ECONOMIC SURVEY

1. THE EXTERNAL ENVIRONMENT AND THE EURO AREA

In the third quarter of 2024, real GDP expanded at a stronger pace in the United States, was flat in the United Kingdom and grew at a faster rate in the euro area. During the quarter under review, the unemployment rate rose modestly in the United States and the United Kingdom, whereas it eased slightly in the euro area.

Consumer price inflation eased in the United States, the United Kingdom and in the euro area, mainly reflecting energy price dynamics. In the United States, inflation fell to 2.4% in September from 3.0% in June, in the United Kingdom, inflation declined to 1.7% in September from 2.0% in June, while, in the euro area, inflation declined to 1.7% in September from 2.5% three months earlier. The Federal Reserve, the Bank of England and the ECB lowered their key interest rates during the quarter under review.

Brent oil prices continued to fall in the review period, reflecting concerns about the outlook for global demand. By contrast, the price of European natural gas rose further mainly on the back of geopolitical developments which could reinforce already tight global market conditions.

Key advanced economies

US economic activity expands at a slightly faster pace

In the United States, real GDP grew at a quarterly rate of 0.8% in the third quarter, up from 0.7% in the preceding quarter (see Table 1.1). Higher personal consumption expenditure was the main contributor to growth, followed by government consumption. Both components, moreover, rose at a faster pace compared to the second quarter. Fixed private investment also contributed to growth, albeit to a lesser extent than in the previous quarter. Non-residential fixed investment also rose at a slightly faster rate, driven by outlays on equipment and intellectual property products. In contrast, residential investment shrank at a more pronounced pace. Net exports contributed negatively to economic growth, as imports notably outpaced exports. Also, a decline in private inventory investment deducted from GDP growth.

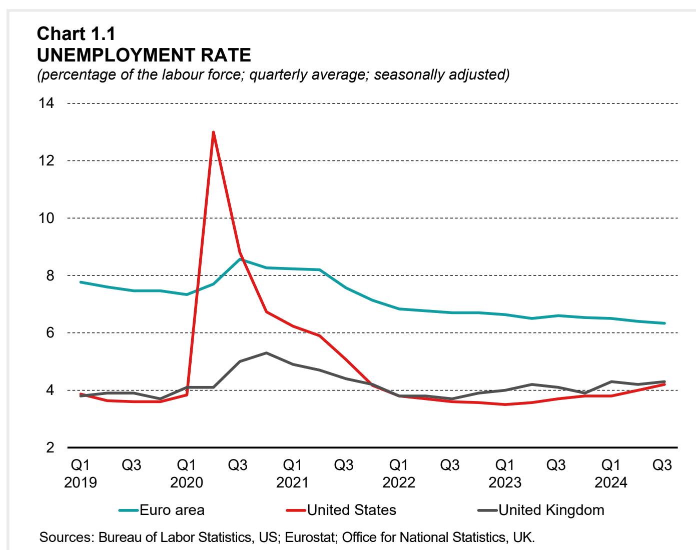
Meanwhile, labour market conditions remained favourable. Non-farm payroll data show that employment grew by 0.3% on average during the quarter, slightly less than in the previous quarter. These data suggest that the increase in employment was largely driven by private services.

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

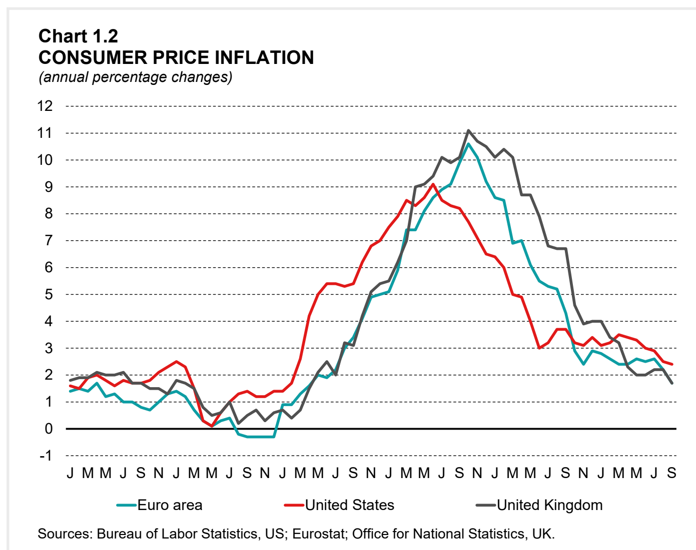
	2022		2023				2024		
	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3
United States	0.7	0.8	0.7	0.6	1.1	0.8	0.4	0.7	0.8
Euro area	0.6	-0.1	0.0	0.1	0.0	0.0	0.3	0.2	0.4
United Kingdom	0.1	0.3	0.1	0.0	-0.1	-0.3	0.7	0.4	0.0

