

### Box A: Inflation Developments in 2022 and Short-Term Outlook

In 2022, the inflation rate determined by the HICP for Malta recorded an increase of 6.1% over the previous year. Prices of 'food and non-alcoholic beverages' had the highest increase out of all the composite items of HICP, increasing by an annual rate of 10.8%. Food inflation intensified significantly from 2021 to 2022, rising by 9.0 pp to 11.6%, and non-alcoholic beverages increased by 5.2 pp to 5.0%. The food items with the highest increases in inflation rates were oil and fats (16.4%), dairy goods (12.3%), bread and cereals (12.2%).<sup>25</sup> Another component that experienced rapid price increases is 'housing, water, electricity, gas and other fuels' with a growth of 8.5%, mostly emanating from increasing prices in maintenance and repair of dwellings and actual rentals for housing, followed by 'recreation and culture' which increased by 6.6%. The EU-27 registered an annual rate of change in the HICP inflation rate of 9.2%, which is 3.1 pp higher than the HICP inflation rate registered for Malta. The 'housing, water, electricity, gas and other fuels' division had the highest rate of change in the EU-27 inflation rate with 18.0%, followed by 'transport' (12.1%) and 'food and non-alcoholic beverages' (11.9%) (see Chart 3.7).

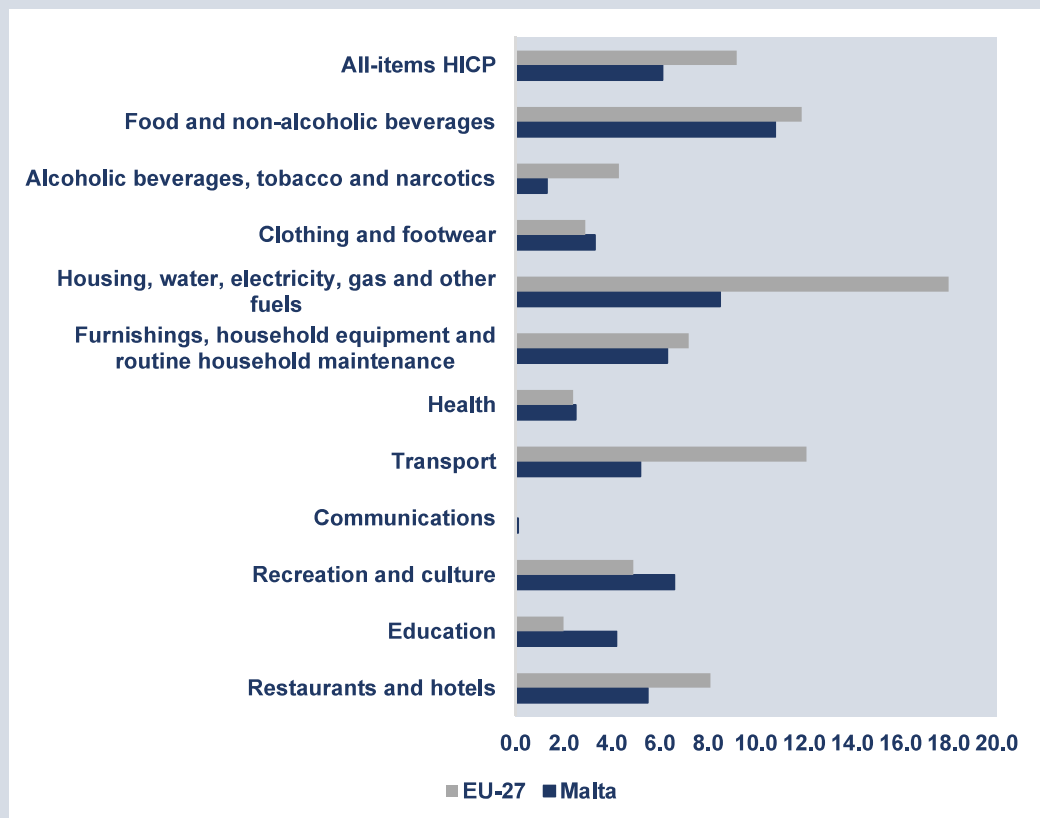
The Maltese Government is addressing the impact of rising energy costs by providing energy subsidies. This partly explains the 9.5 pp gap between Malta and the EU-27 in the inflation rate of 'housing, water, electricity, gas, and other fuels'. Indeed, Malta had the biggest net budgetary impact of energy measures out of any EU country in 2022, at 2.9% of GDP, compared to the EU's budgetary impact of 1.2%.<sup>26</sup> Food price increases in the EU-27 (11.9%) were slightly greater than those in Malta (10.8%). The Maltese government provided subsidies on certain food items to partly counteract the international price hikes. Nonetheless, the increase is still significant which may partly be due to the upward pressure from heightened import costs that Malta faces as an island due to its insularity.

