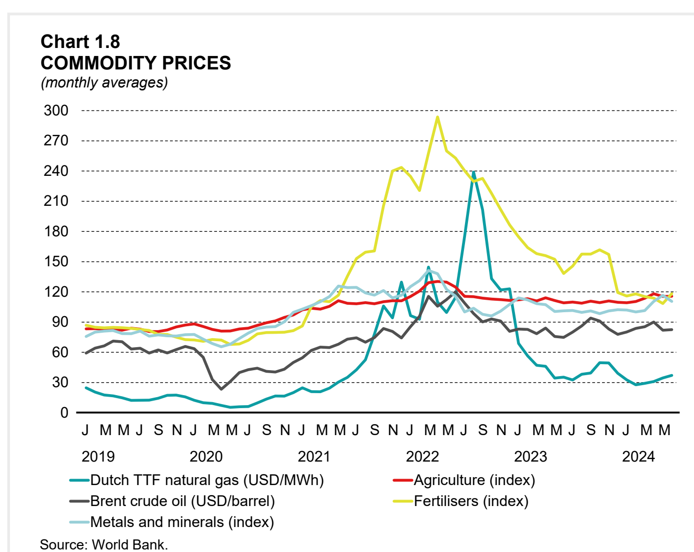
Commodities

Oil price drops but natural gas and other commodity prices rise during the quarter

Oil prices eased in the second quarter in the context of slowing growth in world oil demand and higher oil supply. The drop in oil prices was reinforced after the OPEC+ group of producer countries announced plans to gradually unwind last year's extra voluntary output cuts, starting in the fourth quarter 2024. The price of Brent crude oil averaged USD 82.6 per barrel in June, 3.4% lower than the level prevailing three months earlier. By contrast, the price of European natural gas rebounded in the quarter under review mainly on account of higher gas use in the power and industrial sectors and a tighter global market for liquified natural gas. The average price of Dutch TTF natural gas stood at USD 37.1 per megawatt hour in June, or 27.1% higher than in March (see Chart 1.8).

World Bank data show that non-energy commodity prices rose by 3.9% during the quarter under review. This reflected higher prices for metals and minerals, fertilizers and agricultural products. Meanwhile, prices of precious metals were up by 9.6%.

Chart 1.8
COMMODITY PRICES
(monthly averages)



Source: World Bank.

[7] The EER-18 is based on the weighted averages of the euro exchange rate against the currencies of Australia, Bulgaria, Canada, China, Czech Republic, Denmark, Hong Kong, Hungary, Japan, Norway, Poland, Romania, Singapore, South Korea, Sweden, Switzerland, the United Kingdom and the United States.

BOX 1: THE DEGREE OF SPILLOVERS FROM US TREASURIES TO THE EURO AREA GOVERNMENT BOND YIELDS INCLUDING THE MALTESE YIELD CURVE[1]

Introduction

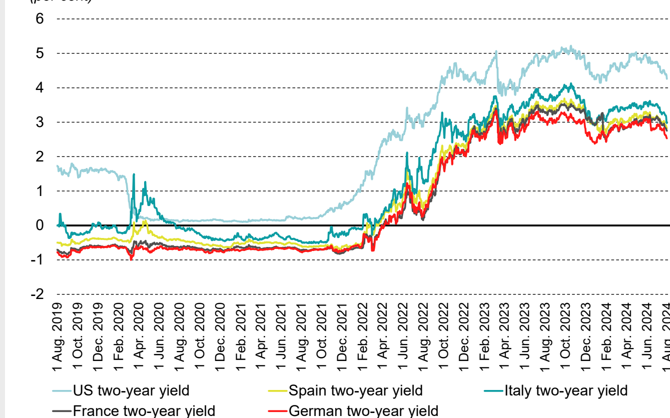
This box analyses the extent of spillovers from US Treasury yields to euro area sovereign bond yields, with particular focus on instances of very high and low correlation. It particularly focuses on the relationship between US Treasuries and the German sovereign bond market, with Germany being the benchmark for the euro area countries. Other major euro area government bond markets are also being referred to in this analysis. The indirect spillovers from the US Treasuries to the Maltese government bond yield curve, are also analysed hereunder.

Sovereign bond yield movements are usually driven by several factors. Due to the close interlinkages between markets globally, certain factors influencing yields in one jurisdiction tend to have spillover effects on another country's yields. This box studies the main factors driving the US and selected euro area government bond yields over the five-year period covering 1 August 2019 – 31 July 2024.

Over the period under review, sovereign bond yields were driven by different factors. These include, but are not limited to, the interest-rate decisions taken by major central banks, public comments made by central bank policymakers, the release of economic data and country specific factors.

Charts 1.1, 1.2 and 1.3 clearly show that yield movements across the two, five, and ten-year tenors for the United States and the selected euro area countries (Germany, France, Spain and Italy) moved in the same direction during the period under review. It can also be noted that between Q3 2019 and Q1 2022, the benchmark yields of Germany and other selected euro area countries, were in

Chart 1.1
TWO-YEAR US TREASURY AND SELECTED EURO AREA SOVEREIGN BOND YIELDS (1 AUGUST 2019 - 31 JULY 2024)
(per cent)



Source: Refinitiv.

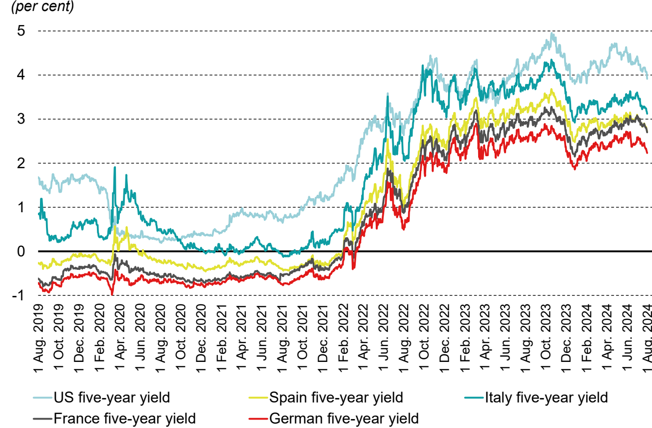
[1] Prepared by Ms Maria Dimech, Senior Market Analyst and Mr Audrin Tanti, Market Analyst, Market Analysis Office and Ms Maria Micallef, Assistant Executive, Government Securities Office and reviewed by Ms Josette Grech, Head, Monetary Operations and Government Securities Department and Mr André Psaila, Chief Officer, Financial Markets Division. The views expressed in the Box are the authors' own and do not necessarily reflect the views of the Bank.

negative territory whereas those in the United States remained positive.

Spillover from US Treasuries to euro area sovereign yields

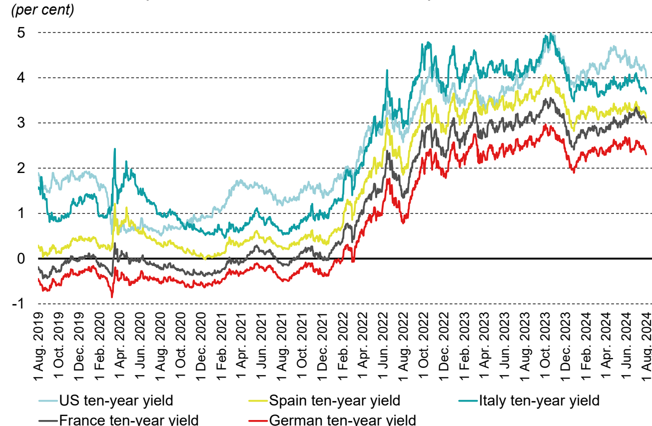
As shown in Charts 1.1, 1.2 and 1.3, during most of the review period, yields moved in tandem across the two continents. However, there were instances where the path of yields diverged somewhat. This may have been led by factors such as different central bank policies and the prevailing macroeconomic news emerging from the respective jurisdiction.

Chart 1.2
FIVE-YEAR US TREASURY AND SELECTED EURO AREA SOVEREIGN BOND YIELDS (1 AUGUST 2019 - 31 JULY 2024)
(per cent)



Source: Refinitiv.

Chart 1.3
TEN-YEAR US TREASURY AND SELECTED EURO AREA SOVEREIGN BOND YIELDS (1 AUGUST 2019 - 31 JULY 2024)
(per cent)



Source: Refinitiv.

The slowdown in economic activity due to disruptions in supply chains experienced in the euro area in 2021 may have been amongst the region-specific factors that contributed to this divergence in yields. Weak economic conditions led to an accommodative monetary policy by the ECB. Over this period, the ECB kept its three key interest rates at very low levels and intensified its open-market purchases of European sovereign bonds, further supporting bond prices and pressuring yields lower.

Apart from the adverse economic effects arising from the pandemic, another supply shock hit Europe when it was starting to recover from pandemic-related lockdowns. The Russian invasion of Ukraine brought about disruptions which unleashed cost-push inflation that resembled the 1970s OPEC-led oil crisis.

However, the timing of the monetary policy response by the respective central banks in these two jurisdictions was different. The Fed acted earlier than the ECB to try to curb

inflation pressures. In fact, the Fed hiked the range of the Fed Funds rate in March 2022, while the ECB acted in July of the same year.[2]

Against this background, the degree of spillover from yields in the US Treasury bond markets to yields in Eurozone government bond markets, was highest in 2022 as illustrated in Tables 1.1 to 1.4. This strong correlation was particularly evident for Germany, from Q1 2022 onwards,[3] as shown in Table 1.5.

Table 1.1
FULL-YEAR CORRELATION STATISTICS
Correlation between the two, five and ten-year yields on the US and DE benchmark bonds (1 August 2019 - 31 July 2024)
Annual data except for 2019 and 2024

	Correlation between two-year US and DE	Correlation between five-year US and DE	Correlation between ten-year US and DE
01/08/2019 - 31/12/2019	0.3833	0.8115	0.8851
2020	0.3819	0.4800	0.5059
2021	0.0467	0.6898	0.8159
2022	0.9586	0.9725	0.9831
2023	0.8481	0.7508	0.7842
01/01/2024 - 31/07/2024	0.8912	0.8308	0.8103

Sources: Refinitiv; Central Bank of Malta staff calculations.

Table 1.2
FULL-YEAR CORRELATION STATISTICS
Correlation between two-year yields of US treasuries and selected euro area bond yields (1 August 2019 - 31 July 2024)
Annual data except for 2019 and 2024

	Correlation between two-year US and DE	Correlation between two-year US and IT	Correlation between two-year US and ES	Correlation between two-year US and FR
01/08/2019 - 31/12/2019	0.3833	0.1245	0.4391	0.3865
2020	0.3819	-0.0885	0.0548	0.1203
2021	0.0467	0.5145	-0.6242	-0.5977
2022	0.9586	0.9576	0.9696	0.9572
2023	0.8481	0.8438	0.9191	0.9272
01/01/2024 - 31/07/2024	0.8912	0.9013	0.9070	0.4268

Sources: Refinitiv; Central Bank of Malta staff calculations.

Table 1.3
FULL-YEAR CORRELATION STATISTICS
Correlation between five- year yields of the US treasuries and selected euro area bond yields (1 August 2019 - 31 July 2024)
Annual data except for 2019 and 2024

	Correlation between five-year US and DE	Correlation between five-year US and IT	Correlation between five-year US and ES	Correlation between five-year US and FR
01/08/2019 - 31/12/2019	0.8115	0.1889	0.8126	0.7624
2020	0.4800	-0.0036	0.0428	0.3242
2021	0.6898	0.5671	0.4147	0.8230
2022	0.9725	0.9754	0.9755	0.9761
2023	0.7508	0.6972	0.8039	0.7823
01/01/2024 - 31/07/2024	0.8308	0.6843	0.7732	0.6798

Sources: Refinitiv; Central Bank of Malta staff calculations.

[2] The US headline CPI stood at 7.9% y/y in February 2022, whilst that in the Eurozone was 5.8% y/y. Even core inflation was higher in the United States. This justifies the Fed's intervention prior to that of the ECB.
[3] The correlation was low only in Q4 2022 during this period.

Table 1.4
FULL-YEAR CORRELATION STATISTICS

Correlation between ten-year yields of US treasuries and selected euro area bond yields (1 August 2019 - 31 July 2024)

Annual data except for 2019 and 2024

	Correlation between ten-year US and DE	Correlation between ten-year US and IT	Correlation between ten-year US and ES	Correlation between ten-year US and FR
01/08/2019 - 31/12/2019	0.8851	0.2964	0.8293	0.8593
2020	0.5059	-0.0862	-0.1799	0.1385
2021	0.8159	0.5928	0.8221	0.7546
2022	0.9831	0.9687	0.9768	0.9818
2023	0.7842	0.6869	0.7719	0.8035
01/01/2024 - 31/07/2024	0.8103	0.4293	0.6869	0.5436

Sources: Refinitiv; Central Bank of Malta staff calculations.

Table 1.5
QUARTERLY CORRELATION STATISTICS

Correlation between two, five and ten-year yields on the US and DE benchmark bonds (1 August 2019 - 31 July 2024)

Quarterly data

Period	Correlation between two-year US and DE	Correlation between five-year US and DE	Correlation between ten-year US and DE
01/08/2019 - 31/12/2019	0.3833	0.8115	0.8851
Q1 2020	0.6751	0.4966	0.6971
Q2 2020	0.4933	0.6487	0.7126
Q3 2020	0.5901	0.4941	0.5518
Q4 2020	-0.1016	0.1033	0.1092
Q1 2021	0.3687	0.7405	0.8939
Q2 2021	0.3391	-0.1312	-0.1250
Q3 2021	0.5350	0.7338	0.8375
Q4 2021	-0.0052	0.0810	0.7454
Q1 2022	0.7750	0.9330	0.9594
Q2 2022	0.9037	0.9299	0.9021
Q3 2022	0.9614	0.9755	0.9804
Q4 2022	-0.0044	0.1803	0.6213
Q1 2023	0.9126	0.9460	0.9377
Q2 2023	0.8787	0.7830	0.6668
Q3 2023	0.8909	0.7097	0.8804
Q4 2023	0.9778	0.9751	0.9790
Q1 2024	0.8926	0.8328	0.9062
Q2 2024	0.8289	0.8350	0.4951
01/01/2024 - 31/07/2024	0.8912	0.8308	0.8103

Sources: Refinitiv; Central Bank of Malta staff calculations.

From the beginning of March to end of Q3 2022, the yield on the ten-year US benchmark Treasury note rose by 211 basis points, with the German ten-year Bund yield rising by 218 basis points. The pronounced downward correction in yields in Q1 2024 was likely driven by the shift in market expectations that central banks would soon start cutting rates after an extended period of rate hikes. This broad shift in market participants' expectations likely led to a high correlation between yields in the United States and major euro area sovereign bond markets, especially evident in the two-year tenors.

Moreover, changes in fiscal stances by governments can also affect yields. For instance, in September 2022 the United Kingdom elected a new government and announced an aggressive tax plan. The new tax reduction plan was not substituted by other sources of government revenue. Investors thought that this would weigh on the debt sustainability of the country. Consequently, in October 2022 long-dated UK gilts sold off triggering a spill-over to European bond yields.

Other factors which can affect bond yields are specific banking turmoil such as the case of the Silicon Valley bank and Signature bank in March 2023. These two American banks collapsed as they held too much long-term debt in their portfolio. In a rising interest rate environment, these banks held more long-dated than short maturity bonds on their balance sheets. In turn, they both suffered significant losses and failed. In this environment, investors opted for safer securities like government bonds rather than corporate bonds. The higher demand for government bonds led to an increase in their prices and yields falling across the board, both in the United States and in selected euro area government bond markets.[4]

During Q1 2023, the correlation of the two, five and ten-year US and German bond yields was high as shown in Table 1.5 and remained elevated for the rest of the year. This episode, highlighted that the degree of spillover from US bond yields to European peers, remained strong especially during a financially stressful environment, as the safe haven characteristics of markets in both regions dominated.

Moreover, there are cases where other exogenous factors drove yields across both continents. One of these instances, is a change in monetary policy in countries other than the United States. The recent change in the Yield Curve Control policy by the Bank of Japan, impacted yields in the United States and the Eurozone in a similar way.

However, within the euro area, country-specific factors may also limit the correlation between sovereign yields in that country relative to the United States. For instance, political instability triggered by snap elections in countries like Italy (September 2022), Spain (May 2023), and France (July 2024) led to a temporary divergence in the direction of US Treasury yields versus these specific countries. The correlation may also be limited by divergent fiscal paths across these countries, taking into account debt sustainability considerations.

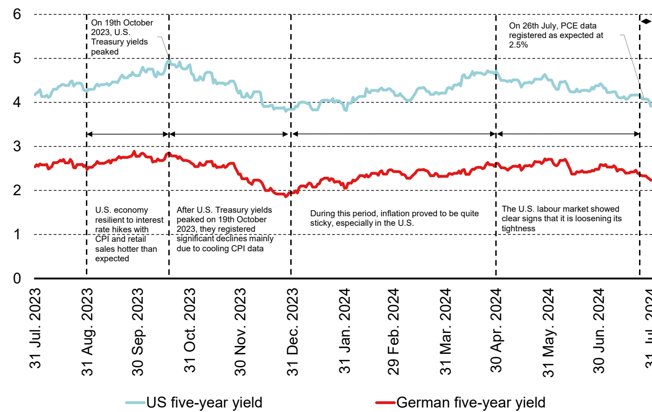
Episodes depicting spillovers from US Treasuries to German sovereign bonds

This section takes the one-year period 31 July 2023 till 31 July 2024 and delves into further detail on the spillover effect from five-year US Treasuries to their euro area counterpart. In this part, episodes that accentuate this spillover effect are examined. It is worth noting that the most significant movements in yields throughout this period can be explained by inflation releases and monetary policy response.

[4] Credit Suisse also failed during the same period of the collapse of the two American banks. This brought a sharp drop in euro area bond yields due to a plunge in European banking stocks which directed investment flows towards safer assets such as government bonds.

As highlighted in Chart 1.4, until October 2023 the US economy was quite resilient to interest rate hikes adopted by the Fed which cumulatively amounted to 525 basis points.

Chart 1.4
US AND GERMAN FIVE-YEAR SOVEREIGN BOND YIELDS (31 JULY 2023 - 31 JULY 2024)
(per cent)



Source: Refinitiv.

During the period 31 August – 19 October 2023, US Treasury yields rose significantly. This was mainly due to higher US CPI and retail sales data. In turn, European government bond markets also exhibited a rise in yields. In this period, the yield on the five-year US Treasury rose by 70 basis points while that of the German counterpart, increased by 37 basis points.

Between 19 October (when yields peaked) till end December 2023, yields on US government bonds registered significant declines, a move which was triggered by the release of the October 2023 CPI data. This showed that the US CPI remained unchanged from the previous month and that US inflation had possibly peaked. In turn, Fed policymakers' tone turned dovish with markets moving, from pricing in another rate increase, to no further hikes during the two remaining FOMC meetings for 2023. In Europe, however, inflation was also showing signs of easing with the annual consumer price growth slowing in all categories. In November, Germany's HICP stood at 2.3%, the lowest level in more than two years.[5] Thus, during this interval, the spillover from the US market might have been more limited due to softening of inflationary pressures in the euro area. The yield on the five-year US Treasury declined by 111 basis points while that of the German five-year, declined by 91 basis points during this period.

The following period under review, which is from 1 January till 30 April 2024, inflation figures from the United States turned out to be quite sticky mainly driven by housing rents. On the other hand, in Europe, the headline inflation was stable at 2.4%, year on year. Still, during this period, the yield on the five-year US Treasury rose by 88 basis points whereas that of the German five-year bond, increased by 67 basis points. Thus, the spillover on the European market was quite evident even as inflation remained stable in Europe while that in the United States came in higher for three consecutive months.

Between 1 May and 31 July 2024, the US labour market conditions eased. In the United States, the unemployment rate rose to 4.3% while in Europe, it was at 6.4%. At the same time, euro area inflation ticked up by 0.1%. When comparing the drop in yields of the

[5] That was down from 3% a month earlier, and from a peak of 11.6% a year before.

five-year benchmark across the two continents, one can notice again that the magnitude of the decline in yields in the United States was larger when compared to that of the German counterpart, with the former declining by 74 basis points while in the latter dropping by 38 basis points.

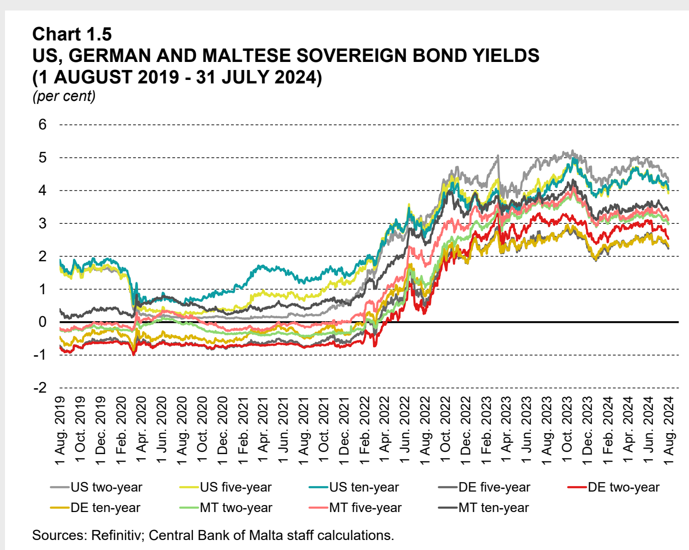
Spillover on Maltese sovereign yields

Maltese government bond yields are usually benchmarked against a group of euro area jurisdictions. Hence, it is understandable that spillover effects from the US Treasury market on the German government bond market also indirectly impact the Maltese sovereign yields. Chart 1.5 shows that the Maltese government bond yields[6] followed their euro area counterparts over the period under review. In fact, Maltese yields dropped during the COVID-19 period, between March 2020 and March 2022. As from May 2022, when major central banks started hiking rates in response to elevated inflation rates, yields followed an upward trend.

Bond yields remained at elevated levels throughout 2023 as central banks continued their aggressive interest-rate hiking policies. The following year, bond yields experienced significant fluctuations, mainly driven by shifting market expectations for policy rate cuts by the Fed and the ECB following weak economic data and mixed inflation readings.

The spillover effect from the US Treasury market to the Maltese sovereign bond market is analysed through the correlation coefficients of the two, five and ten-year benchmark yields of the bund and Maltese government bond yields. Table 1.6, shows the annual correlation coefficients for all benchmark tenors. Results show that the correlation was substantially high during the years under review, except for the year 2020 and some quarters in 2021,[7] which were comparatively low, as both countries were impacted by an exogenous shock (COVID-19 pandemic). The same pattern was observed in Table 1.7 where quarterly correlation coefficients were computed.

Chart 1.5
US, GERMAN AND MALTESE SOVEREIGN BOND YIELDS
(1 AUGUST 2019 - 31 JULY 2024)
(per cent)



Sources: Refinitiv; Central Bank of Malta staff calculations.

[6] Two, five, ten-year MT yields are an average of the qualifying two, five, ten-year bonds for each year.

[7] The Maltese economy is a more open economy than the United States. During this period, it may have been more directly hit by supply chain disruptions.

Table 1.6
FULL-YEAR CORRELATION STATISTICS

Correlation between the two, five and ten-year yields for the German and MT benchmark bond yields during the period 1 August 2019 - 31 July 2024

Annual data except for 2019 and 2024

	Correlation between two-year DE and MT	Correlation between five-year DE and MT	Correlation between ten-year DE and MT
All years	0.99572664	0.99487501	0.99269990
01/08/2019 - 31/12/2019	0.83635561	0.93793425	0.92313774
03/01/2020 - 31/12/2020	0.35963195	0.39031043	0.40337542
03/01/2021 - 31/12/2021	0.52020031	0.65790602	0.73258974
03/01/2022 - 31/12/2022	0.98637058	0.97968036	0.98019079
03/01/2023 - 31/12/2023	0.85923852	0.87295991	0.94336637
01/01/2024 - 31/07/2024	0.72387914	0.79219300	0.81361860

Source: Central Bank of Malta staff calculations.

TABLE 1.7
QUARTERLY CORRELATION STATISTICS

Correlation between two, five and ten-year yields on the US and MT benchmark bond yields during the period 1 August 2019 - 31 July 2024

Quarterly data

	Correlation between two-year DE and MT	Correlation between five-year DE and MT	Correlation between ten-year DE and MT
Q1 2020	-0.00656960	0.62347608	0.58615558
Q2 2020	0.15205669	0.19161164	0.23582492
Q3 2020	0.59409673	0.57643006	0.62691025
Q4 2020	0.12187141	-0.02535046	0.28818373
Q1 2021	0.12313379	0.46036355	0.84737795
Q2 2021	0.85881848	0.75845442	0.91554332
Q3 2021	0.89076587	0.93436787	0.89750903
Q4 2021	0.32289616	0.44004870	0.82903837
Q1 2022	0.91651539	0.93690709	0.93737825
Q2 2022	0.96240781	0.96758613	0.97290248
Q3 2022	0.97361183	0.97962623	0.97748965
Q4 2022	0.94875484	0.88927356	0.85114273
Q1 2023	0.87059182	0.79610148	0.78851305
Q2 2023	0.91593320	0.83875999	0.80829819
Q3 2023	0.90510566	0.88798076	0.92259289
Q4 2023	0.97148714	0.98162258	0.98696633
Q1 2024	0.57952747	0.63238517	0.73408331
Q2 2024	0.54310866	0.73863375	0.68890891

Source: Central Bank of Malta staff calculations.

Concluding remarks

Overall, it can be noted that there have been instances when the correlation between US and European bond markets was rather high. This analysis shows that the correlation tends to be greater if central bank policy direction and shocks in both countries are similar. For instance, this was particularly evident during 2022, when central bank policy across major central banks was restrictive in order to try to address high inflation. More recently, expectations for the two major central banks to start their rate cutting cycle have likely re-strengthened the correlation between yields in both regions, particularly in the short end of the yield curve. It is also quite evident that the release of macroeconomic data in the United States can lead to differing degrees of spillovers onto the European government bond market. On the other hand, country idiosyncratic factors such as political instability, banking turmoil and instances of severe market distress may limit the correlation among the jurisdictions examined.

2. OUTPUT AND EMPLOYMENT

Annual real GDP growth rose by 4.4% in the second quarter of 2024, following a 7.6% increase in the previous quarter. Growth was mainly driven by net exports, as the contribution of domestic demand, while still positive, was smaller. When adjusting for imports, exports remained the main driver of GDP growth.

Sectoral data show that the expansion in output was primarily driven by the services sector. GVA also rose slightly in the manufacturing and construction sectors. Growth in the GDP deflator moderated, mostly reflecting a year-on-year decline in unit profits, albeit from a high level.

During the second quarter of 2024, developments in the labour market remained positive. The unemployment rate remained low and well below that in the euro area.

The labour market remained tight. The number of job vacancies increased by slightly less than 14% when compared to the second quarter of 2023. Meanwhile, the job vacancy rate and the labour tightness indicator, which is the ratio of the job vacancy rate to the unemployment rate, declined slightly but remained high in relation to recent outcomes.

Potential output and Business Conditions Index

Potential output grows at a slower rate

The Bank estimates that potential output growth stood at 5.4% in the second quarter of 2024, below that of 6.1% estimated for the first quarter of 2024.

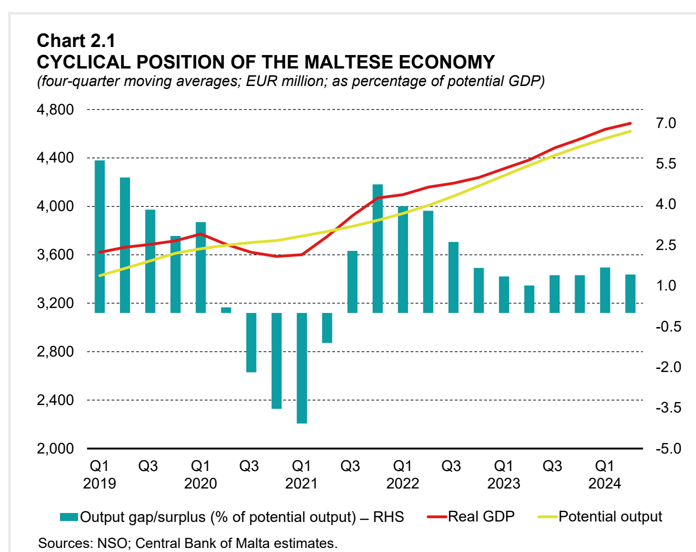
On a four-quarter moving average basis, the level increase in potential output relative to the previous quarter was stronger than that in GDP, resulting into a slightly smaller positive output gap. The latter is estimated at 1.4%, down from 1.7% in the first quarter of 2024 (see Chart 2.1).

This implies a slight easing in the degree of over-utilisation of the economy's productive capacity.

BCI suggests growth is reverting to historical average

The Bank's BCI continued to edge down in the second quarter of 2024 and is in line with its historical average (see Chart 2.2).[1] This partly reflects GDP

Chart 2.1
CYCLICAL POSITION OF THE MALTESE ECONOMY
(four-quarter moving averages; EUR million; as percentage of potential GDP)



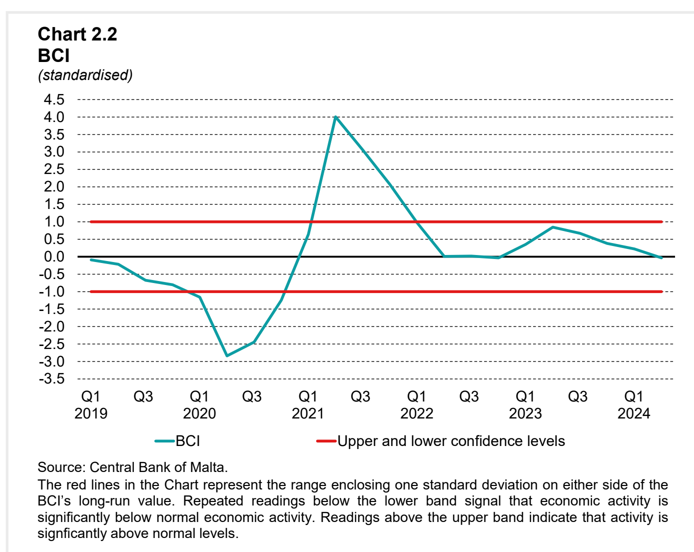
Sources: NSO; Central Bank of Malta estimates.

[1] The BCI is a synthetic indicator, which includes information from a number of economic variables such as the term structure of interest rates, industrial production, an indicator for the services sector, economic sentiment, tax revenues and private sector credit. By construction, it has an average value of zero over the estimation period since 2000. A full time series can be found at In-House Economic Indicators section on the website. For further details on the methodology underlying the BCI, see Ellul, R., (2016), "A real-time measure of business conditions in Malta," *Working Paper* 04/2016, Central Bank of Malta.

growth which was broadly in line with its long run average.

During the quarter under review, the BCI was affected by below-average growth in several sub-components, particularly by year-on-year declines in the issuance of development permits for residential buildings and in the ESI. Additionally, although there has been a strong year-on-year increase in inbound tourism, this was lower than that observed in the last two years which featured a recovery from the COVID-19 pandemic. These developments were partly offset by above-average growth in credit, in tax receipts, and industrial production. The contrasting developments of these indicators brought the BCI around its long-term average.

Chart 2.2
BCI
(standardised)



Source: Central Bank of Malta.
The red lines in the Chart represent the range enclosing one standard deviation on either side of the BCI's long-run value. Repeated readings below the lower band signal that economic activity is significantly below normal economic activity. Readings above the upper band indicate that activity is signficantly above normal levels.

GDP and industrial production

Real GDP growth largely driven by net exports

Real GDP rose by 4.4% on an annual basis, following a 7.6% increase in the previous quarter.[2] This mainly reflects a, a smaller contribution from domestic demand, although that of net exports also decreased (see Table 2.1).

Domestic demand growth moderated compared with its performance in the first quarter of the year. It rose by an annual 2.5% in the second quarter of 2024, following an increase of 5.8% in the previous quarter. The increase in domestic demand was largely driven by private consumption, and to a lesser extent gross fixed capital formation (GFCF). By contrast, the contribution of government consumption turned negative. Overall, domestic demand added 2.1 percentage points to GDP growth in the quarter under review.

Private consumption expenditure increased by an annual 4.1% in the second quarter of 2024, following a 6.4% increase in the previous quarter. Despite the recent slowdown, private consumption remained the key driver of domestic demand, adding 1.8 percentage points to real GDP growth in the quarter under review.

Data on the Classification of Individual Consumption by Purpose (COICOP) show that the strongest increase in absolute terms was recorded in spending on restaurants and accommodation services. This was followed by higher spending on insurance and financial services, information and communication, and transport. Most other COICOP categories of spending also show increases. On the other hand, spending on housing and utilities as well as spending on furnishings, household equipment and routine household maintenance declined.

[2] The analysis of GDP in this chapter of the *Quarterly Review* is based on NSO *News Release* 159/2024, which was published on 28 August 2024.

