MALTA EMPLOYERS' ASSOCIATION

Report on Survey

Impact of COLA on Employers in Times of Recession

SEPTEMBER 2009

1. Objectives

The objective of this questionnaire is to look into:

- how companies are affected by the recession,
- whether they envisage that their business will recover in the short/medium term
- how the recession has affected their employment
- the extent to which the COLA increase will affect their business

2. Demographics (Q2):

We received a total of 90 replies to the questionnaire. These came from the following sectors:

Manufacturing – Pharmaceuticals and electronics	7
Manufacturing – others	20
Hotels/restaurants	5
Financial services	4
Wholesale/retail	18
Construction	2
Other services	34

The survey has also been distributed by the MHRA to a number of hotel and catering establishments. The results for this sector will be issued in a separate report.

Some of the respondents replied on behalf of groups of companies. The actual number of companies represented by the sample is 120.

2.1 Size of Company (Q3)

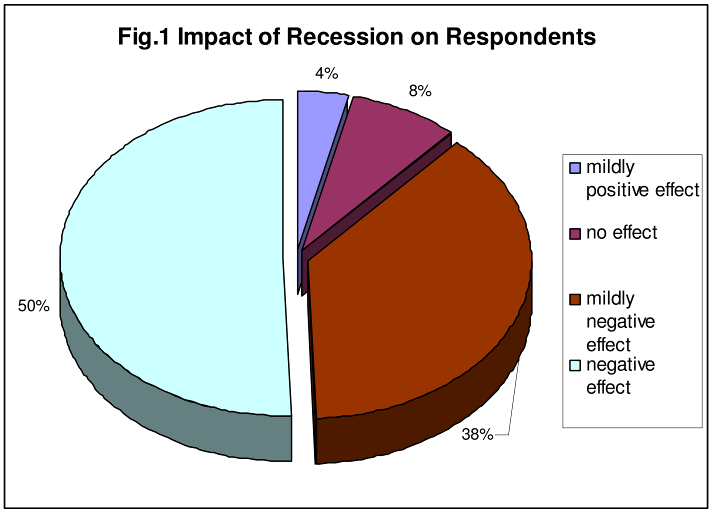
The sample includes companies that range from small to relatively large companies, and is therefore quite representative of the full spectrum of employers in Malta.

27 companies employ less than 30 employees
9 companies employ between 31 and 50 employees
20 companies employ between 51 and 100 employees
15employ between 101 and 150 employees
7 employ between 151 and 300 employees
12 employ more than 300 employees

3. Impact of recession on company (Q4)

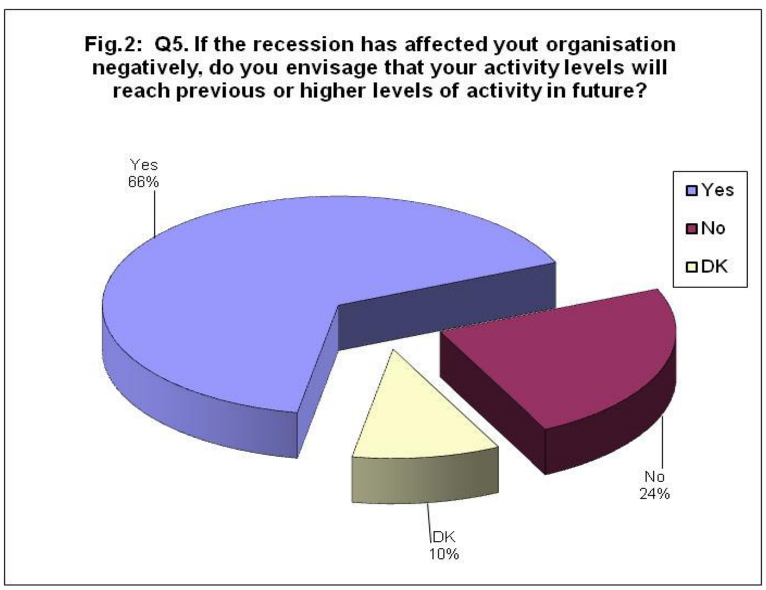
Figure 1 provides the replies to question 4 of the survey: How has the international recession affected your organization?

