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THE IMPACT OF BUDGET 2023 TARGETS ON THE BANK'S FISCAL PROJECTIONS

Article published in the Outlook for the Maltese Economy 2022:4, pp. 18-21

BOX 3: THE IMPACT OF BUDGET 2023 TARGETS ON THE BANK'S FISCAL PROJECTIONS[1]

This box assesses the impact of Government fiscal targets as announced in the Budget 2023, and the Draft Budgetary Plan 2023, on the Bank's latest projections.

Budget 2023 measures

With this Budget, the Government is seeking to support economic growth and protect households and firms from the surge in commodity prices. Vulnerable and low-income persons also benefit from additional social measures. The Budget also promotes supply-side reforms and facilitates the green economy and digital transition.

Newly announced measures mainly reflect an extension of the welfare system. This includes a rise in pensions and benefits for low-income beneficiaries, more generous allowances to carers and parents with children, as well as extended in-work benefits. A new benefit for first-time buyers of property has been introduced. Government also launched a new mechanism, separate from COLA, which will determine a new benefit to low-income households during periods with inflation above 2%. Meanwhile, certain government employees and workers under a public contract will be offered a one-time increase in wages, in order to retain relativity in grades agreed in collective agreements.

Existing measures supporting first time property buyers and purchases of vacant property or buildings in village cores will be renewed. A tax exemption scheme on pension income, first introduced in 2022, will be extended. Tax refunds and other measures to address past anomalies will also be continued in 2023. Meanwhile, Government intends to continue supporting electricity, fuel, and gas distributors in order to retain fixed retail utility prices.

The budget reaffirms the Government's commitment to reduce carbon emissions and the transition towards the green economy. The Speech references the introduction of free public transport and highlights ongoing projects such as the shore-to-ship electricity infrastructure, new waste treatment facilities and building renovations. Many of these projects form part of the milestones listed in the Recovery and Resilience Plan, by means of which Government is eligible for grants from the EU's Recovery and Resilience Fund.

The Budget Speech also mentions ongoing efforts to restructure Air Malta. Talks with the European Commission on the possibility of state aid are ongoing.

As shown in Table 1, in marginal terms, the main budget measures are set to have a deficit-reducing impact in 2023. This is mostly due to the end of support measures introduced in the wake of the COVID-19 pandemic. The Wage Supplement Scheme ended in May 2022. A temporary reduction on stamp and capital gains duty on property purchases, which applies to promise of sale agreements entered into by end-2021, will remain in force until June 2023. Meanwhile, outlays on treatment and vaccinations are

[1] This box was prepared by John Farrugia, Manager within the Fiscal Affairs and Reports Office.

Table 1
IMPACT OF MAIN BUDGET MEASURES
(% of GDP)

	2022	2023
Revenue	**0.21**	**1.53**
No Income tax on pension income, lower income tax on overtime and part-time employment	-0.10	0.01
Schemes for property buyers	-0.11	0.05
COVID measures – reduction in stamp duty and capital gains tax on property sales/purchases	0.73	0.88
COVID measures – lower excise tax on fuel and reimbursement of commmercial and tourism licences	0.10	0.06
Inflation support measures– minimum excise duty applicable on petroleum products	-0.14	0.34
Revenue from Individual Investor Programme and citizenship by investment	-0.45	0.21
Revised interest rates on unsettled tax balances	0.17	-0.01
Expenditure	**0.23**	**0.33**
Increase in pensions	0.17	0.28
Higher social benefits	0.14	0.07
Additional outlays on tax rebates to employees and schemes to address past anomalies	0.03	0.03
COVID measures – support to employers and households and liquidity measures	-2.20	-0.81
COVID measures – health treatment, repatriation and safe reopening of schools	-0.33	-0.18
COVID measures – social measures	0.00	0.00
Inflation support measures – commodity price support measures	1.82	1.03
Inflation support measures – economic stimulus cheques; COLA adjustments for vulnerable persons, Government employees and workers under government contract	0.29	-0.16
Support to national airline	0.31	0.06
Impact on balance	**-0.02**	**1.20**

Sources: Budget Speech 2023; Draft Budget Plan 2023.

set to decline substantially in 2023. The end of these measures is set to boost government revenue by 0.9% of GDP and reduce expenditure by 1.0% of GDP in 2023.

This effect is set to be partly offset by the above-mentioned introduction of new social measures and support measures to retain fixed utility prices. In 2023, their marginal impact is expected to reach 1.3% of GDP.

Revised Government targets

The 2023 Draft Budget Plan (DBP) envisages a continued decline in the deficit-to-GDP ratio. In 2022, this is set to decrease to 5.8%, from 7.8% in the previous year (see Table 2). It is then expected to decline to 5.5% in 2023 and to fall below 3.0% by 2025. Meanwhile, the debt ratio is set to increase from 56.3% of GDP in 2021 to around 60.0% of GDP by 2024 and 2025.

