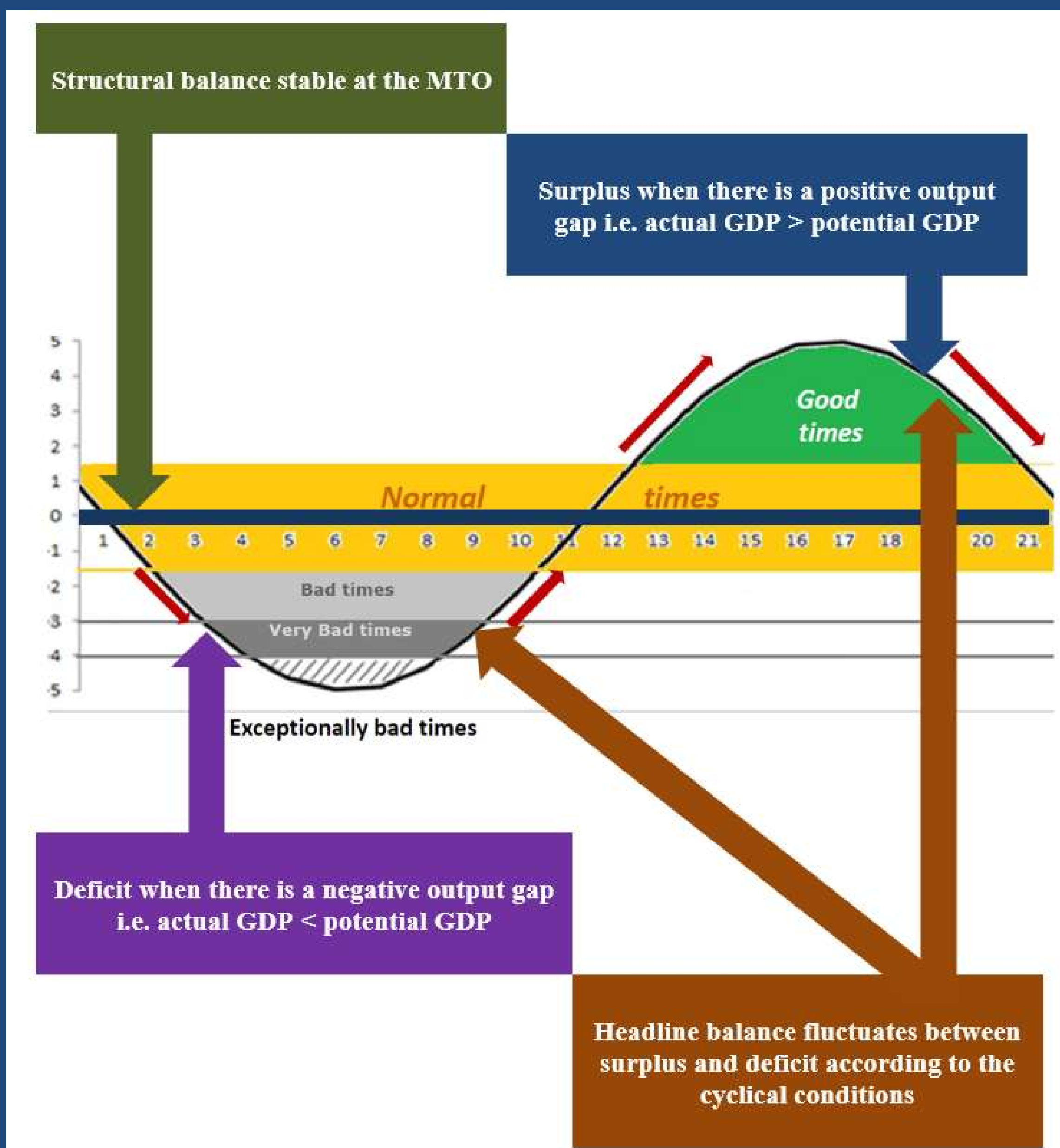
Box 2: STYLISED FISCAL FRAMEWORK

The preventive arm of the SGP works on the premise that the country's underlying fiscal position (as measured through the structural balance) is stable, with the headline fiscal balance shifting between a small surplus and deficit depending on whether the economy is operating slightly above or slightly below potential (see Diagram A). On the other hand, when the economy's output gap is significantly positive (i.e. when actual GDP is significantly above potential GDP), a larger fiscal surplus is prescribed. In the case of a significant negative output gap (i.e. when actual GDP is significantly below potential GDP), this would allow a higher deficit, which would only breech the 3.0% deficit-to-GDP limit when economic conditions are very bad.