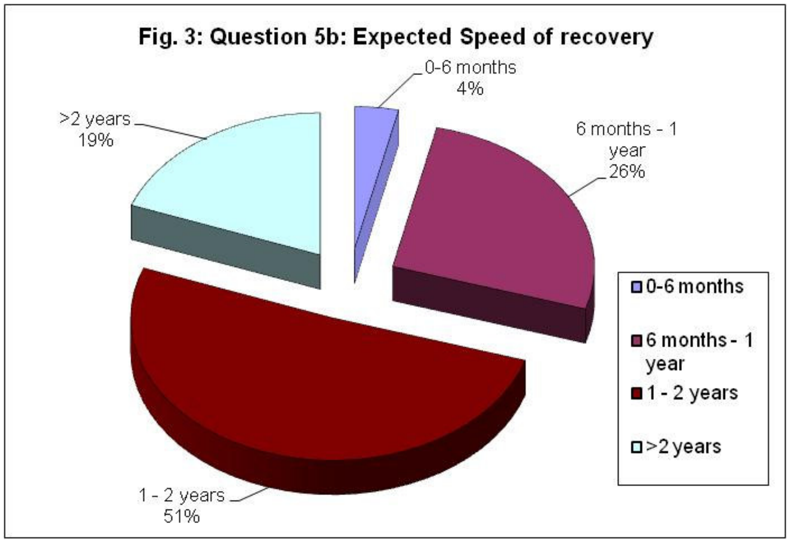
As expected, 88% of respondents replied that they have either been mildly or strongly affected by the recession.



4. Business Expectations

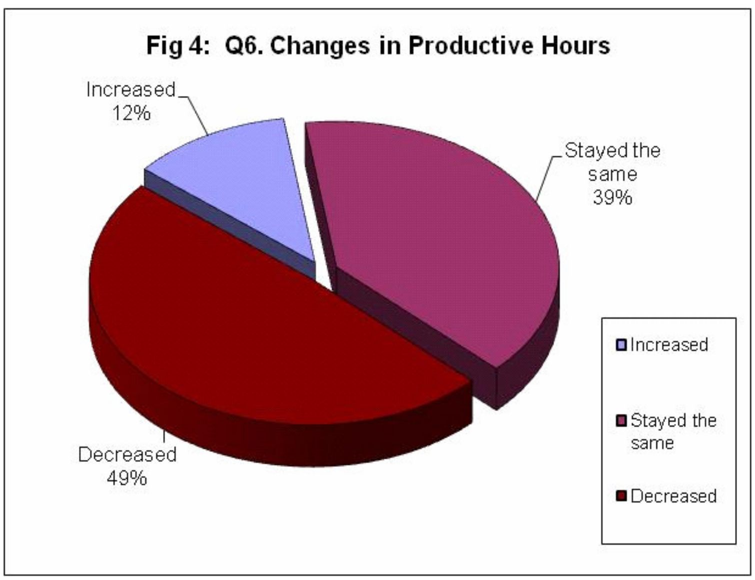
24% of respondents do not envisage that they will reach previous levels of activity in the future, whereas 66% anticipate a return to previous levels of activity. Half of respondents expect that the recovery will take between one and two years to materialize, and an additional 26% expect the recovery to take between 6 months to a year. Only 4% anticipate a recovery in the coming six months.





