



## **MALTA EMPLOYERS' ASSOCIATION**

### **Proposals for National Budget 2012**

#### **Introduction**

During the past months, hopes of a recovery in the global economy have been dashed, as the green shoots which were anticipated to flourish into a global recovery have withered into yet another international recession. The growing uncertainty in the EU, in the Eurozone in particular, and major world economies who are also our major trading partners are witnessing a contraction of their economies, coupled with general unrest among the population, as witnessed in the recent protests around the financial district in New York.

The past year has also seen the uprisings in North Africa, and these have also affected our economy negatively, as many companies who had commercial links with Libya had to stall, or close, their operations.

An assessment of the state of the Maltese economy has to be placed within this context of a gloomy world situation, where economists are questioning and reviewing the traditional cyclical models on fluctuations in economic activity.

This year Malta is expecting a modest increase in real GDP of 2.8%, which is not spectacular in itself but rates among the highest in the eurozone. Unemployment has declined to 6,500, but it is doubtful whether this trend will persist as the impact of the recession in our trading partners starts to affect us. The current situation is one where many employers are experiencing a shortage of skilled labour in various sectors, and an increase in foreign workers in Malta.

Tourism figures have increased over 2010, as have the number of bed nights, but hoteliers point out that profitability has not picked up owing to lower room rates.

In spite of efforts towards fiscal consolidation, Malta has still experienced a downgrading by Moody's, which is reflection of both the uncertainties facing the EURO and reservations about government's ability to achieve its fiscal targets. It is evident that Malta has been spared from the effects of the financial recession, but has been vulnerable to the second round effects as the recession spilled over into the real economy. On the other hand, the deficit for 2011 is expected to fall below 3%, which may give government some room to manoeuvre for the coming budget.

The economy is experiencing uneven growth, as the growth in real GDP is concentrated in the services sector, while other areas lag behind. While this has a positive aspect in that there is a shift in activity towards higher value added sectors, the downside is a greater dependency on these sectors which may be more volatile than traditional sectors. This is also reflecting on people's income. While

the average increase in wages is 4%, there is a disparity between wage increases in various sectors, leading to widening income inequalities. Although it is evident that Malta is one of the most egalitarian economies around, employees in low value added sectors still feel the pinch of falling real incomes. This was the rationale behind MEA's proposal of topping up COLA with a welfare supplement for the last budget, as the expected (which proved to be actual during this year) rate of inflation had immediately eroded the COLA increase of €1.16, which was the increase in income for low skilled persons not covered by collective agreements and pensioners. There is a lack of consumer confidence which is also affecting business negatively, in spite of the respite provided by the welfare benefit issued in August.

Unions are being pressured to ask for high collective agreement increases to compensate for a fall in purchasing power, but many companies in the private sector - e.g. manufacturing and tourism- are not in a position to match union's expectations at a time when many companies are struggling to maintain a fragile competitive edge. There have been no major FDI projects announced this year, and SMART City progress has lagged behind expectations, again mainly due to the international environment.

Malta has had mixed, sometimes conflicting, reviews on aspects of its economy. It does not rate high on the competitiveness index, but has been ranked fourth in the reliability of its financial institutions. Our educational system is ranked ninth in the world, but Malta is also rated as having a high number of school leavers.

Based on this general assessment, MEA is forwarding the following recommendations for the national budget.

## **1. Revision of Income Tax Bands**

Government should conduct a tax elasticity exercise to determine the impact of a revision on income taxes to increase the disposable income of middle income earners. Pushing up the ceiling of the 35% band would increase aggregate demand. Even if it is argued that the multiplier effect resulting from increased consumer expenditure in Malta is low, the measure will also act as an incentive to increase the supply of labour, especially among young women, as the returns on labour will be higher and increase the opportunity cost of staying at home.

This should be given a higher priority than allocating funds for the public sector collective agreement, and in itself, should reduce the burden of such an expense as many grades in the public sector will also be benefitting from the tax deductions. In the public sector, it will also partially address the issue of narrow wage relativities (especially after tax) which act as a disincentive to many to perform.

## **2. Maternity Leave**

Government should consider paying part of the maternity leave to relieve employers of this cost. It is reminded that Malta is one of the few countries where maternity leave is paid at full pay by the employer. This will lower the cost of family friendly measures and also reduce the gap in the relative cost between employing males and female employees.

## **3. Enhance incentives for female participation**

MEA supports the view that an enhancement of family friendly measures is necessary to induce a higher activity rate, in particular among the female segment of the labour supply. This is a

precondition to having a sustainable welfare system, provided that sufficient jobs are generated to cater for an increased labour supply.

It is important to distinguish between two main categories of family friendly measures – those that encourage people to stay away from the place of work (e.g. extended maternity and parental leave, career breaks) and others that incentivise stronger attendance (e.g. tax incentives, child care).

The latter have been proven to be more effective in retaining and attracting people in the labour market, since long breaks often discourage people from returning to the labour force. The distinction between these two types of family friendly measures is of strategic importance, since the design of such measures will have an impact on their effectiveness.

Although there needs to be a balance between the two (e.g. a minimum break for maternity leave is indispensable), MEA proposes that the main thrust of ffms should be in the direction of incentivising attendance, rather than absence.