Table 2.1
GDP[1]

	2023			2024	
	Q2	Q3	Q4	Q1	Q2
	Annual percentage changes				
Private final consumption expenditure	11.0	10.6	11.4	6.4	4.1
Government final consumption expenditure	-1.2	4.7	7.2	2.2	-1.6
GFCF	-15.5	-22.3	-22.4	7.8	2.1
Domestic demand	**1.1**	**0.2**	**0.2**	**5.8**	**2.5**
Exports of goods and services	4.6	2.4	4.5	8.5	5.2
Imports of goods and services	0.0	-4.6	-0.7	7.3	3.9
GDP	**6.9**	**8.9**	**6.7**	**7.6**	**4.4**
	Percentage point contributions				
Private final consumption expenditure	4.8	4.8	5.0	2.9	1.8
Government final consumption expenditure	-0.2	0.8	1.3	0.4	-0.3
GFCF	-3.7	-5.3	-6.1	1.4	0.4
Changes in inventories	0.1	-0.1	0.0	0.0	0.1
Domestic demand	**1.0**	**0.2**	**0.2**	**4.8**	**2.1**
Exports of goods and services	5.9	3.1	5.7	10.5	6.4
Imports of goods and services	0.0	5.6	0.8	-7.6	-4.1
Net exports	**5.9**	**8.7**	**6.5**	**2.9**	**2.3**
GDP	**6.9**	**8.9**	**6.7**	**7.6**	**4.4**

Sources: NSO; Central Bank of Malta calculations.

[1] Chain-linked volumes, reference year 2020.

COICOP data measure domestic consumption and thus, include the expenditure of non-residents in Malta while excluding the expenditure of Maltese residents abroad. Certain COICOP categories continued to be supported by a strong increase in non-residents expenditure in Malta. Nonetheless, the expenditure of Maltese residents in Malta also rose significantly. Meanwhile, the expenditure of Maltese residents abroad also increased on its year-ago level, partly reflecting an increase in trips over the same period.

Government consumption expenditure declined by 1.6% in annual terms, following an increase of 2.2% in the first quarter of 2024. While outlays on compensation of employees and to a lesser extent intermediate consumption increased, these were offset by a significant increase in revenue from sales, which is netted out of consumption expenditure. Furthermore, expenditure on social benefits in kind decreased.

Real GFCF increased by 2.1% in the second quarter of 2024, following an increase of 7.8% in the previous quarter. The latter increase mostly reflected higher outlays on intellectual property and growth in residential investment. In absolute terms, pending on non-residential construction and cultivated biological resources rose marginally while outlays on machinery and equipment decreased. GFCF contributed 0.4 percentage point to overall growth.

The contribution of changes in inventories in the second quarter of 2024 was marginally positive.

Table 2.2
IMPORT-ADJUSTED CONTRIBUTIONS TO GDP GROWTH[(1)]

	2023			2024	
	Q2	Q3	Q4	Q1	Q2
	Percentage point contributions				
Private final consumption expenditure	3.4	4.0	3.5	1.9	1.3
Government final consumption expenditure	-0.1	0.8	1.1	0.3	-0.2
GFCF	-1.1	-1.4	-2.0	0.7	0.2
Changes in inventories	-0.1	-0.2	-0.2	0.0	0.0
Domestic demand	**2.1**	**3.1**	**2.5**	**2.9**	**1.3**
Exports of goods and services	**4.7**	**5.9**	**4.3**	**4.7**	**3.1**
GDP	**6.9**	**8.9**	**6.7**	**7.6**	**4.4**

Source: Central Bank of Malta estimates.
[(1)] Chain-linked volumes, reference year 2020.

Imports grew by 3.9%, while exports increased by 5.2% on a year earlier. As a result, net exports increased, adding 2.3 percentage points to annual real GDP growth. The increase in net exports reflected a larger surplus from trade in services as the deficit from trade in goods widened.

The contributions shown in Table 2.1 are consistent with the approach normally followed in official databases and economic publications. However, they do not account for the variation in import content across different expenditure components and thus, fail to represent the true underlying relative contribution of domestic and external demand to economic growth.

Table 2.2 presents import-adjusted contributions, which address this limitation by apportioning imports to the respective demand components.[3]

As in the traditional approach, import-adjusted contributions continued to show that exports remained the main contributor to real GDP growth in the second quarter of 2024.

When adjusting for import content, both domestic demand and exports retained a positive contribution to GDP growth. However, the superior contribution of the external trade component relative to domestic demand is amplified in this approach. Private consumption remains the largest contributor to growth within domestic demand.

Services remain the main driver of economic growth[4]

Data based on the output approach show that in the second quarter of 2024, nominal GVA rose by 5.2% in annual terms, following a 10.3% increase in the previous quarter. It added 4.9 percentage points to GDP growth (see Table 2.3).[5]

Services remained the main driver behind the latest economic expansion, adding 4.7 percentage points to nominal GDP growth. The sectors behind most of this increase are those comprising professional, scientific, administrative and related activities and public administration and related

[3] The process with which components are adjusted is currently being reviewed to consider the August 2024 benchmark revision to the national accounts.
[4] This analysis is based on nominal GVA data, unlike in previous Quarterly Review publications where real data was used. The latter was unavailable by the statistical cut-off date.
[5] The difference between GDP and GVA is made up of taxes on products, net of subsidies.

Table 2.3
CONTRIBUTION OF SECTORAL GVA TO NOMINAL GDP GROWTH
Percentage points

	2023			2024	
	Q2	Q3	Q4	Q1	Q2
Agriculture, forestry and fishing	-0.1	-0.1	0.1	0.0	-0.2
Mining and quarrying; utilities	1.5	0.4	0.9	0.2	0.2
Manufacturing	0.8	0.4	0.4	0.5	0.6
Construction	0.2	0.4	0.5	0.6	0.3
Services	12.2	10.8	9.7	8.9	4.7
of which:					
Wholesale and retail trade; repair of motor vehicles; transportation; accommodation and related activities	2.7	0.5	0.7	1.6	0.3
Information and communication	0.3	0.4	0.3	0.1	0.0
Financial and insurance activities	2.4	2.2	1.7	1.4	0.7
Real estate activities	2.4	2.8	2.5	1.6	1.0
Professional, scientific, administrative and related activities	3.2	2.7	2.9	2.4	1.2
Public administration and defence; education; health and related activities	0.7	1.1	1.2	1.2	1.1
Arts, entertainment; household repair and related services	0.5	1.0	0.4	0.4	0.5
GVA	**13.8**	**11.6**	**11.1**	**9.6**	**4.9**
Taxes less subsidies on products	**-1.1**	**3.2**	**0.7**	**2.2**	**2.7**
Annual nominal GDP growth (%)	**12.7**	**14.8**	**11.8**	**11.8**	**7.6**

Source: NSO.

activities, which contributed 1.2 and 1.1 percentage points, respectively. The sector comprising real estate activities added a further 1.0 percentage point, while the financial and insurance sector contributed 0.7 percentage point to nominal GDP growth. The remaining services sectors together added another 0.8 percentage point to growth.

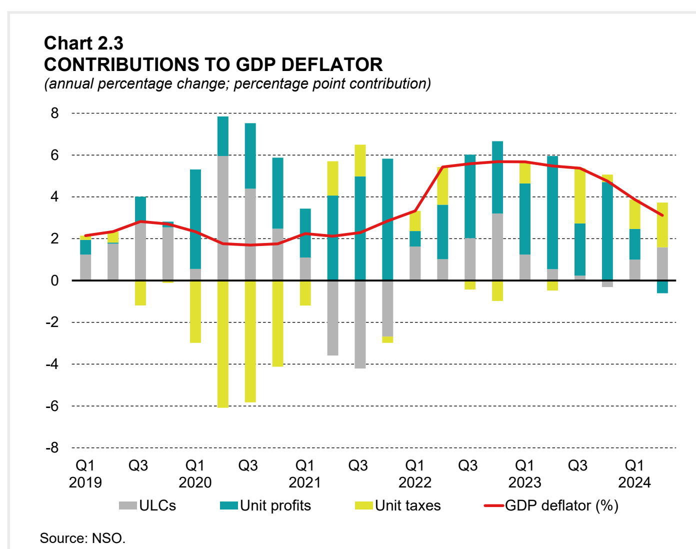
The manufacturing sector added 0.6 percentage point to growth, while the construction sector added 0.3 percentage point.

Net taxes on products increased on a year earlier.

Nominal GDP growth remains strong

Nominal GDP rose by 7.6% in annual terms in the second quarter of 2024, after increasing by 11.8% in the previous quarter. All components from the income side – compensation of employees, operating surplus and net taxes rose in annual terms. Nevertheless, the contributions of gross operating surplus moderated significantly. Although compensation of employees also slowed down, the decrease in its contribution was more limited. Hence, the slowdown in nominal GDP was mostly driven by weaker growth in operating surplus.

Chart 2.3 shows the main contributors to growth in the GDP deflator. Annual growth in the GDP deflator moderated. However, it remained elevated from a historical perspective. It stood at 3.1% in the second quarter of 2024, having decreased from the previous quarter's 3.9%.



The contribution of unit labour costs (ULCs) and unit taxes exhibited a larger positive increase. Meanwhile, the contribution of unit profits decreased, turning negative in the second quarter of 2024. Unit profits showed the first year-on-year decrease since 2018, although their level remains high from a historical perspective.

Industrial production increases following a contraction in previous quarter

Industrial production rose at an annual rate of 3.9% in the second quarter of 2024, following a contraction of 2.4% in the first quarter.[6]

Production in the manufacturing sector increased at an annual rate of 5.3%, after contracting by 1.8% in the preceding quarter. During the quarter under review production in the quarrying sector moderated. Annual growth stood at 1.2% in the second quarter of 2024 compared to 16.0% in the preceding quarter. Meanwhile, in the energy sector, production contracted at a faster pace. The rate of decline stood at 18.1% compared with 12.5% in the first quarter of 2024.[7]

In the manufacturing sector, output increased sharply among firms classified in 'other manufacturing' – which includes firms that produce medical and dental instruments – as well as among firms that manufacture furniture, rubber, plastic products and textiles. Significant increases were also recorded among firms involved in the production of machinery and equipment, wood products and paper products. Production of computer, electronic and optical products as well as food products also increased.

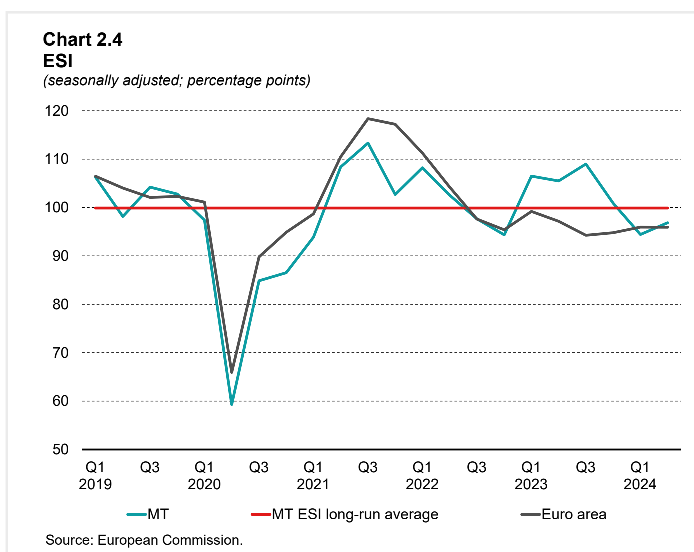
By contrast, output fell markedly among firms involved in the printing and reproduction of recorded media. Smaller declines were recorded in selected other sectors, including those that manufacture chemicals and basic pharmaceutical products.

[6] Methodological differences may account for divergences between developments in GVA in the manufacturing sector and industrial production. GVA nets input costs from output to arrive at value added and is expressed in nominal terms. Industrial production is a measure of the volume of output and takes no account of input costs. The sectoral coverage between the two measures also differs since industrial production data also include the output of the energy and quarrying sectors.

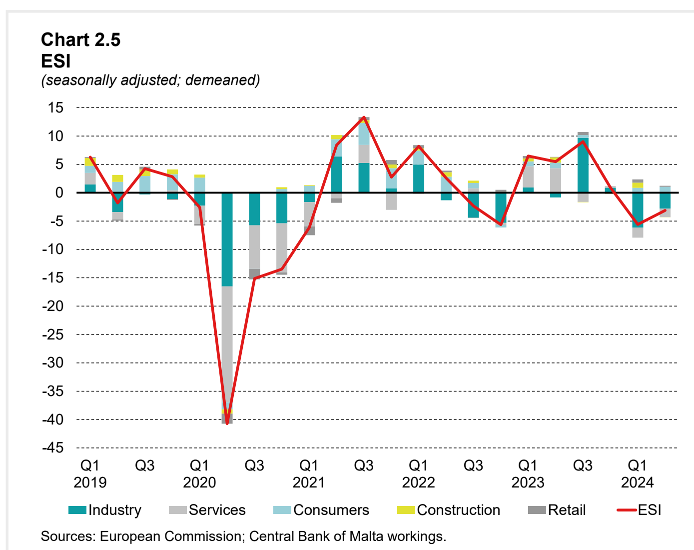
[7] Industrial production in the energy sector excludes energy generated abroad and imported through the interconnector.

Business and consumer surveys

During the second quarter of 2024, the European Commission's ESI for Malta increased to 96.9, from 94.4 in the preceding quarter, thus remaining below its long-term average of around 100.0. However, the overall indicator stood slightly above that in the euro area, which averaged 95.9 (see Chart 2.4).[8,9]



When compared with the first quarter of 2024, confidence improved in industry and to a lesser extent in the services sector and among consumers. By contrast, it deteriorated in the remaining sectors, most notably in construction.



When accounting for the weights assigned to each sector, and the time variation of the confidence indicator for each sector, the increase in the ESI relative to the first quarter of 2024 was mainly driven by industry.[10] Industry and the services sector explain why the overall ESI stood below the long-term average (see Chart 2.5).

Industrial confidence remains below its long-term average[11]

The industrial confidence indicator increased to -10.4, from an average of -20.8 in the previous three-month period but remained well below its long-term average of -4.2 (see Chart 2.6).

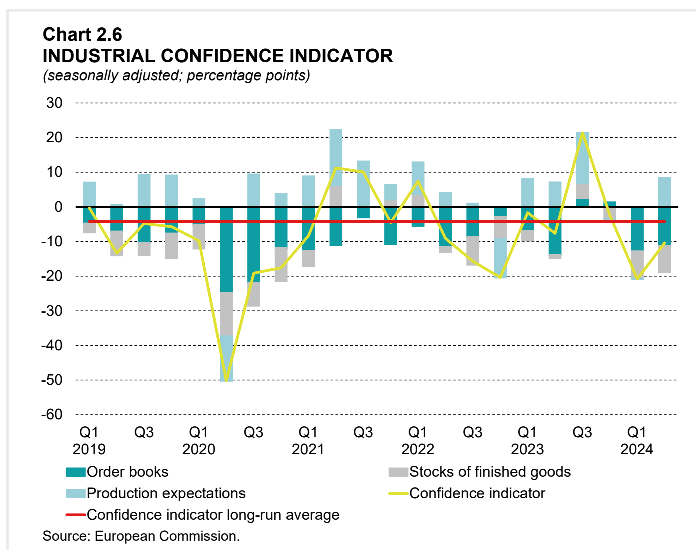
[8] The ESI summarises developments in confidence in five surveyed sectors: industry; services; construction; retail; and consumers. Quarterly data are three-month averages.

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

[10] Weights are assigned as follows: industry 40%; services 30%; consumers 20%; construction 5%; and retail trade 5%.

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

The recent amelioration for this sector reflected improvements in all its components, notably a strong increase in the production expectations for the months ahead. This contrasts with a negative assessment in the previous quarter.

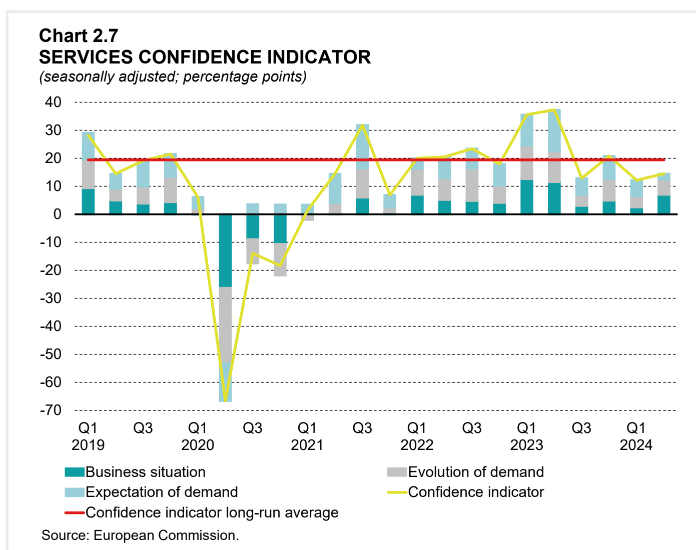


Source: European Commission.

Additional survey data reveal that the share of respondents in industry anticipating higher selling prices turned positive.

Confidence in the services sector improves[12]

The confidence indicator in the services sector increased to 14.5, from 12.2 in the previous quarter. Sentiment in this sector remained below its long-term average of 19.4 (see Chart 2.7). Firms' assessment of the business situation and of demand over the past three months, stood more positive than in the previous quarter. By contrast, their expectations of demand for the next three months declined, though they remained positive.



Source: European Commission.

Supplementary survey data indicate that the net share of respondents with positive price expectations increased marginally compared to the first quarter of 2024, standing at just under 20%. However, selling price expectations remained below their recent peak.

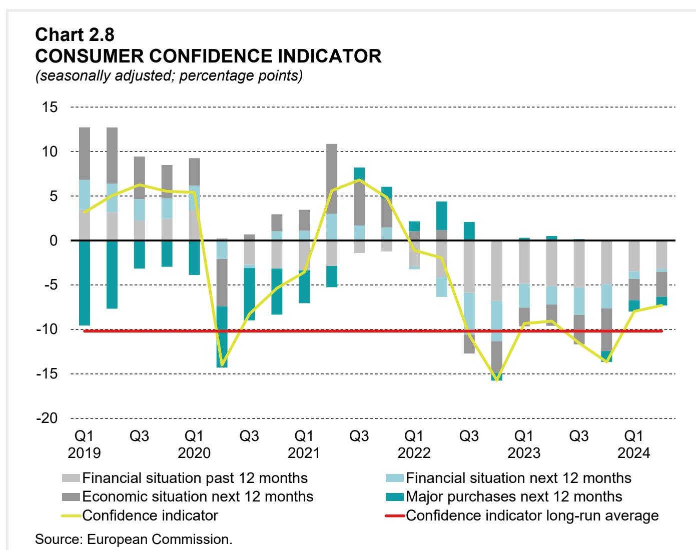
Consumer confidence improves but remains negative[13]

The consumer confidence indicator averaged -7.3 during the second quarter of 2024, above the -8.0 recorded in the previous quarter, and its long-run average of -10.2 (see Chart 2.8). The

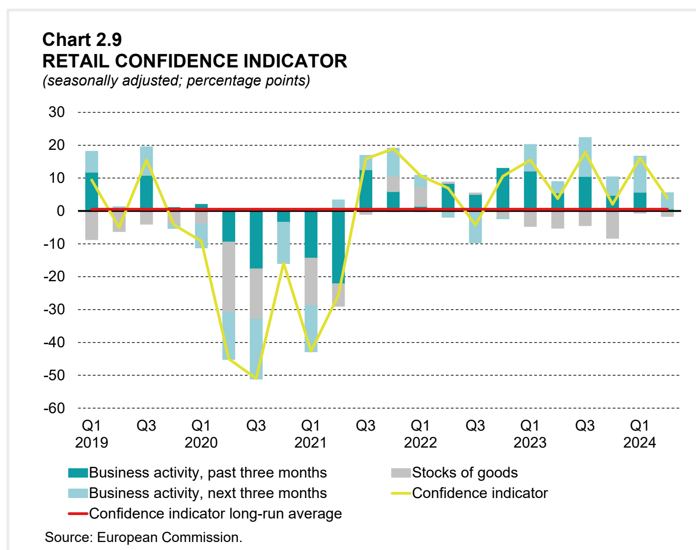
[12] The services confidence indicator is the arithmetic average of the seasonally adjusted balances (in percentage points) of replies to survey questions relating to the business climate, the evolution of demand in the previous three months, and demand expectations in the subsequent three months.

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

improvement in consumer sentiment reflected a less negative assessment and outlook of their finances. Expectations of major purchases were also less negative than in the last quarter. On the other hand, consumers' expectations of the general economic situation over the next 12 months became more negative.



Supplementary survey data show that a larger share of respondents expects unemployment to increase in the next twelve months. At the same time, the share of respondents expecting prices to rise, decreased to around 18% from 20% in the previous quarter.



Sentiment among retailers declined but remained above its long-term average[14]

The indicator of sentiment in the retail sector stood at 3.9 in the second quarter of 2024, down from 16.1 in the previous quarter, but still above its long-term average of 0.5. All components of the indicator contributed to the latest decrease in sentiment. However, the recent fall in sentiment was largely driven by a significant deterioration in the assessment of business activity over the previous three months and the near-term business outlook (see Chart 2.9).[15]

Supplementary survey data indicate that, in contrast to the previous quarter, short-term orders expectations stood negative. Meanwhile, the share of respondents anticipating prices to increase over the coming months, decreased to around 13%.

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

[15] Above-normal stock levels indicate lower turnover and affect the overall indicator in a negative way.

Confidence in construction turns negative[16]

In the second quarter of 2024, the indicator measuring confidence in the construction sector stood below its long-term average of -7.8. It averaged -9.4, down from 17.8 in the previous three-month period (see Chart 2.10).

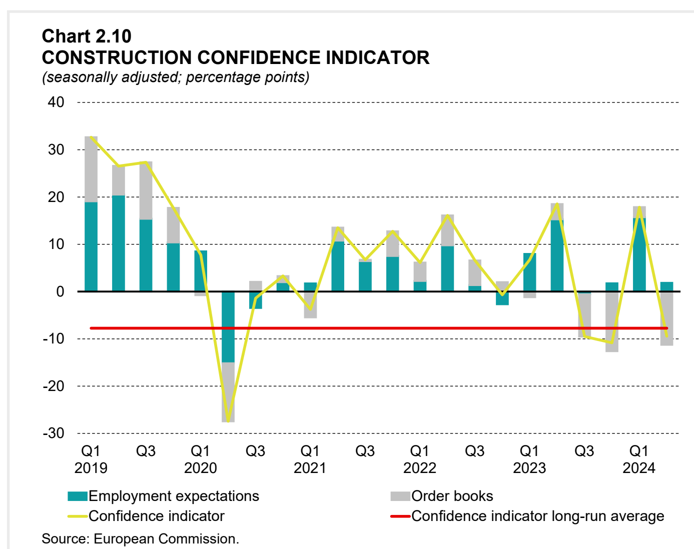


Chart 2.10
CONSTRUCTION CONFIDENCE INDICATOR
(seasonally adjusted; percentage points)

Source: European Commission.

Both order books and employment expectations declined significantly compared with the previous quarter, with the former turning negative.

Meanwhile, the net share of respondents expecting price increases over the next three months decreased significantly, to 12% from 43% in the first quarter of the year.

Employment Expectations Indicator (EEI) decreases further below its long-run average

The EEI – which is a composite indicator of employment expectations in industry, services, retail trade and construction – edged down in the second quarter of 2024. During the quarter, it averaged 93.3, below 99.2 in the preceding quarter, standing below its long-term average of around 100.0. The index also remained below the euro area average of 100.8.[17]

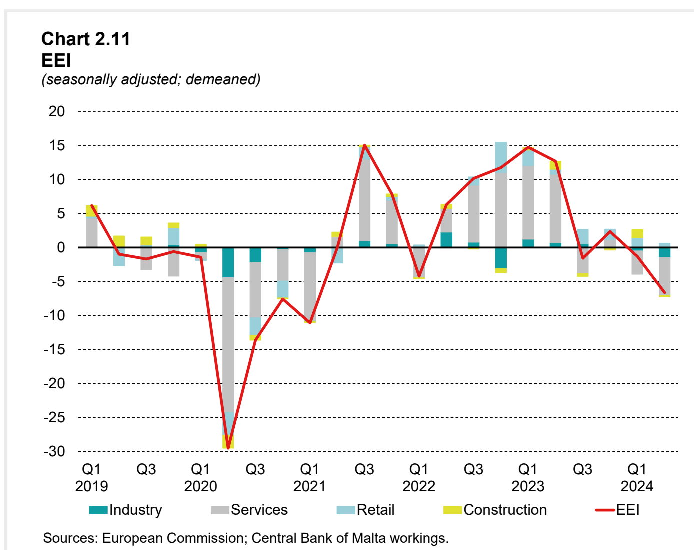


Chart 2.11
EEI
(seasonally adjusted; demeaned)

Sources: European Commission; Central Bank of Malta workings.

During the quarter under review, employment expectations were positive across all productive sectors, except in industry. The most positive reading was recorded in the retail sector.

Demeaned data suggest that the decrease relative to the preceding quarter was broad-based across sectors, yet mostly driven by the services and construction sectors (see Chart 2.11). The services sector

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

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

largely explains why the overall EEI stood below its long-term average.

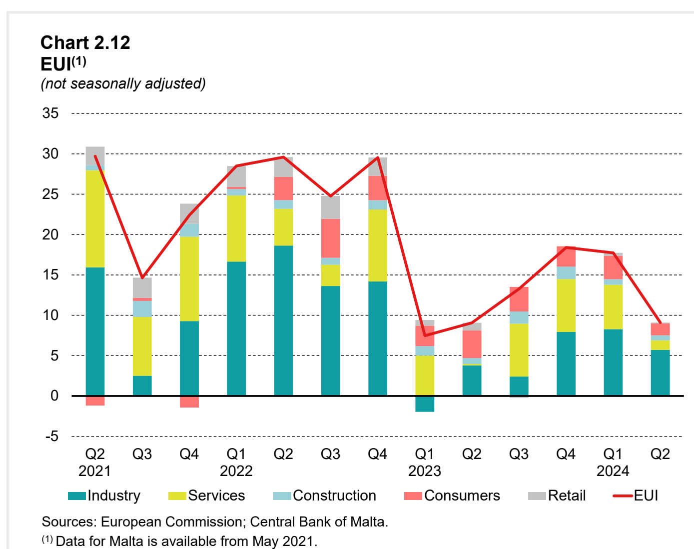


Chart 2.12
EUI[(1)]
(not seasonally adjusted)

Sources: European Commission; Central Bank of Malta.
(1) Data for Malta is available from May 2021.

Economic Uncertainty Indicator (EUI) decreases further

The European Commission's EUI is a composite indicator which measures how difficult it is for sectors to make predictions about their future financial or business situation. In Malta, this indicator decreased to 9.1 in the second quarter of the year, from 17.7 in the preceding quarter (see Chart 2.12). The indicator also remained below that in the euro area, which averaged 18.4.[18,19]

Lower uncertainty was recorded across all domestic sectors. The strongest fall, though, was recorded in the services sector.

When considering each sector's weight and past volatility, industry and consumers had the highest contributions to uncertainty during the quarter under review, while uncertainty was least widespread among retailers.

The labour market[20]

Labour force increases at a faster pace and activity rate increases at a slower pace

Labour Force Survey (LFS) data show that in the second quarter of 2024, the labour force grew by 17,268 persons, or 5.6% on an annual basis, faster than the 4.1% increase recorded in the previous quarter (see Table 2.4).[21]

The activity rate stood at 81.1% in the quarter under review, higher than the 79.8% registered a year earlier.[22] This was due to increases in both the female participation rate, and that of males. The male participation rate increased by 1.1 percentage points to 87.5%, while that of females

[18] The EUI is made up of five balances (in percentage points) which summarise managers'/consumers' answers to a question asking them to indicate how difficult it is to make predictions about their future business/financial situation. The series are not seasonally adjusted. The five-balance series are summarised in one composite indicator using the same weights used to construct the ESI. The questions asked correspond to Q51 of the industry survey, Q31 of the services survey, Q41 of the retail trade and construction surveys and Q21 of the consumer survey.

[19] Data on consumer uncertainty became available in October 2020, while data for industry, services, retail, and construction became available in May 2021.

[20] This section draws mainly on labour market statistics from two sources: the LFS, which is a household survey conducted by the NSO based on definitions set by the International Labour Organization (ILO) and Eurostat; and administrative records compiled by Jobsplus according to definitions established by domestic legislation on employment and social security benefits.

[21] The LFS defines the labour force as all persons aged 15 and over who are active in the labour market. This includes those in employment, whether full-time or part-time, and the unemployed, defined as those persons without work but who were actively seeking a job during the previous four weeks and available for work within two weeks of the reference period.

[22] The activity rate measures the number of persons in the labour force aged between 15 and 64 as a proportion of the working age population, which is defined as all those aged 15 to 64 years.

Table 2.4
LABOUR MARKET INDICATORS BASED ON THE LFS
Persons; annual percentage changes

	2023 Q2	2024 Q2	Annual change %
Labour force	**308,786**	**326,054**	**5.6**
Employed	297,128	315,545	6.2
By type of employment:			
Full-time	262,397	279,819	6.6
Part-time	34,731	35,726	2.9
Unemployed	11,658	10,509	-9.9
Activity rate (%)	**79.8**	**81.1**	
Male	86.4	87.5	
Female	71.9	73.2	
Employment rate (%)	**76.8**	**78.4**	
Male	83.0	84.5	
Female	69.3	71.0	
Unemployment rate (%)	**3.8**	**3.2**	
Actual hours worked (per week)	**35.3**	**34.9**	

Source: NSO.

increased by 1.3 percentage points to 73.2%. Both rates exceeded the corresponding rates for the euro area.

Employment increases at a faster pace

Employment rose by 6.2% in annual terms, following a rise of 4.6% in the previous quarter. Most of the increase in absolute terms was driven by full-time employment, as this rose by 17,422 persons, or 6.6% on a year earlier. This increase was mainly coming from the sector comprising human health, accommodation and food service activities, followed by industry and construction.

The number of persons in part-time jobs – which also includes those employed full-time on reduced hours – rose by 995, or 2.9% in annual terms. This increase was mostly driven by the sectors comprising education, financial and insurance activities, and the sector comprising administrative and support service activities.

The overall employment rate rose by 1.6 percentage points on the same period of 2023, to reach 78.4%.[23] The increase was broad-based across age brackets but was more significant among individuals aged up to 54 years. The female employment rate rose by 1.8 percentage points to 71.0%, and that of males rose by 1.4 percentage points to 84.5%.

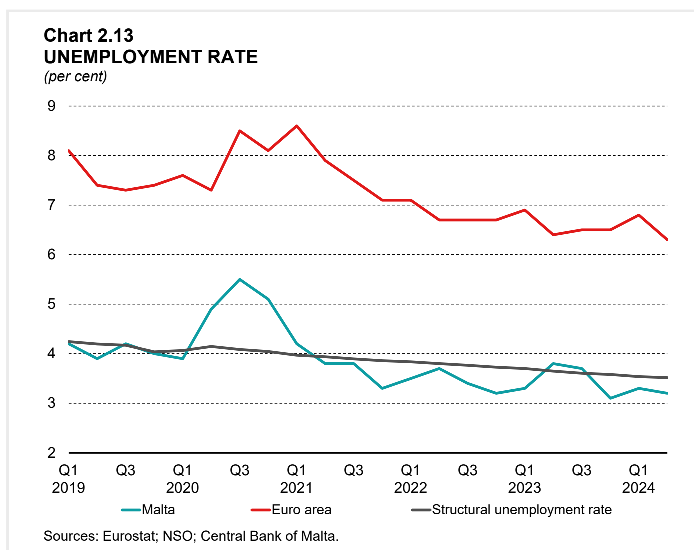
During the quarter under review, average weekly hours worked derived from the LFS declined to 34.9, from 35.3 a year earlier (see Table 2.4).[24] This reflected a decrease in average hours worked reported by both full-time and part-time employees.

[23] The employment rate measures the number of persons aged between 15 and 64 employed on a full-time or part-time basis as a proportion of the working-age population.

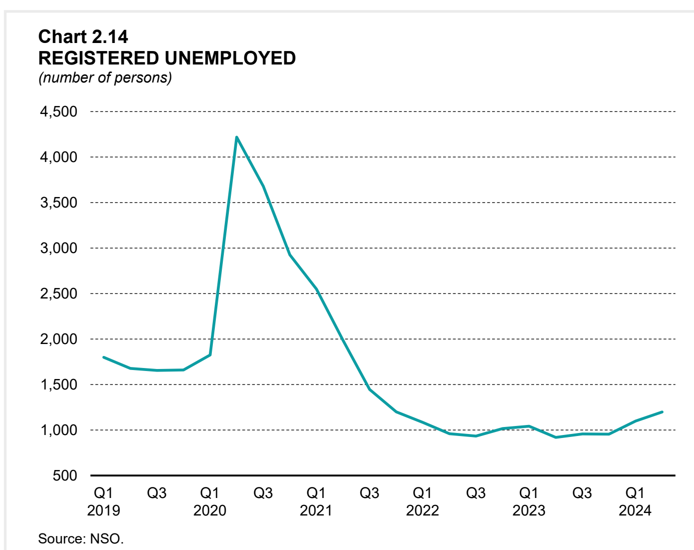
[24] Actual hours refer to the number of hours actually spent at the place of work during the reference week for LFS. A person may work extra hours (e.g. overtime, variable hours) or work less hours than usual (e.g. vacation leave, education, sick leave or slack work) due to various reasons. Owing to increased flexibility at workplaces coupled with technology, the place of work may also include one's home. In this regard, actual hours worked also include the hours of work conducted by persons who telework.