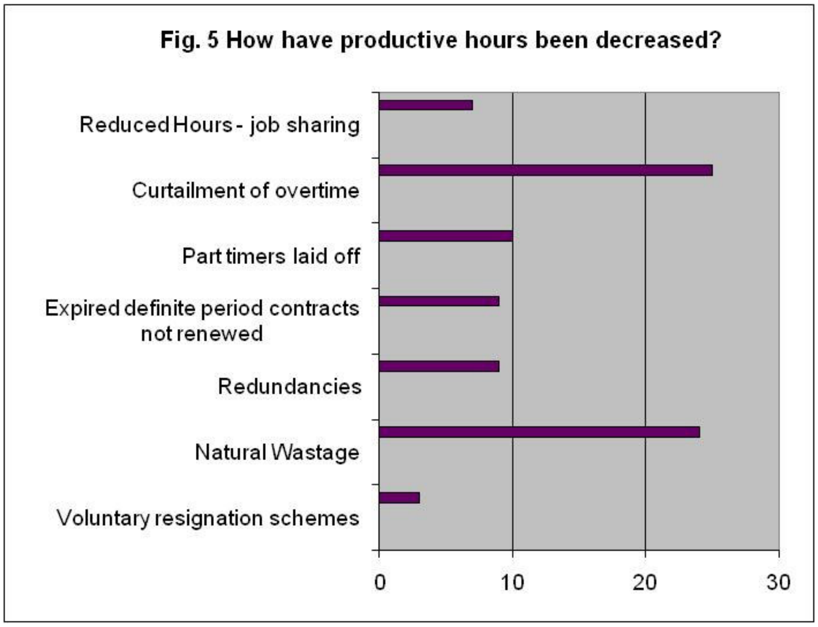
5. Changes in the number of Productive Hours

As seen in figure 4, almost half of the respondents have suffered a decrease in productive hours over the past twelve months. 39% replied that their productive hours have remained the same.



6. How productive hours were reduced (Question 7)

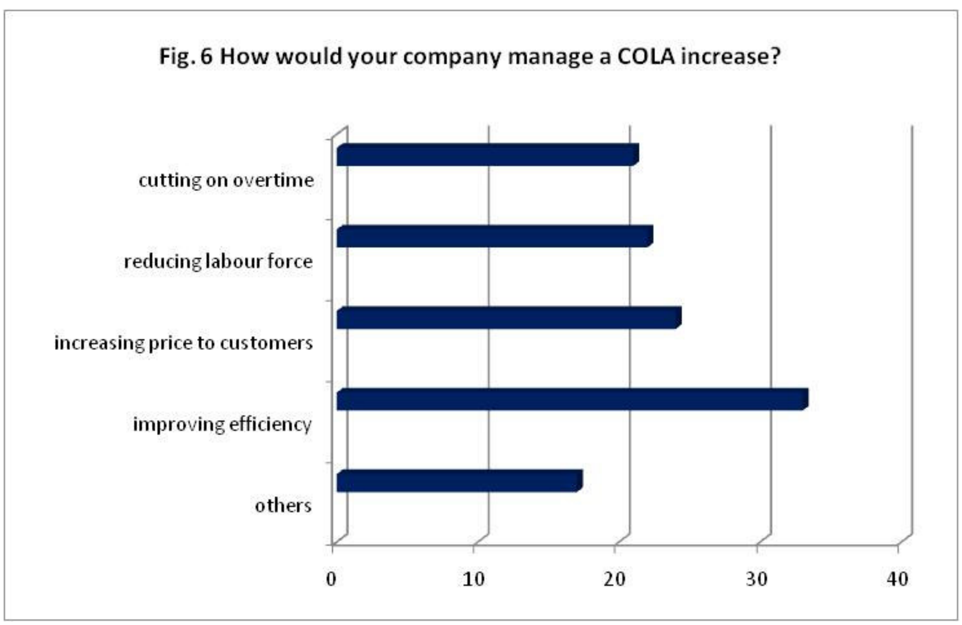
Figure 5 shows that many employers have resorted to natural wastage and curtailment of overtime to deal with a contraction of business. This is an indication that many have tried to hold on to their human resources in anticipation of a short term recovery, rather than making employees redundant. This may explain the fact that there has been no dramatic increase in unemployment in Malta over the past twelve months. However, it also highlights the fact that many companies cannot sustain the situation indefinitely and that the decision whether to declare redundancies depends strongly on the expectations and developments in the coming months.