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

In turn, within private services, employment growth was most pronounced in education and health, followed by leisure and hospitality. Government employment also increased during the review period. The participation rate rose to 62.7% during the review period, from 62.6% in the previous quarter. On average, the unemployment rate increased to 4.2% in the third quarter, compared to 4.0% in the previous quarter (see Chart 1.1).



Headline inflation continued to ease in the quarter under review, largely reflecting a marked decline in energy prices and a drop in commodities prices, excluding food and energy. Thus, the annual inflation rate based on the consumer price index (CPI) stood at 2.4% in September, compared to 3.0% three months earlier (see Chart 1.2). Annual energy inflation fell to -6.8% in September, as against 1.0% in June. The prices of commodities, excluding food and energy, fell by -1.0% in the year to September, a smaller fall than the -1.8% drop in the twelve months to June. Services inflation eased slightly, but remained high, declining to 4.7% in September, from 5.0% three months earlier. Meanwhile, food inflation (including beverages) stood at 2.2% in September, unchanged from June. However, underlying inflation, as measured by inflation excluding food and energy, remained somewhat elevated, standing at 3.3% in September, the same as in June.



On 18 September, the Federal Open Market Committee (FOMC) decided to lower the target range for the federal funds rate by 0.50 percentage points to 4.75-5.00%, judging that inflation had made further progress toward the 2% objective, though it remains somewhat elevated (see Chart 1.3). This was the first adjustment in the federal funds rate since July 2023. The Committee restated that it would be prepared to adjust the stance of monetary policy as appropriate if risks emerged that could impede the attainment of its goals. The FOMC also reaffirmed that it would continue

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

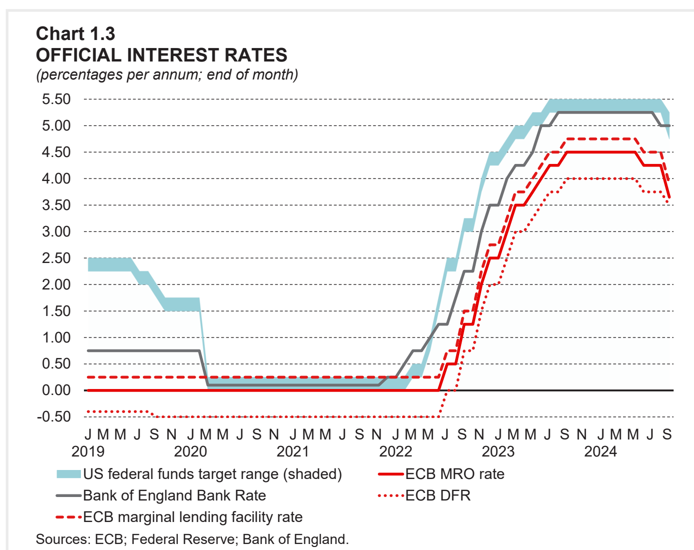


Chart 1.3
OFFICIAL INTEREST RATES
(percentages per annum; end of month)

Sources: ECB; Federal Reserve; Bank of England.

UK economic growth stagnates

Real GDP growth in the United Kingdom slowed down to 0% in the review period, following a 0.4% expansion recorded in the second quarter (see Table 1.1). A marked decrease in inventories counterbalanced increases in consumption expenditures by households and government, higher business investment, as well as an improvement in the trade balance. The latter reflected a drop in imports that outweighed lower exports.

