



# Proposals for **NATIONAL BUDGET**

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## **June 2020**

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## 1. A Budget within a Context

The eruption of COVID -19 in the last quarter of 2019 sent a worldwide tsunami that dealt a heavy blow to the global economy. Malta has not been spared. The impact on public health has been addressed through well-managed interventions by the Public health Authorities, and, since March 2020, Government decisions have been constrained to thread a fine line between safeguarding public health priorities and keeping the economy from coming at a standstill.

Although jobs have been lost, unemployment has thus far not increased dramatically for a number of reasons:

- A resilient and diversified economy, whereby the relatively strong performance in some sectors has compensated for a slowdown or outright cessation of activity in others.
- Social dialogue has led to the design and implementation of numerous government schemes that have to some extent incentivised companies to retain their labour force. Research carried out in April by MEA revealed that just 9% of companies surveyed resorted to redundancies as a measure to counter the impact of the crisis, even though the reception to the schemes was not very positive.
- Many foreign employees, third country nationals in particular, did not have their contracts renewed, with thousands being repatriated and therefore not showing up on the unemployment register.
- As has occurred in past crisis, employers in Malta have shown that they are less likely to shed labour when things turn south. In many other countries, unemployment has increased at a much faster rate than Malta, in spite of government schemes and incentives that are similar to those that have been implemented locally.

The number of registered cases is on a steep decline, both in Malta and many European countries, but the economic side effects will be drawn out, even in the absence of a second wave. The negative impact has not been the same in all sectors, with travel

related companies being the worst affected. Expectations in those sectors are that recovery will be slow and may take between 2-3 years to reach pre-COVID levels of activity.

What many affected firms are deciding at this stage is whether to downsize, and the extent to which they can postpone downsizing if business does not pick up. This will depend on:

- The duration of the outbreak
- Domestic demand
- External demand
- The extension of government assistance

These factors could also serve as a basis for Government actions. The decision to have a budget at this stage is a commendable one. The current situation is a classic Keynesian scenario, with fiscal policy taking the fore to stimulate demand through government expenditure, thus kick starting the economy and steer it towards pre-COVID levels of activity. Under these circumstances, a budget deficit is not evil, it is necessary. The Maltese economy has the required fiscal manoeuvrability that allows government to engage in focused short to medium term spending to shore up business activity and generate aggregate demand. At EU level, the Commission has endorsed a handsome financial package to minimise unemployment, to provide guarantee funds for loans to companies, and supporting member states (through the European Stability Mechanism). Malta should benefit from these measures.

The challenges here are:

- Extending assistance schemes will stretch government resources
- One of the causes of a fall in domestic demand is fall in local population brought about by the drop in tourism and repatriation of TCNs. On average there are approximately 75k fewer persons/consumers living in Malta (including tourists and TCNs) than there were in June 2019. As trends over the past five years pointed towards an expansion in total population, businesses catering for the

domestic market – catering, retailing, rentals etc. - increased their capacity accordingly.

- Domestic demand has also decreased because many employees have suffered a drop in income -through loss of overtime, a reduced hour week etc. - even if they have been retained in employment.
- The openness of the economy implies that many businesses' performance is not dependent on domestic demand. (e.g. language schools).
- External demand is governed by variables over which government has little to no control.

One characteristic of the crisis is the extent that different economic sectors have been affected. At the extremes, the accommodation sector has contracted by 18% in the first quarter. Construction, on the other hand, has expanded by 14%, real estate by 9% and real estate by 5%. Such figures underscore the need for a targeted approach to assist businesses. It is also an indication of an economy that is relying more heavily on construction activity, which is a volatile sector itself and comes at a cost to Malta's natural resources which in themselves are a source of income to other sectors, tourism amongst them.

Although the budget is addressing what is essentially a force majeure situation, it should also act as a catalyst for discussion and planning to shape the economy to move towards higher value added activities which place quality over quantity. The crisis has also had some positive side effects, especially with respect to the environment. We should be proactive and start thinking now about how to address air and noise pollution, which have been reduced during the past three months, to improve people's quality of life. Other environmental matters, such as food security and the transition to green technology should also move up in the hierarchical ladder of national priorities. It would be a lost opportunity if these issues are not addressed.

The measures proposed in this document are based on the above considerations.