7. Collective Agreements and COLA

36% of respondents replied that there is a collective agreement in force ion the company. Of these, 11 companies stated that the collective agreement increases are inclusive of COLA.

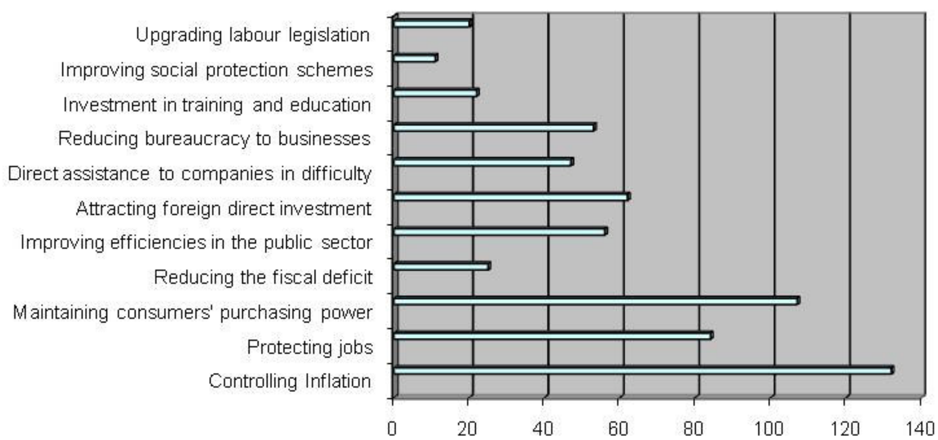
In response to Question 10, 74% of respondents replied that they are not in a position to absorb a COLA increase of between €5 and €7 for 2010.



8. Short term objectives

As seen in Fig.7, the three overriding short term objectives recommended by respondents are the control of inflation, followed by maintaining consumers' purchasing power and protecting jobs. Employers are concerned about the impact of inflation on their organizations, since this is hitting them through the COLA and also through other cost items like the utility charges.

Fig. 7 Proposed priorities to Government to combat recession



9. Question 12 Proposed budgetary Measures

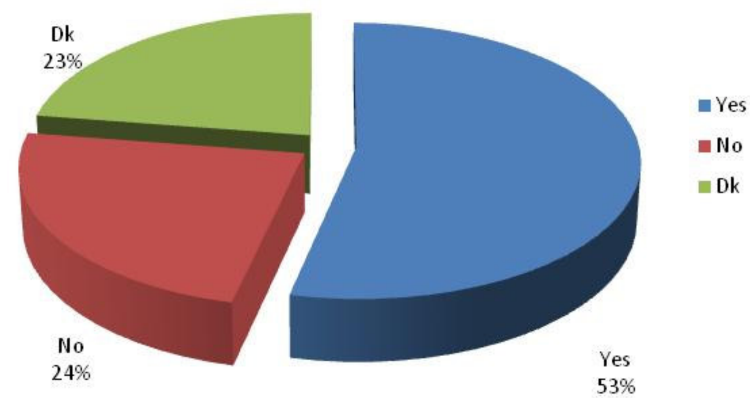
Various suggestions were made by the respondents for budget measures. The ones which were most repeated were:

1. Freeze/Lower water and electricity tariffs: 22 respondents
2. Revision of tax bands/reduce income tax: 21 respondents
3. COLA freeze/remove COLA/COLA to minimum wage earners only: 19 respondents
4. Reduce VAT: 16 respondents
5. Reduce bureaucratic hurdles and costs to businesses: 8 respondents
6. Cut Corporate taxes: 4 respondents
7. Invest in improving the tourism product: 4 respondents
8. Control tax evasion: 4 respondents
9. Embark on a wide ranging capital expenditure programme: 4 respondents

10 Do you envisage that your company will expand its business activities in the coming three years?

The replies to this question are fairly optimistic. 53% envisage an expansion in their business activity in the coming three years, whereas 24% replied in the negative. The indications are that many businesses expect their markets to pick up and that will surpass current levels of activity as the recession subsides.