Compared with the targets set in last April's Stability Programme (SP) Update, a higher deficit ratio is now forecast throughout the projection horizon. This is mainly due to an upward revision of outlays on subsidies. This category captures most of ongoing price-mitigating

Table 2
GOVERNMENT REVENUE AND EXPENDITURE TARGETS
(% of GDP)

	Budget /Draft Budget Plan 2023					Stability Programme Update 2022				
	2021	2022	2023	2024	2025	2021	2022	2023	2024	2025
General government balance	**-7.8**	**-5.8**	**-5.5**	**-4.2**	**-2.8**	**-8.0**	**-5.4**	**-4.6**	**-2.8**	**-2.4**
Revenue	**37.0**	**36.9**	**36.9**	**35.4**	**35.3**	**37.5**	**38.1**	**38.1**	**37.6**	**36.9**
Tax revenue	31.0	31.7	31.2	30.8	30.7	31.4	32.7	32.6	32.7	32.5
Other revenue	6.1	5.2	5.7	4.6	4.6	6.1	5.4	5.5	4.8	4.4
Expenditure	**44.8**	**42.7**	**42.5**	**39.7**	**38.1**	**45.5**	**43.6**	**42.7**	**40.3**	**39.3**
Compensation of employees	12.0	11.4	11.1	10.9	10.8	12.2	12.1	12.1	12.2	12.2
Intermediate consumption	8.9	8.6	8.0	7.6	7.5	9.4	9.9	9.3	9.0	8.8
Social payments	9.5	9.1	9.2	9.0	8.9	9.6	9.8	9.6	9.6	9.4
Interest payments	1.1	1.0	1.3	1.6	1.6	1.5	1.1	1.1	1.1	1.1
Subsidies	4.7	4.7	4.9	4.0	3.2	4.7	2.9	2.9	1.6	1.4
Gross fixed capital formation	3.9	4.0	3.9	3.0	2.9	4.2	4.1	4.2	3.7	3.4
Capital transfers	1.2	1.1	1.1	0.7	0.7	1.1	1.1	1.2	1.0	0.9
Other expenditure	3.5	2.8	3.0	2.9	2.5	2.8	2.6	2.3	2.1	2.1
General government debt	**56.3**	**57.0**	**59.1**	**60.3**	**60.0**	**57.0**	**58.6**	**59.4**	**58.6**	**57.2**

Sources: Budget Speech 2023; Draft Budget Plan 2023; Stability Progamme Update 2022.

support measures. In addition, for 2023, a relatively more conservative profile for tax revenue is expected.

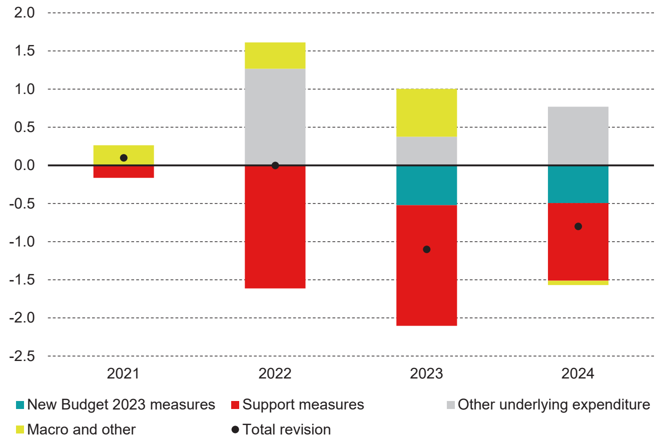
Compared with the SP targets, outlays on intermediate consumption and compensation of employees are set to reach a lower share in GDP. The targeted share of capital expenditure in GDP, particularly in the outer years of the forecast horizon, has also been revised down.

Owing to the higher deficits, the 2023 DBP envisages the debt-to-GDP ratio to be higher than the SP targets. The debt ratio will also peak a year later (in 2024 rather than 2023).

Impact on Bank's fiscal forecasts

Chart 1 decomposes the revisions in the Bank's deficit projection, compared with the August exercise. The impact of newly announced 2023 Budget and ongoing support measures are shown separately. The chart also shows revisions in the projected impact of underlying expenditure, such as wages, previously enacted measures,

Chart 1
REVISIONS COMPARED WITH THE PREVIOUS CBM FORECAST
(positive values indicate a downward revision to the deficit, and vice versa; % of GDP)



Sources: Authors' estimate.

and the profile of capital expenditure. Revisions to the macro-outlook on the deficit ratio are also shown separately.

The Bank's forecasts do not include the impact of measures which have not yet been adopted (i.e., the proposed state aid to the national airline) or those which are hard to determine (i.e., the impact of increased interest rate charges on outstanding tax balances).

On balance, revisions to past data and changes in the recording of certain support measures contribute to a small improvement in the deficit ratio for 2021.

Overall, revisions to the impact of Budget and support measures are deficit-increasing throughout the forecast horizon. This impact is partly mitigated by a revised assessment of the profile of underlying expenditure (particularly capital spending). Revisions in the macroeconomic and price projections exert a deficit-reducing impact in 2022 and 2023, (mainly though a revised profile of tax revenue) and a small deficit-increasing impact in 2024.