The unemployment rate remains low

The unemployment rate based on the LFS fell to 3.2%, from 3.8% a year earlier (see Table 2.4). This reflects continued strong demand for labour.[25] Labour market conditions remained more favourable than those in the euro area, where the unemployment rate on average stood at 6.3% (see Chart 2.13).



During the quarter under review, the unemployment rate also stood below the Bank's structural measure of 3.5%.[26] This indicates a degree of labour market tightness, which is also confirmed by the Bank's *Business Dialogue* publication and other indicators (see below).



Jobsplus data show that the number of persons on the unemployment register increased, both on a quarterly basis and in annual terms. During the second quarter of 2024, the average number of persons on the unemployment register stood at 1,198, compared with 919 a year earlier, and 1,099 in the first quarter of 2024 (see Chart 2.14).

The vacancy rate declined but remained elevated

In absolute terms the number of vacancies increased from 7,117 in the second quarter of 2023 to 8,092 in the same quarter of 2024, that is, a 13.7% increase. Eurostat's job vacancy rate for industry, construction and services increased in year-on-year terms, but decreased in quarterly terms,

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[25] According to the LFS, the unemployed comprise persons aged between 15 and 74 years who are without work, available for work and who have actively sought work during the four weeks preceding the Survey. In contrast, the number of unemployed on the basis of the Jobsplus definition includes only those persons registering for work under Part 1 and Part 2 of the unemployment register.

[26] The structural unemployment rate in this chapter refers to the non-accelerating inflation rate of unemployment (NAIRU), that is, the unemployment rate that is consistent with stable inflation. This measure of the unemployment rate is based on an unobserved components model (UCMPF). For further details, see Borg, I. (2023). "Box 1: Latest Estimates of the NAIRU" *Outlook for the Maltese Economy* 2023:1, pp.7-9 and Ellul, R. (2019). "Box 1: An Unobserved Components Model for potential output in Malta", *Quarterly Review* 2019:2, pp. 17-21.

reaching 3.0% in the quarter under review (see Chart 2.15).[27] The highest vacancy rates were recorded in the information and communication sector (6.0%), the water supply; sewerage, waste management and remediation activities sector (4.6%), the other service activities sector (4.5%), and the administrative and support service activities sector (4.1%).

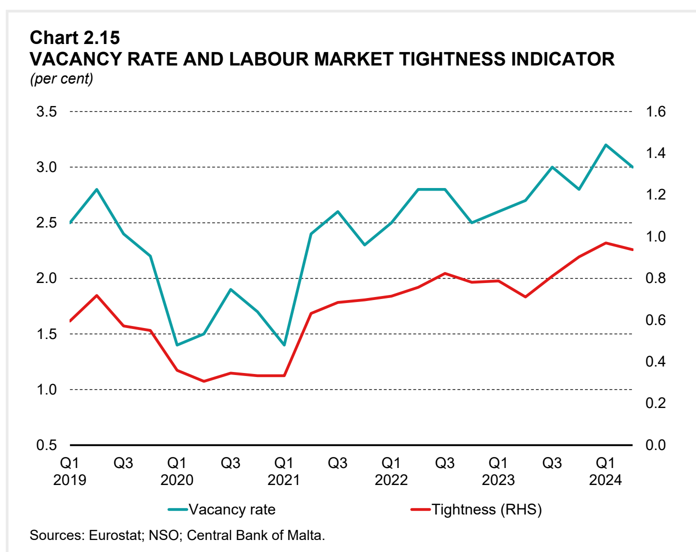


Chart 2.15
VACANCY RATE AND LABOUR MARKET TIGHTNESS INDICATOR
(per cent)
Sources: Eurostat; NSO; Central Bank of Malta.

The ratio of the job vacancy rate to the unemployment rate is an indicator of the imbalance between labour demand and supply and, therefore, of labour tightness. During the quarter under review, this ratio stood at 0.9, slightly lower than in the previous quarter, but above the ratio of 0.7 recorded a year earlier. Market conditions thus remained very tight compared to recent outturns. This contrasts with the euro area average, where the tightness indicator declined to around 0.4. Labour market conditions in the euro area continue to be significantly less tight compared to those in Malta.

To measure better labour market slack (unemployed and underutilised labour), one can consider an extended labour force definition, which in addition to the unemployed, also includes persons available to take up work but not seeking it, persons seeking work but not immediately available, and underemployed part-time workers. By this measure, on a four-quarter moving average basis, labour market slack was equivalent to 5.4% of the extended labour force in the second quarter of the year (see Chart 2.16).[28] This rate appears to have stabilised in recent quarters, to a level which is well below its average of around 8.0% estimated since 2010. It is also significantly lower than the 13.0% recorded for the euro area.

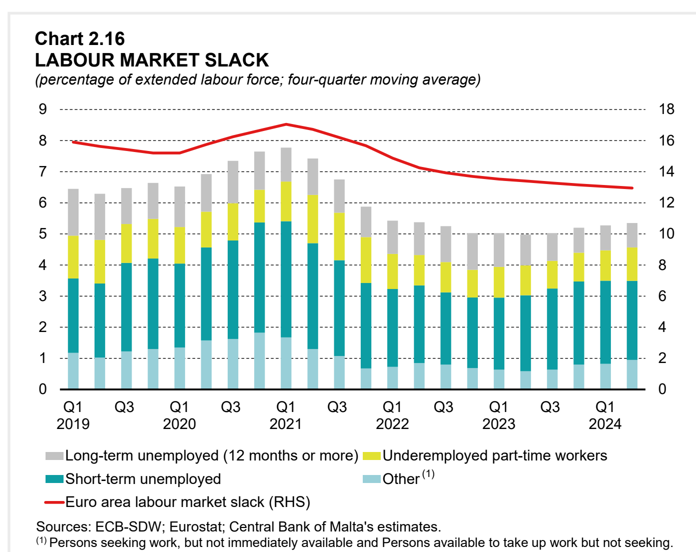


Chart 2.16
LABOUR MARKET SLACK
(percentage of extended labour force; four-quarter moving average)
Sources: ECB-SDW; Eurostat; Central Bank of Malta's estimates.
(1) Persons seeking work, but not immediately available and Persons available to take up work but not seeking.

[27] The job vacancy rate measures the number of job vacancies as a percentage of total jobs (occupied and vacant). Data for Malta are available since 2017.

[28] For further details on the methodology underlying the measure of labour market slack, see Ellul, R. (2019). "Labour Market Slack," *Quarterly Review* 2019:1, pp. 37-41, Central Bank of Malta. Given that this methodology partly relies on internal estimation, the slack indicator reported in this *Review* may differ slightly from that published by Eurostat.

The gap between the broader measure of labour market slack and the unemployment rate declined considerably since the second quarter of 2021, indicating a reduction in the share of underutilised labour. However, this gap registered a slight uptick during the last three quarters.

In the second quarter of 2024, almost two-thirds of the labour market slack stemmed from unemployment (primarily from short-term unemployment). Underemployed part-time workers, i.e., those working part-time but willing and able to work additional hours, accounted for slightly more than half of the underutilised component of labour market slack.

BOX 2: THE IMPACT OF MITIGATING CLIMATE CHANGE ON MALTESE FIRMS' EMPLOYMENT PLANS[1]

As the global community intensifies its efforts to mitigate the impact of climate change, businesses worldwide, including those in Malta, face increasing pressure to adapt their operations and workforce to align with a carbon-neutral future. The transition towards a green economy requires more than just investment in new technologies and infrastructure. It also necessitates a fundamental reshaping of the workforce to meet the demands of sustainability.

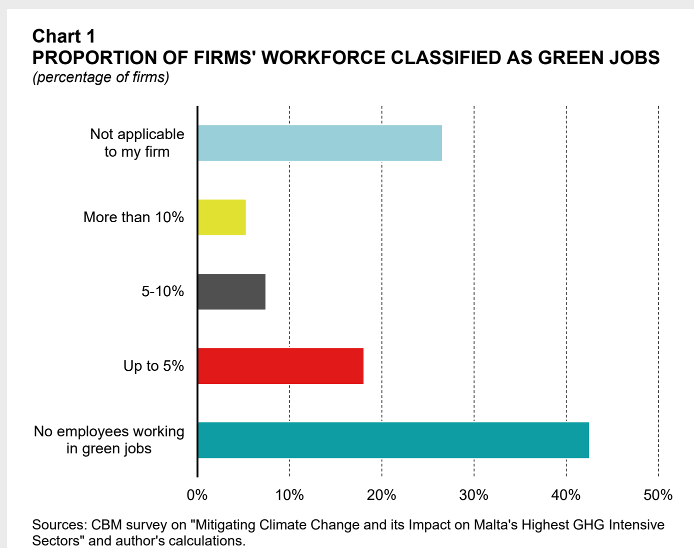
Building on a recent survey by the Central Bank of Malta, this box delves deeper into how local firms plan to adapt their employment practices in response to climate change. This survey, which used a quota sampling framework, specifically targeted firms which employ at least ten employees. Sectors were classified into high, mid, and low greenhouse gas (GHG) emissions intensity by scaling each sector's GHG emissions against its gross value added (GVA). Only companies in sectors with high and mid-level GHG emissions intensity were targeted.[2]

Employment shifts in response to climate change

Green jobs refer to any role that contributes to preserving or restoring the environment. This includes jobs that directly reduce the carbon footprint, promote energy efficiency, utilize renewable energy sources, reduce waste and pollution, or support sustainability practices.[3] Green jobs are integral to the transition towards a low-carbon economy and involve the development, implementation, and maintenance of strategies that mitigate the impact of climate change.

According to the survey, while a substantial 43% of firms reported having no employees classified as working in green jobs, there is a notable minority making progress in this area (see Chart 1). About 7% of firms have 5-10% of their workforce engaged in green jobs, and 5% have more than 10% of their workforce in such roles. This was more prominent amongst

Chart 1
PROPORTION OF FIRMS' WORKFORCE CLASSIFIED AS GREEN JOBS
(percentage of firms)



Sources: CBM survey on "Mitigating Climate Change and its Impact on Malta's Highest GHG Intensive Sectors" and author's calculations.

[1] Prepared by Mr Warren Deguara, Principal Economist within the Economic Projections and Conjunctural Analysis Office. The views expressed are those of the author and do not necessarily reflect the views of the Central Bank of Malta. Any remaining errors are the sole responsibility of the author.

[2] For further details see The impact of mitigating climate change on Maltese firms, Deguara, et al. (2024).

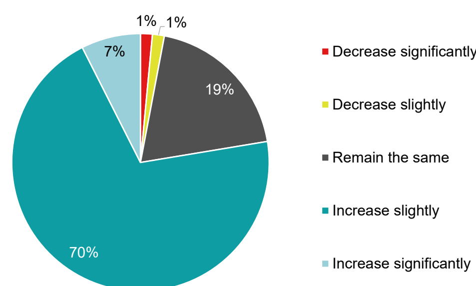
[3] See Green jobs, green economy, just transition and related concepts: A review of definitions developed through intergovernmental processes and international organizations, Castillo (2023).

firms operating in mid-GHG intensive emitting sectors and in the construction sector. The remaining 18% have up to 5% of their workforce engaged in these roles.

These figures indicate a growing recognition among some Maltese firms of the importance of green jobs in driving sustainable business practices. Nonetheless, such figures are likely to be less than those reported in the ninth report on economic, social and territorial cohesion where an estimated 20% of total employment in Malta were classified as green jobs in 2020.[4] Another interesting finding from this survey is that 63% of firms disagree that climate change or adaptation to it will cause the company to relocate some of its staff.

When it comes to future employment plans, most firms (70%) who consider green jobs to be relevant for their operations expect their green workforce only to increase slightly in the coming years, and this was common across emissions intensity levels and across sectors. A further 7% anticipate a significant increase in green employment (see Chart 2). Nonetheless, almost a fifth of surveyed firms expect their level of green workforce to remain the same in the coming years. This cautious approach may reflect the broader challenges firms face in adapting to climate change, particularly in the context of financing and skill development. It could also hint at the tightness of the Maltese labour market whereby several skills shortages have been reported by firms interviewed in the Central Bank of Malta's Business Dialogue over the past few years.

Chart 2
EXPECTED CHANGE IN GREEN WORKFORCE OVER THE COMING YEARS
(percentage of firms)



Sources: CBM survey on "Mitigating Climate Change and its Impact on Malta's Highest GHG Intensive Sectors" and author's calculations.
Note: Replies conditional on the respondents' answer to whether green occupations are relevant to their operations i.e. conditional on the results in Chart 1.

Labour and skill requirements

Maltese companies identified several key skills and roles needed for their transition to a green economy, reflecting both the nature of their operations and their environmental impact. A clear takeaway from company replies is the need for their workforce to develop the necessary green skills to aid in the transition. The Inter-Agency Working Group on Work-based Learning defines skills for the green transition as 'skills and competences but also knowledge, abilities, values and attitudes needed to live, work and act in resource-efficient and sustainable economies and societies'.[5]

[4] See Ninth Report on Economic, Social and Territorial Cohesion, European Commission (2024). This report utilises NUTS2 regional data for 56 NACE sectors and hence results might differ from survey data.
[5] See Work-based learning and the green transition, Inter-Agency Working Group on Work-based Learning (2022).

In the manufacturing sector, companies in high-GHG intensive emitting sectors consistently emphasized the need for enhanced engineering skills, particularly in energy efficiency, sustainability, and compliance. These companies highlighted the importance of upskilling their existing workforce, especially in areas such as engineering and environmental management, to integrate green practices into their operations. For instance, traditional roles like chemists and engineers are expected to incorporate sustainability into their daily tasks. Meanwhile, companies in mid-GHG intensive emitting sectors also point out the need for environmental engineers, energy auditors, and specialists in logistics and product design. There is a clear demand for both technical expertise and a shift in operations to meet green economy goals. These findings are very much in line with other local studies and with the most in demand green jobs in 2023 as reported by the European Labour Authority.[6]

In the wholesale and retail sector, high-GHG intensive emitting sector companies exhibited a wider range of needs, including consultancy services to guide employees, expertise in ecosystem management, clean energy, and ESG (Environmental, Social, and Governance) practices. These firms also noted the importance of transitioning to electric vehicles and managing carbon footprints. Mid-GHG intensive emitting companies focused on more practical skills, such as the need for trained installers for renewable energy technologies like photovoltaic systems and electric vehicle chargers. Additionally, there was a call for greater awareness and training among staff to adapt to green economy requirements.

The services sector presented varying needs depending on the GHG intensity. High-GHG intensive emitting sector companies stressed the importance of sustainability managers, engineers with green technology expertise, and personnel knowledgeable in EU Taxonomy and environmental certifications. These companies are looking for individuals who can bring a green mindset into their operations and help integrate sustainability into existing structures. On the other hand, mid-GHG intensive emitting firms highlighted the need for renewable energy advisors, data collection specialists, and experts in waste management. They also emphasized the need for training programs to change employee mindsets and improve understanding of new technologies.

Respondents from the construction and real estate sector, who mostly operated in mid-GHG intensive emitting companies, highlighted waste and sustainability management, along with the need for general education on environmentally friendly practices. These firms are particularly focused on adopting new technologies and machinery, and ensuring their workforce is trained in sustainable practices.

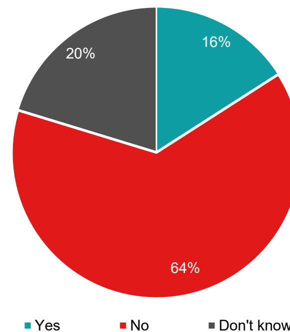
Challenges in developing a green workforce

One of the most significant findings from the survey is the perceived inadequacy of the current Maltese labour force to support the transition to carbon neutrality. A striking 64% of firms believe that the local labour force is not adequately equipped to help achieve this goal, with only 16% expressing confidence in the labour force's readiness (see Chart 3). These views are practically identical across emissions intensity levels and economic sectors. This is in

[6] Based on a representative survey amongst Maltese companies, employers, training providers and/or agencies, in a 2022 Intercept Project study about green jobs in Malta, Dr Vincent Marmara found that the most needed occupations are Solar (82.9%) and Wind (66.9%) Energy Engineers. See also In-demand green jobs in 2023, European Labour Authority (2023).

line with findings from the 2022 Intercept Project study about green jobs in Malta which shows that across different skills levels (low, medium and high), most Maltese companies report that there will be a need of both new skills and upgrading of existing skills. Moreover, the report finds that motivation, creativity, communication, and critical thinking are among the top four soft skills considered by the respondents as most important for green jobs. As such, training opportunities for upskilling are essential for employment in green jobs This sentiment underscores a critical gap in the current skills landscape, which could impede Malta's progress towards its climate goals.

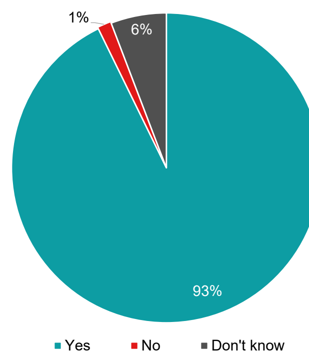
Chart 3
MALTESE LABOUR FORCE ADEQUACY TO AID IN ACHIEVING CARBON NEUTRALITY
(percentage of firms)



Yes No Don't know

Sources: CBM survey on "Mitigating Climate Change and its Impact on Malta's Highest GHG Intensive Sectors" and author's calculations.
Note: Replies conditional on the respondents' answer to whether green occupations are relevant to their operations i.e. conditional on the results in Chart 1.

Chart 4
WILLINGNESS TO TRAIN EMPLOYEES IN DEVELOPING GREEN SKILLS
(percentage of firms)



Yes No Don't know

Sources: CBM survey on "Mitigating Climate Change and its Impact on Malta's Highest GHG Intensive Sectors" and author's calculations.
Note: Replies conditional on the respondents' answer to whether green occupations are relevant to their operations i.e. conditional on the results in Chart 1.

On a positive note, local firms have a strong willingness to invest in training their employees to gain green skills. In fact, 93% of companies that consider green jobs to be relevant for their operations are willing to train their workforce in green skills, highlighting their commitment to improve operations, become more sustainable, and achieve their climate goals (see Chart 4). On the other hand, a small proportion (1% of firms) is unwilling to do so, and a further 6% are uncertain. This reluctance or indecision could stem from the perceived costs and logistical challenges associated with training, further complicating efforts to build a green economy. In fact, the survey reveals that financing the transition to a green economy remains a significant challenge for Maltese firms. While the survey indicates that many companies are making changes in response to climate change, the financial burden of these investments is a recurring theme. The cost of upgrading infrastructure, adopting new technologies, and training employees can be prohibitive, particularly for smaller firms with limited resources.

This financial burden is worsened by the lack of awareness of available funding opportunities, especially from national sources. Without knowing about these support options, firms may struggle to get the resources they need for a sustainable transition, thus slowing their progress.

Main conclusions

Considering the challenges identified in the survey, it is essential for Maltese firms to adopt a more strategic approach to workforce development for a successful transition to a green economy. This requires not only ensuring the existing workforce is adequately trained for a carbon-neutral future but also attracting talent capable of contributing to the shift towards sustainability.

Investment in education and training must be prioritized. Firms should focus on upskilling employees, particularly in critical areas such as renewable energy, sustainability management, and green technologies. By doing so, they can build a workforce that not only supports current operations but also drives innovation and growth in the green economy. Collaboration with educational institutions, government bodies, and industry associations will be key in bridging the existing skills gap. Together, these stakeholders can develop targeted training programs that align with the specific needs of Maltese firms, ensuring the labour force is prepared for the challenges of climate change.

The survey highlights both progress and ongoing challenges in adapting to the demands of a green economy. While there is increasing recognition of the importance of green jobs and skills, significant gaps remain in workforce readiness, environmental awareness, and access to financing. To address these gaps, firms must take a proactive stance on workforce development, focusing on building technical skills in areas like engineering, sustainability, and environmental management. Upskilling initiatives, whether through formal training or hiring experts in green technologies, are recognized across sectors as essential.

The transition to a green economy is not only a technical challenge but also one requiring a shift in mindset and operational practices. Greater awareness and utilization of available funding and support mechanisms will be critical to easing the financial burden of this transition. By addressing these issues, Maltese firms can ensure a sustainable future for both their businesses and the wider community.

3. PRICES, COSTS AND COMPETITIVENESS

Consumer price pressures eased further during the quarter under review. Annual inflation, as measured by the HICP, stood at 2.2% in June, down from 2.7% in March. This was driven by a smaller contribution from processed food inflation as all other main components retained the same contribution. Annual inflation based on the RPI – which only considers expenditure by Maltese residents – fell to 1.3% in June, from 1.9% in March.

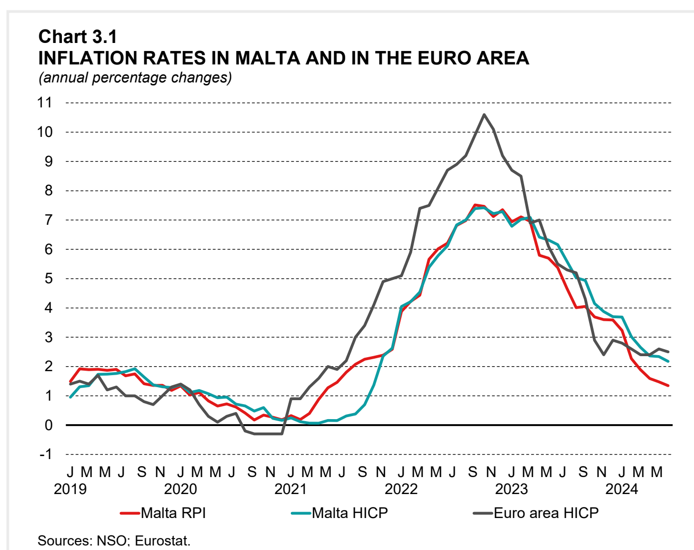
When measured over four quarters, ULC increased at a faster pace in the second quarter of 2024, with its growth rate reaching 1.4%, from 0.6% in the previous quarter. Meanwhile, annual growth in other input cost indicators regularly monitored by the Bank generally continued to moderate, with the exception of the CCI which recorded a small year-on-year increase after contracting in the first quarter.

Inflation

HICP inflation eases

Annual HICP inflation eased to 2.2% in June, from 2.7% in March (see Table 3.1).[1] Chart 3.1 shows that overall HICP inflation in Malta stood lower than that recorded in the euro area, which ended the quarter at 2.5%. Malta's lower inflation rate in June when compared to that of the euro area reflects a lower contribution from services inflation (see Chart 3.2). Furthermore, energy inflation in Malta retained an unchanged

Chart 3.1
INFLATION RATES IN MALTA AND IN THE EURO AREA
(annual percentage changes)



Sources: NSO; Eurostat.

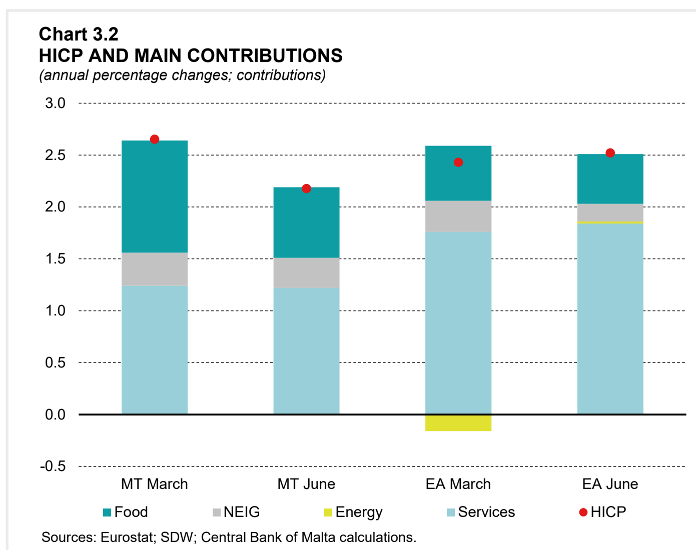
Table 3.1
HICP INFLATION
Annual percentage change

	2023						2024					
	July	Aug.	Sep.	Oct.	Nov.	Dec.	Jan.	Feb.	Mar.	Apr.	May	June
Unprocessed food	5.4	8.5	8.2	4.0	6.7	12.2	13.4	5.2	3.5	4.3	5.2	3.7
Processed food including alcohol and tobacco	9.9	9.7	9.0	8.2	7.3	7.1	7.4	6.1	5.4	4.7	3.9	3.1
Energy	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
NEIG	3.8	3.4	3.6	2.6	2.2	2.2	1.6	1.7	1.2	1.3	0.9	1.1
Services (overall index excluding goods)	5.6	4.3	4.3	4.0	3.9	3.0	3.1	2.8	2.7	2.1	2.4	2.3
All Items HICP	5.6	5.0	4.9	4.2	3.9	3.7	3.7	3.0	2.7	2.4	2.3	2.2

Source: Eurostat.

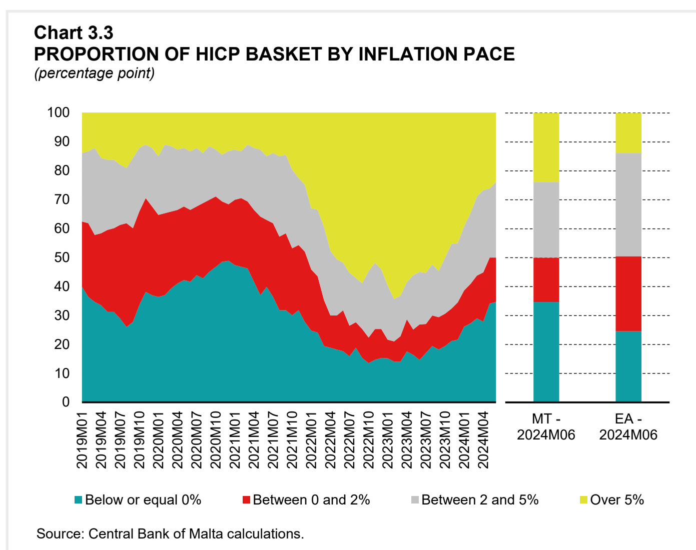
[1] The HICP weights are revised on an annual basis to reflect changes in overall consumption patterns. In 2024, the weight allocated to services stood at 44.7%, while that of NEIG was 27.5%. Food accounted for 21.5% of the index, while the share allocated to energy stood at 6.2%. These were revised from 44.3% for services, 27.9% for NEIG, 21.4% for food and 6.5% for energy in 2023.

contribution, while it no longer remained negative in the euro area. On the other hand, the contributions of food and NEIG to HICP inflation in June were higher in Malta than in the euro area.



Core inflation, or the annual rate of change of HICP excluding energy and food, stood at 2.0%, and thus also below the 2.9% recorded in the euro area.

Chart 3.3 shows a distribution of price changes whereby subcomponents of the HICP are categorised into four classes of inflation rates: i) below or equal to 0%; ii) between 0% and 2%; iii) between 2% and 5%; and iv) over 5%.[2] This analysis indicates whether developments in inflation are broad-based across HICP items or driven only by selected components of the consumption basket.



The share of subcomponents registering inflation rates of more than 5% declined further during the quarter under review as the impact of recent shocks on imported inflation continued to dissipate. Compared to three months earlier, this ratio dropped by 5.1 percentage points to reach 23.9%. Likewise, the bracket holding items with inflation between 2% and 5% decreased by 1.1 percentage points since March, to stand at 26.1% in June.

On the other hand, the bracket holding items with negative inflation rates grew by 5.7 percentage points in Malta, standing at 34.7%. The increase in this bracket mainly reflects a drop in the prices of a number of food products, including dairy products such as eggs and yoghurt, and sugar. Similarly, the bracket holding items with inflation between 0% and 2% increased by 0.6 percentage points, to stand at 15.3% in June.

[2] The calculation of the shares in this chart does not take into account the weights of individual HICP sub-components. This analysis includes 176 sub-indices of the HICP for Malta and 289 sub-indices for the euro area based on the five-digit COICOP classification. On average since 2001, 30.5% of items in Malta's basket fell in the 0% or negative inflation rates interval, while this figure stood at 17.5% for the euro area. Around 47% of the Maltese basket fell in the 0-2% and 2-5% intervals – in almost equal parts. These shares stood at 39.7% and 32.6%, respectively, in the euro area. While 22.4% of the Maltese basket fell in the over 5% interval, only 10.3% of the euro area basket fell in this interval.

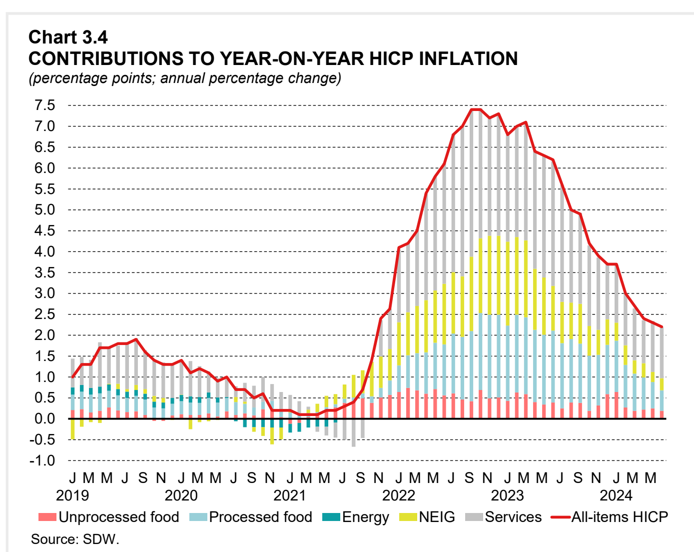
In the euro area, the share of items with price increases exceeding 5% also decreased during the second quarter of 2024. Furthermore, the share of items in this bracket remained significantly lower than that in Malta, with a difference of 10.0 percentage points in June. In part, this reflects higher price increases for some food products including milk, fish and vegetables, which in turn is reflected in a higher food inflation rate for Malta as compared to that of the euro area, as well as higher price increases for a number of household items. However, while items with price increases of between 2% and 5% accounted for almost 36% of the euro area basket in June, in Malta this share was significantly lower at 26.1%, as was the share of items with inflation rates of between 0% and 2%. On the other hand, Malta had a higher share of items with negative inflation rates.

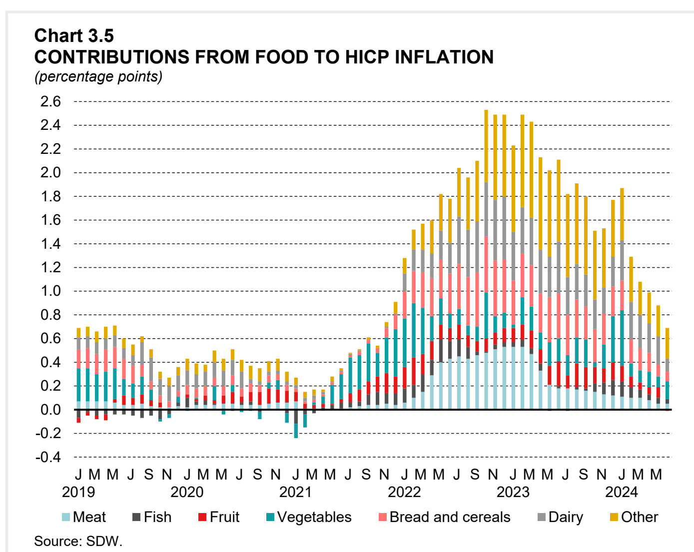
Main components of inflation

The drop in Malta's HICP inflation relative to March stemmed from processed food inflation as all other main components retained the same contribution (see Chart 3.4).

Processed food inflation (including alcohol and tobacco) fell to 3.1% from 5.4% in March, supported by lower imported prices and the Stabbilta' scheme. Consequently, the contribution of processed food to HICP inflation decreased by 0.4 percentage points, standing at 0.5 percentage points in June. On the other hand, unprocessed food inflation edged up to 3.7% from 3.5% in March. As a result, overall food inflation including alcohol and tobacco, eased significantly during the quarter under review, standing at 3.3%, as compared to 5.0% in March, which is lower than the historical average of 3.6%.

The main contributors to the moderation in processed food inflation since March were dairy products. These were followed by bread and cereals. Fruit, meat and fish products also contributed to the moderation in food inflation, although to a lesser extent (see Chart 3.5). On the other hand, there was an increase in the contribution from vegetables following higher vegetable prices.





