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Recommendation for a

COUNCIL RECOMMENDATION

on the 2016 national reform programme of Malta

and delivering a Council opinion on the 2016 stability programme of Malta

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THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Articles 121(2) and 148(4) thereof,

Having regard to Council Regulation (EC) No 1466/97 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies[1], and in particular Article 5(2) thereof,

Having regard to the recommendation of the European Commission[2],

Having regard to the resolutions of the European Parliament[3],

Having regard to the conclusions of the European Council,

Having regard to the opinion of the Employment Committee,

Having regard to the opinion of the Economic and Financial Committee,

Having regard to the opinion of the Social Protection Committee,

Having regard to the opinion of the Economic Policy Committee,

Whereas:

(1) On 26 November 2015, the Commission adopted the Annual Growth Survey[4], marking the start of the 2016 European Semester of economic policy coordination. The priorities of the Annual Growth Survey were endorsed by the European Council on 17-18 March 2016. On 26 November 2015, on the basis of Regulation (EU) No 1176/2011, the Commission adopted the Alert Mechanism Report[5], in which it did not identify Malta as one of the Member States for which an in-depth review would be carried out. On the same day, the Commission also adopted a recommendation for a Council recommendation on the economic policy of the euro area[6]. This recommendation was endorsed by the European Council on 18-19 February 2016 and adopted by the Council on 8 March 2016. As a country whose

1 OJ L 209, 2.8.1997, p. 1.
2 COM(2016) 338 final.
3 P8_TA(2016)0058, P8_TA(2016)0059, and P8_TA(2016)0060.
4 COM(2015) 690 final.
5 COM(2015) 691 final.
6 COM(2015) 692 final.

currency is the euro and in view of the close interlinkages between the economies in the economic and monetary union, Malta should ensure the full and timely implementation of the recommendation.

(2) The 2016 country report for Malta was published on 26 February 2016[7]. It assessed Malta's progress in addressing the country-specific recommendations adopted by the Council on 14 July 2015 and Malta's progress towards its national Europe 2020 targets.

(3) On 15 April 2016, Malta submitted its 2016 national reform programme and its 2016 stability programme. To take account of their interlinkages, the two programmes have been assessed at the same time.

(4) Relevant country-specific recommendations have been addressed in the programming of the European Structural and Investment Funds for the 2014-2020 period. As foreseen in Article 23 of Regulation (EU) No 1303/2013, where it is necessary to support the implementation of relevant Council recommendations, the Commission may request a Member State to review and propose amendments to its Partnership Agreement and relevant programmes. The Commission has provided further details on how it would make use of this provision in guidelines on the application of the measures linking effectiveness of the European Structural and Investment Funds to sound economic governance.[8]

(5) Malta is currently in the preventive arm of the Stability and Growth Pact and subject to the debt rule. In its 2016 stability programme the government plans the headline balance to improve to a surplus of 0.1% of GDP by 2019. The structural balance will gradually improve so that Malta's medium-term budgetary objective - a balanced budgetary position in structural terms – is reached by 2019. According to the stability programme, the general government debt-to-GDP ratio is expected to fall to 62.6% in 2016 and decrease further to 55.5% in 2019. The macroeconomic scenario underpinning these budgetary projections is plausible for 2016 and cautious for 2017-19. However, the measures needed to support the planned deficit targets from 2017 onwards have not been sufficiently specified. Based on the Commission 2016 spring forecast, there is a high risk of a significant deviation from the recommended adjustment towards the medium-term objective in 2015 and 2016 taken together, essentially stemming from the slippage in 2015 which needs to be corrected for in 2016, and under unchanged policies in 2017. The slippage in 2015 is partly explained by the surge in investment largely due to the exceptionally high absorption of EU funds in the run up to the conclusion of the 2007-2013 programming period. In order to reduce the deviation over the two-years 2015-2016, the 2016 stability programme includes additional measures for 2016 that could not yet be included in the spring forecast. These measures are targeted at reducing primary expenditure (by 0.16% of GDP), especially in the areas of compensation of employees, intermediate consumption and capital transfers. In addition, the estimates of some of the revenue measures for 2016-2019 have been revised to reflect more up to date information, as well as the actual impact of the measures for 2015. Taken together, these measures have a net deficit-reducing impact of 0.2% of GDP. Compared to the Commission forecast, factoring in these measures would improve the structural effort, and the structural balance pillar would point to some deviation on average over the two years

7 SWD(2016) 86 final.
8 COM(2014) 494 final.

2015-2016, whereas a risk of a significant deviation would remain in 2017. Malta is forecast to comply with the debt reduction benchmark both in 2016 and 2017. Based on its assessment of the stability programme and taking into account the Commission 2016 spring forecast, the Council is of the opinion that there is a risk that Malta will not comply with the provisions of the Stability and Growth Pact. Therefore, further measures will be needed to ensure compliance in 2016 and 2017.