Labour market conditions were stable. The employment rate rose to 74.9%, on a quarterly-average basis, from 74.6% in the previous three months, while the unemployment rate averaged 4.3% during the review period, up slightly from 4.2% in the previous quarter (see Chart 1.1).

Consumer price inflation in the United Kingdom rebounded in July and August but then dropped in September, with the annual inflation rate hitting 1.7% that month, compared to 2.0% in June (see Chart 1.2). Energy prices fell further during the quarter, and did so at a slightly faster pace than that recorded in the previous quarter. Thus, the annual rate of energy price inflation fell to -16.2% in September, compared to -16.0% three months before. Although most of the other major components of inflation continued to ease, both food and especially services inflation remained high, with the latter standing at 4.9% in September. In contrast, non-energy industrial goods (NEIG) inflation rose to 0.2% in September, as against -0.1% in June. The annual rate of inflation based on the CPI excluding energy, food, alcohol and tobacco fell to 3.2% in September, from 3.5% in June.

On 1 August 2024, the Bank of England's Monetary Policy Committee (MPC) announced that it had reduced the Bank Rate by 25 basis points, to 5.0%. This was the first change in the Bank Rate since August 2023. The MPC stated that it was appropriate to reduce the degree of policy restrictiveness as the impact from past external shocks had abated and some progress was registered in moderating risks of persistence in inflation. 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 (see Chart 1.3).[2] It also noted that a gradual approach to the removal of monetary restrictiveness seemed appropriate.

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[1] On 7 November and again on 18 December 2024, the FOMC decided to lower the target range for the federal funds rate by 0.25 percentage points, bringing the target range down to 4.25-4.50%.

[2] On 6 November 2024, the MPC reduced the Bank Rate by 25 basis points, to 4.75%, reflecting the continued progress in disinflation. The Committee restated that it would continue to monitor closely the risks of inflation persistence and would decide the appropriate degree of monetary policy restrictiveness at each meeting. On 18 December, the MPC kept the Bank Rate unchanged.

The euro area

GDP in the euro area continues to recover

Economic activity in the euro area continued to gradually recover in the third quarter of 2024. In real terms, GDP rose by 0.4% on a quarter-on-quarter basis, compared to 0.2% recorded in the previous quarter, with the acceleration driven by domestic demand (see Table 1.2). Growth continued to be mainly driven by the services sector whereas the construction sector continued to contract. The Economic Sentiment Indicator (ESI) remained broadly unchanged, below the long-term average. Improved confidence among firms in the construction sector, reflecting builders' improved assessments of their order books and their employment expectations, the still strong dynamics in contact-intensive services and improving consumer confidence were offset by a decrease in confidence in both industry and the retail sector.

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

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

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

In the third quarter, domestic demand contributed 1.3 percentage points to GDP growth. In turn, the expansion in domestic demand mainly reflected increases in private consumption expenditure as well as business inventories and gross fixed capital formation (GFCF). The latter reflected a notable rise in investment in intellectual property products, whereas investment in machinery and equipment, as well as in construction, contracted. Government consumption rose moderately. In contrast, net exports deducted 0.9 percentage points from GDP growth, as exports declined while imports rose slightly.

