

REACTIONS TO THE
2019 BUDGET SPEECH
AND SUPPLEMENTARY DOCUMENTS

6TH NOVEMBER 2018

Preamble

Further to its preliminary public reactions issued on the 22nd of October 2018, the Malta Chamber of Commerce, Enterprise and Industry has undertaken an in-depth and fully comprehensive analysis of the 2019 Budget Speech within the broader parameters outlined in the Economic Survey and the financial estimates presented with the budget. The reactions presented in this document are the result of an internal consultation process collecting feedback from committees and individual members. Hereunder are the Malta Chamber's detailed reactions.

1. Introduction

There is no doubt that the focus of the 2019 Budget Speech to a large extent concentrated on further supporting low-income earners and pensioners through the redistributive role of government, which follows up on the budget speech presented last year. The Chamber already commented that this redistributive exercise must be made in full recognition of the private sector and its wealth generation role in the economy. In this context, it is also important to note that, as had been done with the 2018 Budget, the 2019 Budget focused more on a string of small measures which in their totality can lead to further positive social and economic development in the country.

In this year's budget the Chamber noted measures aimed at rectifying some of the structural issues that significantly impact the state of public finances through continued fiscal consolidation and elimination of abuse, leakages, the myriad of undeclared economic activity and abuse in free movement of goods amongst others. The Chamber must also note from the onset **that its calls for government not to introduce any surprise measures and new taxes were once again heeded**. This is to the advantage of business momentum.

The Chamber is also cognisant of the fact that this was the third budget in a row to be drafted in a situation where public finances are showing a surplus. This indeed bodes well for the future, and when one analyses the finer details of the fiscal situation, the Chamber immediately notices that the revenue dependency from the Individual Investor Programme (IIP) is also steadily decreasing with a projected surplus of 0.5% of GDP when excluding IIP revenue for next year.

Indeed, the overall position of the consolidated fund will remain positive in 2018 and 2019 with major gains in 2020 and 2021.

Nevertheless, the Chamber is concerned that there seems to be no defined intention to channel part of the earnings made during today's success to counter any potential slowdowns or challenges in the near future. In spite its numerous announcements that it is following a pre-defined plan, the Chamber feels that Government is still lacking an overall holistic economic strategy for the country. The Ministry of Finance's reports that Medium Term Objectives (MTOs) exist and long-term plans in accordance to EU requirements exist are objectively positive. Nevertheless, these are purely fiscal in nature and do not look at the full spectrum of how resources available or potentially available to the economy should be managed and led forward.

The Malta Chamber of Commerce, Enterprise and Industry in its pre-budget suggestions proposed that the authorities address the Budget from a multi-annual perspective. This would be closer to what happens at a European Union level where a seven-year multi annual financial framework is drawn. This would entail planning well ahead on what is required in the medium to long term rather than looking at the budget as purely an annual fiscal exercise. This would go beyond what the MTO requirements currently establish.

The Chamber is of the belief that policy makers at a national level must be made aware that, in spite the positive economic results achieved in the last years, there are areas that continue to impede further enhancement in competitiveness which need to be addressed. There exist a number of long-term threats that must be properly addressed through effective action plans. At the same time, Malta remains very strong in a number of areas while notable opportunities exist for the country's taking, in order to maintain this positive momentum in the longer term.

The Chamber also suggested that in this budget the Government initiates a thorough impact assessment of the country's ongoing growth with a view to set sustainable targets for maximum carrying capacities (output levels) in the country's economic segments. The study would have further recommended a way forward towards reaching the set output levels and maximising returns with the highest efficiency of resources. Once this analysis was concluded, the Chamber further proposed that Government initiates a national debate on a new long- term economic, societal and environmental master plan for the country post 2020.

A long-term plan will have to depart from the envisaged evolution of both the European Union and the eurozone. Malta will have to decide on its vision for both. In the end one has to seek out the sustainability of the euro as the single currency for a group of countries/area. Come next March there

will be UK's exit from the Union if an agreement is found. The Union will have to see how this will be implemented and over what time frames. The current debate on the Italian budget and Poland's threats to exit the Union could further trigger the issue of the eurozone's and Union's evolution and sustainability. It is under such a scenario that the Migration issue can be meaningfully addressed. As the position stands at present, every EU state is assessing its own short-term needs and applying ad hoc labour market policy decisions. The 'target' is the particular state and not the EU/eurozone as a whole. Labour market policies have to do with competitiveness, exchange rate, monetary and fiscal policy. Instead, they are being discussed in isolation.

It is the Chamber's opinion that in the **current positive economic climate the Maltese government should do more to set aside the funds being made during these years of surplus especially in view of potential future slowdowns in the economy** and more so in view of Malta's transition country status in the upcoming EU multi-annual financial framework debate which could mean a huge loss in cohesion fund for the country.

