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The Hon Mr Clyde Caruana B.Com. (Hons) Economics, M.A. Economics
Minister for Finance and Employment
30, Maison Demandols,
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Honourable Minister,

**ASSESSMENT OF THE MACROECONOMIC FORECASTS CONTAINED
IN THE UPDATE OF THE STABILITY PROGRAMME 2023 - 2026**

The Malta Fiscal Advisory Council (MFAC) is required, under Article 13 of the Fiscal Responsibility Act, to endorse, as it considers appropriate, the macroeconomic forecasts prepared by the Ministry for Finance and Employment. These forecasts serve as the basis for the Update of the Stability Programme. The Ministry provided the Council with provisional macroeconomic forecasts on 20 April, followed by a revised set received on 27 April, and the finalised set confirmed on 01 May 2023 (see Appendix 1). These forecasts update the macroeconomic outlook, which was published by the Ministry and endorsed by the Council in October 2022 as part of the Draft Budgetary Plan. The cut-off date for these macroeconomic projections is 13 March 2023.

The Fiscal Council has reviewed the plausibility of the assumptions used by the Ministry in their latest forecast round. A meeting took place on 25 April 2023 with the Ministry's senior officials to examine the drivers underpinning the updated macroeconomic outlook and the factors contributing to the revisions from the previous forecast. The macroeconomic forecasts were further assessed in light of the available market information and statistical data and compared to those prepared by independent institutions. The Fiscal Council acknowledges the significant challenges that are present when preparing macroeconomic forecasts covering a four-year horizon.

In 2023, the Ministry for Finance and Employment is expecting real GDP to increase by 4.1%, following a strong rebound of 11.8% and 6.9% in 2021 and 2022, respectively, from the contraction experienced in 2020 due to the pandemic. Growth in 2023 is expected to be primarily driven by the external side of the economy and, to a lesser extent, by domestic demand. Private consumption expenditure is expected to increase by 3.8% in real terms in 2023, following strong growth in the previous two years. Government consumption expenditure is expected to increase by 3.4%. Gross fixed capital formation is expected to contract by 6.8% following the significant increase recorded in the previous year, the latter attributed to extraordinary investment in transport equipment. Real exports are expected to increase by 4.3% as Malta is expected to continue gaining export market shares. Imports are expected to increase by 2.4%, reflecting developments in exports and domestic demand.

Over the remaining years of the forecast horizon, economic growth is expected to accelerate to 4.5% and 4.6% in 2024 and 2025 before decelerating again to 4.2% in 2026. Contrary to 2023, growth in the following years is expected to be primarily supported by the domestic side of the economy, while the external side of the economy is expected to contribute positively, albeit to a lesser extent. Private consumption expenditure is expected to continue increasing moderately, supported by increasing income, strong labour demand conditions and population growth. Growth in government consumption expenditure is projected to remain rather subdued by historical standards, increasing by an average rate of 2.4%. Investment is expected to increase by an annual average of 4.7% between 2024 and 2026. Exports are expected to increase by 5.2% and 5.3% in 2024 and 2025 before decelerating in 2026, reflecting mainly the trajectory of the exogenous assumptions.

Economic growth is expected to remain rather job-rich, and as a result, employment growth is forecasted to remain sustained over the forecast horizon. The unemployment rate is expected to remain practically at the same level of 2022 over the forecast horizon; thus labour market conditions are expected to remain tight over the forecast period. Inflationary pressures are expected to remain elevated in the short term but are expected to return to the European Central Bank's price stability target of around 2% in 2025.

The Fiscal Council notes that the official real GDP growth forecast for 2023 has been increased compared to that which had been indicated in the Draft Budgetary Plan. The outlook for the period 2023 to 2026 adequately factors in the macroeconomic information available to date. The outlook of moderate GDP growth across the forecast horizon is

somewhat more positive than the profile indicated in the forecasts that independent institutions published by the date of this letter.

The Fiscal Council acknowledges that the presented macroeconomic projections hinge on the assumptions employed and given the high degree of openness of the Maltese economy, any material departure from the exogenous assumptions could significantly alter the growth outlook. In particular, the outlook is conditional on developments surrounding the key sectors in the Maltese economy, such as manufacturing, tourism, wholesale and retail trade, remote gaming, professional services, and financial and insurance services, performing in line with current expectations, as well as the materialisation of the fiscal plans which underpin the Update of the Stability Programme.

Based on the information available to the Malta Fiscal Advisory Council by the date of this letter, and after considering the inherent risks and uncertainty surrounding these macroeconomic projections, the Council considers the full set of macroeconomic projections for the period 2023 to 2026 prepared by the Ministry for Finance and Employment as part of the Update of the Stability Programme 2023 – 2026 to lie within its endorsable range.

The Council would like to express its gratitude for the ongoing collaboration and assistance with the Ministry's employees. Considering the cut-off date assumed for these projections, the Council urges the Ministry for Finance and Employment to submit their projections in the future as early as possible to provide sufficient time for the Council to process the information. Nonetheless, the Council would like to express its satisfaction with the reception of the Ministry for Finance and Employment to its recommendations and proposals when discussing the macroeconomic projections.

A detailed assessment of the macroeconomic forecasts carried out by the MFAC to support its endorsement decision will be published in the Council's forthcoming Report.

Yours sincerely,



Dr Moira Catania
Chairperson of the Malta Fiscal Advisory Council

Appendix 1: Main Macroeconomic Indicators

	2021	2022	2023	2024	2025	2026
Real GDP components chain-linked volumes, reference year 2015						
Private final consumption expenditure (including NPISH) (y-o-y %)	8.1	10.1	3.8	3.9	4.0	3.6
General government final consumption expenditure (y-o-y %)	6.9	2.4	3.4	3.2	2.4	1.7
Gross fixed capital formation (y-o-y %)	10.9	30.4	-6.8	3.8	4.6	5.6
Exports of goods and services (y-o-y %)	6.3	6.4	4.3	5.2	5.3	4.2
Imports of goods and services (y-o-y %)	3.8	9.7	2.4	4.8	5.0	3.9
Real GDP (y-o-y %)	11.8	6.9	4.1	4.5	4.6	4.2
<i>Contribution to real GDP growth:</i>						
<i>Domestic demand (pp)</i>	7.2	10.9	0.6	3.2	3.3	3.2
<i>Inventories (pp)</i>	-0.3	-0.1	0.0	0.0	0.0	0.0
<i>Net exports (pp)</i>	4.9	-4.0	3.5	1.2	1.3	1.0
Nominal GDP (y-o-y %)	13.9	12.5	8.6	7.7	7.2	7.0
Inflation rate (based on the HICP) (%)	0.7	6.1	5.7	3.5	2.0	2.4
Employment growth (National Accounts definition) (%)	2.9	6.0	3.5	3.7	3.7	3.6
Unemployment rate (based on the LFS) (%)	3.4	2.9	3.0	3.1	3.1	3.1

Note: GDP growth rates for 2021 and 2022 are based on the provisional values published by the National Statistics Office on 28 February 2023 (News Release 036/2023), while figures for the period 2023 to 2026 represent the forecasts prepared by the Ministry for Finance and Employment.

Source: Ministry for Finance and Employment