NEIG inflation eased marginally from 1.2% in March to 1.1% in June. Looking at the sub-components, prices of durables contracted at a faster pace dropping by 1.1% in annual terms, following a drop of 0.7% three months earlier. At the same time, prices of non-durables rose at a slower pace of 3.6%, down from 4.1% in March. On the other hand, prices of semi-durables rose by 1.3% year-on-year, up from 0.4% in March.

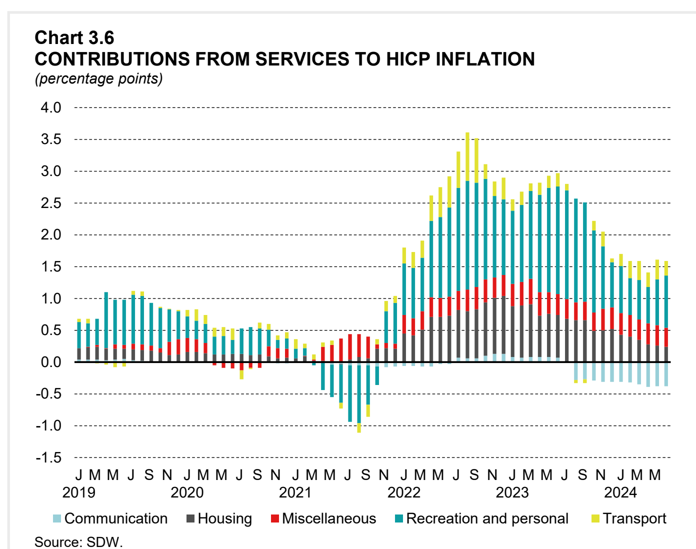


Chart 3.6
CONTRIBUTIONS FROM SERVICES TO HICP INFLATION
(percentage points)
Source: SDW.

Services inflation decreased from 2.7% in March to 2.3% in June, contributing 1.2 percentage points to overall HICP inflation (see Chart 3.6). This mostly reflected a smaller contribution from the housing component, largely reflecting lower price increases in rents. The contribution from transport services also decreased, though to a lesser extent, on the back of lower prices for international flights. Year-on-year declines in communication services also continued to dampen services inflation, extending the pattern of recent months.

On the other hand, the contribution from the recreation and personal component, which is the main contributor to services inflation, increased as the prices charged for package holidays contracted at a slower pace than three months earlier. Meanwhile, the contribution from miscellaneous services remained largely unchanged.

Energy inflation was unchanged at 0.0% in June, as electricity, gas, and transport fuel prices were kept unchanged from their level a year earlier, through government support measures shielding the economy from changes in international energy prices.

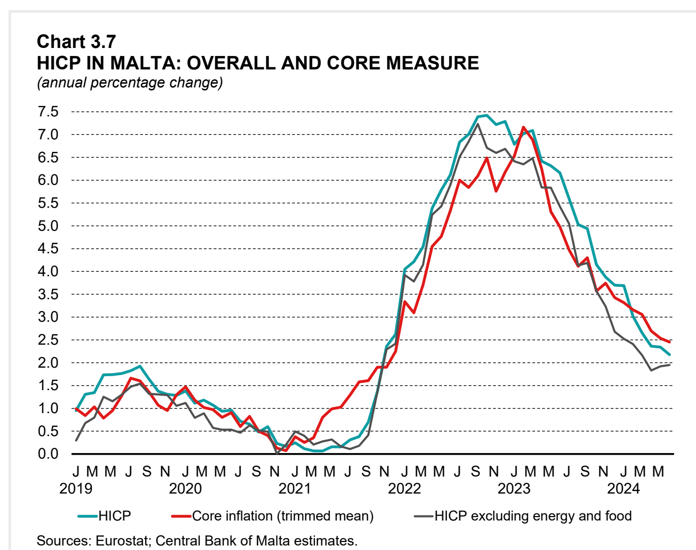


Chart 3.7
HICP IN MALTA: OVERALL AND CORE MEASURE
(annual percentage change)
Sources: Eurostat; Central Bank of Malta estimates.

Core HICP inflation declines

The Bank's measure of core inflation, which excludes the more volatile items in each month, fell to 2.5% in June 2024, from 3.1% three months earlier (see Chart 3.7).[3] An alternative measure of underlying

[3] The Bank uses a 'trimmed mean' approach to measure core inflation, whereby the more volatile subcomponents of the index are removed from the basket of consumer goods so as to exclude extreme movements from the headline inflation rate. See Gatt, W. (2014), "An Evaluation of Core Inflation Measures for Malta", *Quarterly Review* 2014(3), pp. 39-45, Central Bank of Malta.

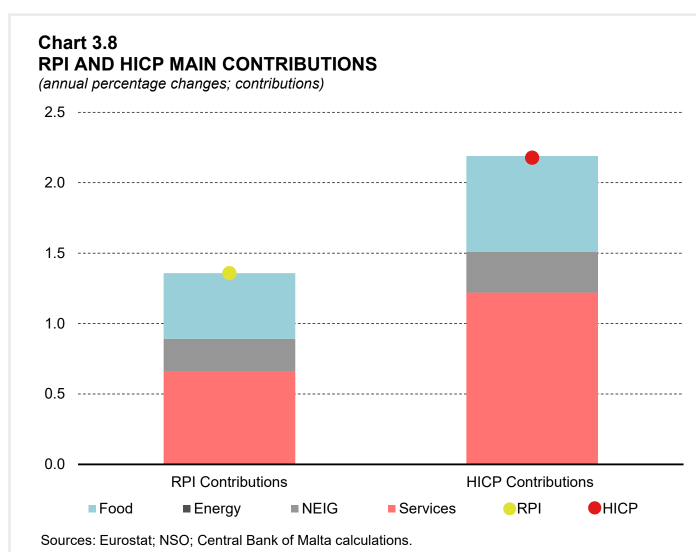
inflationary pressures – HICP excluding energy and food – also eased in June, reaching 2.0%, from 2.2% in March.

RPI inflation edges down

Annual inflation based on the RPI index fell to 1.3% in June, from 1.9% in March, mainly due to lower contributions from prices of food (see Table 3.2).[4] Despite the moderation, food remained the main contributor to RPI inflation. Prices of housing also contributed to reduce inflation, though to a lesser extent. On the other hand, the contribution from transport and communication turned less negative. Meanwhile, clothing and footwear had a neutral impact on overall RPI inflation as did energy tariffs.

While the methodology underlying RPI and HICP is similar, they differ in that the RPI includes private households only, while HICP covers also institutional households and foreign visitors to Malta. Consequently, the difference between HICP and RPI inflation in part reflects the different structure of weights applied to the two indices. Furthermore, unlike the RPI weights, which were last updated in 2017, weights applied to the HICP index are updated annually. Chart 3.8

Chart 3.8
RPI AND HICP MAIN CONTRIBUTIONS
(annual percentage changes; contributions)



Sources: Eurostat; NSO; Central Bank of Malta calculations.

Table 3.2
CONTRIBUTIONS TO YEAR-ON-YEAR RPI INFLATION
Percentage points

	2023						2024					
	July	Aug.	Sep.	Oct.	Nov.	Dec.	Jan.	Feb.	Mar.	Apr.	May	June
Food	1.9	2.0	1.9	1.5	1.6	1.9	1.9	1.2	1.1	1.0	0.8	0.6
Beverages and tobacco	0.4	0.4	0.4	0.3	0.2	0.2	0.2	0.2	0.1	0.1	0.1	0.1
Clothing and footwear	-0.1	-0.1	0.1	-0.1	-0.1	-0.1	0.0	0.1	-0.1	0.0	0.0	0.0
Housing	0.7	0.7	0.6	0.5	0.4	0.4	0.2	0.2	0.2	0.1	0.1	0.1
Water, electricity, gas and fuels	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Household equipment and house maintenance costs	0.4	0.2	0.3	0.3	0.2	0.3	0.2	0.2	0.2	0.1	0.1	0.1
Transport and communications	0.0	-0.6	-0.5	0.0	-0.1	-0.3	-0.4	-0.5	-0.6	-0.8	-0.5	-0.4
Personal care and health	0.4	0.4	0.4	0.4	0.4	0.4	0.3	0.3	0.3	0.3	0.3	0.4
Recreation and culture	0.1	0.1	0.1	0.1	0.1	0.0	0.0	0.0	0.1	0.1	0.1	0.1
Other goods and services	0.5	0.5	0.5	0.5	0.5	0.5	0.4	0.4	0.4	0.5	0.4	0.3
RPI (annual percentage change)	**4.7**	**4.0**	**4.1**	**3.7**	**3.6**	**3.6**	**3.2**	**2.3**	**1.9**	**1.6**	**1.5**	**1.3**

Source: NSO.

[4] The RPI index differs from the HICP index in that RPI weights are based on expenditure by Maltese households, while HICP weights also reflect expenditure patterns by tourists in Malta, such as accommodation services. See Darmanin, J. (2018). "Household Expenditure in Malta and the RPI Inflation Basket", *Quarterly Review* 2018(3), pp. 33-40, Central Bank of Malta.

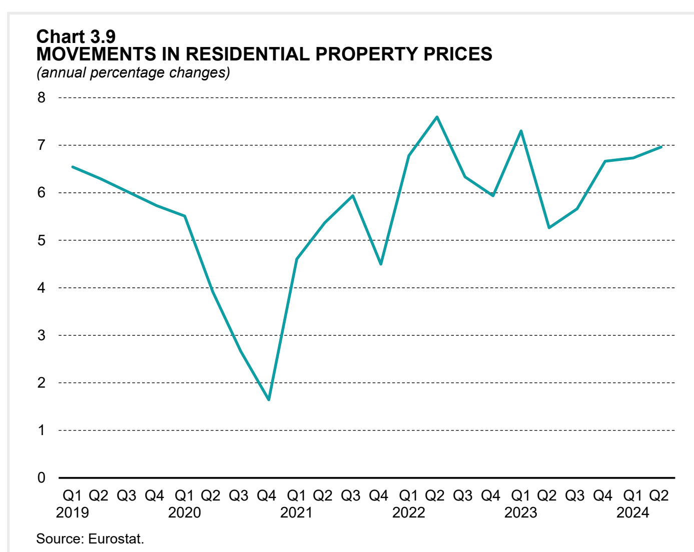
shows the contributions of the main sub-components to overall RPI and HICP inflation, respectively. While the contributions of HICP are official Eurostat figures, the RPI contributions are internal estimates based on an approximate mapping of individual RPI sub-items into corresponding HICP categories.[5,6] These estimates indicate that the largest difference between RPI and HICP in June, stemmed from services inflation.

The housing market

Residential property price inflation up from the previous quarter

The NSO's Property Price Index (PPI) – which is based on actual transactions involving apartments, maisonettes, and terraced houses – continued to increase in annual terms. The annual rate of change stood at 7.0% in the second quarter of 2024, up from 6.7% in the previous quarter (see Chart 3.9).[7] Meanwhile, in the euro area, prices on average increased at an annual rate of 1.3%.

Chart 3.9
MOVEMENTS IN RESIDENTIAL PROPERTY PRICES
(annual percentage changes)



Source: Eurostat.

Residential property prices in Malta continue to be supported by a number of Government schemes supporting demand for property, including the first-time and second-time buyers' schemes, the purchase of properties located in Urban Conservation Areas (UCA) and in Gozo, as well as refund schemes for restoration expenses. Moreover, a dynamic tourism sector, and significant migrant worker flows continue to support demand for accommodation and hence, property prices.

Misalignment indicator suggest prices are moderately below fundamentals

As part of its ongoing macroeconomic analysis, the Bank calculates a house price misalignment index to provide an indication of the evolution of house prices against fundamentals.[8,9] This indicator consists of five sub-indices that capture household, investor, and system-wide factors, with the weights being derived using principal component analysis.

[5] The RPI grouping of sub-components is intended to be as close as possible to the HICP grouping. For example, restaurants services and take-aways were included within 'Services' sub-component rather than within the 'Food" sub-component.

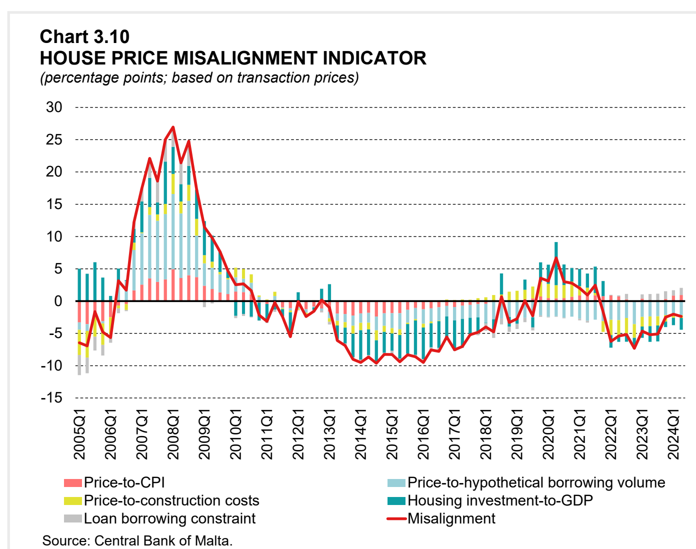
[6] The contributions of RPI sub-components are made to sum to the overall inflation by allocating a residual chain-linking component to the aforementioned sub-components.

[7] 'Apartments' are defined as dwellings with self-contained rooms or a suite of rooms that have a separate entrance accessible from a common passageway, landing or stairway. 'Maisonettes' have a separate entrance that is accessible from the street and are either at ground-floor level with overlying habitation, or at first-floor level with underlying habitation. 'Terraced houses' are dwellings with at least two floors, own access at street level and airspace, and with no underlying structures that are not part of the house itself. They are attached to other structures on both sides.

[8] See Micallef, B. (2018). "Constructing an index to examine house price misalignment with fundamentals in Malta", *International Journal of Housing Markets and Analysis*, 11(2), pp. 315-334.

[9] The actual numerical results presented in this section should not be overstated given the limitations in the construction of this indicator. For example, relevant variables such as foreign capital inflows are not included, and the unavailability of an official rental index precludes the use of the price-to-rent ratio in the indicator.

According to this indicator, house prices, as measured by the NSO's PPI, were moderately below the level consistent with fundamentals in the second quarter of 2024. The degree of undervaluation increased somewhat when compared with the first quarter of 2024 (see Chart 3.10).[10] The misalignment was driven mainly by the house price to hypothetical borrowing ratio followed by the ratio of housing investment to GDP. By contrast, the loan borrowing constraint and house price to CPI ratio contributed positively to the misalignment index.



The housing investment-to-GDP ratio was the main contributor behind the widening of the negative misalignment gap.

Number of final deeds increased in both quarterly and annual terms

NSO data on residential property transactions show that 3,192 final deeds of sale were registered in the quarter under review, an increase of 1.0% compared to the number of sales concluded in the previous quarter, and 6.2% higher than the same level registered in the same quarter a year earlier (see Table 3.3). Over 90% of transactions concluded in the second quarter of 2024 involved purchases by individuals.

In the second quarter of 2024, increases were recorded in all regions, apart from the Southeastern region where the number of deeds decreased in annual terms. In value terms, there was a year-on-year increase of 9.4%.

At 3,493, the number of promise-of-sale agreements was 0.2% lower than the number registered in the previous quarter, and in line with the same quarter of 2023. Half of all regions recorded year-on-year increases while the other half recorded decreases.

Table 3.3
RESIDENTIAL PROPERTY TRANSACTIONS
Levels

	2022	2023				2024	
	Q4	Q1	Q2	Q3	Q4	Q1	Q2
Residential transactions							
Promise of sale	3,353	3,118	3,494	3,076	3,502	3,499	3,493
Final deeds of sale	3,764	3,101	3,007	2,870	3,202	3,161	3,192

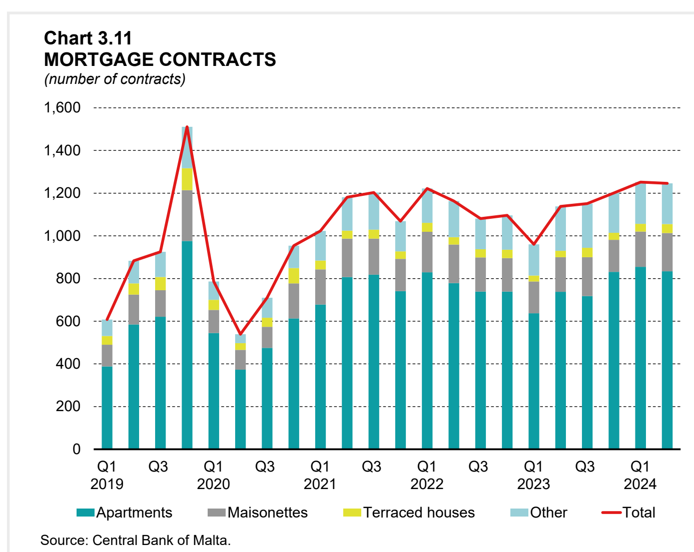
Source: NSO.

[10] A separate assessment based on advertised house prices can be found in Gatt, W., Micallef, B. and Rapa, N. (2018). "A macroeconometric model of the housing market in Malta", *Annual Research Bulletin*, Central Bank of Malta, pp. 11-18.

Mortgage transactions increase year-on-year[11]

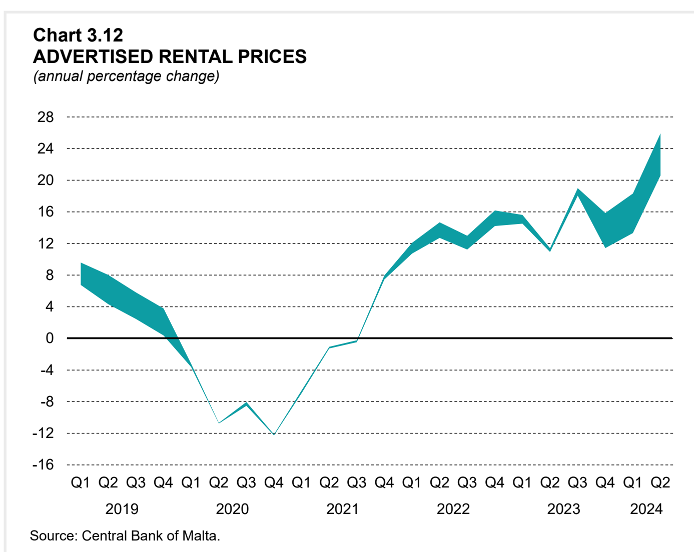
In the second quarter of 2024, the number of new mortgage contracts stood at 1,246. When compared with the second quarter of 2023, they increased by 9.5% (see Chart 3.11). Increases were observed for all main property categories except for 'other' properties, reflecting fewer loans for houses of character. However, almost 90% of the increase reflected a larger number of loans financing apartments.

The total number of mortgage contracts in the second quarter of 2024 stood below the peak of 1,511 transactions recorded in the last quarter of 2019 but significantly above the average of 963 transactions per quarter recorded since 2017.



Advertised rent prices continue to increase at a significant rate

The annual rate of change of advertised rents collected by the Bank from internet sources increased in the second quarter of 2024.[12] The range of estimates from various methods indicate that rents have increased at annual rates of between 20.6% and 25.9% in the quarter under review (see Chart 3.12). Compared with the previous quarter, the rate of increase included in the range of estimates has widened slightly and shifted up. In the quarter under review, the level of advertised rents stood around 40% above the average in recent years.[13]



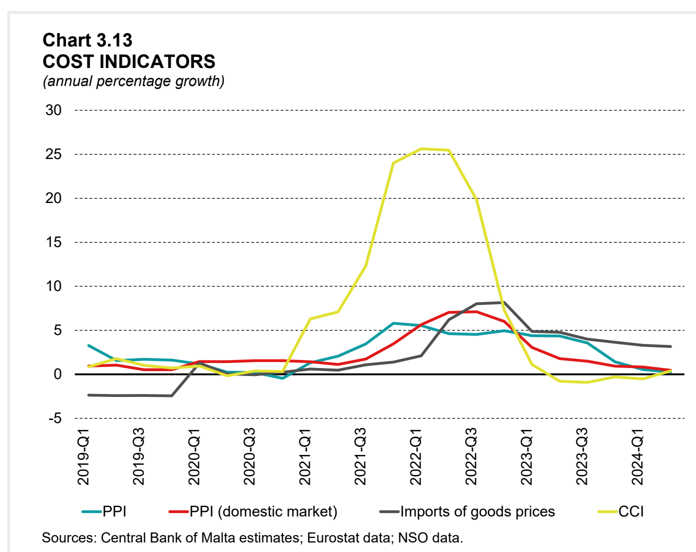
[11] The data used in the section are collected by the Central Bank of Malta from four commercial banks and relate only to properties which have been purchased with a mortgage. The dataset excludes properties that have either been transacted using other means of financing, as well as mortgages that have been refinanced. The property types included are flats, penthouses, maisonettes, terraced houses, town houses, houses of character, farmhouses, bungalows, and villas. Other property types included in the previous section such as airspace, boathouses, garages, and plots of land are excluded.

[12] The empirical analysis is based on hedonic regression models as described in Debono et al. (2020) and different indices are constructed using alternative methodologies, namely the time dummy method, the rolling time dummy method with a window length of two periods (Q=2) and the average characteristics method chained using the Laspeyres, Paasche and Fisher methods. The properties considered in this analysis include apartments, maisonettes, and penthouses.

[13] This index is available from 2017Q4.

Cost indices

Most indicators of producer costs grow at a slower pace



The industrial producer price index is a measure of the prices of goods sold by producers in the industrial sector. Annual inflation according to this index eased to 0.2% on average in the quarter under review, down from 0.6% in the previous quarter (see Chart 3.13).[14] This moderation was largely driven by developments in producer prices for intermediate goods, whose annual rate of change became more negative, standing at -3.2% in the second quarter of 2024, compared to -1.3% previously. At the same time, producer prices of consumer goods rose at a marginally slower annual rate of 1.6% in this quarter, from 1.8% in the previous quarter. By contrast, the annual rate of change of producer prices of capital goods grew at a faster pace of 6.2% in the quarter under review, up from 3.3% in the previous quarter. Meanwhile, energy producer price inflation remained unchanged.

Other indicators affecting the domestic market also show easing cost pressures. The domestic producer price index rose at a slightly slower annual rate of 0.5%, from 0.8% in the first quarter, mainly driven by slower growth in producer prices of consumer goods.[15] The imports of goods deflator also shows marginally weaker growth of 3.2%, from 3.3% in the first quarter of 2024.[16] The CCI for new residential buildings published by Eurostat increased in the second quarter of 2024, standing at 0.3% after it had declined by 0.5% in the previous quarter. Notwithstanding the recent declines, its level remains above that observed before 2020.

ULCs increase at a faster rate

Malta's ULC index – measured as the ratio of CPE to labour productivity – increased in annual terms, as well as in quarter-on-quarter terms in the second quarter of 2024.[17]

When measured on a four-quarter moving average basis in headcount terms, ULCs in Malta rose at an annual rate of 1.4%. This followed an increase of 0.6% in the previous quarter (see Chart 3.14). The pick-up in ULC growth largely reflects an acceleration in CPE. This rose by 3.1% in annual terms, from 2.5% in the first quarter. To some extent, the increase in ULC

[14] The industrial producer price index measures the prices of goods at the factory gate and is commonly used to monitor inflationary pressures at the production stage. The index used here refers to the B-E36 aggregate of the EU's statistical classification of economic activities.
[15] The domestic producer price index refers to the producer prices relating to the domestic market only, whilst the producer price index relates to the total market, i.e., including both the domestic and non-domestic markets.
[16] This index is derived from national accounts data published by the NSO.
[17] Annual growth in ULC, CPE and labour productivity is measured on a four-quarter moving average basis. A degree of caution is required in the interpretation of ULC in view of contemporaneous structural shifts in the composition and factor-intensity of production, notably the shift to labour-intensive services. See Micallef, B. (2015). "Unit labour costs, wages and productivity in Malta: a sectoral and cross-country analysis", *Policy Note* August 2015, Central Bank of Malta, and Rapa, N. (2016). "Measuring international competitiveness", *Quarterly Review* 2016(1), pp. 53-63, Central Bank of Malta.

growth also reflected slower growth in productivity per person. This rose by an annual rate of 1.7% in the second quarter, from 1.9% in the previous one.

When measured on a four-quarter moving average basis, growth in CPE was fastest in the real estate activities sector, which had a year-on-year growth rate of 11.7% (see Chart 3.15). Wage growth was also significant in the information and communication sector, where compensation per person grew by 7.6%. Overall, compared with the previous quarter, CPE grew at a faster rate across most sectors, including the two aforementioned ones. Only two sectors displayed slower growth compared to the first quarter, these being the financial and insurance activities sector and the sector comprising professional, scientific and technical activities, which recorded increases of 6.0% and 2.3%, respectively.

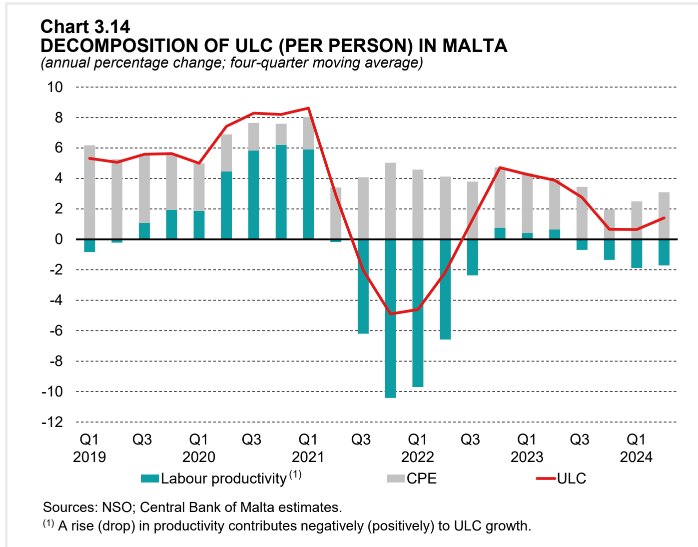


Chart 3.14
DECOMPOSITION OF ULC (PER PERSON) IN MALTA
(annual percentage change; four-quarter moving average)

Sources: NSO; Central Bank of Malta estimates.
(1) A rise (drop) in productivity contributes negatively (positively) to ULC growth.

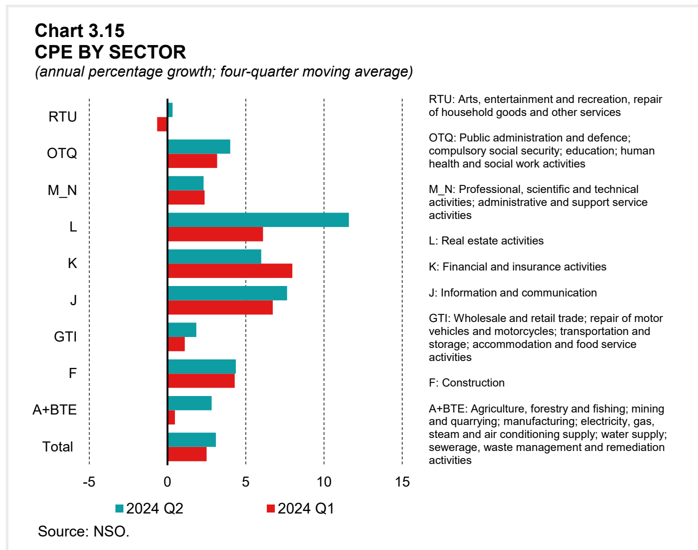


Chart 3.15
CPE BY SECTOR
(annual percentage growth; four-quarter moving average)

Source: NSO.

4. THE BALANCE OF PAYMENTS

During the second quarter of 2024, the current account surplus widened compared to the same quarter of the previous year. This was mainly due to higher net receipts from services, although a narrower merchandise trade deficit also contributed. By contrast, net outflows on the primary income accounts increased and net inflows on the secondary income account decreased.

In the quarter under review, net inflows on the capital account increased when compared to the corresponding quarter of 2023, while the financial account showed higher net lending.

The current account balance registered a surplus equivalent to 7.0% of GDP in the second quarter of 2024. This compares with a current account surplus of 2.6% of GDP in the euro area.

The cyclically-adjusted current account balance is estimated to have recorded a surplus of 10.3% during the quarter under review.

As balance of payments data are undergoing substantial revisions, readers are advised to exercise caution in interpreting changes over time.

In the second quarter of 2024, the tourism sector reported further gains. The number of inbound tourists, nights stayed, and tourist expenditure in Malta all increased when compared with a year earlier.

The current account

The current account surplus widens

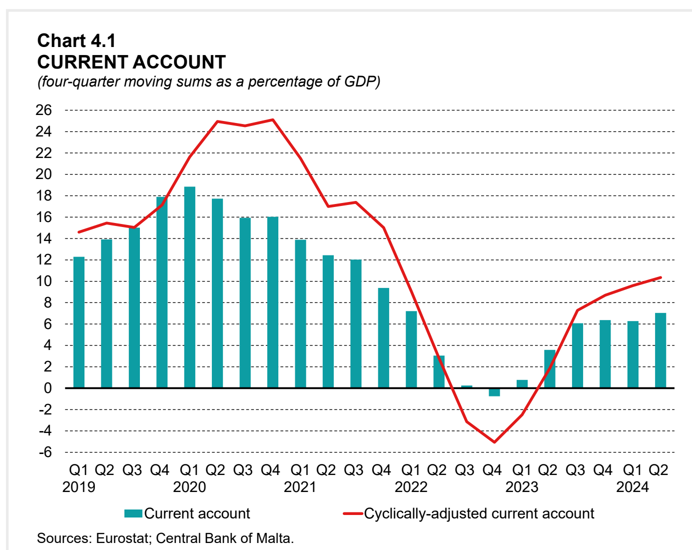
Between April and June 2024, the current account of the balance of payments recorded a surplus of €406.5 million, a €190.8 million increase from the surplus recorded in the same quarter of 2023 (see Table 4.1). This mostly reflected higher net receipts from services, although a slight narrowing in the goods deficit also contributed. These offset higher net outflows on the primary income account and lower net inflows on the secondary income account.

Table 4.1
BALANCE OF PAYMENTS
EUR millions

	Four-quarter moving sums						
	2023 Q2	2023 Q3	2023 Q4	2024 Q1	2024 Q2	2023 Q2	2024 Q2
Current account	**694.9**	**1,220.5**	**1,315.5**	**1,330.1**	**1,521.0**	**215.7**	**406.5**
Goods	-2,996.8	-2,488.9	-2,446.6	-2,449.1	-2,443.1	-743.0	-737.0
Services	5,824.5	6,001.9	6,153.2	6,292.4	6,606.1	1,486.0	1,799.6
Primary income	-2,053.5	-2,217.8	-2,303.1	-2,477.2	-2,599.6	-541.5	-664.0
Secondary income	-79.4	-74.7	-88.0	-36.1	-42.5	14.3	7.9
Capital account	**221.3**	**234.2**	**255.8**	**306.1**	**366.6**	**38.9**	**99.4**
Financial account[1]	**637.6**	**1,470.8**	**1,917.1**	**1,833.5**	**2,267.9**	**346.7**	**781.1**
Errors and omissions	**-278.5**	**16.1**	**345.9**	**197.3**	**380.4**	**92.2**	**275.2**

Sources: Eurostat; Central Bank of Malta.
[1] Net lending (+) / net borrowing (-).

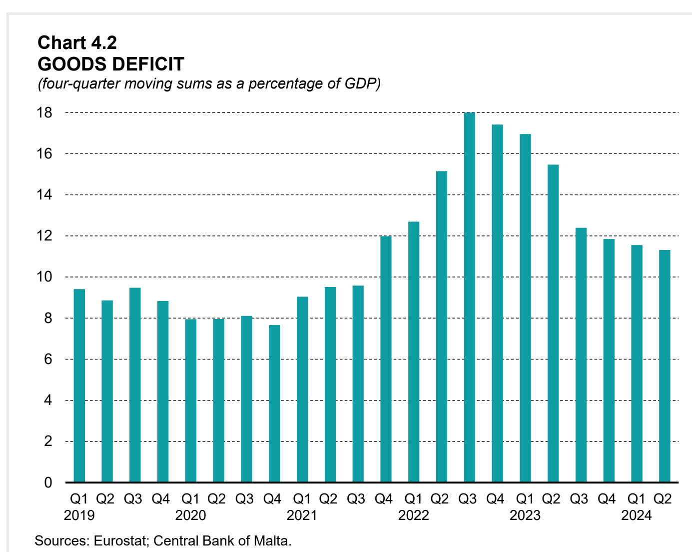
On a four-quarter moving sum basis, the current account surplus broadly doubled to €1,521.0 million, from a surplus of €694.9 million a year earlier. This reflected a lower merchandise trade deficit, a higher surplus on the services account, as well as marginally smaller net outflows on the secondary income account. These offset higher net outflows on the primary income account. As a result, the current account balance-to-GDP ratio reached 7.0%, from 3.6% a year earlier (see Chart 4.1). Malta's cyclically-adjusted current account surplus is estimated to have stood at 10.3% of GDP in the second quarter of 2024, and thus more positive than the headline measure (see Chart 4.1).[1]



The merchandise trade deficit narrows slightly

In the second quarter of 2024, the merchandise trade deficit stood at €737.0 million, down from €743.0 million in the corresponding period of 2023. This was driven by a decrease in imports which was only partly offset by a decrease in exports. The former mostly reflected a decrease in imports of semi-manufactured goods and food, followed by lower imports of machinery.