2. Macro Economy and Public Finances

The data for the Maltese economy as presented in the Budget 2019 document is encouraging and in line with one of the Chamber's objectives for the Budget, namely continued convergence to the Stability and Growth Pact in terms of the reduction of general government debt and public finance consolidation which is also positively noted.

Meanwhile, for 2018, it is expected that the General Government Gross Debt ratio reaches 46.9 per cent of GDP and to decline further to 43.8 per cent of GDP in 2019.

The Chamber is encouraged by the rate of economic expansion over recent years and the manner in which government is seriously tackling consolidation of public finances. General government debt is expected decrease to 46.9% by the end of this year, with further reductions being noted for the next three years. It is positive to note, that extended government debt is expected to decrease not only as a percentage of GDP but also in absolute terms over the period 2018-2021. When compared with the average debt in the Euro area (86.3%) and the EU 28 (81%), one can immediately notice the positive results, the country is achieving in this indicator not least because of the economic growth being experienced in the last five years.

Malta's GDP growth remains one of the highest growing in the EU with growths in real terms of 5.6% in 2018 and 5.1% next year.

Such forecasts for 2018 and 2019 are based on assumptions that the labour market conditions and international economic and political context will remain favourable, resulting in a continued upward trend in private consumption and positive foreign direct investment. The potential output growth is projected to average 4% for the period 2018 to 2021 which is above the pre-2008 financial crisis average and well above the EU and Euro area average.

3. Reactions to most notable Budget Measures and effects on Competitiveness

Overall, the Chamber feels that it is a neutral to positive budget for businesses in the sense that no new taxes or fiscal measures were introduced. The Chamber had specifically asked that no surprises of any kind would be announced in the budget recommendations, a call which has been heeded. The Chamber further welcomed measures aimed at promoting fair enforcement, the promotion of new emerging segments in the economy such as the establishment of Tech.mt and the strong focus on pensions.

Nevertheless, this budget does not address the more adverse challenges we are facing as a country including the need to refocus our aims towards scaling up our companies in the value chain, the provision of adequate human resources needed for the traditional and emerging sectors to grow, the issue of increased traffic congestion. At the same time, the Chamber was also expecting the authorities to listen to the Chamber calls for a national debate on a long-term economic plan for the country which is direly needed in order to sustain the current growth levels in the future. Following careful analysis, the Malta Chamber lays out its reactions to the most notable competitiveness-related measures included and overlooked in Budget 2019.

3.1 Fiscal matters

The Chamber welcomes very positively the fact that government heeded the organisation's calls not to introduce any new fiscal measures. The Chamber further welcomes the investment being made on new equipment at Customs to curb abuse in free movement of goods. Indeed Government announced that it will be investing € 5million in equipment to scan merchandise coming through the grand harbour similar to scanning equipment at the Freeport.

Nevertheless, the Chamber remains disappointed that its calls to reverse the introduction of excise duties as a replacement to Eco-Contribution announced in the last successive Budgets went unnoticed.

The Chamber has gone on record in stating that this measure has exacerbated the un-level playing field situation that exists amongst reputable, tax-abiding companies and others that are not. Responsible operators that self-complied or subscribed to private waste management schemes in order to recover or recycle their waste were exempt from eco-contribution. Yet, with the introduction of excise duties in previous budgets, the same operators are still paying excise duties on top of the scheme fees, hence incurring additional tax burdens and administrative costs. This reality makes abuse of the system all the more attractive while bona fide operators will see market shares eroded in favour of non-compliant operators. The Chamber once again calls for the removal of those excise duties on products which fall within the scope of the soon to be established Beverage Container Deposit and Refund system (BCRS) in 2019.

In the interest of safeguarding a fair level playing field for all operators across all economic sector, the Chamber welcomes measures announced in the strengthening of national structures and administrative units responsible for border controls and market surveillance. The Chamber has been advocating such enhancements for several years. Equally important are all those measures which tend to strengthen the regulatory bodies including those whose task is to ensure fiscal responsibility.

3.2 Transport

The Chamber welcomes the continued drive to invest heavily in the country's ageing infrastructure. Besides human capital issues, possibly the other single largest issue straining businesses and society at present is the inefficiency of Malta's transportation infrastructure and the severe traffic congestion at virtually all hours of the day. This congestion is taking its toll on the cost-effectiveness of many businesses' operations that in some way involve transportation of goods, people or other resources.

With this issue featuring daily on the national media and coupled with the 2016 launch of the National Transport Strategy and Masterplan, the Malta Chamber expected the Budget to contain more measures that aim to alleviate traffic congestion and enhance the island's transport infrastructure. The Chamber is therefore compelled to express its disappointment and growing concerns on this issue. Despite government being armed with the necessary tools, studies and plans, the concerns of citizens and businesses have not been addressed.