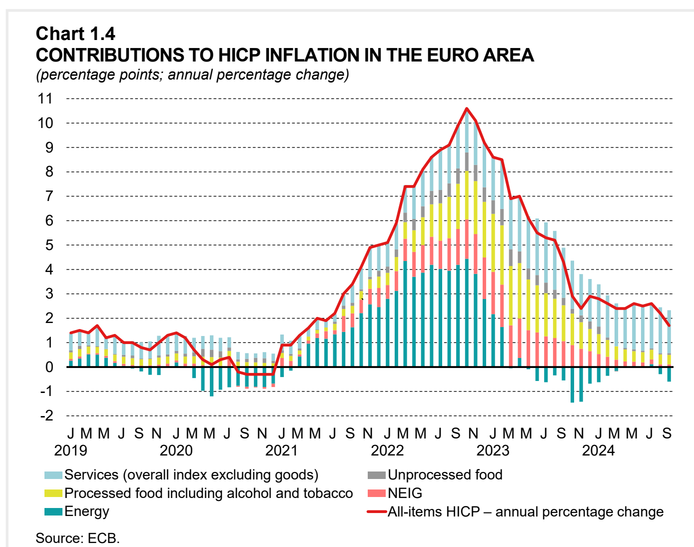
Labour market remains strong

The labour market in the euro area remained robust during the third quarter. Employment continued to expand, growing at a quarterly rate of 0.2% during the review period, the same as in the preceding quarter.[3] Meanwhile, the seasonally adjusted unemployment rate fell to 6.3% in September, compared to 6.4% in June. Similarly, it averaged 6.3% in the quarter under review, down from 6.4% in the second quarter (see Chart 1.1).

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

Inflation resumes its downward path

Inflationary pressures in the euro area eased in the third quarter, following a marginal rebound in the previous three months. The annual rate of inflation based on the HICP stood at 1.7% in September, down from 2.5% in June (see Chart 1.4). The decrease in overall inflation was broad-based, but largely reflected a drop in energy prices.



Turning to the major HICP components, energy prices dropped at an annual rate of 6.1% in September, as against an increase of 0.2% in June. This drop partly reflects a base effect, as energy prices had risen sharply in September 2023. The annual rate of NEIG inflation slowed down to 0.4% in September, compared to 0.7% three months earlier. Similarly, services inflation eased to an annual rate of 3.9% in September, from 4.1% three months earlier, though it remained elevated. Also, the annual rate of processed food inflation eased marginally to 2.6% over the review period, compared to 2.7% in June. On the other hand, unprocessed food prices increased at an annual rate of 1.6% in September, up from 1.3% in June.

Underlying inflationary pressures moderated further, on average, during the review period. One measure of underlying inflation, the annual rate of HICP inflation excluding energy and food prices, edged down to 2.7% in September, from 2.9% in June.

Real GDP expected to continue to recover gradually, inflation projected to ease further

According to the Eurosystem staff macroeconomic projections for the euro area, published in December 2024, real GDP growth in the euro area is estimated to increase to 0.7% in 2024. Real GDP is then expected to expand further by 1.1%, 1.4% and 1.3% in 2025, 2026 and 2027, respectively (see Table 1.3). Although the euro area economy continued to expand moderately during 2024, recent indicators point to a weakening of growth in the short term. Persistently weak consumer confidence as well as elevated geopolitical and policy uncertainty are expected to induce households to postpone their consumption. However, subsequently, Eurosystem staff foresee a strengthening of economic growth mainly on the back of rising real wages and robust labour markets which, alongside an easing of financing conditions, will likely reinforce domestic demand. Also, the dampening effects of past monetary policy tightening are expected to fade over the projection horizon. Although fiscal policies are surrounded by heightened uncertainty, a degree of consolidation is expected. Meanwhile, funds from the Next Generation EU programme should underpin economic growth until the expiry of the programme in 2027. The projections assume that the trade policies of Europe's key trading partners remain unchanged, implying that foreign demand is expected to expand and support euro area exports. The unemployment rate will likely continue to fall to historically low levels while productivity is expected to pick up over the next three years.

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

	2023	2024	2025	2026	2027
GDP	**0.5**	**0.7**	**1.1**	**1.4**	**1.3**
Private consumption	0.8	0.9	1.3	1.3	1.2
Government consumption	1.5	2.3	1.2	1.2	1.0
GFCF	1.8	-1.7	1.2	2.2	1.6
Exports	-0.2	1.0	1.6	3.0	3.0
Imports	-0.7	0.1	2.3	3.1	2.9
HICP	**5.4**	**2.4**	**2.1**	**1.9**	**2.1**
HICP excluding energy and food	4.9	2.9	2.3	1.9	1.9

Source: ECB.

[1] Eurosystem staff macroeconomic projections for the euro area, December 2024.