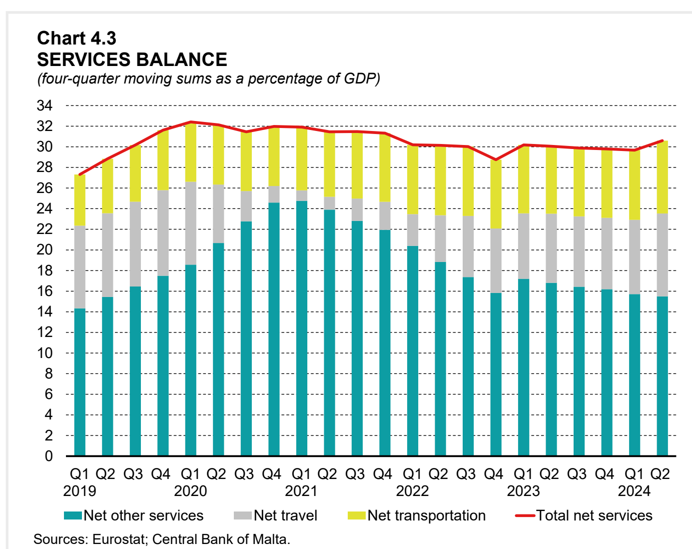
The visible trade gap also declined when measured on a four-quarter cumulative basis, reaching €2,443.1 million, from €2,996.8 million in the same period a year earlier. This reflected a €555.8 million decline in goods imports, mainly because of a decrease in imports of machinery and semi-manufactured goods, and a marginal decrease in exports of €2.1 million. As a result, the share of the goods deficit in GDP declined to 11.3% during the second quarter of 2024, from 15.5% a year earlier (see Chart 4.2).



[1] For more information on Malta's cyclically-adjusted current account see Grech, A. G., & Rapa, N., "An evaluation of recent shifts in Malta's current account position", in Grech, A.G., & Zerafa, S. (eds.), *Challenges and Opportunities of Sustainable Economic Growth: the Case of Malta,* Central Bank of Malta, 2017.

The surplus on services widens

In the quarter under review, net receipts on the services account amounted to €1,799.6 million, €313.7 million more than in the corresponding period of 2023. Both services exports and imports increased on a year earlier. However, the increase in the former was stronger.



Sources: Eurostat; Central Bank of Malta.

Higher net receipts from travel were the key factor behind the increase in the overall surplus on the services account. However, net receipts related to transport and 'other' services also contributed.

On a four-quarter cumulative basis, the overall surplus from services stood at €6,606.1 million, an increase of €781.6 million over the surplus recorded in the same period last year. The main contributors to this increase were the transport and travel components, although net receipts from 'other services' also rose. These were mainly supported by higher receipts from personal, cultural and recreational services as well as financial services. The share of net services receipts in GDP stood at 30.6%, from 30.1% registered during the same period last year (see Chart 4.3).

Net outflows on the primary income account increase[2]

Between April and June 2024, net outflows on the primary income account stood at €664.0 million, €122.4 million more than in the second quarter of 2023. This was mainly due to higher net outflows on the investment income account, as a result of lower net receipts on the portfolio investment and direct investment accounts.

In the four-quarter period to June 2024, net outflows on the primary income account increased by €546.1 million, to stand at €2,599.6 million. Transactions relating to primary income continued to be strongly influenced by internationally-oriented firms, which transact predominantly with non-residents. During this period, net outflows on the primary income account amounted to 12.0% of GDP, up from net outflows of 10.6% a year earlier.

Inflows on the secondary income account decrease year-on-year[3]

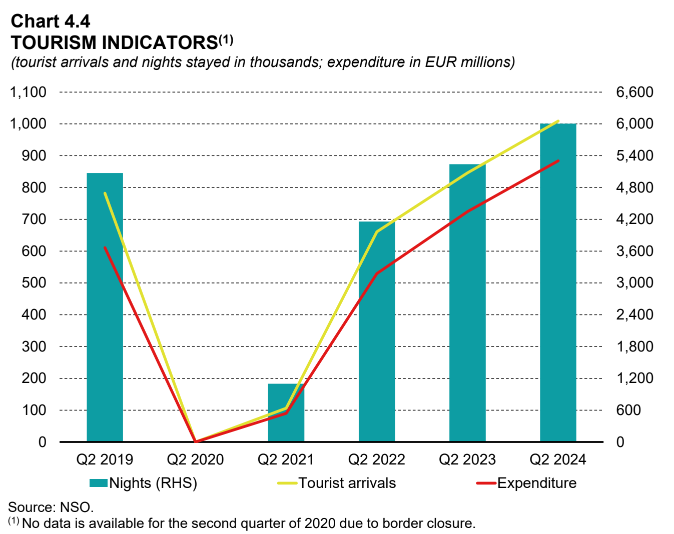
In the second quarter of the year, net inflows on the secondary income account decreased by €6.4 million on a year earlier, to reach €7.9 million.

In the four quarters to June 2024, however, net outflows decreased. They stood at €42.5 million, equivalent to -0.2% of GDP, less than -0.4% of GDP a year earlier.

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

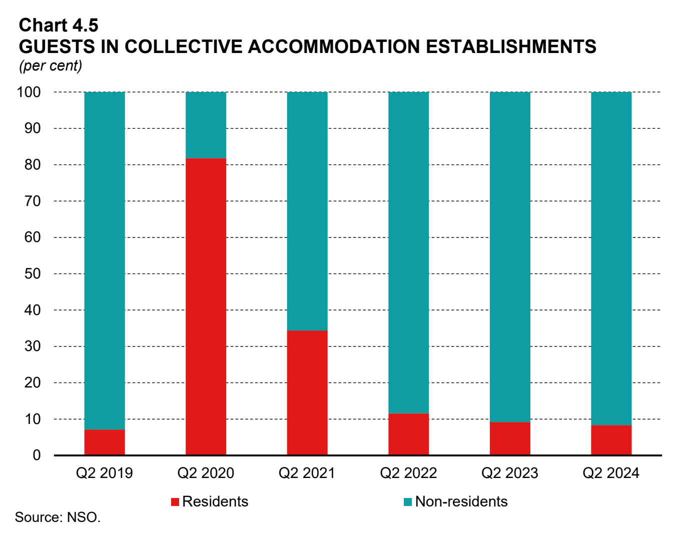
Tourism activity

In the quarter under review, the number of inbound tourists amounted to 1,009,028, up from 846,230 a year earlier (see Chart 4.4). Visitors from the United Kingdom accounted for almost a third of the increase. They were followed by visitors from Poland and Italy. In absolute terms, tourists visiting for holiday purposes accounted for nearly all of this rise. Visitors coming for business purposes increased somewhat, while those citing 'other' motives declined.



Source: NSO.
(1) No data is available for the second quarter of 2020 due to border closure.

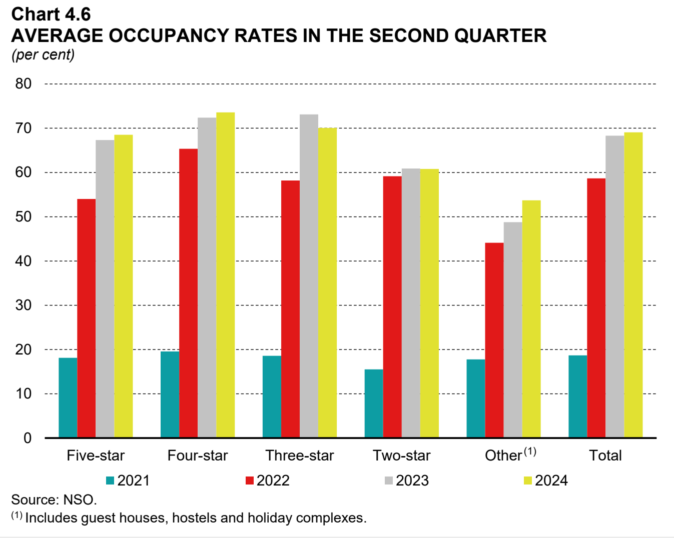
The total number of guest nights that tourists spent in Malta during the second quarter of 2024 totalled 6.0 million, up from 5.2 million a year earlier. Stays in rented collective accommodation accounted for most of this increase.



Source: NSO.

In the second quarter of 2024, the share of non-residents in collective accommodation establishments stood at 91.7%, up from 90.8% in the second quarter of 2023 (see Chart 4.5).

The total occupancy rate in collective accommodation establishments in the second quarter of 2024 rose to 69.1%, from 68.3% a year earlier (see Chart 4.6). The "other" accommodation category registered the largest increase of 4.9 percentage points. It was followed by the five-star and four-star categories, both of which recorded a rise of 1.2 percentage points. Occupancy in the three-star category declined, but was broadly unchanged in



Source: NSO.
(1) Includes guest houses, hostels and holiday complexes.

the two-star category. The latter retained the lowest occupancy rate across all hotel categories.

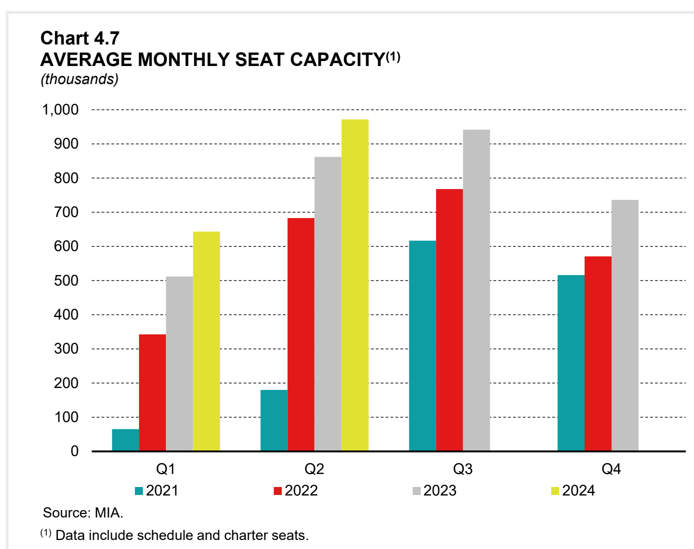


Chart 4.7
AVERAGE MONTHLY SEAT CAPACITY[1]
(thousands)

Source: MIA.
[1] Data include schedule and charter seats.

Tourist expenditure in Malta totalled €884.0 million in the second quarter of 2024, up from €724.4 million a year earlier. All expenditure categories registered gains over this period.

Expenditure per capita increased to €876.1, from €856.0 in the seond quarter of 2023, as expenditure per night increased, offsetting a decline in the average length of stay, which stood at 6.0 nights from 6.2 nights a year earlier.

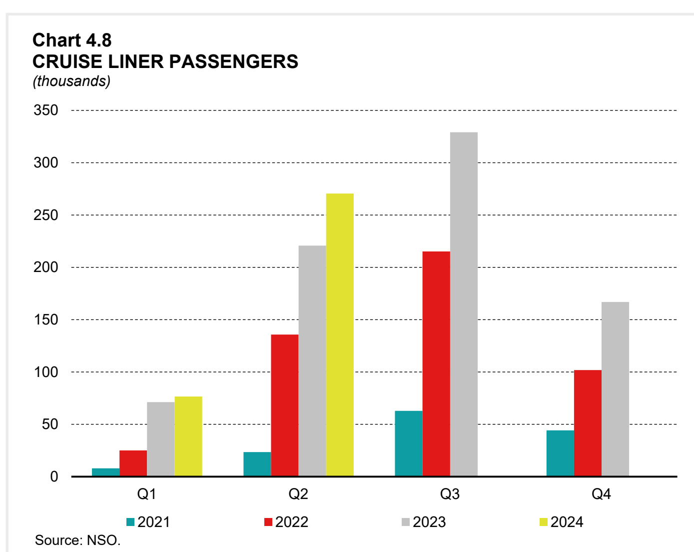


Chart 4.8
CRUISE LINER PASSENGERS
(thousands)

Source: NSO.

According to Malta International Airport (MIA) data, in the second quarter of 2024, average seat capacity stood at 971,786 seats per month, up from 862,128 a year earlier (see Chart 4.7).

A total of 128 cruise liners visited Malta in the second quarter of 2024, 30 more than a year earlier. Foreign passengers reached 270,567 persons, up from 220,805 visitors in the second quarter of 2023 (see Chart 4.8).

The United States was the most important source market for cruise passengers – in part reflecting an increase in calls by cruise liners that are frequently used by US travellers compared to a year earlier – followed closely by the United Kingdom. Together they made up almost half of total cruise passengers. They were followed by Italy and Germany, which together accounted for around a fifth of ship tourists.

The capital account

Net inflows on the capital account stood at €99.4 million in the second quarter of 2024, up from €38.9 million in the same quarter of 2023 (see Table 4.1). When measured on a four-quarter cumulative basis, capital inflows increased to €366.6 million, from €221.3 million during the 12 months to June 2023. Their share in GDP increased to 1.7% from 1.1% in the second quarter of 2023.

5. GOVERNMENT FINANCE

In the second quarter of 2024, the general government balance recorded a surplus which contrasts with a deficit in the corresponding period of 2023. When measured on a four-quarter moving sum basis, the general government deficit ratio narrowed by 0.4 percentage points, to reach 3.4% from 3.8% in March 2024. Similarly, the cyclically-adjusted deficit narrowed.

The general government debt-to-GDP ratio declined by 0.5 percentage points to stand at 46.7% at the end of June. Meanwhile, the net financial worth as a share of GDP improved, though it remained negative.

Quarterly developments

General government balance registers a surplus in the second quarter
In level terms, the general government registered a surplus of €55.2 million in the second quarter of 2024, which contrasts with a deficit of €17.7 million registered in the corresponding period of 2023. This was due to a strong increase in government revenue offsetting a rise in government expenditure. The primary balance registered a surplus of €114.8 million in the quarter under review, higher than the primary surplus of €35.9 million recorded a year earlier.

Tax inflows support revenue growth
In the second quarter of 2024, general government revenue increased by €233.7 million, or 13.3%, when compared with the same quarter of 2023 (see Table 5.1). This was mainly driven by higher tax revenue, particularly inflows from current taxes on income and wealth, which increased by €82.4 million. This is due to higher income tax inflows from households. Moreover, receipts from taxes on production and imports rose by €65.0 million, mainly reflecting higher inflows from VAT. Social contributions received rose by €21.5 million, reflecting favourable labour market conditions. Inflows from capital and current transfers increased by €27.1 million, mainly reflecting higher inflows from grants. Furthermore, income from sales increased and was the main factor behind the €37.6 million increase in 'other' revenue.

Expenditure growth underpinned by current spending
Total government expenditure increased by €160.8 million, or 9.1%, when compared with the second quarter of 2023. This increase mostly reflects higher current expenditure, due to a rise of €140.5 million in current transfers payable. This surge in outlays partly reflects the timing of tax refund cheques distributed to households, which were delivered earlier in 2024. It also reflects higher payments to the EU budget.

Spending on social benefits and compensation of employees also increased. The former rose by €42.5 million, largely on the back of higher spending on retirement pensions and children's allowances. Spending on compensation of employees increased by €31.7 million, mainly due to higher outlays in the health, public administration and education sectors. Meanwhile, spending on intermediate consumption rose by €17.4 million. This rise was largely due to higher outlays in the public administration sector, which outweighed a decline in spending in the health, residential care and education sectors. Interest payments increased by €6.1 million in line with higher debt levels and the financing cost of debt.

Table 5.1
REVENUE, EXPENDITURE AND DEBT
EUR millions

	2023			2024		Change 2024Q2-2023Q2	
	Q2	Q3	Q4	Q1	Q2	Amount	%
Revenue	**1,750.9**	**1,655.1**	**1,722.8**	**1,692.8**	**1,984.6**	**233.7**	**13.3**
Taxes on production and imports	462.9	525.2	505.1	521.3	527.9	65.0	14.0
Current taxes on income and wealth	771.9	617.0	611.7	690.9	854.3	82.4	10.7
Social contributions	264.9	263.5	296.7	272.6	286.4	21.5	8.1
Capital and current transfers receivable	62.4	80.5	121.0	40.2	89.6	27.1	43.5
Other[1]	188.9	168.9	188.3	167.8	226.5	37.6	19.9
Expenditure	**1,768.6**	**1,733.4**	**2,322.2**	**1,801.4**	**1,929.4**	**160.8**	**9.1**
Compensation of employees	479.3	493.4	493.7	511.7	510.9	31.7	6.6
Intermediate consumption	374.0	326.8	448.6	357.2	391.4	17.4	4.7
Social benefits	418.8	379.1	400.7	501.4	461.3	42.5	10.1
Subsidies	178.9	150.9	277.1	117.7	103.2	-75.7	-42.3
Interest	53.6	52.4	64.2	63.2	59.6	6.1	11.3
Other current transfers payable	54.9	119.7	148.2	82.5	195.4	140.5	256.0
GFCF	164.6	157.8	275.9	122.2	150.5	-14.1	-8.6
Capital transfers payable	39.7	51.4	206.3	41.8	52.6	12.9	32.6
Other[2]	4.8	1.9	7.5	3.6	4.4	-0.4	
Primary balance	**35.9**	**-25.9**	**-535.2**	**-45.4**	**114.8**	**78.9**	
General government balance	**-17.7**	**-78.2**	**-599.4**	**-108.6**	**55.2**	**72.8**	
General government debt	**9,172.0**	**9,420.8**	**9,791.4**	**10,000.2**	**10,084.0**		

Source: NSO.

[1] "Other" revenue includes market output as well as income derived from property and investments.

[2] "Other" expenditure principally reflects changes in the value of inventories and in the net acquisition of valuables and other assets.

These increases were partly offset by a €75.7 million decline in subsidies, reflecting lower spending on support measures to mitigate energy price pressures.

Meanwhile, GFCF and capital transfers declined by €14.1 million and €12.9 million respectively, mostly due to a decline in domestically-financed projects.

Debt increases

In June 2024, the stock of general government debt amounted to €10,084.0 million, €83.8 million higher than the level registered at end-March 2024. This reflects an increase in short-term debt securities outstanding (composed of Treasury bills), which offset a decline in long-term debt securities outstanding (composed of MGS). The former rose by €92.6 million, with its share in total debt increasing by 0.9 percentage points to 5.3%. Holdings of long-term debt securities declined by €14.2 million, with their share in total debt decreasing by 0.8 percentage points to 80.8%.

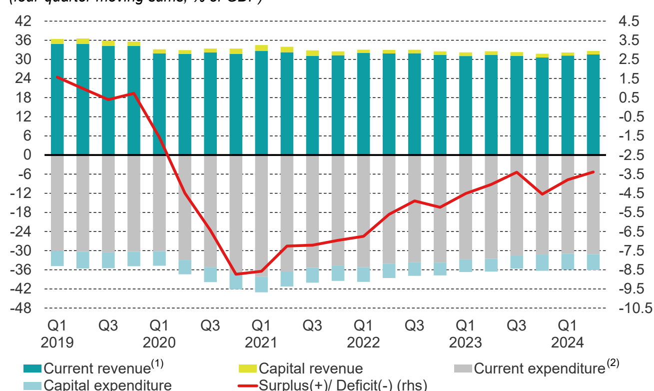
The value of loans outstanding increased by €5.1 million, due to an increase in long-term loans. The share of loans outstanding in total debt remained broadly unchanged at 9.7%.

Headline and cyclically-adjusted developments

Headline deficit and debt ratios decline

When measured on a four-quarter moving sum basis, the general government deficit-to-GDP ratio narrowed by 0.4 percentage points, from 3.8% in the first quarter of 2024 to 3.4% in the quarter under review (see Chart 5.1). This was mostly driven by a 0.5 percentage point rise in the revenue-to-GDP ratio, which reached 32.7%, due to a rise in the share of current revenue in GDP. This offset a marginal increase in the expenditure-to-GDP ratio, which reached 36.1%. The latter increased due to a 0.2 percentage point increase in the share of current expenditure in GDP.

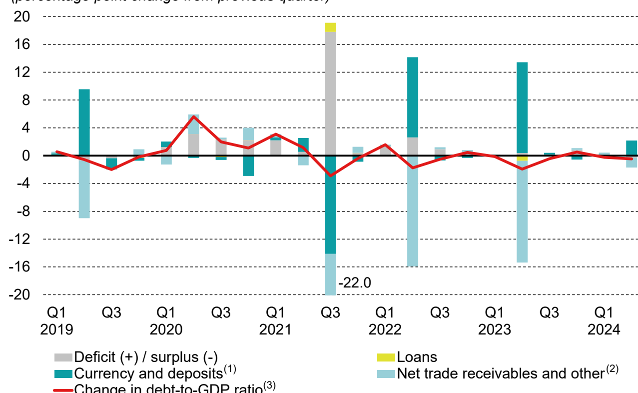
Chart 5.1
GENERAL GOVERNMENT REVENUE AND EXPENDITURE
(four-quarter moving sums; % of GDP)



Sources: NSO; Central Bank of Malta.
(1) The term 'current revenue' represents most tax revenue as well as income from investments and sales. 'Capital revenue' mainly represents capital taxes and grants received.
(2) The term 'current expenditure' mainly represents spending on wages, social benefits and operational and maintenance expenses. 'Capital expenditure' mainly represents spending on investment and capital transfers.

Although debt increased in level terms, the increase in nominal GDP over the same period was more significant. Between March 2024 and June 2024, the debt-to-GDP ratio decreased by 0.5 percentage points, from 47.2% to 46.7% (see Chart 5.2). The decrease in this ratio reflects the shift to a surplus as well as transactions in net trade receivables. The latter offset a build-up in government deposits. These transactions reflect the settlement of tax refunds owed by eligible firms.

Chart 5.2
CONTRIBUTION TO CHANGE IN DEBT
(percentage point change from previous quarter)



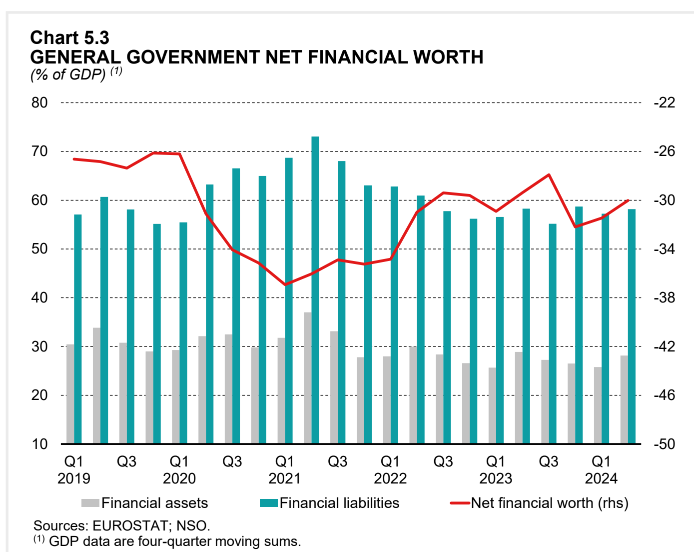
Source: Central Bank of Malta.
(1) Composed mainly of transactions in deposits held with the Central Bank of Malta.
(2) Also includes transactions related to shares and other equity and adjustments for valuation and volume effects.
(3) GDP data are four-quarter moving sums.

Net financial worth improves

The market value of financial assets held by the general government increased to €6,080.4 million by June 2024, €614.8 million higher than the level three months earlier. This was mostly due to a rise in the value of deposits, followed by rises in the values of other accounts receivable, debt securities and shares and other equity. Consequently, the share of financial assets in GDP rose to 28.2% from 25.8% in the previous quarter (see Chart 5.3).

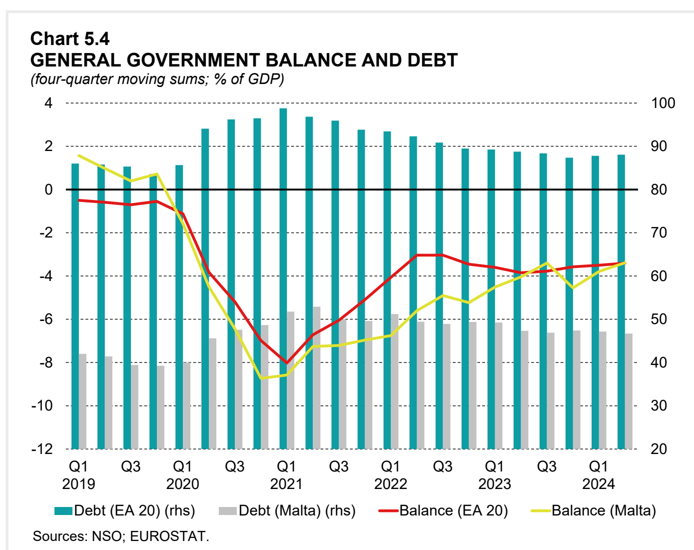
The market value of financial liabilities increased by €426.1 million, to stand at €12,563.0 million. This is driven by a rise in the value of other accounts payable. The decline was partly offset by a decrease in the value of debt securities. Consequently, the share of financial liabilities in GDP

increased by 0.9 percentage points, to stand at 58.2%.



The resulting net financial worth of general government stood at -€6,482.6 million, an improvement of €188.7 million compared with the previous quarter. The net financial worth of general government as a share of GDP improved by 1.4 percentage points, standing at -30.0% by end-June.

Over the same period, the euro area average net financial value as a share in GDP improved by 0.9 percentage points, to -55.7.% of GDP. Thus, the net worth position of the Maltese general government remained more favourable than the euro area average.



Debt ratio continues to compare favourably with the euro area's with the deficit declining to the euro area's

During the quarter under review, the euro area general government deficit stood at 3.4% of GDP on a four-quarter moving sum basis, down from a deficit of 3.5% of GDP at end-March (see Chart 5.4). Over the same period, the euro area debt ratio rose to 88.1% of GDP from 87.8% in the previous quarter.

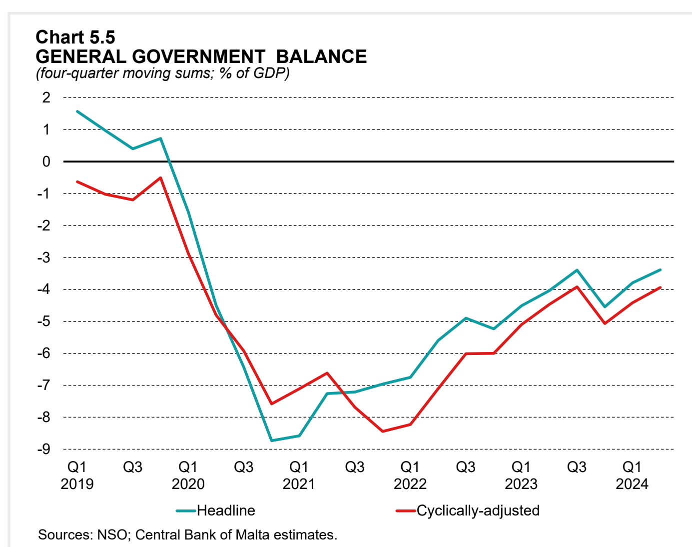
The Maltese government deficit ratio narrowed at a faster rate than the euro area average. As a result, the Maltese ratio converged to the latter. At the same time, Malta's debt-to-GDP ratio remained well below the euro area average.

Cyclically-adjusted deficit narrows[1]

On a four-quarter moving sum basis, the cyclically-adjusted deficit narrowed by 0.5 percentage points compared to March, to stand at 3.9% of GDP in the quarter under review (see Chart 5.5).

[1] The cyclically-adjusted balance is corrected for the impact of the economic cycle on government tax revenue and unemployment assistance. This methodology is in line with the approach used by the European Commission but is based on own estimates for fiscal items' elasticities and the output gap. For an overview of the method used by the Commission, see Mourre, G., Astarita C., and Princen, S. (2014). "Adjusting the budget balance for the business cycle: the EU methodology," European Economy – Economic Papers 536, (DG ECFIN), European Commission.

This is broadly in line with the 0.4 percentage point narrowing in the headline deficit ratio over the same period.



Sources: NSO; Central Bank of Malta estimates.

When compared with March, the share of cyclically-adjusted revenue in GDP increased by 0.5 percentage points (see Table 5.2). This was due to an increase in the share of current taxes on income and wealth and an increase in the 'other' component of revenue. The latter increased due to the aforementioned rise in capital transfers. To a lesser extent, taxes on production and imports also contributed to this positive change in the cyclically-adjusted revenue.

Meanwhile, the share of cyclically-adjusted expenditure remained unchanged. This was mainly due to a decline in the share of intermediate consumption and government investment being counterbalanced by an increase in the ratio of 'other' expenditure. The latter reflects a rise in the ratio of current transfers.

Table 5.2
QUARTER-ON-QUARTER CHANGES IN CYCLICALLY-ADJUSTED FISCAL COMPONENTS
Percentage points of GDP

	2023			2024	
	Q2	Q3	Q4	Q1	Q2
Revenue	**0.4**	**-0.2**	**-0.5**	**0.4**	**0.5**
Current taxes on income and wealth	0.5	-0.3	-0.5	0.5	0.2
Taxes on production and imports	-0.2	-0.1	-0.1	0.1	0.1
Social contributions	0.0	-0.1	0.0	0.0	0.0
Other[1]	0.0	0.3	0.1	-0.2	0.2
Expenditure	**-0.3**	**-0.8**	**0.7**	**-0.2**	**0.0**
Compensation of employees	-0.3	-0.1	-0.1	-0.1	0.0
Intermediate consumption	0.0	0.0	0.1	0.0	-0.1
Social benefits	0.0	-0.1	-0.2	0.0	0.0
Interest payments	0.0	0.0	0.1	0.1	0.0
GFCF	0.0	0.0	0.2	0.0	-0.1
Other[2]	-0.1	-0.6	0.6	-0.3	0.2
Primary balance	**0.7**	**0.6**	**-1.1**	**0.7**	**0.5**
General government balance	**0.6**	**0.5**	**-1.1**	**0.6**	**0.5**

Sources: NSO; Central Bank of Malta estimates.
[1] Includes market output, income derived from property and investments and current and capital transfers received.
[2] Mainly includes subsidies, current and capital transfers.

6. MONETARY AND FINANCIAL DEVELOPMENTS

According to the Bank's FCI, in the second quarter of 2024, financing conditions remained loose from a historical perspective.

In June, Maltese residents' deposits with MFIs in Malta increased from their year-ago level, reflecting higher balances belonging to households and insurance companies.[1] The annual rate of change exceeded that recorded in the first quarter of 2024. Credit to Maltese residents rose at a faster rate, as both credit to general government and credit to other residents picked up.

The weighted average interest rate on outstanding deposits stood above its year-ago level, while the rate on loans decreased compared to a year earlier. Thus, the spread between the two rates narrowed over this period.

In June, the primary market yield on Treasury bills increased from that prevailing three months earlier. Meanwhile, secondary market yields on five and ten-year MGS also rose. As the increase in the domestic ten-year yield was more pronounced than that in the corresponding euro area benchmark, the spread between the two widened slightly. Domestic share prices fell between March and June and were also marginally lower compared with a year earlier.

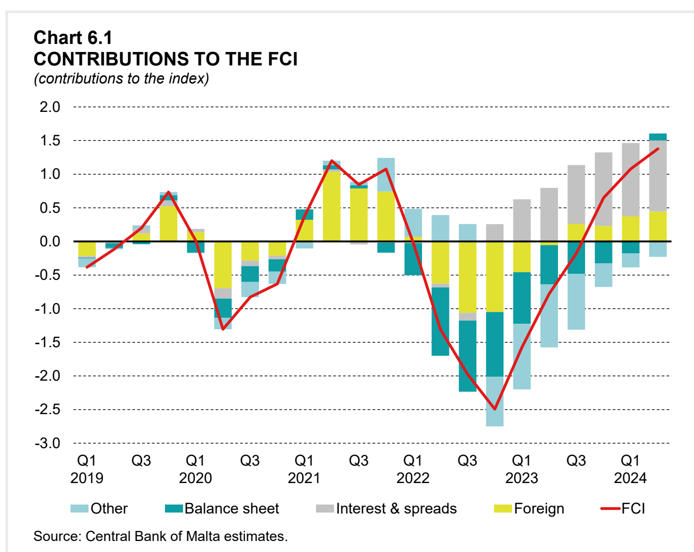
Monetary and financial conditions

Financial conditions continue to loosen[2]

In the second quarter of 2024, the Bank's FCI continued to signal loose financial conditions from a historical perspective. Moreover, these loosened when compared to the previous quarter (see Chart 6.1). As a result, financial conditions according to the FCI are the most accommodative since 2021.