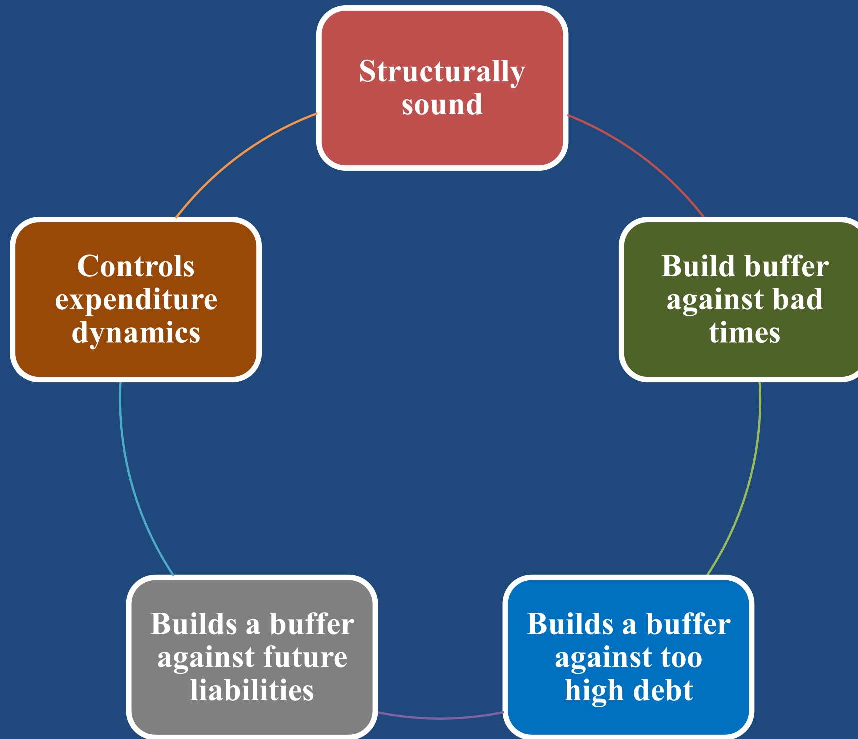
Diagram A: Cyclical conditions and the fiscal balance (% of GDP)



Source: COM

Thus, the MFAC considers that maintaining a fiscal surplus, is not only desirable, but warranted, given the current macroeconomic conditions. Such buffers are necessary to counteract against possible bad times in successive periods and future fiscal liabilities (see Diagram B). Prudent fiscal policy requires that during benign economic times the fiscal strategy should ideally be geared to build buffers.

Diagram B: Elements of a prudent fiscal policy



Source: COM

The **debt rule** requires that a country's debt-to-GDP ratio is below 60% or else approaching that ceiling at a satisfactory pace. In 2016, Malta's debt ratio amounted to 57.6%. According to the MFIN, the anticipated debt dynamics over 2017 and 2018 are such that the debt ratio is expected to fall further, to 54.9% in 2017 and 50.8% in 2018, thus continuing to satisfy fully the 60.0% debt-to-GDP ceiling (see Chart 7).[6] Malta is among the Members States expected to register the lowest debt ratios across the euro area in 2017, based on the information presented in the various countries' DBPs (see Chart 8). This also reflects the fact that, in Malta, the Government did not need to intervene to save failing banks due to the global financial crisis, something which inflated significantly some other countries' debt levels.[7] Malta's planned decline in the debt ratio in 2018, is also in line with similar anticipated developments across most euro area countries.

[6] The COM's forecasts indicate a similar trajectory for the debt-to-GDP ratio, 54.9% in 2017 and 51.6% in 2018.

[7] The European countries which experienced the largest change in government debt over the period 2008 to 2014, due to the support to the financial sector were respectively Ireland, Greece, Spain and Portugal. For further details refer to "The fiscal impact of financial sector support crisis" available on https://www.ecb.europa.eu/pub/pdf/other/eb201506_article02.en.pdf?fadae43a45a35a30cd17d3213277042d.