Compared to the September 2024 projections, the latest projections are conditioned on lower oil and electricity prices but higher gas prices, a weaker exchange rate and lower interest rates. Real GDP growth is revised downwards by 0.1, 0.2 and 0.1 percentage points for 2024, 2025 and 2026, respectively. These revisions reflect weaker investment, mainly owing to revisions to data for the first half of 2024, and net exports in the short term that are partly offset in 2024 by government consumption. Private consumption growth for 2025-2026 was also revised downwards in light of a reassessment of the dynamics of household savings. Having said that, private consumption is still expected to be the main locomotive of economic growth.

Turning to the outlook for prices, Eurosystem staff foresee HICP inflation to decline to an average of 2.4% in 2024 from 5.4% in 2023, and to ease further to 2.1% and 1.9% in 2025 and 2026, respectively. In 2027, it is set to rebound slightly to 2.1%. HICP inflation is expected to increase in late 2024, mainly reflecting base effects in the energy component. Inflation is then expected to decline and eventually fluctuate around the ECB's 2% target from the second quarter of 2025. The introduction of new climate change mitigation measures is expected to bring about a marginal rise in inflation in 2027.

HICP inflation excluding energy and food is expected to lessen to an average of 2.9% in 2024 from 4.9% in 2023, and ease further to 2.3% in 2025 and 1.9% in 2026 and 2027, respectively. The decline in HICP inflation excluding energy and food in the near term is set to be driven mainly by the services component. Although wage growth is expected to remain elevated at first, it will likely fall gradually as inflation compensation pressures wane. Meanwhile, external price pressures are expected to remain modest.

Compared to the September 2024 projections, the outlook for headline HICP inflation is revised downwards by 0.1 percentage points in both 2024 and 2025, as an upward revision to food inflation is outweighed by a downward revision to energy inflation. The inflation projection remains unchanged for 2026. Underlying inflation expectations are kept unaltered for 2024 and 2025. However, they are revised downwards by 0.1 percentage points for 2026, mainly reflecting the impact from downward revisions to the outlook for economic growth and wages.

ECB cuts interest rates further

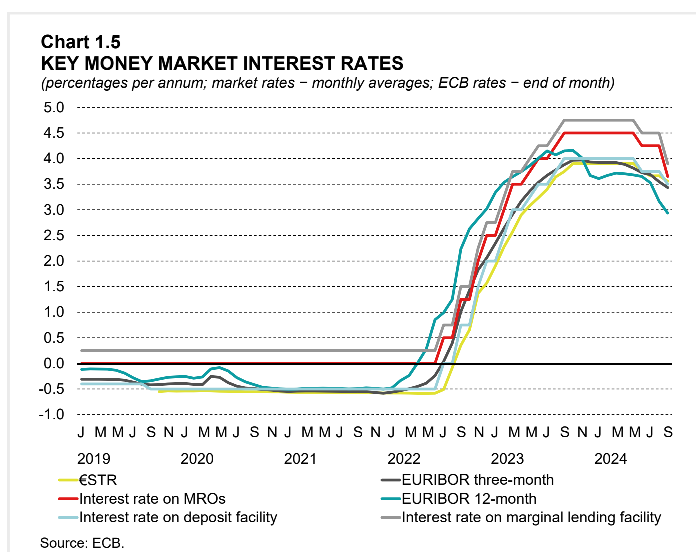
In light of the Governing Council's updated assessment of the inflation outlook, the dynamics of underlying inflation and the strength of monetary policy transmission, on 12 September, the Council decided to lower the DFR – the rate through which it steers the monetary policy stance – by 25 basis points. Additionally, as the Governing Council had announced on 13 March 2024, some changes to the operational framework for implementing monetary policy took effect from 18 September. In particular, 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.

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.[4]

Money market rates drop further

Money market interest rates in the euro area continued to fall during the review period, reflecting the reductions in official interest rates and market expectations of further interest rate cuts. Hence, the euro short-term rate (€STR) averaged 3.56% in September, compared to 3.75% in June, as it responded to the September reduction in official interest rates (see Chart 1.5).[5] The three-month euro interbank offered rate (EURIBOR) averaged 3.43% in September, as against 3.72% three months earlier. The 12-month EURIBOR averaged 2.94% in September, compared to 3.65% in June.[6] The 12-month EURIBOR thus fell further below the DFR, indicating market players' more pronounced expectations of further reductions in key policy rates.