The recent loosening in financial conditions was mainly driven by domestic factors, although foreign factors also contributed. The higher loosening effect of domestic factors mainly reflects improvements in the 'balance sheet' component, which was affected by a smaller negative contribution in real credit and deposits and a positive contribution from the banks' return on equity.

Chart 6.1
CONTRIBUTIONS TO THE FCI
(contributions to the index)



Source: Central Bank of Malta estimates.

The 'interest and spread' component recorded a marginally lower positive contribution, driven by a lower positive contribution from the lending rate to policy

[1] Monetary data analysed in this chapter are compiled on the basis of the statistical standards found in the Statistics section of the Bank's website.

[2] This index is composed of various financial indicators, which are available at a high frequency. This section is based on quarterly averages for each indicator.

spread and from interest rates on deposits. Meanwhile the 'other' component had a slightly higher negative contribution compared to the first quarter, mostly reflecting developments in equity prices.

Foreign factors also showcased a looser stance compared to the previous quarter, reflecting some decline in uncertainty during the second quarter of 2024.

Financial conditions have become significantly more loose compared to the second quarter of 2023, reflecting developments in both domestic and foreign factors, with domestic factors contributing the most.

The stronger loosening effect of domestic factors mostly reflected an increase in the issues of NFC securities (part of the 'other' component) and lower negative contributions from real credit and real deposits (part of the 'balance sheet' component). The loosening effect in foreign factors reflect lower uncertainty.

Maltese residents' deposits continue to increase

Total deposits held by Maltese residents with MFIs in Malta increased by 2.2% in the year to June, a faster rate of increase than the 1.7% growth observed in the year to March (see Table 6.1). The latest increase reflects higher balances belonging to households and insurance companies, offsetting lower balances belonging to other financial intermediaries.

Table 6.1
DEPOSITS OF MALTESE RESIDENTS

	EUR millions	Annual percentage changes				
	2024	2023			2024	
	June	June	Sep.	Dec.	Mar.	June
Overnight deposits	**20,211**	**1.1**	**-3.6**	**-0.2**	**-0.7**	**-0.5**
of which						
Households	14,464	5.0	0.0	1.8	1.2	2.3
NFCs	3,292	-5.2	-6.2	-5.2	-1.7	-2.6
Deposits redeemable at notice of up to three months	**79**	**-10.5**	**9.4**	**-26.0**	**-23.5**	**-33.4**
of which						
Households	0	-0.2	-5.5	-98.6	-99.0	-99.3
NFCs	61	-12.0	28.9	30.4	43.2	23.0
Deposits with an agreed maturity of up to two years	**2,724**	**0.3**	**12.1**	**25.7**	**28.9**	**30.7**
of which						
Households	2,124	3.9	22.9	34.0	36.9	30.7
NFCs	317	10.6	-12.3	23.1	39.3	45.1
Deposits outside M3[1]	**1,011**	**-9.2**	**-2.8**	**0.8**	**0.8**	**2.9**
of which						
Households	902	-5.4	-3.1	-4.5	-5.5	-3.1
NFCs	34	-20.3	-6.4	-2.8	3.8	5.7
Total residents deposits[2]	**24,025**	**0.5**	**-2.2**	**1.7**	**1.7**	**2.2**
of which						
Households	17,490	4.2	1.8	3.8	3.7	4.5
NFCs	3,705	-4.6	-6.2	-3.4	1.3	0.6

Source: Central Bank of Malta.

[1] Deposits outside M3 include deposits redeemable at notice of more than three months and deposits with an agreed maturity of over two years.

[2] Total residents deposits exclude deposits belonging to Central Government.

During the 12 months to June, overnight deposits, which are the most liquid component, decreased by 0.5%, following a 0.7% year-on-year decline recorded three months prior. This contraction reflected a decline in the balances held by financial intermediaries and NFCs, which offset increases in deposits belonging to households. The share of overnight deposits in total deposits decreased to 84.1% in June, compared to 84.7% three months earlier (see Chart 6.2).

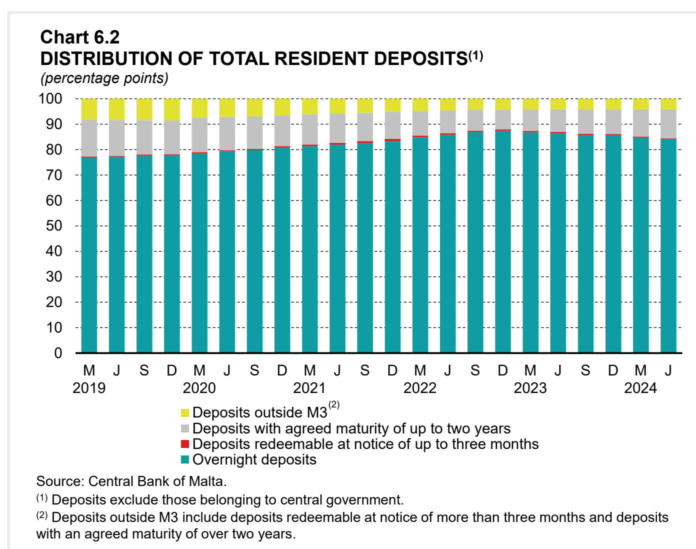


Chart 6.2
DISTRIBUTION OF TOTAL RESIDENT DEPOSITS[1]
(percentage points)

Source: Central Bank of Malta.
[1] Deposits exclude those belonging to central government.
[2] Deposits outside M3 include deposits redeemable at notice of more than three months and deposits with an agreed maturity of over two years.

Deposits with an agreed maturity of up to two years – the second largest component of total deposits – continued to register robust growth of 30.7% in the year to June, compared with 28.9% in March. As a result, their share in overall deposits continued to increase, reaching 11.3% from 10.7% three months prior. The latest increase was driven by higher balances belonging to NFCs, although strong increases were also recorded in balances held by households. This outcome possibly reflects the more attractive terms on fixed deposit accounts being offered by certain credit institutions, in response to the current tight monetary policy stance.

Deposits with an agreed maturity of up to three months declined by around a third year-on-year, following a decrease of 23.5% in the year to March. Consequently, their share of total deposits decreased to 0.3%, from 0.4% recorded three months earlier.

Meanwhile, deposits classified outside M3 – which are mainly composed of deposits with agreed maturity of over two years – recorded an annual growth rate of 2.9% in June, compared to 0.8% growth registered three months earlier. Their share in total resident deposits remained unchanged from March, standing at 4.2%.

Credit to residents grows at a faster pace

Credit to Maltese residents increased by 7.9% in the year to June, exceeding the 6.4% recorded in March. Faster growth was driven by both credit to general government and credit to other residents (see Table 6.2 and Chart 6.3).

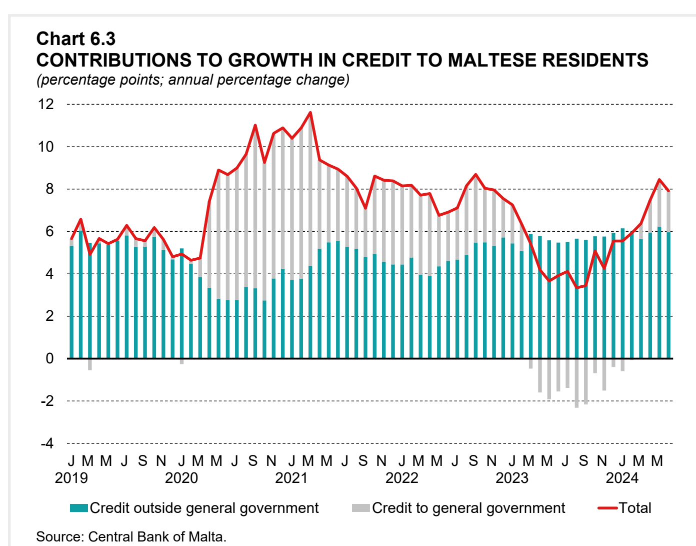


Chart 6.3
CONTRIBUTIONS TO GROWTH IN CREDIT TO MALTESE RESIDENTS
(percentage points; annual percentage change)

Source: Central Bank of Malta.

Table 6.2
MFI CREDIT TO MALTESE RESIDENTS

	EUR millions	Annual percentage changes				
	2024	2023			2024	
	June	June	Sep.	Dec	Mar.	June
Credit to general government	**4,875**	**-5.8**	**-8.1**	**-1.5**	**2.9**	**8.0**
Credit to residents outside general government	**15,189**	**7.5**	**7.7**	**8.0**	**7.6**	**7.9**
Securities and equity	304	-2.6	-3.3	-4.6	-4.3	-4.7
Loans	14,884	7.7	7.9	8.4	7.8	8.2
of which:						
Loans to households	8,739	7.9	7.3	8.2	9.0	9.1
Mortgages	8,061	7.9	7.2	7.9	8.7	8.8
Consumer credit and other lending	677	7.2	8.5	12.2	12.4	13.4
Loans to NFCs[(1)]	5,086	8.1	9.1	8.8	5.4	6.3
Total credit to residents	**20,064**	**3.9**	**3.4**	**5.5**	**6.4**	**7.9**

Source: Central Bank of Malta.
[(1)] NFCs include sole proprietors and non-profit institutions serving households (NPISH).

Credit to general government grew by 8.0% in the year to June, following an increase of 2.9% over the year to March. The latest increase was driven by an increase in MFI holdings of Government stocks, which grew by 14.8% over the 12 months to June. By contrast, MFI holdings of Treasury bills declined in the year to June.

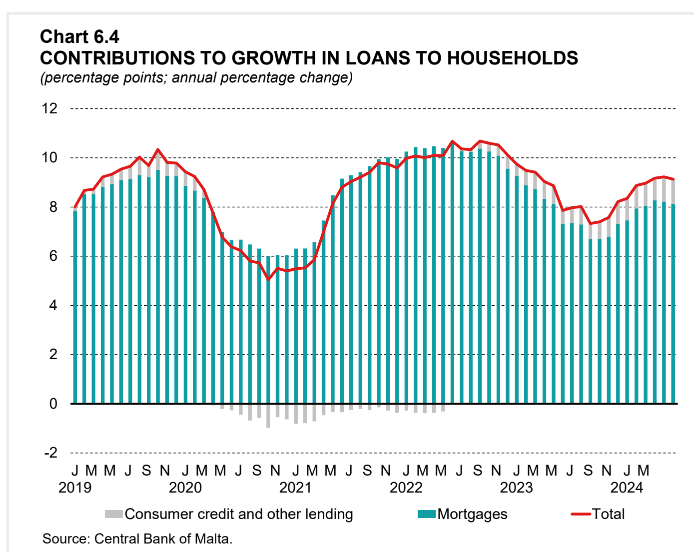
The annual growth of credit to residents outside general government remained strong, increasing to 7.9%, from 7.6% three months prior. Meanwhile, MFI holdings of securities issued by the private sector decreased by 4.7%, following a decline of 4.3% in March.

Annual growth in loans to households reached 9.1%, compared to 9.0% three months earlier (see Chart 6.4). Mortgage lending grew by 8.8% in June, from 8.7% in March. Consumer credit also rose at a faster pace. Growth in this credit component reached 13.4% year-on-year, after 12.4% in March.

Meanwhile, loans to NFCs rose at an annual rate of 6.3%, higher than the 5.4% recorded three months earlier (see Chart 6.5). The higher growth reflected an increase in credit issued to private NFCs, although partially offset by a decline in credit to public NFCs.

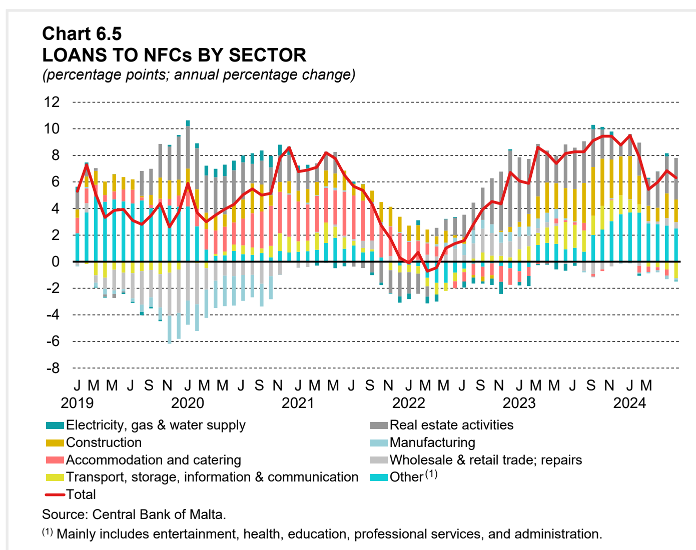
Sectoral data show that the growth in loans to NFCs in the year to June, was largely driven

Chart 6.4
CONTRIBUTIONS TO GROWTH IN LOANS TO HOUSEHOLDS
(percentage points; annual percentage change)



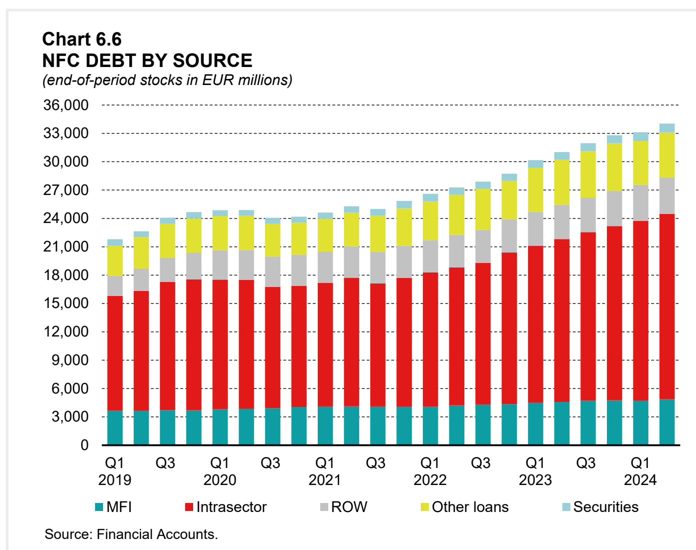
Source: Central Bank of Malta.

by increased lending to the real estate sector and the construction sector. Loans to the sector comprising of professional, scientific and technical activities and the trade and repair sector also increased. On the other hand, credit to the sector comprising information, communication, transportation and storage decreased. This was followed by smaller declines in credit to the energy sector and, the manufacturing sector, while credit to the accommodation and food sector was broadly stable.



Source: Central Bank of Malta.
(1) Mainly includes entertainment, health, education, professional services, and administration.

Financial accounts data show that the share of bank lending in total NFC debt remained unchanged, at 14.3%, compared to March, albeit lower than the share of 14.8% recorded a year earlier (see Chart 6.6).



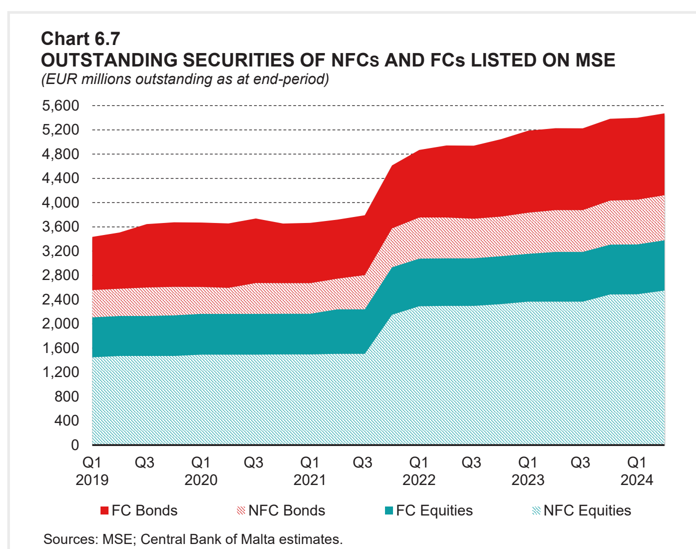
Source: Financial Accounts.

The share of intra-sectoral lending in total NFC debt stood at 57.6%, above the 57.4% recorded in March. This was also 2.1 percentage points higher than the share registered a year earlier. Besides, this component continued to account for most of NFCs external financing.

The share of loans from non-residents decreased marginally to 11.3%, from 11.5% recorded in March, and from 11.7% recorded last year. Meanwhile, the share of 'other loans' remained unchanged compared to March, at 14.0%. It stood below the 15.4% recorded in the second quarter of 2024. This component largely reflects loans from financial institutions other than MFIs and households.

The share of securities increased to 2.7%, from 2.6% recorded a year earlier.

Stock of securities of NFCs and financial corporations (FCs) listed on Malta Stock Exchange (MSE) increases



By June 2024, around €2,094.1 million in outstanding corporate debt securities were listed on the MSE, 2.7% higher than the amount listed a year earlier (see Chart 6.7).[3] 64.5% of the amount was issued by financial entities, other than credit institutions, whilst the rest was issued by NFCs.

Meanwhile, the outstanding amount of equity listed on the MSE increased by 6.0% in annual terms, to reach €3,378.7 million. Over three fourths of this volume was issued by NFCs, with FCs playing a secondary role. The increase over the year to June, was mostly driven by NFCs that operate within the real estate sector. The total amount of outstanding listed equity as of June 2024, exceeded that of bonds by 61.3%.[4]

Spread between deposit and lending rate narrows in annual terms

Interest rates on outstanding resident deposits with MFI increased in June compared to their year-ago level. In particular, the weighted average deposit rate to households and NFCs on outstanding balances increased by 13 basis points to 0.37% (see Table 6.3). This was largely driven by higher rates on time deposits belonging to NFCs and households, as well as by rates on household deposits redeemable at notice up to three months.

At the same time, the weighted average lending rate paid by households and NFCs on outstanding loans decreased by 7 basis points, to 3.51%. This decrease was driven by lower rates charged to both households and NFCs. Rates charged to households decreased by 9 basis points to 2.81%. Both rates for mortgage lending and consumer credit decreased, by 5 and 43 basis points, to 2.66% and 4.15%, respectively.

The spread between the weighted average lending rate and the deposit rate for the second quarter closed at 314 basis points. This was higher than the spread recorded in the previous quarter although still below the spread of 334 basis points recorded a year earlier.

During the year to June, the deposit rates offered on new balances held by households and NFCs in Malta both increased. On the other hand, lending rates to these sectors declined. By June, the weighted average deposit rate for households and NFCs reached 2.88%, while the lending rate to these two sectors declined to 3.09%.

[3] MSE data may differ from financial accounts data due to differences in valuation methodology and coverage. In particular, financial accounts data are at market value and include both listed and privately-placed securities. MSE data on corporates presented in Chart 6.7 are based on the official MSE list and thus exclude securities listed through Prospects. Chart 6.7 includes data on NFCs and FCs other than MFIs.

[4] Apart from the official MSE platform, small and medium-sized enterprises can also obtain finance through the specifically-geared platform – Prospects.

Table 6.3
INTEREST RATES ON DEPOSITS AND LOANS
Percentages per annum to residents of Malta; weighted average rates as at end of period

	2021	2022	2023	2023		2024	
	June	June	June	Sep.	Dec.	Mar.	June
Total deposits[1]	**0.18**	**0.15**	**0.24**	**0.27**	**0.30**	**0.35**	**0.37**
of which							
Overnight deposits							
Households	0.02	0.02	0.04	0.05	0.05	0.05	0.05
NFCs	0.01	0.03	0.07	0.07	0.10	0.10	0.12
Savings deposits redeemable at notice							
Households	0.44	0.38	0.15	0.15	0.31	0.31	0.30
NFCs	0.11	0.08	0.41	0.45	0.47	0.74	0.60
Time deposits (less than two years)							
Households	0.54	0.50	1.32	1.58	1.79	2.05	2.07
NFCs	0.53	0.47	1.15	1.58	1.85	2.28	2.12
Time deposits (more than two years)							
Households	1.79	1.78	1.76	1.77	1.79	1.82	1.89
NFCs	1.15	1.36	1.26	1.38	1.74	1.83	2.00
Total loans[1]	**3.30**	**3.18**	**3.58**	**3.61**	**3.58**	**3.52**	**3.51**
of which							
Households and NPISH	3.12	2.95	2.90	2.87	2.85	2.82	2.81
NFCs	3.62	3.59	4.87	4.98	4.95	4.83	4.81
Spread[2]	**3.12**	**3.03**	**3.34**	**3.34**	**3.28**	**3.17**	**3.14**
ECB MROs rate	0.00	0.00	4.00	4.50	4.50	4.50	4.25

Source: Central Bank of Malta.

[1] Annualised agreed rates on outstanding euro-denominated amounts belonging to households (incl. NPISH) and NFCs.
[2] Difference between composite lending rate and composite deposit rate.

Compared to the first quarter of 2024, interest rates on outstanding deposits with MFIs increased by 2 basis points for households and remained unchanged for NFCs, to 0.39% and 0.27% respectively. The increase in rates for households was driven by higher remuneration on time deposits. Over this period, rates on outstanding loans to NFCs decreased by 2 basis points to 4.81%, while those on loans to households decreased by 1 basis point to 2.81%.

In June, the weighted average deposit rate offered on new balances held by households and NFCs in Malta remained unchanged compared to March. Meanwhile, the weighted average lending rate paid to them decreased by 33 basis points.

Liquidity support measures

By the end of June 2024, 468 facilities were approved and still outstanding under the Malta Development Bank's (MDB) COVID-19 Guarantee Scheme (CGS). These covered total sanctioned lending of €362.3 million, down from €380.3 million, covered by 524 facilities in March.[5] By end-June, the outstanding value of disbursed loans stood at €169.8 million, down from €195.9 million at end-March 2024. Almost all these loans will mature within the next four years.

[5] The MDB CGS provided guarantees to commercial banks with the aim of enhancing access to new working capital loans for businesses. The scheme received applications until 30 June 2022.

The sector comprising wholesale and retail activities had the largest number of outstanding facilities benefitting from the scheme, followed by the sector comprising accommodation and food service activities. The latter had the highest value of sanctioned loans in value terms.

In 2022, the MDB launched additional support measures in response to the war in Ukraine and high inflation. These schemes were closed for new borrowers in December 2023. Three facilities for a total value of €14.2 million, which had been approved under the Subsidised Loans Scheme (SLS), have been paid in full by June 2024.[6] Moreover, a total of €24.5 million was approved and disbursed under the Liquidity Support Guarantee Scheme (LSGS).[7]

Bank Lending Survey (BLS) mostly indicates unchanged credit standards, terms and conditions
According to the July BLS, in the second quarter of 2024, all participating banks reported unchanged credit standards and terms and conditions for lending to NFCs, consumer credit and other lending in Malta. The majority of participating banks also reported unchanged credit standards for lending for house purchase, while all banks reported unchanged terms and conditions for these types of loans. For the third quarter, no bank foresaw changes in credit standards for all types of credit.

As regards the demand for credit by NFCs, the majority of respondent banks claimed that it had remained unchanged during the quarter under review. Moreover, all surveyed banks did not anticipate changes in demand in the third quarter of 2024.

Demand for loans for house purchases, was assessed to have remained unchanged by half of the surveyed banks, while the results were mixed for the other half. The majority of surveyed banks did not anticipate changes in demand in the third quarter of 2024.

In the case of consumer credit and other lending, all participating banks reported unchanged demand during the second quarter and were expecting no changes in the following quarter.

The July BLS also posed ad hoc questions on changes in banks' access to wholesale and retail funding, and in their risk transfer capacity as a result of the prevailing situation in financial markets. No impacts were reported as regards access to interbank unsecured money markets, debt securities, securitisation, and the ability to transfer risks off balance sheet in the preceding three months. However, some tightening effect was reported in terms of access to retail deposit funding. This assessment was also reflected in expectations for the third quarter.

Participating banks claimed that their non-performing loan (NPL) ratio and other indicators of credit quality had not affected their lending policies in the preceding six-month period and expected no effects in the six months ahead.

Respondent banks were also asked to state how their credit standards, terms and conditions on new loans, and demand for loans have changed across the main sectors of economic activity – namely manufacturing, construction, services, wholesale and retail trade, and real estate. The

[6] The SLS provided temporary urgent liquidity support, backed by government guarantees, to importers and wholesalers of grains and animal feed, thereby ensuring the security of supply of such products.
[7] This LSGS consisted of two measures: LSGS-A provides bank financing support to all undertakings affected by the extraordinary circumstances caused by the war in Ukraine, while LSGS-B was specific to fuel and oil importers. A total portfolio of €100 million and €50 million in working capital loans were available under LSGS-A and LSGS-B, respectively. Government guarantees cover 90% of each working capital loan under LSGS-A and 80% under LSGS-B.

majority of banks reported no change in credit standards and the terms and conditions in the past six months and were foreseeing no changes in the next six months for all the five sectors. With regards to demand for loans, half of the surveyed banks experienced no changes over the past six months and foresaw no changes in the upcoming six-month period. The other half witnessed some changes. These included an increase in demand for loans from firms that operate in the manufacturing sector, and somewhat lower demand from firms active in the construction sector. Their expectations for the fourth quarter were also mixed and included lower demand in the construction and manufacturing sectors and higher demand in the services sector.

Participating banks were also asked whether climate-related risks and measures to cope with it led to changes in the bank's credit standards, terms and conditions and demand for loans to enterprises. Some easing in credit standards for green and transition firms was reported to have taken place in the 12 months preceding the survey. By contrast credit terms and conditions for brown firms had tightened or was expected to tighten according to some banks.[8]

As regards credit terms and conditions, half of the banks reported no changes as a result of climate change factors, while the other half reported more mixed effects. In the coming year, most banks anticipated some changes to credit terms and conditions.

Turning to demand for loans, half of the banks said that due to climate change, the demand for loans by green firms and by firms in transition had increased, driven by fiscal support related to climate change. The remaining half said that they experienced no such changes. Looking at demand in the coming 12 months, half of the banks expected climate change to be reflected in an increase in demand for loans in the case of green firms and firms in transition.

Finally, when asked whether the change in banks' excess liquidity held with the Eurosystem had led to a change in their bank's lending conditions and loan volumes, all banks reported no changes. For the next six months, the situation was expected to remain the same, compared with the previous six-month period.

The money market

During the second quarter of 2024, the Government issued €461.3 million in Treasury bills (net of redemptions), €150.6 million more than the amount issued in the first quarter of 2024.

In the domestic primary market, the yield on three-month Treasury bills rose to 3.56% by the end of June, from 2.92% at end-March.

The capital market

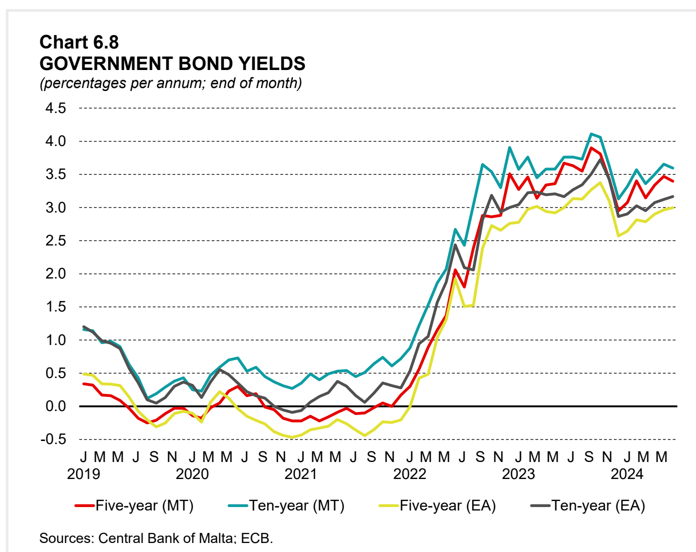
There were no new MGS issues in the second quarter of 2024. Two private sector institutions launched new bond issues on the MSE. Best Deal Properties Holding plc and Burmarrad Group Assets plc issued secured bonds worth €15.0 million and €16.0 million, respectively.

By the end of June, 19 firms had bonds that were listed on the MSE through Prospects, an unchanged number compared with three months earlier.[9] There was also one company which had shares issued through Prospects.

[8] The BLS uses the following terms: "Green firms" – Firms that do not contribute or contribute little to climate change; "Firms in transition" – Firms that contribute to climate change, which are making considerable progress in the transition; "Brown firms" – Firms that highly contribute to climate change, which have not yet started or have so far made only little progress in the transition.

[9] Prospects is a multi-lateral trading facility operated by the MSE with the aim of facilitating access to capital markets for SMEs.

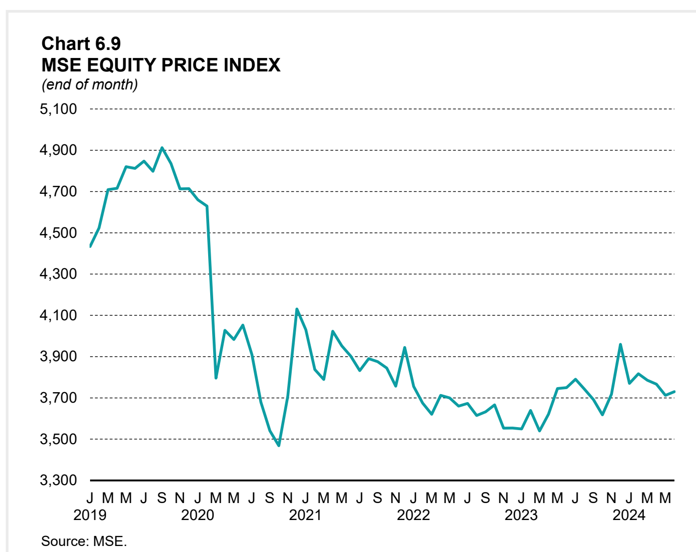
In the secondary market, turnover in government bonds increased to €37.0 million, from €27.7 million in the first quarter of 2024. Meanwhile, turnover in corporate bonds increased to €36.5 million from €24.5 million, previously.



The yield on five-year Government bonds rose to 3.40% at the end of June, from 3.15% three months earlier (see Chart 6.8). The yield on ten-year bonds also increased, reaching 3.60% from 3.36% in March. Meanwhile, the euro area benchmark yield on five-year bonds rose to 3.00% from 2.79%, and that on ten-year bonds increased to 3.17% from 2.95%. As the rise in the domestic ten-year yield was larger than that in the euro area benchmark, the spread between the two widened to 43 basis points from 41 basis points in March.

MSE Equity Price Index declines during the quarter

Share prices in Malta declined further during the second quarter of 2024. The MSE Equity Price Index ended the quarter 1.5% below its level at end-March and was also 0.5% lower than its reading a year earlier (see Chart 6.9). On the other hand, the MSE Equity Total Return Index, which accounts for changes in equity prices and dividends, was 0.3% higher than its level at end-March.



Equity turnover fell to €10.1 million during the second quarter of 2024, from €15.8 million in the previous quarter.

BOX 3: MALTA GOVERNMENT STOCKS MARKET: 2023 IN REVIEW[1]

Global economic recovery and tighter monetary policy by major central banks to tame high inflation characterised financial markets in 2023. Such circumstances pushed yields on fixed income securities higher, reaching levels last seen a decade ago, for which the local market was no exception.

The analysis examines the primary and secondary markets for MGS throughout the year 2023. The issued MGS for the year are detailed in terms of wholesale and retail participation, as well as the allotment amounts across both investor types. Participating patterns are examined, showcasing the varying levels of demand across five different investor categories. The Treasury received robust demand from both retail and wholesale investors, across four issuances and one private placement,[2] offering €1.59 billion out of the €1.60 billion borrowing plan targeted for 2023. This analysis also sheds light on wholesale investor's return appetite as revealed through the Average Weighted Yield (AWY) of individual issues held during the year. The choice of maturity terms and coupons by the issuer are explored, before delving into the secondary market. The local sovereign paper emerged as the most traded security on the secondary market, supported by the Central Bank of Malta's role as market maker. Turnover in this paper is further evaluated for 2023 and for a ten-year period, where on-exchange trading slightly surpassed levels recorded in the previous three years though remaining well below peak figures. Lastly, movements in MGS holdings across investor categories are analysed.

Primary market developments

During 2023, the Treasury targeted to raise up to a maximum of €1.60 billion through MGS issuance. The market responded with strong demand, for nine new fixed rate MGS spread across four regular issuances and a rollover in a 62+ Malta Government Savings Bond (MGSB). Applications reached a total of €1.73 billion, out of which €1.46 billion were allotted, underscoring the strong appetite among investors for Maltese government paper.

Trends in applications varied throughout the year with the highest bid-to-cover ratio of 2.11 times observed in the July issuance, showing the highest number of applications submitted from both retail and wholesale investors. In contrast, the September issuance was the least popular, with a bid-to-cover ratio of 1.26 which was mostly held back by the limited interest of retail investors, placing only €81.62 million in this particular issuance. More information on the MGS issuances of 2023 can be viewed in Table 1.

Wholesale investors accounted for 70.5% of total participation across the year, while retail investors applied for 29.5% of total applications. At a glance, one may depict retail participation as weak. However, when analysing take up of amounts offered to both the retail and wholesale sector in combined issuances, it can be noted that demand levels in 2023 reached those seen earlier in the presented decade (see Chart 1). Retail issuances were halted for

[1] This box is a summary of "The Malta Government Stocks Market - 2023 in Review", a report published on the Bank's website. It is prepared by Kimberley C. Agius, Emmanuel Farrugia and Therese Lethridge, Senior Research Analysts within the Monetary Operations and Government Securities Department. The views expressed are those of the authors and do not necessarily reflect those of the Central Bank of Malta. Any remaining errors are the sole responsibility of the authors.