The few transport related budget measures namely that of extending free public transport to 14 - and - 15-year olds and all full-time students aged 20 and over, continued investment of €100 million allocated for road infrastructure, and the extension of all vehicle related exemptions to electric vehicles, autogas conversions, scrappage scheme and motorbikes are positive but they remain deeply inadequate to solve this challenge. The Chamber, in its pre-budget recommendations made strong recommendations in this respect and its key suggestion was that the National Development and Social Fund established through the revenue from the Individual Investor Programme (IIP) would be put to the best possible use if it were to finance the holistic transport strategy to shift towards a sustainable and effective multimodal transportation system including analysing and studying the viability of a mass rapid transit system.

The Chamber looks forward to contributing its feedback and ideas on this matter.

3.3 Public Holidays falling on a weekend

The Malta Chamber noted the announcement and decision to add a further day of vacation leave in lieu of public holidays falling on a weekend. The Chamber reiterates its position that discussions with the Employer bodies remain ongoing with a view to ensure that the final effect of this measure is cost-neutral to employers. The Chamber now looks forward to a positive response to a document it submitted in conjunction with the other employer bodies outlining measures for government to compensate for the loss of productivity this measure will bring about.

3.4 Education and Labour Market

European Commission, Eurochambres and Malta Chamber internal surveys of Malta's business sector carried out over the last four years have shown that availability and recruitment of skilled human resources has steadily grown to become the largest hindrance to the continued growth of enterprises in all economic sectors.

Unfortunately, this budget fell short of addressing this important issue which the Chamber has been very vociferous in the past years about. In its pre-budget document which was presented to the Minister of Finance, the Malta Chamber made a number of practical recommendations to address this crucial issue, none of which were taken on board.

Amongst the Chamber's suggestions were strengthening Identity Malta with more resources to deal with increased volume of permits; organising a marketing campaign promoting living and employment in Malta targeted at selected EU markets which have a surplus of skilled workers; creating a public campaign highlighting the valuable contributions that older workers provide as mentors and role models to the many younger employees; and extending types of work-based learning across all the post-secondary and tertiary level educational institutes.

The Chamber has also suggested that the National Skills Council ought to be re-dimensioned to focus solely on skills forecasting needed by Industry in the years to come. The Chamber has on innumerable occasions suggested to re-establish the entity on a sector by sector-based agency which would include experts on the various economic sectors represented in the economy. These sector-based skills councils would be able to analyse their particular segments in order of demand and supply and forecast the skills required by the particular sector. The Chamber acknowledges steps taken in this area, which helped by for example postponing retirement thereby reducing demand for workers, measures to promote STEM among students, as well as measures to lower early school leaving.

3.5 Pensions

The Chamber noted the improved incentives linked to voluntary occupational pension schemes. This is in line with the Chamber's recommendations ahead of this and previous budgets as it increases the sustainability of pensions for the State and adequacy for the beneficiary. After discussions with experts in the field the Chamber feels that the incentives are adequate to start incentivising even more employees and employers to voluntarily join the system. Nevertheless, during discussions with the same experts the Chamber was informed that there are still some technical issues related to the rate at which beneficiaries will be taxed upon maturity. This requires immediate discussion to rectify the matter so as not to hamper take-up of such schemes unnecessarily.

3.6 Lack of Investment in Research, Development and Innovation (RD&I)

In line with its previously stated recommendations, the Chamber must once again show its disappointment that despite its numerous calls to re-invest part of today's financial gains in scaling up our private sector, especially our more traditional segments, these calls remained largely unheeded. It is clear, that a number of economic segments require additional financial and technical support in moving up the value chain, not least our manufacturing, construction, retail and importation and tourism segments. The Chamber is nevertheless satisfied to note that new segments of the economy are being attracted (this is further elaborated under section 4.3 – New Sectors) and the country is being innovative in attracting such emerging segments like Artificial Intelligence, Fintech and Blockchain by being a trailblazer in terms of providing the right regulatory frameworks for these sectors to thrive.

The Chamber reaffirms its belief that Research, Development and Innovation (RD&I) is one of the foremost pillars upon which the country's sustainable economic growth rests, as this can provide Malta with the much-needed competitive edge over competing neighbouring states. The availability of a proper and sustainable infrastructure in RD&I provides the Maltese industry with a better chance of building and retaining a more resilient and competitive position. Indeed, this is a pre-requisite for investment attractiveness in any industry or sector.