(6) The long-term sustainability of public finances in Malta remains a challenge. This is mainly due to the budgetary impact of ageing-related costs, such as healthcare and long-term care and pensions. The pension system faces the double challenge of achieving sustainability while ensuring adequate retirement incomes. Pension expenditure was lower than the EU average in 2013, at 9.6 % of GDP, but it is projected to increase to 12.8 % by 2060, one of the highest in the EU. In March 2016, the government adopted several measures to address the sustainability and the adequacy of the pensions system, but the budgetary impact has not yet been assessed. In order to improve the adequacy of the system, the contributory national minimum pension continues to evolve in 2016, with a view to reaching 60 % of median income by 2027, and to extend its coverage. Effectiveness of the reform will depend on safeguarding the employability of older cohorts. In addition to pensions, public expenditure on healthcare and long-term care is projected to increase faster than the EU average, at 2.1% and 1.2% of GDP. The authorities have adopted a national health systems strategy and are conducting a healthcare spending review with a view to improving the efficiency of expenditure. However, the savings from these efforts have yet to materialise. Sustainability in the long run would benefit from using potential savings to address the projected expenditure growth.

(7) Significant investments have been made, but education and training outcomes are still below target. This affects the quality of labour supply and the labour market participation rate. The educational attainment of Malta’s workforce is still among the lowest in the EU. Malta is implementing a comprehensive strategy for lifelong learning, but participation in lifelong learning programmes is still limited, particularly among those with low educational attainment. Challenges in this area include targeted outreach, improved access to training and partnerships between education and training institutions and employers. A legal notice establishing an institute for the continuous professional development of teachers (the Institute for Education) was approved in 2015. The Institute’s main objectives are to: (i) provide teachers with skills needed in their daily professional activities; (ii) act as a hub for educators to meet and share their experiences and (iii) promote educational leadership. The Institute is now becoming operational and is expected to become the main driver in addressing teachers’ professional development needs. Progress in this area will need to be monitored.

(8) Apart from one-off large-scale projects in 2014-2015, investment in Malta has been muted, reflecting structural changes in the economy and bottlenecks. This is mainly linked to the increasing importance of less capital-intensive service sectors, which lowers the economy’s future investment needs. Nevetherless, some challenges that affect investment activity in the country persist, such as the insufficient capacity to innovate, skills bottlenecks, inefficiencies in the public administration and the justice system, the regulatory burden and significant traffic congestion.

(9) The transport and logistical infrastructure is one of the major barriers to foreign investment. The external costs of transport borne by Malta’s economy are substantial. These stem mainly from an inefficient use of the country’s transport

network and the lack of real alternatives to using private passenger cars. In addition, the high number of private vehicles, pollution and traffic congestion pose challenges to the sustainability of the national transport sector. No comprehensive transport strategy has yet been implemented, despite the fact that the development of a national transport strategy and master plan is a pre-condition for accessing EU structural and investment funds (2014-2020), which will be used to co-fund transport investments.

(10) The government has taken several steps to improve access to finance for small and medium-sized enterprises (SMEs). These steps were geared to providing equity and venture capital, which had been identified as a bottleneck in recent years. In addition, future measures include setting up a central credit register and a development bank and the launch by the Malta Stock Exchange of a platform designed specifically to help SMEs raise funds through the capital market. Difficulties in the area of access to non-bank instruments remain, but SMEs in Malta benefit from a better financing environment than many of their EU peers.

(11) In the context of the European Semester, the Commission has carried out a comprehensive analysis of Malta's economic policy and published it in the 2016 country report. It has also assessed the stability programme and the national reform programme and the follow-up given to the recommendations addressed to Malta in previous years. It has taken into account not only their relevance for sustainable fiscal and socioeconomic policy in Malta but also their compliance with EU rules and guidance, given the need to strengthen the EU's overall economic governance by providing EU-level input into future national decisions. The recommendations under the European Semester are reflected in recommendations (1) and (2) below.

(12) In the light of this assessment, the Council has examined the stability programme and its opinion[9] is reflected in particular in recommendation 1 below.

HEREBY RECOMMENDS that Malta take action in 2016 and 2017 to:

1. In view of the high risk of a significant deviation, achieve an annual fiscal adjustment of 0.6 % of GDP towards the medium-term budgetary objective in 2016 and in 2017, by taking the necessary structural measures. Step up measures to ensure the long-term sustainability of public finances.

2. Take measures to strengthen labour supply, notably through increased participation of low-skilled persons in lifelong learning.

Done at Brussels,

For the Council
The President

[9] Under Article 5(2) of Council Regulation (EC) No 1466/97.