[2] Private placement refers to the rollover of the 62+ MGSB.

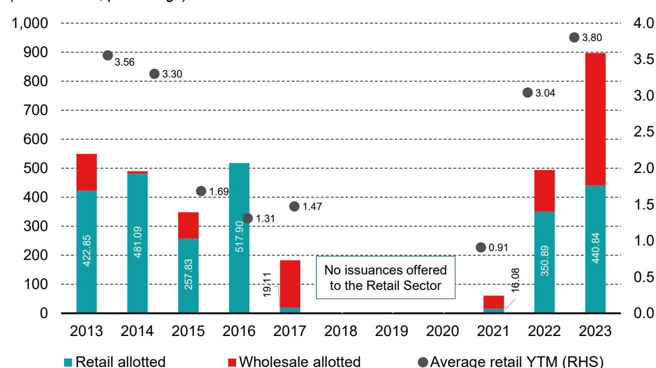
Table 1
LIST OF 2023 ISSUANCES

	February	June	July	September	October	
	3.50% MGS 2028 VI	62+ MSGB Issue 2023[1]	3.55% MGS 2026 V	4.00% MGS 2033 IV	3.85% MGS 2026 VI	
	4.00% MGS 2043 I		3.75% MGS 2033 III	4.30% MGS 2038 II	3.95% MGS 2028 VII	
			4.00% MGS 2038 I			**Totals**
	EUR	EUR	EUR	EUR	EUR	EUR
Total amount on offer	**350,000,000**	**85,971,100**	**400,000,000**	**400,000,000**	**350,000,000**	**1,585,971,100**
Original issue	200,000,000	85,971,100	270,000,000	260,000,000	200,000,000	1,015,971,100
Overallotment option	150,000,000	-	130,000,000	140,000,000	150,000,000	570,000,000
Total applications	**415,679,500**	**70,092,200**	**569,049,000**	**327,115,400**	**351,900,000**	**1,733,836,100**
Retail	179,179,500	70,092,200	180,049,000	81,615,400	-	510,936,100
Wholesale	236,500,000	-	389,000,000	245,500,000	351,900,000	1,222,900,000
Total amount allotted[2]	**349,179,500**	**70,092,200**	**399,549,000**	**303,615,400**	**341,900,000**	**1,464,336,100**
Bid-to-cover ratio[3]	**2.08**	**-**	**2.11**	**1.26**	**1.76**	**1.71**

[1] Eligible bondholders of this security were offered to rollover their maturing holdings in the new savings bond issue.
[2] Total applications from Retail Investors were fully allotted.
[3] Bid-to-cover ratio is applied on the original issue amount.
Source: Malta Treasury Department.

a three-year period due to ultra-low yields prevailing at the time. Following the increase in returns given by rising yields, the Treasury reopened applications for retail investors in mid-2021 for only one issuance. Furthermore, the low participation rate of 29.5% may be attributed to a significant increase in the Treasury's debt supply, with the volume of debt offered to the retail sector in 2023 reaching its highest level since 2013.

Chart 1
RETAIL PARTICIPATION IN COMBINED MGS ISSUANCES[(1)]
(EUR millions; percentage)



Source: Malta Treasury Department.
(1) The chart aggregates only issuances offered to the retail sector on a yearly basis, thus omitting issuances offered exclusively to wholesale investors. The wholesale allotment is shown to depict the magnitude of the retail vis-à-vis the wholesale participation. The 62+ MGSB rolled over in 2023 is not included for comparability reasons.

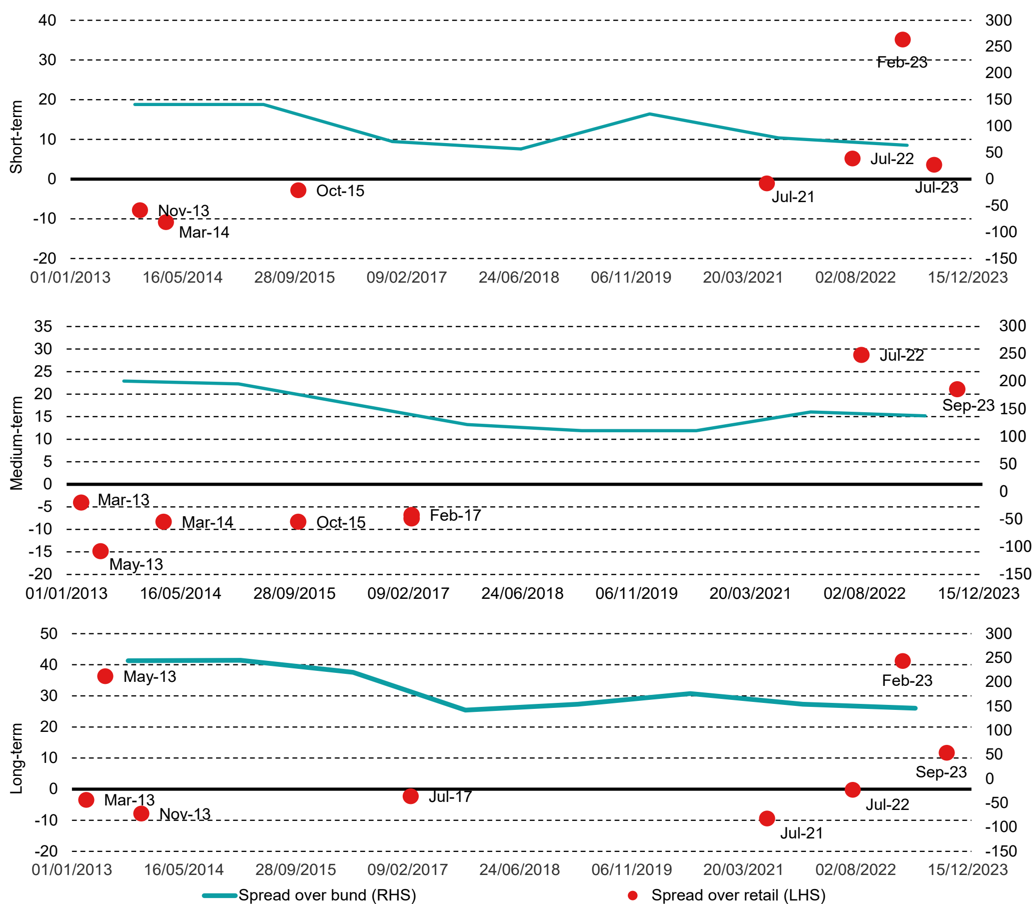
At issuance, participants are classified into five investor categories, of which financial companies showed most interest in the MGS offerings, applying for a total amount of €1.11 billion, or 67.1% of total submissions. The individual and household, and non-profit entity[3] categories followed with €299.45 million and €134.74 million, respectively in applications. The final two categories, namely government[4] and non-financial companies, collectively represented 14.9% of total applications.

Analysing the resulted AWYs by wholesale investors over the set retail yield to maturity (YTM) gives insight on wholesale investors' yield requirements. In the issuances opened

[3] The largest portion of the non-profit entity classification is made up of Resident Nominees who are not necessarily non-profit. These investors do not hold a direct account with the MSE and place their applications through a broker. In the secondary market, this category also includes movements in both resident and non-resident nominees.
[4] The government category refers mainly to government agencies and public sector entities.

to both investor types, wholesale investors demanded higher yields than those offered to retail investors, as per price setting published by the Treasury. The most notable premium was seen in the first issuance of the year for the 4.00% MGS 2043 I, with 41 basis points in AWY over that locked in by retail investors. The income goals of the investor could provide one explanation for this premium. However the possibility of yield fluctuations between the publication of retail prices and the opening of the wholesale auction could potentially contribute to the higher AWY. Moreover, the Government's increased borrowing needs from 2020 onwards may have also signalled investors the opportunity to request higher returns and constrain the Treasury to entertain such bids. This becomes more pronounced after considering that the deviations across a ten-year period were persistently negative between the years 2013 and 2017, with only one exception in the long-term bracket, as seen in Chart 2. Deviations in spreads turned positive after 2020 even though the Maltese risk premium over the German bund[5] declined over this ten-year period by 77 basis points, 63 basis points, and 98 basis points in the short, medium and long-term, respectively in line with other euro area sovereigns that share similar economic fundamentals. This may signal

Chart 2
DEVIATION OF SUCCESSFUL AWY FROM RETAIL YTM



Sources: Malta Treasury Department; Central Bank of Malta.
Note: Only issuances which were open to both wholesale and retail investors are shown.

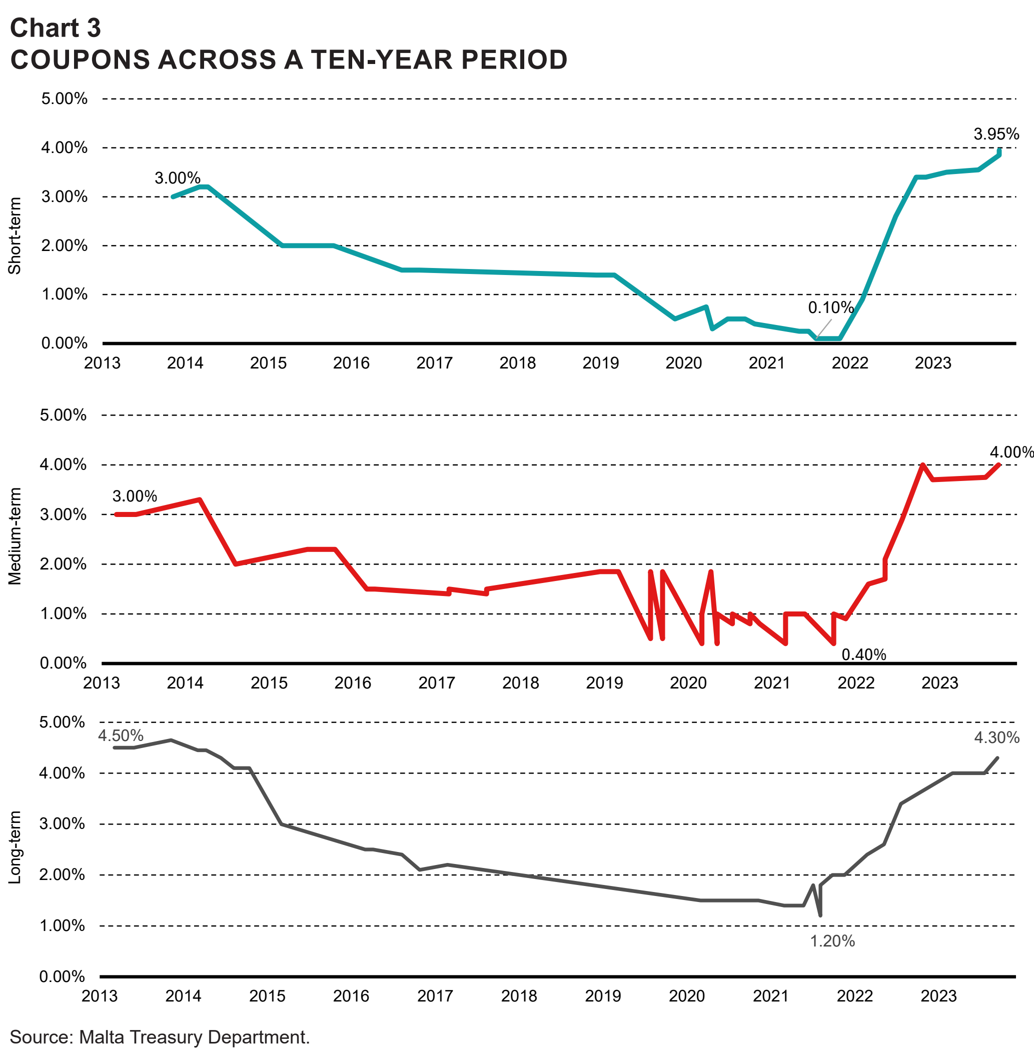
[5] Based on Indicative Secondary Market prices published by the Central Bank of Malta.

that wholesale investors require a higher return premium over the bund than that indicated through secondary market pricing. Nevertheless, confidence in the secondary market does not seem to be waning as such prices were utilised by brokers in secondary market trading in 2023, with most of the traded prices having only slight deviations.

All issuances in 2023 introduced new bonds in the central government's portfolio, having different maturities[6] spanning from three to 21 years paired with coupons that ranged from 3.50% to 4.30%. MGS coupons across all tenors in 2023 approached or exceeded those seen a decade ago as global yields surged, reflecting the high inflation rates in 2022. Restrictive monetary policy to tame inflation inevitably pushed interest rates higher.

As illustrated in Chart 3, MGS coupons were relatively high in 2013, declined gradually and rose again over the last two years. The downward trend in coupon rates after 2013

Chart 3
COUPONS ACROSS A TEN-YEAR PERIOD



Source: Malta Treasury Department.

[6] Maturity terms between one and six years are categorised as short-term bonds, including both years. Those of seven till 14 years are medium-term tenors, whilst those of 15 years and higher are considered long-term issues.

was influenced by several factors, mostly by the ECB's monetary policy decisions, including negative interest rates starting in mid-2014 and the Quantitative Easing Programme introduced in March 2015 amid a period of disinflation. Coupon rates continued to decline, reaching their lowest point in 2021 during the COVID-19 pandemic, as negative interest rates were maintained to counter the sharp economic contraction. Since the end of 2021 yields started to increase, reaching high levels in 2023.

The choice of maturity terms for new issues reflects issuers' strategic objectives and financial planning. Issuing longer-dated debt when yields are low allows for the collection of funds locked at lower borrowing costs. Given the high yields in 2023, the Treasury only allotted €197.38 million over three long-term bonds as shown in Chart 4. The issuance of long-term debt was preferred until 2016, possibly due to lower interest rates, which is also noted in 2021 when issuances in the medium maturity bracket reached €620.50 million. Short-term bonds, however, gained prominence in the primary market from 2020, with the largest amount allotted in 2023. Given the general expectation of a drop in short-term interest rates, issuing short-term debt during 2023 may have been strategic to reissue at lower rates in the near future.

Debt sustainability also takes a role, whereby considerations towards maintaining low debt servicing costs whilst ensuring long-term feasibility, are taken. Additionally, an issuer should seek to evenly distribute debt across years to avoid large redemptions within a short timeframe, and therefore curbing what is known as refinancing risk. The chart displays that generally issuances always included different maturity terms, irrespective of the yield environment. The variable in each case, however, was the amount to be allotted.

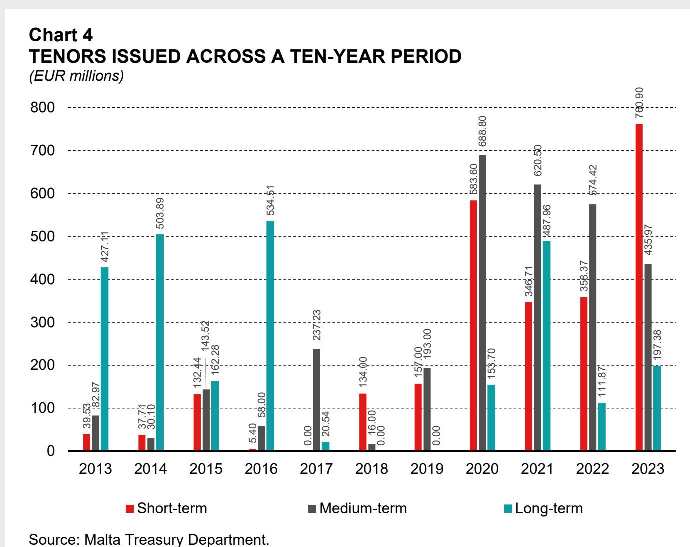


Chart 4
TENORS ISSUED ACROSS A TEN-YEAR PERIOD
(EUR millions)
Source: Malta Treasury Department.

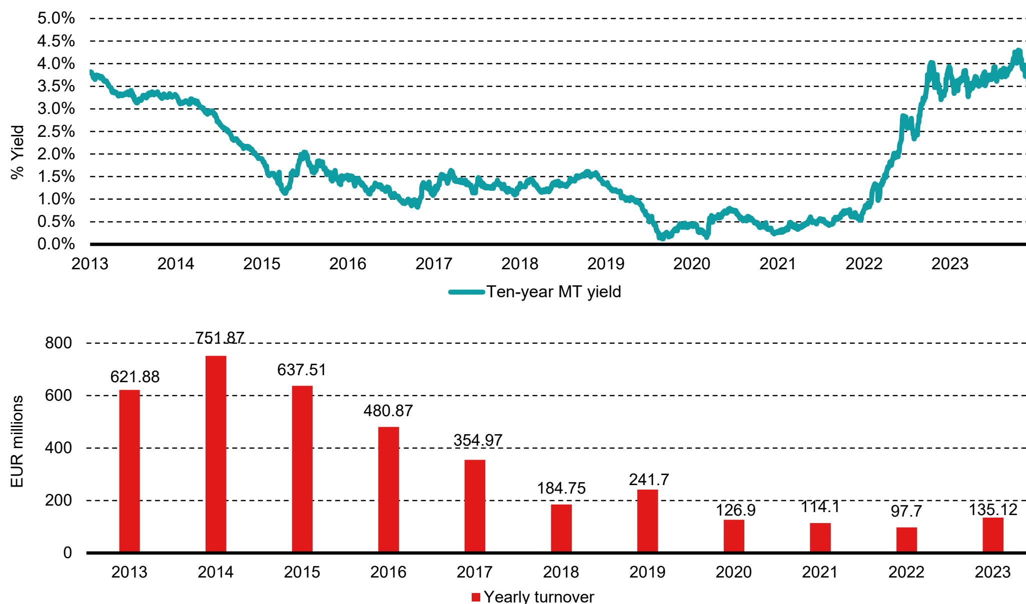
The secondary market

A total market value of €169.26 million was traded in local sovereign debt securities, equivalent to 51.3% of total on-exchange turnover in all prominent security types. More specifically, 40.1% of total market value trading (€132.36 million) was exchanged in MGS alone, with an additional 11.2% (€36.90 million) dealt in Malta Treasury Bills (MTBs). Corporate bonds were the second most traded security type overall (30.2%), followed by Ordinary Shares (17.6%), with Prospects and Preference Shares trailing behind accounting for less than 1% of the total market value traded throughout the year.

Chart 5 visualises the trading activity in MGS during the last decade. Throughout the earlier years of the timeline, expansionary monetary policy decisions were needed to support slowing economies, directly contributing to a lower yield environment. Yields dropped between 2013 and 2016, as shown through the ten-year MT-yield curve in Chart 5, with sharp drops in 2014, which may have created avenues for profit and in turn, offloads on the secondary market. In fact, turnover touched a peak in 2014 for a nominal amount of €751.87 million. Yields kept tumbling thereafter, following the introduction of the Public Sector Purchase Programme by the ECB in 2015 and continued to fall to their lowest points between 2019 and 2020. Due to such low yields and in turn low coupon rates, the Treasury refrained from opening applications to the retail sector between 2018 till 2020. This could possibly partly explain the low turnover volumes in these respective years. Yields sharply reversed their trajectory in 2022, reaching levels last seen in 2013, supported with the release of high inflation prints, pushing bond prices lower. Turnover picked up in 2023, surpassing volumes seen in the previous three years.

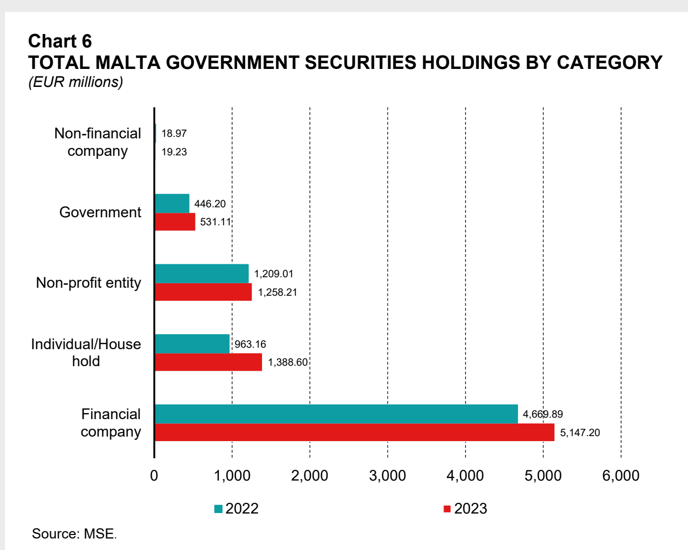
The Central Bank of Malta maintained its role as a market maker by providing liquidity on the secondary market for MGS and MTBs. The Bank continues to operate in the local secondary market, taking guidance from its indicative prices published daily on its official website. The Bank accounted for 41.2% (€55.70 million) of total on-exchange transactions in MGS during the year and acted on behalf of public entities for another 18.3% (€24.78 million). The Bank was relatively more active in MTBs trading, responsible for 83.8% (€30.95 million) of the security's total on-exchange turnover, with only one other broker purchasing the remaining 16.2% (€6.00 million). Total outstanding government debt by the end of 2023

Chart 5
TEN-YEAR MT YIELDS AND MGS TURNOVER



Sources: MSE; Central Bank of Malta.

reached €8.34 billion following a net issuance of €1.01 billion. As a result, all five main category groupings grew in volume as shown in Chart 6. The investor base in the secondary market was primarily composed of financial institutions, holding 61.7% of the total outstanding amount. The individuals and households' category increased their holdings by €425.44 million over the previous year, taking over the non-profit entities category placing with the second-highest volume in holdings.



Concluding remarks

The Treasury's plan to issue up to €1.60 billion in MGS was received with robust demand. Higher coupons were necessary to attract substantial interest from both wholesale and retail investors, fulfilling the original allotment in every issuance. Financial companies dominated applications throughout the year in those issues opened to wholesale bidders. Individuals and households also demonstrated strong participation, indicating a particular interest in short-term MGS, closely followed by long-term bonds. Through the analysis of the AWY emanating from wholesale bidding revealed that the highest requested premium reached 41 basis points above the yield offered to the retail investor, indicating a rise in the cost of borrowing for the Government in recent years. The MGS secondary market experienced a modest recovery in 2023, when compared to recent years. The Bank's involvement as a market maker was crucial, accounting for a substantial portion of the total on-exchange transactions, underscoring its importance in the local financial market. Data on the distribution of MGS holdings across various investor categories showed financial companies as the dominant holder category of MGSs, followed by Individual and household and non-profit entities investors.

The insights gained from the 2023 market performance coupled with considerations of the prevailing market conditions may provide a solid foundation for future borrowing strategies, ensuring that Malta can effectively manage its public debt while fostering a robust investment environment. Further monitoring of such trends and patterns could provide valuable insights that contributes towards maintaining the local sovereign debt security's stability and attractiveness among a wide investor base.

BOX 4: THE TRANSMISSION OF MONETARY POLICY IN MALTA: A FOCUS ON RETAIL BANK INTEREST RATES[1]

The setting of policy interest rates is typically the conventional tool for central banks to achieve their monetary policy objectives. Following a number of years characterised by a low-interest rate environment, the ECB embarked on a cycle of tightening monetary policy as of July 2022. In the following months, interest rates were consistently raised in response to high inflation in the euro area (EA), largely resulting from fast-accelerating demand, supply shortages, and higher energy prices. This period of rapidly tightening monetary policy continued until May 2024, by which time the DFR had increased from the -0.50% rate applicable until 26 July 2022 to 4.00% until 11 June 2024.

The effectiveness of policy rate changes to achieve monetary policy objectives depends on the ability to affect money market rates, commercial banks' refinancing costs and retail bank rates (Lane, 2022).[2] For instance, a hike in interest rates by the ECB increases the borrowing costs for commercial banks. If this additional cost is passed on in the form of higher lending and deposit rates charged to customers, customer borrowing becomes more expensive and savings more attractive. In turn, these developments affect the consumption and investment decisions of households and firms, and consequently aggregate activity and prices (Altavilla et al., 2020).[3] As such, the effectiveness of policy rate changes depends on the extent to which monetary policy decisions trickle down to households and firms.

In this light, this study analyses the extent to which lending rates and deposit rates charged by Maltese banks have changed in response to the recent cycle of tightening monetary policy implemented by the ECB. Moreover, this study also begins to shed light on the potential sources of heterogeneity between the extent of this transmission in Malta and that observed in the EA.[4]

Developments in retail lending and deposit rates in Malta

Chart 1 illustrates the evolution of two key lending rates in Malta between January 2008 and May 2024 – the month before which policy rates were cut by 25 basis points by the ECB Governing Council. The rates considered are those charged on (1) lending to households for house purchases (measured by the *annual percentage rate of charge [APRC]*), and (2) lending to non-financial corporations (NFCs).[5] Mortgage rates have generally been lower and less volatile than rates charged on NFCs' lending. In addition, while both rates have,

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[1] Prepared by Nathaniel Debono, a Senior Research Economist within the Modelling Office. Helpful comments by Mr Alexander Demarco, Dr Aaron G. Grech, Mr Noel Rapa and Mr Owen Grech are gratefully acknowledged. The views expressed are those of the author and do not necessarily reflect those of the Central Bank of Malta. Any errors are the author's own.

[2] Lane, P. R. (2022). "Monetary policy and the money market", Speech at Meeting of the Money Market Contact Group.

[3] Altavilla, C., Canova, F. and Ciccarelli, M. (2020). "Mending the broken link: Heterogeneous bank lending rates and monetary policy pass-through", *Journal of Monetary Economics*, 110, pp. 81-98.

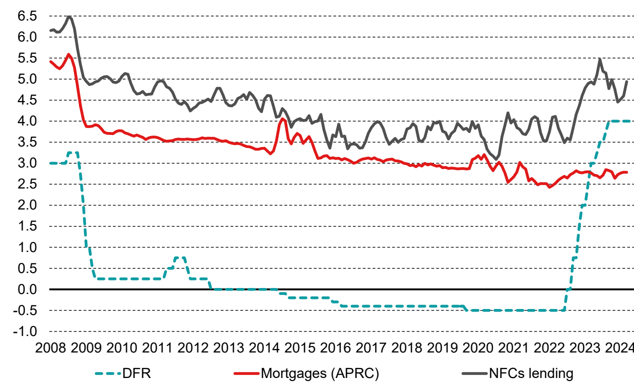
[4] This study can be considered an update to the work conducted in Debono, N. (2024). "The transmission of monetary policy in Malta: a focus on retail bank interest rates", Central Bank of Malta *Policy Note*. This article extends the analyses until May 2024 (i.e. the month before the key ECB interest rates were lowered), compared to the August 2023 cut-off date considered in the *Policy Note*.

[5] The respective retail interest rates charged by MFIs in Malta are the MFI interest rate statistics (MIR) on new business volumes with residents of the euro area.

in large part, followed a downward trend, rates applied to NFCs' lending somewhat stabilised as of 2016 and picked up from the second half of 2022.

These developments begin to shed light on the transmission of monetary policy to lending rates in Malta. In an indication of weak pass-through during a time characterised by expansionary monetary policy, the spread between the DFR and the respective lending rates widened by 60 basis points for mortgages and 106 basis points for NFCs' lending between January 2008 and December 2021. The tightening of monetary policy experienced from July 2022 onwards did not really affect the mortgage rates set by commercial banks in Malta. In fact, mortgage rates rose by just 27 basis points in response to a 450 basis point hike in the DFR between December 2021 and May 2024. The change in NFCs' lending rates has been slightly more pronounced at 122 basis points, but this is still markedly less than the hike in the policy rate during the same period.[6]

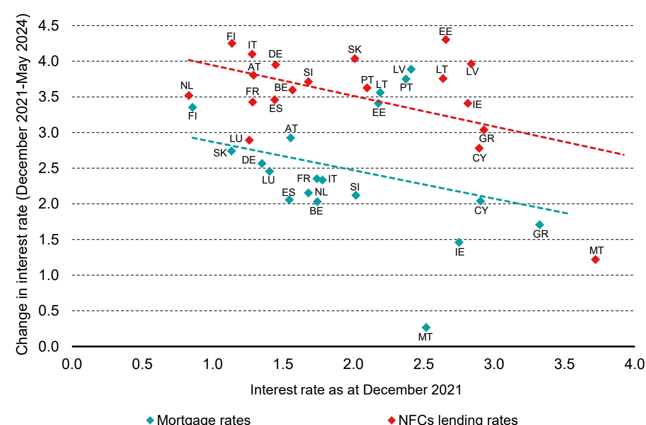
Chart 1
RETAIL LENDING RATES IN MALTA
(% per annum; three-month moving average of new business volumes)



Source: Central Bank of Malta.
Notes: All retail bank lending rates refer to MFIs' interest rates on new business volumes with euro area residents. Mortgage rates reflect the annual percentage rate of charge (APRC), covering the total cost of a loan, comprising the interest rate component and other related charges.

Chart 2 plots the cumulative change in mortgage rates and NFCs' lending rates between December 2021 and May 2024 in the EA, vis-à-vis the respective interest rates charged as at December 2021. In December 2021, average mortgage rates in Malta stood at 2.52%, among the highest in the EA, where mortgage rates averaged 1.60%. However, cross-country divergences in the reaction of mortgage rates to the subsequent cycle of tightening monetary policy, led to Malta having the lowest

Chart 2
CHANGES IN MORTGAGE RATES AND NFCs LENDING RATES
(percentage points; % per annum (three-month moving average of new business volumes))



Sources: ECB SDW; author's calculations.

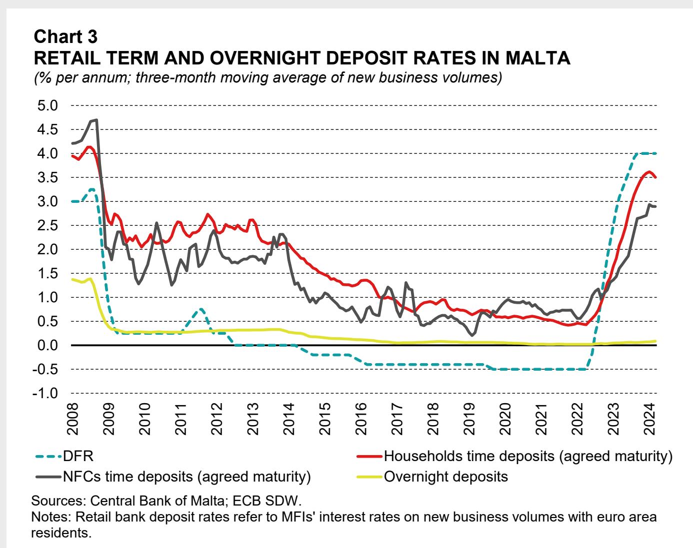
6 The respective changes in mortgage rates and the lending rates charged to NFCs are estimated on the basis of interest rates calculated on a three-month moving average basis.

mortgage rates as of May 2024, standing at 2.78%. Similar to the patterns observed in the case of mortgage rates, the reaction of rates charged to NFCs by Maltese banks in the recent tightening cycle was also much less pronounced than in other EA countries. Indeed, while such rates rose by an average of 3.75 percentage points in the EA, the corresponding increase in Malta was limited to 1.22 percentage points. As a result, NFCs' lending rates in Malta were among the lowest in the EA by May 2024. This represents a marked shift from the position at the end of 2021, when rates charged by Maltese banks were the highest among all EA countries.

Assessing the cumulative changes in bank lending rates relative to the initial interest rate levels, Chart 2 exhibits a negative relationship, with countries that had relatively high retail bank interest rates in December 2021 generally recording smaller subsequent hikes in their lending rates. However, even when accounting for initial lending rate levels, the subsequent rise in lending rates in Malta remains exceptionally low. Particularly in the case of mortgages, the increase in rates charged in Malta even lagged behind other EA countries that started off with even higher lending rates. These patterns suggest that although the initial levels of lending rates are important, there are likely other considerations which might also explain the relative stability in the lending rates charged by Maltese banks.

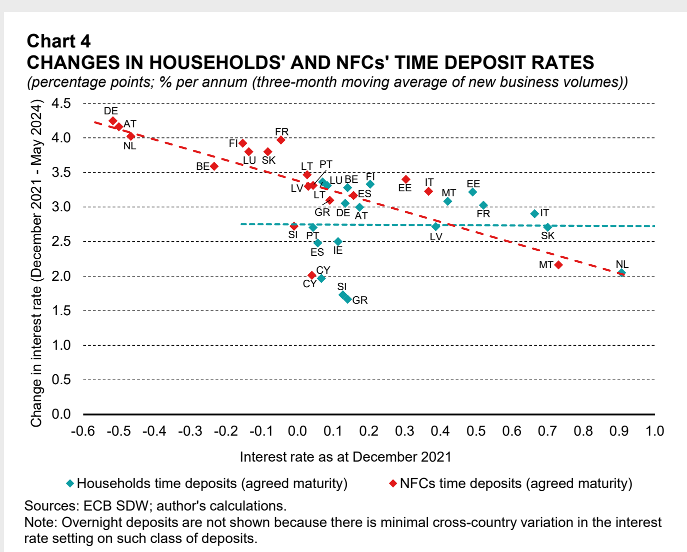
Turning to developments in deposit rates, Chart 3 shows the evolution of the interest rates offered by Maltese banks on time deposits and overnight deposits. Notwithstanding some volatility in the NFCs' time deposits, time deposit rates have generally followed movements in the policy rate set by the ECB. Among the main developments in recent years, the rate offered on new households' time deposits in Malta increased from 0.42% in December 2021 to 3.50% in May 2024. The increase in NFCs' time deposit rates was slightly more muted, increasing from 0.73% to 2.89% over the same period. Rates offered on overnight deposits remained practically unchanged during the latest cycle of monetary policy tightening. Indeed, the rate on such deposits, which are overwhelmingly the largest class held by Maltese banks, moved only marginally from the 0.02% rate applied in December 2021, and were remunerated at less than 0.1% by May 2024.