4. Sector Specific Measures

4.1 Manufacturing Industry

The Chamber feels that the Manufacturing industry deserved a stronger focus in this budget. Constant improvements in export competitiveness factors is of crucial importance to industry, for which the Chamber is constantly advocating with the relevant authorities. It is clear from the data published that industry requires more attention, especially within the context of its 2018 gross value added (GVA) which registered an overall significant decline compared to 2017. The Chamber is a strong believer in Manufacturing and believes that with further assistance to help increase value, and lower operating costs, the country can manage to scale up some of these companies in the value chain. A concerted effort by Government needs to be done in terms of reorienting industry towards research, development and innovation in order to make it more sustainable in the years to come.

4.2 Tourism

It seems that Tourism is being acknowledged as an important sector and this year's budget mentions a number of measures aimed at this particular segment. The Chamber welcomes the news that Air Malta has successfully registered positive results in performance and its growth prospects are encouraging. Specifically, the Chamber notes the vision being set for Air Malta as the Airline for the Mediterranean. An overall expansionary strategy that incorporates development of new routes and new airlines. These growth prospects are supported by the substantial increase in MTA's budget from €55 million to €72 million.

Furthermore, the Chamber is aware that segments of the sector were directly impacted by the new free school transport system introduced in September. Indeed, private unscheduled bus operators are now operating at full capacity during the academic year with little spare capacity for any other service especially during the morning and afternoon schedules. Destination Management Companies (DMCs) and travel agents amongst others have found themselves in difficulty to find a solution during the scholastic period October- June given that they cannot offer collective transport services to incoming travellers. The Chamber was expecting Government to be aware of this matter given that the Chamber's section, amongst others, had communicated with the MTA on the issue and was expecting the Budget speech to set aside resources to mitigate the impact of this measure on tourism.

The Malta Chamber welcomes the emphasis on an improvement of tourism zones and not just certain zones, with the focus on cleanliness, increased safety and security measures especially in the Paceville zone and general greening of the environment. The Chamber considers the above measures favourable. Nevertheless, the Chamber also reiterates that a longer-term vision for this sector is required in order to ascertain whether the country wishes to focus in attracting the quality tourist rather than numbers.

4.3 New Sectors

The Chamber welcomes the renewed focus on attracting new sectors to the economy. The drafting of a strategy on Artificial Intelligence is indeed a positive development following the enactment of the regulatory framework on Blockchain and Distributed Ledger Technology (DLT) this year. Further to this, the Chamber welcomes the renewed focus on the Fintech industry through the recent establishment of a Fintech accelerator within the Malta Stock Exchange.

At the same time, the Chamber is pleased to note the setting up of new entities that will serve to promote Malta's efforts in lucrative and innovative sectors such as fintech, blockchain, artificial intelligence and internet of things. To this end, the announcement regarding Tech MT, which is being established following a Chamber recommendation, is welcomed.

4.4 Incentives for small and micro Enterprises and Start-ups

The Chamber is disappointed that very few support measures aimed at small and micro enterprises and start-ups were included in this year's budget speech especially in terms of assisting the scaling up of companies originating in the more traditional segments of the economy. Nevertheless, new measures called for by the Chamber aimed at enhancing the national action plan for entrepreneurship are welcomed particularly those announced in the area of support for start-up such as the VISA start-up for budding third country entrepreneurs and establishment of a new co-working space. Similarly, it looks forward to the announced new schemes which will be launched under the Malta Development Bank including the new financial instrument for Family Businesses first introduced at the Malta Chamber in early October, as well as the extension of the concession, introduced in the 2018 Budget, to reduce the stamp duty from 5 to 1.5% in the case of family business transfers.

5. Conclusions

In the days since the Budget 2018 speech, the Chamber has endeavoured to perform an analysis of both the measures introduced by the Budget as well as those that may have been overlooked.

The need for planning long-term was the central tenet of the Chamber's pre-budget proposal document. In fact, the Chamber called on Government to capitalise on the present economic resilience to invest in the necessary infrastructure and safeguard future sustainability.

The Chamber called for further competitive enhancing measures with a view to protect the recent economic achievements and ensure further sustainable growth. Considering the dynamic business environment of the country, the Chamber warned that a series of internal and external challenges existed and needed to be addressed.

With this in mind, the Chamber, called on the authorities to design the Budget from a multi-annual perspective. This would entail planning well ahead on what is required in the medium to long term rather than looking at the budget as purely an annual fiscal exercise.

The Chamber reiterates that a thorough impact assessment of the country's ongoing growth should be initiated with a view to set sustainable targets for maximum carrying capacities and output levels, in the country's economic segments. This study would further recommend a way forward towards reaching the set output levels and maximising returns with the highest efficiency of resources. Once this analysis is concluded, a national debate on a new long-term economic, societal and environmental master plan for the country post 2020 would be in order.

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