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<sup>25</sup> These were all impacted by international price developments following Russia's invasion of Ukraine in February 2022.

<sup>26</sup> This information was presented to the MFAC by EUNIFI in a virtual meeting held on 17 March 2023 titled 'Fiscal Support measures in response to high energy prices'. It is noteworthy that some EU countries have curbed food inflation through VAT reductions. Such measures have not been adopted in Malta.

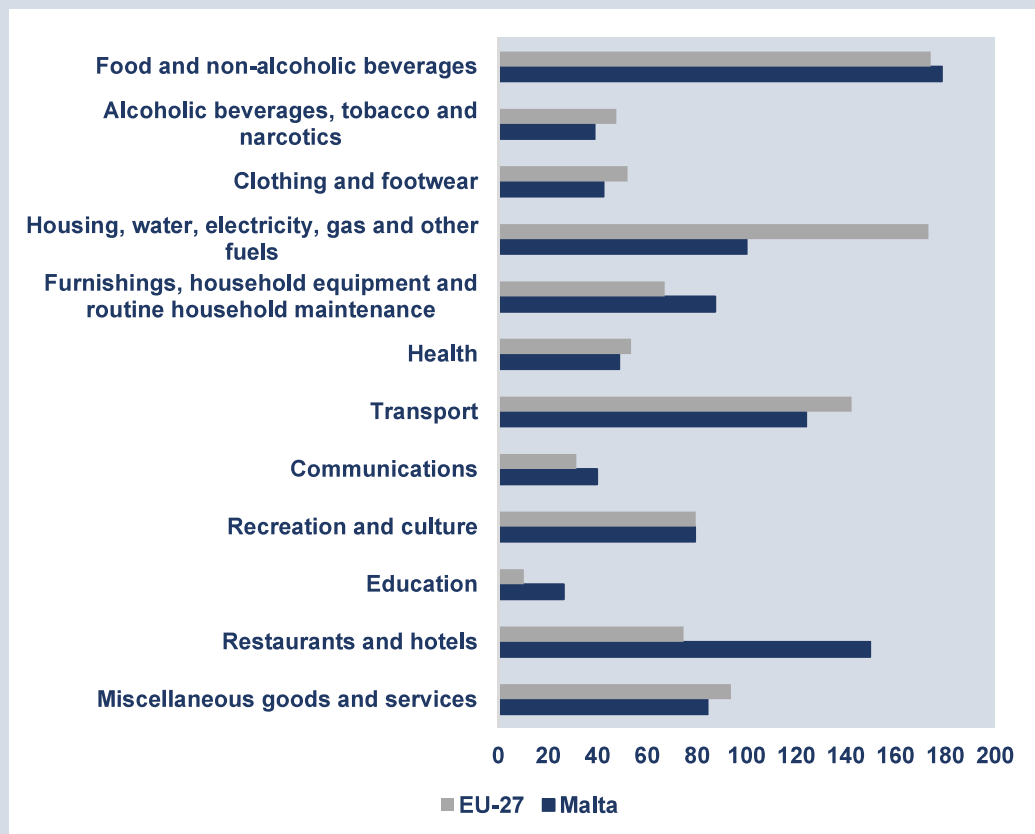
**Chart 3.7: Annual rates of 2022 at component level**



Source: Eurostat

In 2022, 'food and non-alcoholic beverages' (178.71), followed by 'restaurants and hotels' (149.75) and 'transport' (124.02) had the highest weights in the consumption basket of Malta. Similarly, 'food and non-alcoholic beverages' (174.21) and 'transport' (142.39) had amongst the highest weights in the EU-27 consumption basket, but the division of 'housing, water, electricity, gas and other fuels' had a much higher weight (173.24). 'Education' had the lowest weight in both Malta and the EU-27 (see Chart 3.8).