Chart 3
RETAIL TERM AND OVERNIGHT DEPOSIT RATES IN MALTA
(% per annum; three-month moving average of new business volumes)



Sources: Central Bank of Malta; ECB SDW.
Notes: Retail bank deposit rates refer to MFIs' interest rates on new business volumes with euro area residents.

Analysing the movements in term deposits in the EA, Chart 4 shows that changes in the rates offered on households' time deposits between December 2021 and May 2024 have been largely unrelated to the corresponding rates offered before the start of the tightening period of monetary policy. In contrast, countries that offered relatively high rates on NFCs' time deposits in December 2021 generally had a smaller subsequent increase in this rate in response to policy rate hikes. The analysis elicited from Chart 4 indicates that recent developments in the time deposit rates offered by Maltese banks have been in line with the rest of the EA, when accounting for the level of interest rates set by banks prior to the recent policy rate hikes.



Monetary policy pass-through estimates for Malta

The descriptive evidence discussed above highlights the limited pass-through onto bank lending rates, especially mortgage rates, in Malta during the recent tightening of monetary policy. In contrast, movements in local time deposit rates have been somewhat stronger, while demand deposit rates have persisted at the very low levels observed over previous years. The relatively small movements in the overnight deposit rates offered by Maltese banks since 2022 are in line with those observed in many other EA countries. The following analysis seeks to formalise this evidence through an empirical estimation of pass-through rates in Malta, and an assessment of how these compare to those observed in the EA bloc.

The baseline specification used is adapted from the work of Holton and Rodriguez d'Acri (2018), taking the following general form:[7]

$$\Delta ir_t = \sum_{j=1}^{n} \alpha_j \, \Delta ir_{t-j} + \sum_{j=0}^{n} \beta_j \, \Delta mr_{t-j} + \theta \, ir_{t-1} + \delta \, mr_{t-1} + \sum_{j=0}^{n} \gamma_j \, \Delta X_{t-j} + \epsilon_t \qquad (1)$$

and is estimated separately on monthly interest rate data for Malta and the EA between December 2021 and May 2024. Under this framework, monthly changes in lending and deposit rates (Δir_t) depend on their respective lagged changes (Δir_{t-j}), contemporaneous and past changes in the monetary policy stance, captured by the three-month EURIBOR (Δmr_{t-j}), and deviations from the long-run relationship between retail rates (ir_{t-1}) and the

[7] Holton, S. and Rodriguez d'Acri, C. (2018). "Interest rate pass-through since the euro area crisis", *Journal of Banking and Finance, 96* (2018), pp. 277-291.

three-month EURIBOR in the previous period (mr_{t-1}). The vector X captures important macroeconomic variables that may independently also influence the setting of lending and deposit rates by banks, namely a country's HICP inflation rate, unemployment rate and ten-year government bond yield.[8]

This work focuses on the overall pass-through of monetary policy in Malta and the EA. The overall pass-through can be straightforwardly estimated from the specification in equation (1) through the calculation of $-\frac{\delta}{\theta}$, where a value of 1 reflects a full and complete pass-through of changes in monetary policy onto retail bank rates. This exercise is applied to two lending rates, namely those on *mortgages* and *NFCs' lending*, and three deposit rates, namely those in relation to *households' time deposits, NFCs' time deposits* and *overnight deposits*. The estimated long-run pass-through estimates are presented in Chart 5. The robustness of the pass-through estimates is assessed by computing the ratio of the change in the respective bank rate to the change in the three-month EURIBOR between December 2021 and May 2024.

Results presented in Chart 5 confirm that the transmission of the restrictionary policy in Malta has been markedly low in the case of mortgage rates. Estimated at 0.05 between December 2021 and May 2024, this reflects the decision of Maltese banks to maintain mortgage rates at very stable levels despite progressive hikes in the policy rates set by the ECB. The extent of transmission in Malta is much weaker than that observed across the EA, which stood at 0.53 over the same period. Moreover, the 'simple pass-through' estimates show the pass-through onto mortgage rates in Malta to be the weakest among all countries in the EA. The overall pass-through onto lending rates charged to NFCs in Malta has been slightly stronger than that onto mortgage rates, estimated at just below 0.30.[9] Nonetheless, this still lagged well behind other EA countries, where the pass-through over the same time horizon typically exceeded 0.70 and averaged 0.85. These cross-country divergences are congruent to the descriptive statistics shown previously and are in part driven by the initial lending rate conditions. As already illustrated, lending rates in Malta were relatively high up to December 2021. Then,

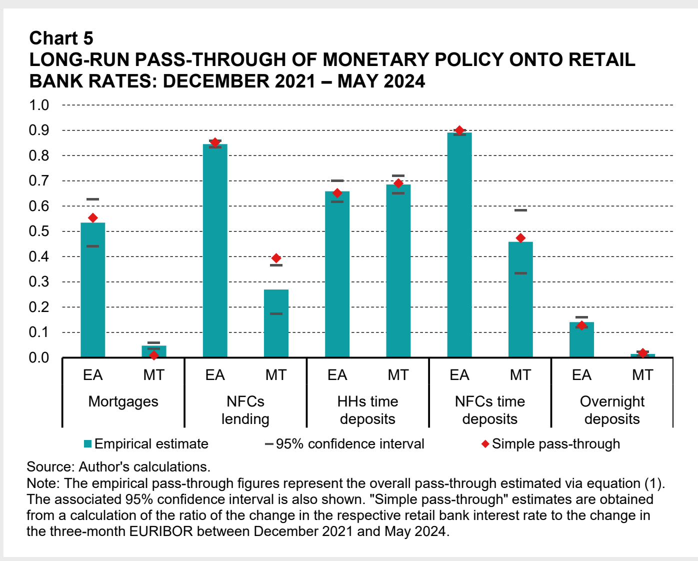


Chart 5
LONG-RUN PASS-THROUGH OF MONETARY POLICY ONTO RETAIL BANK RATES: DECEMBER 2021 – MAY 2024

Source: Author's calculations.
Note: The empirical pass-through figures represent the overall pass-through estimated via equation (1). The associated 95% confidence interval is also shown. "Simple pass-through" estimates are obtained from a calculation of the ratio of the change in the respective retail bank interest rate to the change in the three-month EURIBOR between December 2021 and May 2024.

[8] When estimating the model in equation (1), standard errors are adjusted for heteroscedasticity, autocorrelation, and cross-sectional correlation.

[9] While the point estimate is subject to some uncertainty, the "simple" calculation of the pass-through yields a value of around 0.40, which is still around half of that recorded in the EA.

as monetary policy started tightening, lending rates charged by Maltese banks were moving from higher initial levels than their EA counterparts. As a result, hikes in lending rates by Maltese banks in response to rising policy rates were always likely to be less pronounced than other EA countries. Nonetheless, the initial interest rate levels charged by Maltese banks do not fully explain the difference in the pass-through of Maltese banks compared to that in the EA.

Turning to the transmission of monetary policy onto deposit rates, Chart 5 also shows that the pass-through onto households' term deposit rates has been highly comparable (in the range of 0.65-0.70) to that in other EA countries over the recent tightening cycle. In contrast, the pass-through onto the rates offered to NFCs on their time deposits between December 2021 and May 2024 has been relatively low, when compared to the rest of the EA. Indeed, while the pass-through onto NFCs' time deposit rates in Malta hovered around 0.50, the average in the EA approached 0.90. The pass-through onto overnight deposit rates has been largely limited in the EA, just exceeding 0.10 on average, while in Malta, this pass-through is recorded at 0.01. These results reflect the developments in deposit rates offered by Maltese banks, as illustrated in Chart 3. Indeed, the somewhat pronounced movements in time deposit rates over the recent tightening cycle, compared to overnight deposit rates, are reflected in a stronger pass-through estimate for time deposit rates, relative to that on demand deposit rates.

Overall, these empirical results reaffirm the descriptive evidence of Malta being a clear outlier in the EA in terms of the pass-through of tightening monetary policy onto its retail bank lending rates. In contrast, the pass-through onto deposit rates, especially households' time deposits, has been much more in line with other EA countries, although changes in the rates offered on demand deposits and NFCs' time deposits have been comparatively quite low.

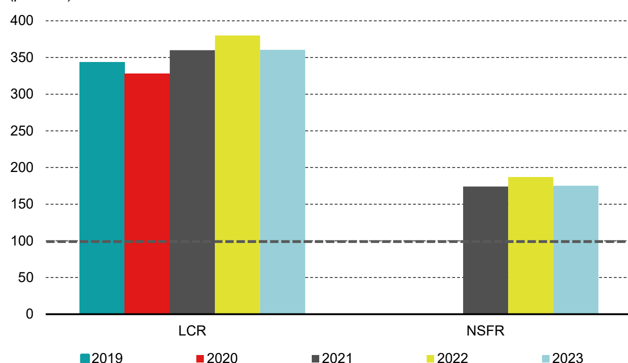
Maltese banks' characteristics and their potential role in explaining the low pass-through onto lending rates

Previous economic research has shown that the extent of monetary policy transmission onto retail bank lending rates depends to some extent on particular characteristics of the banking sector and individual commercial banks. In this light, this section analyses the main features of the Maltese banking sector in order to better understand whether these features could explain, at least in part, the low pass-through of monetary policy onto bank lending rates in Malta over recent months.

The Maltese banking sector is characterised by relatively high liquidity, enhancing banks' ability to insulate their lending behaviour from monetary policy changes. In an indication of the excess liquidity enjoyed by Maltese banks, the share of funds held with the Central Bank of Malta to satisfy minimum reserve requirements as of May 2024 stood at just 6.6% of all amounts deposited with the Bank. Maltese banks also perform well in terms of regulatory liquidity indicators, such as the Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR). As shown in Chart 6, the levels recorded by core Maltese banks in recent years have comfortably exceeded the current 100.0% minimum requirement set for both

ratios. Compared to other EA countries, Maltese core banks had the third highest LCR and the fourth highest NSFR in the EA in 2023.[10]

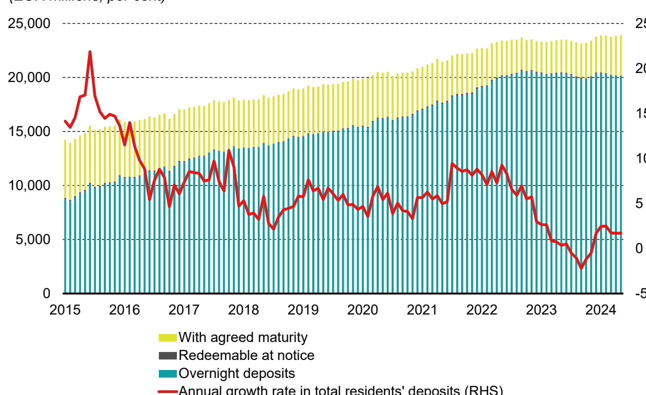
Chart 6
LIQUIDITY INDICATORS OF MALTESE BANKS
(per cent)



Source: Central Bank of Malta *Financial Stability Report* 2023.
Notes: Figures cover the respective ratios among core Maltese banks. Credit institutions must maintain a LCR and NSFR of at least 100%. The NSFR became mandatory in the EU in the second half of 2021 and therefore data for previous years is not available.

Maltese banks have also continued to benefit from a large inflow of customer deposits in recent years (see Chart 7). In fact, total resident deposits with credit institutions in Malta grew at an average annual rate of 6.6% between the start of 2015 and May 2024. This increase has largely been driven by the rapid rise in overnight deposits, which grew by 130% over the same period. As a result, overnight deposits now constitute 84% of Maltese banks' total resident deposits and, in light of the very low interest rates offered on overnight deposits, they represent a source of very cheap liquidity for Maltese banks. The strong accumulation of customer deposits also allows Maltese banks to comfortably support their loan commitments, with the loans-to-deposits ratio of core Maltese banks averaging less than 60% in 2023, well below the 94% figure recorded in the EA.[11]

Chart 7
RESIDENTS' DEPOSITS HELD WITH MFIs IN MALTA
(EUR millions; per cent)



Source: Central Bank of Malta.
Notes: Deposits by EA residents are not shown due to their volatility and their relatively small size compared to the deposits of Maltese residents.

Overall, the low pass-through onto lending rates charged by Maltese banks in recent months could potentially also be explained by signs of their healthy balance sheet positions. In theory, healthy balance sheets should afford banks the opportunity to limit the extent of lending rate hikes. Among the main indicators of the healthy balance sheets in the domestic banking sector, Maltese banks consistently record strong capital positions,

[10] Figures for other EA countries are based on ECB SDW data [Consolidated Banking Data] on domestic banking groups and stand-alone banks.
[11] Figures for core Maltese banks are derived from Central Bank of Malta (2024), "Sixteenth *Financial Stability Report* 2023". See also footnote 10.

with data published by the Central Bank of Malta showing that the Tier 1 capital ratio of Maltese core banks stood at 21.0% at the end of 2023, higher than the 17.0% average in the EA.[12,13] Core Maltese banks are also not overly exposed to non-performing loans (NPLs). Indeed, their total NPLs expressed as a share of their total gross loans stood at 2.52% at the end of 2023, and has declined consistently in recent years.[14] Moreover, core Maltese banks also enjoy high profitability with their Return on Equity (ROE) and Return on Assets (ROA) reaching 18.2% and 1.6%, respectively, by the end of 2023.[15] These figures represent a marked improvement over the respective 8.19% and 0.66% levels recorded a year earlier. These developments were further complemented by higher net interest income (NII) received in recent months, largely owing to increased lending activities and the remuneration of banks' excess liquidity at the DFR as from 2022 (Central Bank of Malta, 2024).[16] Maltese banks' performance under these indicators of credit risk and profitability compares favourably to banks operating in other EA countries.[17]

Concluding remarks

In the light of commercial banks' crucial role in the transmission of monetary policy onto the real economy, this analyses revisited the pass-through of monetary policy decisions onto retail bank lending and deposit rates in Malta. The analysis clearly shows that the transmission of policy tightening via lending rate setting has been rather muted in recent months. Mortgage rates, in particular, have barely moved despite the rapid increase in policy rates, while movements in the interest rate on lending to NFCs have also lagged behind other EA countries. This study also shows that lending rates charged by Maltese banks were among the highest prior to any of the recent hikes in the policy rate by the ECB, which suggests a relatively weak pass-through in Malta even during years characterised by accommodative monetary policy. On the other hand, the transmission of tightening monetary policy onto time deposit rates, particularly those of households, is closer to that witnessed in the EA. Rates offered on overnight deposits have remained stable at very low levels during the latest cycle of tightening monetary policy, although similar developments were also observed in other countries within the EA.

Among the main factors that could potentially explain the low pass-through of monetary policy onto lending rates in Malta, this study shows that Maltese banks enjoy ample liquidity and have a strong accumulation of retail deposits, the vast majority of which are remunerated at very low rates. This allows banks to rely on this source of funding instead of borrowing from the ECB at higher rates, while concurrently being able to comfortably maintain their lending portfolios. In addition, Maltese banks also enjoy rising profitability, strong capital buffers and are subject to relatively low risk associated with non-performing loans. Moreover, lending rates in Malta were already relatively high before the recent tightening of monetary policy. These considerations, alongside others such as a possible desire by

[12] Financial Soundness Indicators – Core Banks 2015 onwards. See also footnote 10.
[13] Tier 1 capital comprises common shares and stock surplus, retained earnings, other comprehensive income, qualifying minority interest and regulatory adjustments (Common Equity Tier 1) plus capital instruments meeting the criteria for 'Additional Tier 1' capital. See Bank for International Settlements, "Definition of capital in Basel III – Executive Summary" for more details.
[14] See footnote 12.
[15] See footnote 12.
[16] See footnote 11.
[17] See footnote 10.

Maltese banks to preserve long-standing client relationships, could all be plausible explanations of the limited transmission of tightening monetary policy onto lending rates in Malta.

This analyses focused exclusively on one channel of monetary policy, namely the transmission of tightening monetary policy via retail bank rates. However, there exist other channels, such as the *exchange rate* and *asset price* channels which, while not addressed in this note, might also be relevant channels of monetary policy in Malta. In addition, the Maltese economy may also be affected indirectly through spillovers from the effects of tighter monetary policy in other countries, in the form of weaker foreign demand for Malta's output and lower import prices, which might lead to downward pressures on export demand and local prices. Therefore, a true understanding of the full extent of overall monetary policy transmission in Malta necessitates an analysis of the effectiveness of such other channels in the local context.

NATIONAL ACCOUNTS BENCHMARK REVISION 2024

Vanessa Dimech, Antoine Tanguy
and Keith Borg[1]

Introduction

In Eurostat's report entitled: '2019 benchmark revisions of national accounts – Impact on sector accounts', it is recommended that EU Member States carry out benchmark revisions, which are revisions of data sources or methods used to estimate national accounts indicators, at least once every five years. The main aims for a coordinated approach to benchmark revisions at EU level are twofold:

1. To achieve consistency within national accounts;
2. To achieve consistency across EU Member States and between statistical domains.

Although the benchmark revision is not carried out contemporarily across the EU, most Member States agreed to carry out the benchmark revision in the year 2024. In Malta, the benchmark revision in National Accounts data, was carried out in August 2024 by the NSO. The entire time series, dating back to the year 1995, was updated bringing about several enhancements to continue to improve the accuracy and richness of national accounts data.

This article aims to provide a comprehensive analysis of the benchmark revision, shedding light on the main improvements made, the sources used in the revision process, and the overall impact on GDP and its components.

The main sources of the revision

This Benchmark Revision served as a good opportunity to also address reservations and action points, which resulted from the ESA 2010 verification cycle.

One of the main revisions carried out emanated from the gambling and betting activities (Reservation 12), which sector includes online gaming companies. In the benchmark revision of 2024 annual data for the output approach from 2017 till 2019 was compiled using financial statements and data for the reference years 2020 and 2021 was derived from the Structural Business Statistics (SBS) dataset. The SBS 2022 was also partially integrated.

Revisions to GVA range between -2.1% in 2022 with a downward revision of €332 million and 3.6% in 2020 with an upward revision of €432 million (see Table 1). Since there was no need to revise the figures of taxes and subsidies on products, the absolute changes recorded in GVA, were identical to the revisions in GDP.

[1] Prepared by Vanessa Dimech, Antoine Tanguy and Keith Borg. Ms Dimech is the Head of the National Accounts Methods, Standards and Sector Accounts Unit within the NSO. Mr Tanguy is the Head of the National Accounts Production Unit within the NSO. Mr Borg is the Director of the Economic Statistics Directorate within the NSO.

Table 1
IMPACT OF THE REVISION IN GAMING AND BETTING ON GDP
EUR millions

		2017	2018	2019	2020	2021	2022
	PRODUCTION APPROACH						
1	Output of goods and services (at basic prices)	216	244	-422	236	-1,831	-2,967
2	Intermediate consumption (at purchasers' prices)	-72	-127	-393	-196	-1,948	-2,635
3	GVA (at basic prices)	289	371	-29	432	116	-332
4	Taxes on products						
5	Subsidies on products						
	EXPENDITURE APPROACH						
6	Total final consumption expenditure						
7	Household final consumption expenditure						
8	NPISH final consumption expenditure						
9	General government final consumption expenditure						
10	Gross capital formation						
11	GFCF						
12	Changes in inventories						
13	Acquisitions less disposals of valuables						
14	Exports of goods and services	216	244	-422	236	-1,831	-2,967
15	Imports of goods and services	-72	-127	-393	-196	-1,948	-2,635
	INCOME APPROACH						
16	Compensation of employees	-84	-97	-99	-43	-30	-26
17	Gross operating surplus and mixed income	373	468	71	475	147	-306
18	Taxes on production and imports	0	0	0	0	0	0
19	Subsidies						
20	GDP (ESA2010)	289	371	-29	432	116	-332

Source: NSO.

Moreover, another four reservations have been addressed with this Benchmark Revision, together with five action points. These are:

- Reservation 3: Cross-border flows of dividends – A revision ensuring that issues of bonus shares, which represent the capitalisation of own funds in the form of reserves and undistributed profits and give rise to new shares to shareholders in proportion for their holdings, are not included.

- Reservation 4: Issues relating to the exhaustiveness of National Accounts – A review of the current estimate for prostitution has been done to address the requirements of GNIC/230 on illegal activities in national accounts.

- Reservation II: Margins on trading financial assets – An adjustment was implemented to ensure that trading gain/(loss) on foreign exchange dealings is included in output in case of banking institutions, for the period 2010-2016.

- Reservation V: Recording of daily allowances – National Accounts estimates for daily allowances were aligned to the technical guidance on per diems established by Eurostat. Daily allowances may include basic costs that would otherwise be bought by the employee on their own account (e.g., for food) as well as some extra remuneration for working later or

on an otherwise free day. These may also include hotel costs or even flight costs, which as the employee would otherwise not incur them on their own account. Member States had heterogeneous recording practice for per diems: being recorded fully as compensation of employees or intermediate consumption or being split across the two categories. The new guidelines categorised these costs to ensure a consistent disclosure across Member States.

- Action point A2: NPISH – NPISH figures have been updated, based primarily on the Non-Governmental Organisations (NGO) survey of 2017, and administrative data thereon.

- Action point A7: Imputed rents for owner-occupied dwellings – Based on the Census of Population and Housing 2021 and in line with the requirements of Commission implementing regulation (EU) 2021/1949, Malta shifted from the user-cost method to the stratification method.[2]

- Action point A8: Rent (D.45) – An adjustment has been introduced to exclude rent on land from intermediate consumption using the information available in SBS 2018 at NACE division level.

- Action point A9: Reclassifications in the subsidies received from the institutions of the European Union – A review of European Agricultural Fund for Rural development (EAFRD) and European Agriculture Guarantee Fund (EAFG) led to the reclassification from subsidies on production (D.39) to investment grants (D.92).

- Action point A10: Wages and salaries in kind – Data extracted from the Labour Cost Survey (LCS) 2020, which is a survey conducted once every four years, have been used to update data for 2017-2020.

There were also other important refinements carried out, entailing the adoption of new methodologies or improved sources. These include:

- This benchmark revision includes the results of the *Supply and Use Tables (SUT) of 2019*, which provides a detailed picture of the supply of goods and services by domestic production and imports and the use of goods and services for intermediate consumption and final use (consumption, gross capital formation, exports). This involves 216 products and 95 industries.

- Output and intermediate consumption, exports and imports of Special Purpose Entities (SPEs) have been revised such that only the costs incurred by these entities in Malta will be included in the sum of costs method, thus eliminating the costs incurred by the non-resident parents as declared in the financial statements of the SPEs residents in Malta. This is in line with the advice provided by Eurostat.

- Pension funds, which started operations in 2012, are now included in the National Accounts series. There are both occupational and non-occupation schemes. Data for 2012 to 2021 has been derived from annual accounts and financial statements. As from 2024, the NSO may shift to administrative data provided by the Central Bank of Malta.

[2] Commission implementing regulation (EU) 2021/1949 of 10 November 2021 on the principles for estimating dwelling services for the purposes of Regulation (EU) 2019/516 of the European Parliament and of the Council on the harmonisation of gross national income (GNI) at market prices (GNI Regulation) and repealing Commission Decision 95/309/EC, Euratom and Commission Regulation (EC) No. 1722/2005

- In line with the recommendations relating to exhaustiveness, there were two main revisions implemented, namely:

  - The reference income method, which basically boils down to deriving per capita ratios from a reference group that could be representative for the scope of non-observed economy, has been adopted. The underlying hypothesis is that the owners of the enterprise should earn at least as much as their employee. The industries whose gross operating surplus per full-time equivalent (FTE) self-employed operating in the household sector was less than the compensation of employees per FTE salaried employees employed in the same industries were identified and adjusted since 1995. The exhaustivity adjustment was performed on output, to target GVA and thus gross operating surplus. This had an impact of €9 million in 1995, rising to €178 million in 2023.

  - Two different sources were considered in the compilation of figures relating to the non-financial corporations (S.11) and Households (S.14) using the employment method. The sources used were administrative data on the number of law infringements and Jobsplus registrations. This had an impact of €1.4 million in 1995, rising to €10 million in 2023.

- Consumption of fixed capital has been reviewed to implement the recommendations presented by Eurostat in the final report published in May 2023 of the Task force on fixed assets and estimation of consumption of fixed capital under ESA 2010.[3] Consumption of fixed capital has also been updated due to routine updates in GFCF based on SBS and the integration of the Census of Population and Housing 2021 in case of dwellings.

- Some refinements in the compilation of employers' actual social contributions (D.121) and employers' imputed social contributions (D.122) have been implemented across the whole time series.

- Enhancements with respect to the compilation of Balance of Payments statistics were also integrated in the National Accounts. However, since the Balance of Payments dataset is only available from 2017 onwards, a consistent time series covering the period 1995 to 2016, is only available through the national accounts domain. The main improvements include:

  a. Two administrative sources have been linked at micro-level to derive an exhaustive measure of cross-border flows for interest, dividends and re-invested earnings. One administrative source provides primary income flows and identifies some cross-border flows. The other source provides the ownership structure of corporations, thus allowing the derivation of dividends and re-invested earnings paid abroad. These data are then complemented with survey data.
  b. Data obtained from Bank of International Settlements (BIS) since 2014 has been used to derive interest received by households in Malta and paid to household abroad. Data compiled by the Central Bank of Malta from resident investment service providers was used to derive primary income flows received by household from investment activity abroad.
  c. Data on insurance undertakings and insurance agents have been updated since 2017. This had an impact on services, primary and secondary income flows.

[3] Directors of Macroeconomic Statistics Task Force on fixed assets and estimation of consumption of fixed capital under European System of Accounts 2010.

d. Administrative data has been used to cross-check interest paid and received by each sector as disclosed in the interest matrix. This matrix is a whom-to-whom matrix which shows transactions between sectors in the economy. This exercise was necessary to derive an estimate for intra-company flows which did not feature before in the interest matrix.
e. On a yearly basis the National Accounts unit compiles a dividend matrix and, in the process, derives an independent estimate of the Rest of the World sector (S.2).

- While this did not lead to any revision in household final consumption expenditure, the GDP at constant prices is now based on COICOP 2018.

As a result of all the changes mentioned above, GNI increased by 1.6 per cent on average between 2010 and 2022, with the average going up to 3.4 per cent in the period 2017-2022. (see Table 2). In the last six years under review, the revisions attributable to the GNI reservations caused an upward revision in GNI of 2.2 per cent annually on average. The revisions in GNI brought about by changes in sources and methods, stood at -1.8 per cent annually on average. The largest upward revisions in GNI for the years 2020, 2021 and 2022, were caused by routine revisions, at 3.5 per cent, 6.7 per cent and 6.5 per cent, respectively.

Table 2
REVISIONS TO GNI (ESA95 BASED) OF MALTA FOR 2010-2013 AND GNI (ESA2010 BASED) OF MALTA FOR 2014-2022 (AS A PERCENTAGE OF GNI FROM THE 2024 QUESTIONNAIRE)
Per cent

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total revision to GNI	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0.5**	**4.8**	**1.6**	**6.2**	**6.2**	**1.2**
of which:													
Total revision caused by GNI reservations	0	0	0	0	0	0	0	0.5	2.4	3.1	4.7	1.8	0.5
Total revision caused by changes in methods and sources (excl. ESA2010 implementation)								0	2.3	-1.5	-2.0	-2.2	-5.8
Total revision caused by routine (current) revisions								0	0	0	3.5	6.7	6.5

Source: NSO.

Chart 1 shows the changes in GVA, taxes less subsidies and GDP when comparing the latest published figures with the previous vintage, taking a production/output perspective. Major increases are observed in the four-year period between 2020 and 2023, mainly due to the fact that certain sectors in the services category performed more buoyantly than estimated originally during and after the COVID-19 breakout. On average, the upward revision in services over the past four years was €1.1 billion annually. The average stood at €0.3 billion annually between 2010 and 2019.

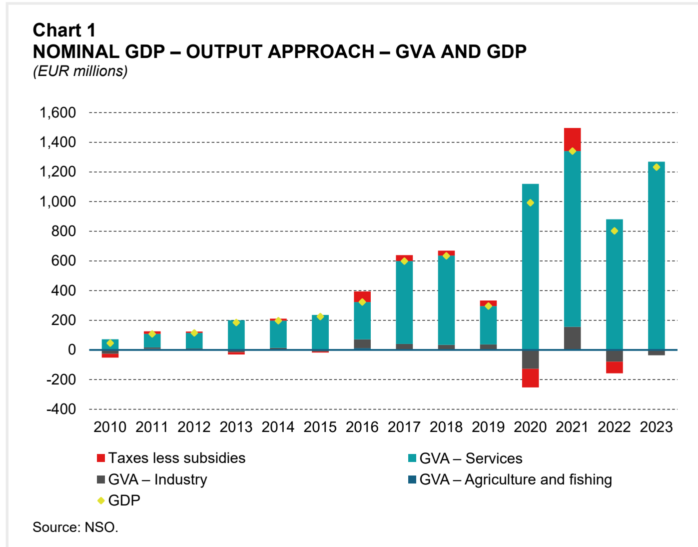
In the last four years, NACEs J, M and N (Information and communication; Professional, scientific and technical activities; Administrative and support service activities), which have clear

interlinkages with NACE R (Arts, entertainment and recreation), accounted for the lion's share of the entire increase on average. Another main contributor to the upward revision was NACE L (Real estate activities), which accounted for around one-fourth of the increase during the same period.

Most of the revision in the period 2010 – 2019 stemmed from the same sectors highlighted above with higher shares for NACEs L (Real estate activities) and R (Arts, entertainment and recreation).

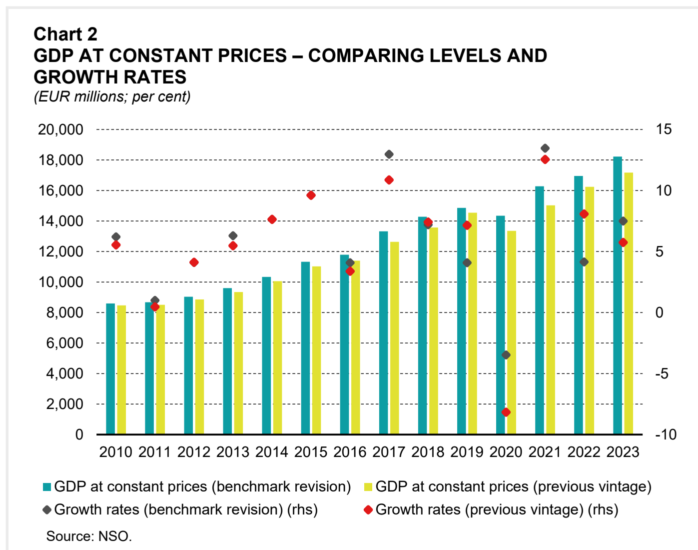
Chart 2 zooms into the differences between the GDP at constant (2020) prices following the benchmark revision and the figures of the previous vintage. The chart shows that in the year 2020 when COVID-19 was declared a pandemic – the slowdown in GDP at constant prices was less pronounced than originally estimated. The growth rate during 2020 increased by 4.7 percentage points, the highest increase, reaching -3.5 per cent.

Chart 1
NOMINAL GDP – OUTPUT APPROACH – GVA AND GDP
(EUR millions)



Source: NSO.

Chart 2
GDP AT CONSTANT PRICES – COMPARING LEVELS AND GROWTH RATES
(EUR millions; per cent)



Source: NSO.

Furthermore, the differences between the growth rates recorded before and after the benchmark revision, are greater after 2016 – with the exception of the year 2018 – mainly due to upward revisions in services highlighted above. The biggest downward revision in growth rates was recorded in the year 2022, with a drop of 3.9 percentage points.

Conclusion

The NSO is committed to continuously refine and enhance the accuracy of economic data, responding to changes in the economy and advances in statistical methodologies. The benchmark revision is a step in that direction, resulting in significant improvements in data accuracy and alignment with international standards.

Going forward, these revisions underscore the importance of regularly updating National Accounts data ensuring that the data remain relevant and reflective of the evolving economic landscape. After all, economic statistics remain a crucial tool for policymakers, economists, and stakeholders and a cornerstone of evidence-based decision-making.