Fig. 8: Q14. Do you envisage that your company will expand its business activities in the coming three years?



Conclusions and recommendations.

The main conclusions that are evident from the survey results are that employers are feeling the brunt of the international recession. However, many companies have not resorted to declare redundancies in the expectation that things will improve within the short to medium term. The results reveal that most companies have preferred to reduce the productive hours through natural wastage and curtailment of overtime than redundancies. This can explain why, in spite of a downturn in exports and tourism arrivals, unemployment has not increased dramatically and, thus far, the economy has continued to generate productive jobs in the private sector.

This result has undoubtedly been helped by the strategy for a targeted intervention at enterprise level for companies in difficulty which has yielded positive results.

Another salient result of the survey is that numerous companies will find it difficult to absorb a COLA increase of €5.8 for 2010, and that many jobs may be in peril if they are constrained to do so. At all cost, the COLA mechanism cannot be allowed to undo the results that the social partners have achieved in the struggle to protect productive jobs.

Therefore it is imperative that a corrective measure is introduced that will maintain aggregate demand - which in itself generates employment - whilst simultaneously safeguarding competitiveness, particularly in export orientated enterprises. It must be acknowledged that the prevailing conditions are abnormal and therefore may require extraordinary actions to counter their negative effects.

For these reasons, the Malta Employers' Association is calling upon Government to intervene by issuing part of the COLA as a bonus that will be paid by the Government. Therefore, for 2010, assuming a COLA of €5.8, €3.5 will be paid for by the employer, and the rest – i.e. €2.3 will be paid by Government.

This arrangement will be limited for 2010, and the €2.3 will be added to the COLA for 2011 provided that economy turns to positive GDP growth during the second and third quarter of 2010.

- The advantages are many. Firstly, it will offer a slight breather to companies in difficulties during 2010. The first half of 2010 is expected to be a critical period as many analysts are expecting economic recovery to gain momentum after that time. Therefore this measure will incentivise many companies to hold on to their human resources until that time, thus curtailing job losses.

- It satisfies the major criteria for short term fiscal interventions. It is a **temporary** action, since there will be no carry over expenses for Government in 2011. It is certainly **timely** as it will be introduced at a critical stage - as explained above – and will also dampen the damaging effects of COLA which many businesses have stated that they cannot afford. The measure is also **targeted**, since the companies that will benefit the most are the ones most likely to declare redundancies and which operate in low value added manufacturing, tourism and services. Since the public sector collective agreement already includes COLA, it will not affect these employees, whose jobs are recession proof. The net effect on government expenditure will also be reduced as a result.

- The reduced COLA will also be a partial compensation to employers to the fact that the inflationary pressure on COLA was partially triggered through the increase in utility tariffs which has bounced back on employers.

- The inclusion of the 'bonus' in the 2011 COLA increase will not be as damaging to employers as the predictions for 2010 point towards a lower level of inflation.

- The bonus can be timed to coincide with a period of heightened seasonal demand – i.e. Christmas or June

- The 'tampering' with the COLA adjustment is not without precedent. Government awarded an additional LM1 in 2008 in anticipation of high inflation due to the introduction of the EURO. This intervention will balance out the expense to employers of that budgetary measure.

An alternative to this could be to give a tax relief instead of a bonus. However, the benefit of a tax relief would not reach the low income earners who are already exempt from tax. Government may still opt to exempt the bonus from taxation for it to have a more potent effect on demand.

This move will also give sufficient time for the social partners, through MCESD, to proceed with their discussions on whether and how to reform the COLA mechanism to ensure that it works to complement economic objectives.

The proposal that emerges from this report is only intended to tackle the destabilizing effect of the COLA mechanism in times of recession, and is by no means intended to offer a complete solution to the challenges facing our economy. The Association also reiterates its position that it does not agree with COLA in principle, and sticks to its position wage increases should be linked to productivity, not inflation.

The Association will be submitting a comprehensive set of proposals for the upcoming budget in the coming weeks.