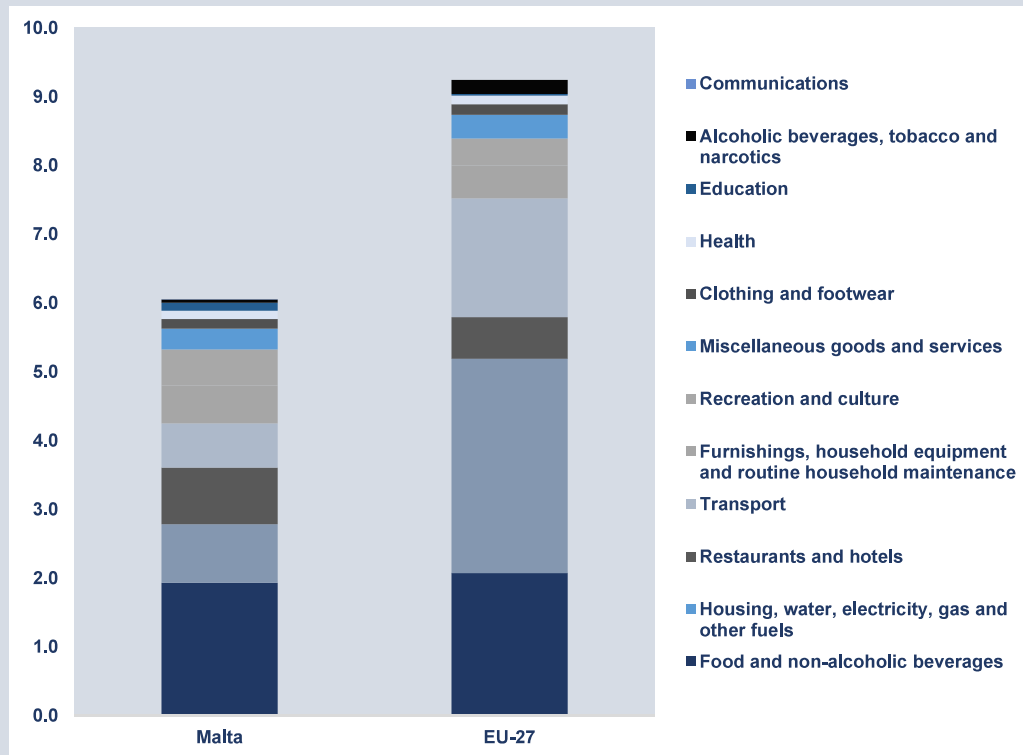
**Chart 3.8: Weights assigned by Malta and EU-27 to COICOP items**



Source: Eurostat

The assigned weights determine how much each item contributes to the overall HICP inflation rate. ‘Food and non-alcoholic beverages’ had the largest contribution of 1.9 pp to Malta’s HICP inflation rate in 2022, followed by ‘housing, water, electricity, gas and other fuels’ (0.9 pp) and ‘restaurants and hotels’ (0.8 pp). In 2022, the considerable rise in this contribution is primarily due to the significant price increases in food, primarily in bread and cereal, meat, and dairy items. Other food items like vegetables and fruits have contributed to the increase in the food inflation rate but to a lesser extent. On the other hand, the ‘housing, water, electricity, gas and other fuels’ division contributed the most to the EU-27 annual rate of change of inflation with 3.1 pp. The ‘food and non-alcoholic beverages’ division is another significant contributor to the EU-27 contributing 2.1 pp, followed by transport which contributed 1.7 pp (see Chart 3.9).