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



Source: ECB.

[4] On 17 October and again on 12 December 2024, the Governing Council decided to lower the three key ECB interest rates by 25 basis points. Accordingly, the DFR, the rate on MROs and the marginal lending facility rate were decreased to 3.00%, 3.15% and 3.40%, respectively. At the December meeting, whilst reiterating that it was not pre-committing to a particular rate path, the Governing Council dropped its restrictive bias with regard to policy rates.

[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.

Euro area government bond yields fall

The euro area ten-year benchmark government bond yield fell during the third quarter, mainly because market participants reviewed their expectations about inflation and official interest rate dynamics in the euro area, as well as developments in the US Treasury bond market. This yield averaged 2.83% in September, compared to 3.17% three months earlier.

Individual sovereign bond yields fell to varying degrees across almost all euro area countries. In Germany, ten-year sovereign bond yields decreased by 31 basis points to 2.17%. Yields fell by 46 basis points, to 3.19%, in Greece and by 41 basis points, to 2.78%, in Portugal. Notable declines in yields also occurred in Ireland, Italy and Spain, where they fell by 38 basis points, to 2.55%, 37 basis points, to 3.57%, and 36 basis points, to 2.99%, respectively. Meanwhile, in France yields dropped by 25 basis points, to 2.90%. Bond yields in almost all the remaining euro area jurisdictions were down.

Spreads between yields on the ten-year German bonds and those on the bonds issued by most of the other euro area jurisdictions narrowed, notably in the case of Greece and Portugal, where they fell by 15 and 10 basis points, respectively (see Chart 1.6). Among the largest euro area countries, spreads also narrowed in Italy and Spain. By contrast, the spread between German benchmark yields and those on French government bonds widened by 6 basis points, by the end of the quarter.

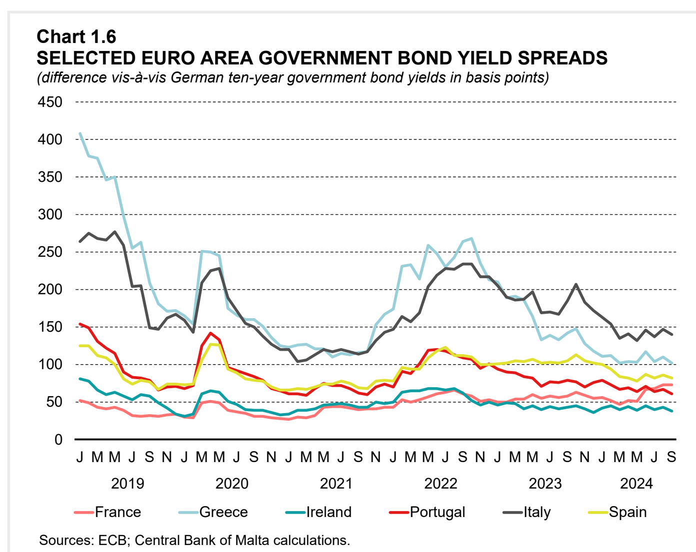


Chart 1.6
SELECTED EURO AREA GOVERNMENT BOND YIELD SPREADS
(difference vis-à-vis German ten-year government bond yields in basis points)

Sources: ECB; Central Bank of Malta calculations.

The euro rebounds versus the US dollar and in effective terms

The euro appreciated by 4.6% against the US dollar, rebounding notably from the previous quarter, as the latter was undermined by market views that US interest rates were likely to fall at a faster pace than previously expected (see Chart 1.7). The euro also registered gains against the Hong Kong dollar, the Canadian dollar, the Australian dollar, the Chinese renminbi and a number of other