On the basis of these arguments, MEA proposes that budget provisions should cater for:

- **Increased incentives for private sector investment in child care services and tax incentives/subsidies for affordable child care services at community level or at strategic locations**
- **Extending the school opening hours to provide the option – possibly at a charge – for parents to leave their children to be looked after at school. This can be achieved by offering extra payment to teaching and school administrative staff to man these hours.**

These measures, combined with others which employers may implement at the workplace (e.g. flexible hours, reduced hours, teleworking etc) will be more effective in incentivising stronger female participation than simply extending ffms applicable in the public sector (e.g. 5 year career breaks) to the private sector, which would be impractical and work against the employment of females.

#### **4. The Public sector collective agreement**

The public sector is still bloated and generally inefficient. Any increases in labour costs in the public sector should be aimed at increasing productivity and to be cost neutral through a decrease in the number of persons employed in this sector. The increased wage bill should be conditioned to proposal 1 above.

Government also has to tackle the issue of debts arising from public enterprises such as Enemalta. Part of the debt generated by these entities is owed to international sources and this increases our exposure. Moreover, the consumer is being made to pay for the inefficiencies of these organisations.

#### **5. Libya**

MEA has issued a document for a strategic approach to the situation in Libya which contains measures that can be given consideration in the budget. Amongst them is to invest in setting up a business driven embassy, and the setting up of an entrepreneurship fund to incentivise business in Libya.

Government should also consider temporarily re-introducing the income tax incentives which were available to Maltese working in Libya.

## **6. Green incentives**

There is a need to intensify the diffusion of infrastructure to accommodate the diffusion of electric cars in Malta. This is important if Malta is to reach the EU 2020 green criteria and to reduce dependency on fossil fuels. Gozo would be an ideal test market for the installation of charging units.

Incentives to households and firms to invest in energy saving technology should be extended. The take up during the past two years has been encouraging and the incentives offered have been successful.

## **7. Education expenditure**

MEA reiterates its position that education expenditure should be subject to an audit to measure the effectiveness of the investment, and to ensure that funds are being used efficiently and directed to areas where they are most effective in building careers. The idea of grading courses according to their employment potential should be considered.

The wisdom of opening the B.Ed courses to all applicants is questionable, and acceptable only if it is made clear to applicants that there is no guaranteed job if they follow that course. Government cannot afford to become an employer of last resort.

Emphasis should be given to reduce the number of early school leavers and to direct students – from an early stage - towards disciplines which match the requirements of industry. For example, the figures at University reveal that only 4% out of the total student university population are taking engineering and another 4% are taking ICT.

Government should consider reviewing the stipend scheme to ensure its sustainability and find ways to increase the incentives to students to follow courses that are more aligned with the future needs of the economy. Additionally more needs to be done to increase the number of students in higher education and to improve the overall qualifications of both students finishing their education and of those already engaged in the workforce.

## **8. Protecting legitimate businesses**

MEA calls on government to protect the interests of legitimate businesses from those who profit by benefitting from legal loopholes or breaking the laws. The vast majority of companies in Malta are law abiding and are the source of decent employment.

- There needs to be equal treatment of cargo being handled by the catamaran and other means of entry into Malta. Parallel traders are still bringing in regular stocks of goods and bypassing customs. This is having a negative impact on many importers.
- In spite of restrictions on tenders, many companies still complain of unfair competition in the awarding of tenders to others who are offering substandard conditions of employment – even in the public sector. It is in the interest of both companies and employees that there should be a level playing field among potential applicants for tenders.

The concept of a level playing field should be a guiding principle for Government and should do anything in its power to create and protect it. Most legitimate businesses are not afraid of competition as they are given reassurances that those with whom they are competing are not being given an unfair advantage.

## **9. Air Malta**

The situation at Air Malta needs to be resolved in the shortest time possible in order to bring it back to profitability as fast as possible. The airline is a key strategic asset to the Country and needs to become viable as soon as possible.

## **10. SME's**

In spite of schemes to provide access to funding to SMEs – (Microcredit, Jeremy, SME development grants and Gateway to Export) there is a need for a strong communication effort to make SMEs and micro enterprises in particular more aware of what these schemes offer.

There should also be a stronger effort to internationalise SMEs, and to provide specific training and support for them to break into international markets.

Access and availability of funding is still an issue in Malta and the right environment should be set up for the creation of venture capital funds and other instruments of funding not just by Government but also by the private sector. The MEA encourages Government to look at foreign institutions and to attract such companies to Malta. This will help stimulate growth of entrepreneurship in Malta.

## **Conclusion**

The budget should send a clear message that, although the economy has shown resilience in view of a hostile and volatile international situation, people should not raise expectations unrealistically. In spite of relatively low unemployment, increase in real GDP growth plus an increase in exports and tourism, the situation remains precarious and will remain so in the foreseeable future. Many companies who are stretching their resources to afford the COLA, among other cost increases cannot possibly face further cost pressures through collective agreements. All the social partners have to act responsibly in such circumstances. The key to our survival remains our flexibility as a small economy and competitiveness.