**Chart 3.9: Contribution of COICOP items to HICP inflation rate of Malta and EU-27**

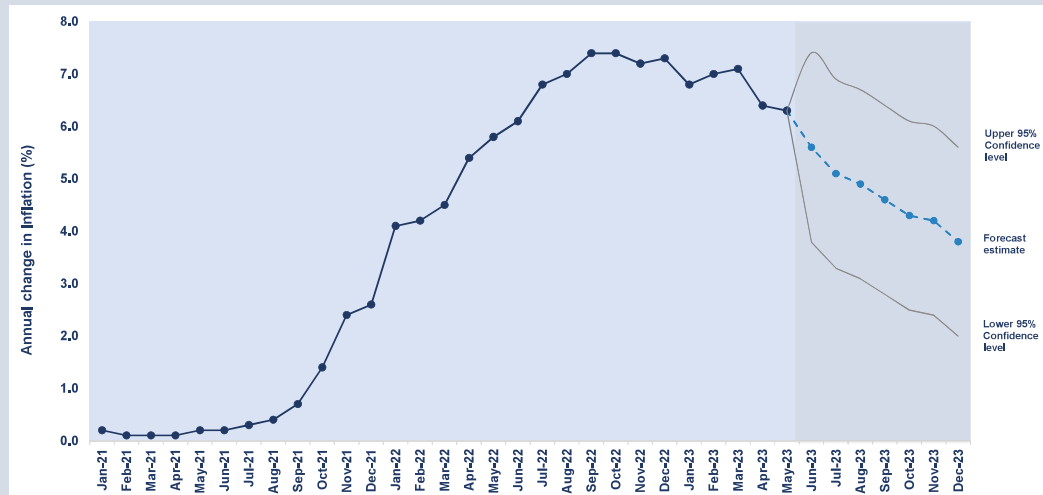


Source: Eurostat

The difference in inflation rates between Malta and the EU-27 is mainly caused by the fact that certain subcomponents of Malta's HICP inflation are determined or partially determined by the government. The variation mainly emanates from the contribution of 'housing, water, electricity, gas, and other fuels'. Government subsidies kept the cost of electricity, gas, and transportation fuels at the same level as the previous year in 2022, thereby avoiding the inflationary impact of energy on this component. Apart from energy, the government subsidizes the price of post-secondary and tertiary education, as well as public transport which thereby lowers the contribution of this division to Malta's HICP inflation rate.

According to the USP, the MFE is projecting the inflation rate for 2023 at 5.7%. Using a simple ARIMA model specification, the MFAC is forecasting a slightly lower inflation rate for 2023 than that forecasted by the MFE, at 5.5% (see Chart 3.10).

**Chart 3.10: MFAC’s Projection for HICP overall annual inflation in 2023 using a simple ARIMA model specification**



Source: Eurostat; MFAC’s Calculations

### 3.8 Labour market

In 2022, employment grew strongly by 6.0% (see Chart 3.11) and expected to continue to growth further stemming from the fact that Malta has a tight labour market, highly characterised by labour shortages and skills gaps.<sup>27</sup> In 2023, employment growth is projected to grow by 3.5% before reaching an average of 3.7% over the forecast horizon.

Tight labour market conditions and rising prices are expected to support an increase in compensation of employees, anticipated to grow by 9.0% in 2023. Thereafter, the compensation of employees is expected to fall slightly in 2024 to 7.8% and average 6.6% in the outer forecast years. This trajectory translates into a compensation per employee growth of 5.3% in 2023, slowing down to 3.9% in 2024 and average 2.8% in 2025 and 2026.

<sup>27</sup> In a [policy note](#) published by the Central Bank of Malta (CBM) on March 2023 find that “Scenarios published in the National Employment Policy 2021-2030 suggest that skills gaps are expected to persist well into the future. These scenarios point to the possibility of growing gaps in almost all occupations. These could be exacerbated if traditional sectors that are more labour intensive continue to grow”.