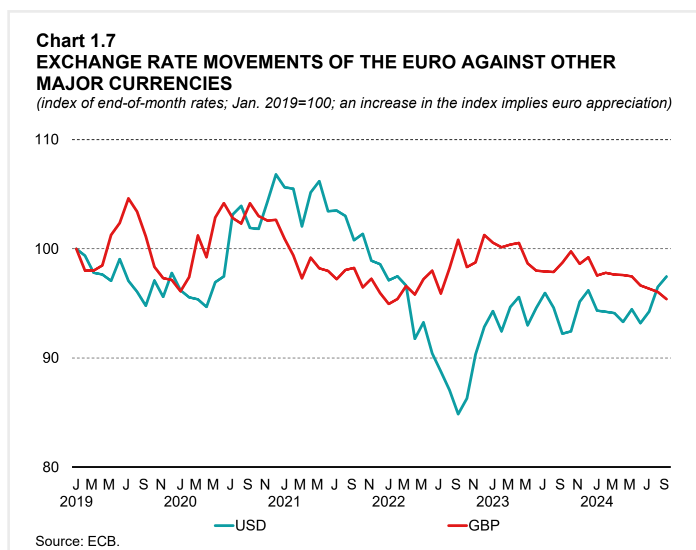


Chart 1.7
EXCHANGE RATE MOVEMENTS OF THE EURO AGAINST OTHER MAJOR CURRENCIES
(index of end-of-month rates; Jan. 2019=100; an increase in the index implies euro appreciation)

Source: ECB.

European currencies. Overall, the nominal effective exchange rate (EER) of the euro against the EER-18 group of countries rose by 0.5% in the three months to end-September 2024.[7]

By contrast, the euro depreciated by a further 1.3% versus the British pound as the latter continued to be underpinned by relatively high interest rates. The single currency also fell against the Japanese yen, which was bolstered by the Bank of Japan's announcement of a tightening monetary policy stance. The euro also depreciated against the Swiss franc and incurred smaller losses versus the Polish zloty, the Singapore dollar and the Korean won.

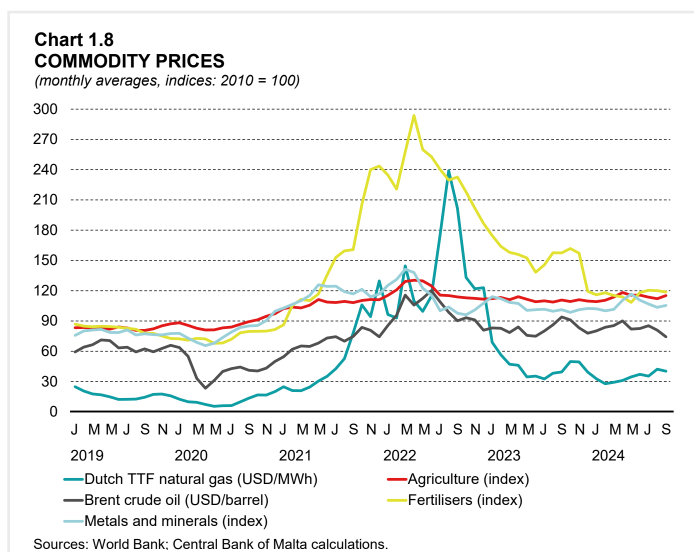
Commodities

Oil prices drop further whereas natural gas prices continue to rise

Oil prices continued to ease in the third quarter, amid concerns about forecast physical demand globally, especially in view of a slowing economy and changes in energy consumption patterns in China. Towards the end of the review period, however, oil prices rebounded somewhat in the context of the beginning of the Israeli bombing of Lebanon coupled with the possible threat of an escalation in the Middle East. Overall, the price of Brent crude oil averaged USD 74.3 per barrel in September, 10.0% lower than the level prevailing three months earlier. By contrast, the price of European natural gas increased further in the quarter under review, mainly reflecting a tighter global LNG market, geopolitical instability and uncertainty surrounding the renewal of a transit agreement governing pipeline flows of Russian gas through Ukraine. The average price of Dutch TTF natural gas stood at USD 40.2 per megawatt hour in September, or 8.4% higher than in June (see Chart 1.8).

World Bank data show that non-energy commodity prices fell by 1.7% during the quarter under review. This reflected lower prices for metals and minerals and, to a lower extent, agricultural products, which outweighed higher prices for fertilizers. Meanwhile, prices of precious metals were up by 9.0%.

Chart 1.8
COMMODITY PRICES
(monthly averages, indices: 2010 = 100)



Sources: World Bank; Central Bank of Malta calculations.

[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.