## 2. Proposed Measures

### 2.1 Sustaining employment

- The current COVID Wage Supplement Schemes should be extended until the end of September.
- Annex B of these schemes should be removed and leave only the benefits falling under Annex A to which any company affected by the COVID crisis will be eligible, in line with the actual loss in business. Although companies falling under more NACE codes will be eligible, the actual number of companies will decline as the economy picks up.
- Companies whose business will be zero will continue to receive the benefits falling under Annex A. for a period of six months. In such extreme cases, National Insurance contributions will be waived and the period will be accredited to the employees for pension eligibility. This will make the cost of employment neutral and employees will remain on the books and receive the wage supplement.
- Government should launch a scheme to subsidise commercial rents for a period of six months, particularly those managed by the Malta Industrial Parks.
- The Teleworking Scheme should be extended indefinitely to encourage a better take-up and implementation of remote working systems. Government should actually give grants to teleworkers, gaining the benefit in less traffic and commuting.
- Commercial Energy rates will be reduced.
- The conditions for returning to work are too confusing and are subject to mixed messages and interpretation, especially to employees. More concise, clear guidelines are expected.
- Child Care and Summer schools should be in a position to accommodate all students. Many parents are reluctant to return to work, saying that their

children will still be at home during the summer months. The situation will worsen if schools do not open normally in September. Some companies are experiencing disruption not because of the loss of work caused by the virus, but because the employees are not turning up for work.

- Government should introduce re-training schemes and employment support programmes for persons who lost their job.
- Identity Malta needs to expedite extension of work permits of TCNs who are still in employment when they expire. In spite of the crisis, there is still a demand for foreign labour in areas where no Maltese employees are available.
- Company tax rate will be reduced to 30% for a period of a year, based on 2019 profits.
- Incentivise businesses to re-launch economy by introducing a number of extraordinary tax incentives for those companies which make investment post Covid in the coming 12 months, with enhanced incentives channelled towards green economic activities, agriculture and innovation. This can be supported and sustained by EU funds.
- Government should incentivise the upgrade of the tourism product to attract higher quality tourism which can compensate for lower numbers in the coming years.
- Resources should be channelled in the public and private health sectors to make up for the backlog of patients whose healthcare has been put on hold.

## **2.2 Stimulating domestic demand**

- Although many of the restrictions have been relaxed, and many businesses are open, people may still be reluctant to visit outlets due to the fear factor. A re-assurance campaign, combined with strict enforcement of regulations, will help to change attitudes.

- Government should issue vouchers to be used exclusively in retail and catering outlets. Recipient owners will be able to cash vouchers. Under the circumstances, this will be better than a cash bonus as the funds will be pumped directly in the economy.
- VAT rates can be temporarily reduced to lower prices. Germany shall be reducing its VAT rates from 19 to 16%, and that on hospitality from 7% to 5%. It is proposed to reduce VAT to 15% and 5% for hospitality.
- A reduction in household utility bills will increase disposable income.
- Introduce a rental subsidy scheme to households suffering from unemployment or a loss in household income of more than 30% as a result of the Corona crisis.

### **2.3 Addressing External demand**

- The opening up of airport routes has to be accompanied with a reassurance campaign to promote Malta as a safe travel destination.
- There should be an intensive marketing campaign to promote Malta and redevelop routes. This can be done with Air Malta.
- Government could issue direct incentives to inbound tourists in the coming six months: i.e. one free night accommodation to visitors spending more than six nights in collective accommodation. Incoming flights could also be subsidised for a limited period.

### **2.4 Greening the Economy**

- Government should set up a special fund to address national food security and promote local agricultural products.
- A national noise reduction strategy is required: this can involve a revision of flight paths to minimise impact in heavily populated areas; strictly



enforcing the use noise reducing equipment and measures in industrial and entertainment areas; slapping fines on noisy vehicles.

- Stronger incentives to switch to electric vehicles.
- A specific fund should be set up to address climate change, increase innovation and incentivise digitisation.

## **2.5 Transparency of Incentives**

Ultimately, all incentives and measures introduced by Government will be carried by the taxpayers, current and future. Companies that make use of these incentives need to be held accountable for the incentives received and there needs to be a transparent procedure on the manner in which the incentives are granted. Transparency is also achieved through an objective compilation and analysis of where these funds have been spent which is communicated to the authorities.