Malta

In 2020, economic growth experienced a significant downturn in line with most other economies as a result of the impact of COVID-19. Thus, in contrast with the increase of 5.5% registered for 2019, in 2020 real GDP fell by 7.0% mostly as a result of lower net exports; whereas the Euro area registered a 6.6% decrease. As may be expected for a small island-state economy, the economic shocks from the pandemic mostly hit sectors comprising wholesale and retail trade, transportation, and accommodation and food service activities. Moreover, the sector was impacted strongly by travel disruptions during the year, the temporary shutdown of non-essential services and other resultant COVID-19 containment measures. Net exports of goods and services accordingly shed 5.9 percentage points from GDP growth, reflecting a stronger decline in exports than imports (in 2019 this item only shed 0.8 percentage points contribution to GDP).

The seasonally-adjusted unemployment rate published by Eurostat averaged 4.3% in 2020, higher than the average of 3.6% recorded in 2019 but lower than pre-2017 levels.

The large degree of underutilisation of the economy's productive capacity mainly reflects the impact of the COVID-19 pandemic and related restrictive measures on total factor productivity and the labour market. Thus, the contribution of total factor productivity turned negative during the year. Moreover, aggregate labour productivity in Malta declined by 8.2% over the level recorded in 2019 (0.2%).

Meanwhile, COVID-19 had a considerable (negative) impact on general government finances. In the first three quarters of 2020, the general government balance shifted to a deficit (€1.1 billion) when compared with a surplus in the same period a year earlier (€67.1 million). Meanwhile, general government debt as a share of GDP increased (over the 2019 position) by 10.7 percentage points to 52.6%.

Annual inflation based on the Harmonised Index of Consumer Prices (HICP) fell to 0.8% in 2020, from 1.5% in 2019. Notwithstanding this drop, HICP inflation in Malta was above that of 0.3% registered in the euro area, but still significantly below the ECB's inflation target. The Retail Price Index (RPI) shows too that inflation moderated over this period – falling to 0.6%, from 1.6%. The drop in inflation in 2020 extends the downward trend exhibited since mid-2019.

Over the past two decades, the banking sector in Malta has grown from four retail banks serving the local population to 24 (operative) licensed banks as at the end of 2020, only three of which are Maltese majority-owned. The ownership of the other banks originates from various EU and non-EU jurisdictions, including Austria, Australia, Belgium, Greece, Kuwait, Turkey and the United Kingdom. As such, around 62% of the banking sector's total assets of around €40.4 billion are foreign-owned.

The sector is very diverse in terms of inter-linkages with the domestic economy, and can be split into three groups, according to the extent of linkage with the Maltese economy: core domestic banks; non-core domestic banks and internationally-oriented banks.

There are six core domestic banks, whose assets (almost €26 billion) represented 200.6% of Malta's GDP. The core banks employ 83% of the sector's workforce numbering around 5,141 employees. Two of these banks are the local market leaders, holding around 76% of this cohort's assets, and in 2020 operated 66 of the 102 branches/offices of the core banks in the Maltese islands. The core banks exercise a conservative business model consisting mainly in the raising of deposits and the granting of loans mainly to Maltese residents. Thus, the core domestic banks rely predominantly on resident deposits for their funding and have a stable deposit base, thanks to the high propensity to save by Maltese households. In fact, customer deposits, of which resident deposits comprise the largest proportion, financed almost 83% of the core banks' balance sheets in 2019.

Their loan-to-deposit ratio stood at 58.4% in 2020 (1.1 percentage points lower than in 2019) and well below the euro area average of approximately 96%. On the asset side, exposures to the households' and individuals' sector continue to constitute the largest sector to which the core domestic banks are exposed to. In fact, almost 96% of all exposures by the aggregate banking sector to this economic sector were advanced by the core domestic banks. At the same time, the latter continued to apply prudent lending norms and loan-to-value ratios, as well as a cautious valuation of collateral. Additionally, their investment portfolios continued to be widely diversified in well-rated securities.

Overall, the core domestic banks are characterised by a sound capital base (Tier 1 capital adequacy to risk-weighted assets of 18.5%) and high liquidity. On the other hand, several factors - such as lower credit demand, and hence slower loan growth, caused by the pandemic leading to higher placements at a negative rate with the Central Bank; heightened economic uncertainties and market volatility - all contributed to a significant drop in the core domestic banks' profitability. These attributes were again acknowledged in the EU Commission's Country Report Malta 2020.

There are six "non-core domestic banks", whose assets of around €3.1 billion represented 23.8% of Malta's GDP. These banks undertake some business with Maltese residents, but not as their core activity. As such, while the linkages with the domestic economy remained limited, both resident assets and resident liabilities picked up momentum somewhat as these banks continued to penetrate the domestic market. With a Tier 1 capital adequacy ratio of 19.85%, well in excess of the requirement, these banks have a good shock-absorbing capacity to cover a potential deterioration in asset quality. Considering also their limited exposure to the domestic economy, these banks are not deemed to pose a threat to domestic financial stability.

Twelve internationally-oriented banks, which are mainly subsidiaries and branches of large international institutions, have almost no links to the domestic economy (only 6% of their assets are domestic). Their combined assets of around €11.6 billion represented 90.3% of Malta's GDP. These banks fund themselves mainly through the wholesale market or through their parent banks, and deal mainly with intra-group activities. Overall, this group is also very well capitalised, has strong liquidity and is profitable.

The Malta Financial Services Authority (MFSA) is the sole regulator for all banking, investment and insurance business carried out in or from the Maltese islands. The Central Bank of Malta is primarily responsible for maintaining price stability through the formulation and implementation of monetary policy. It is also responsible for the promotion of a sound financial system and orderly capital markets. A Joint Financial Stability Board, set up between the MFSA and the Central Bank of Malta, focuses on macro prudential aspects of financial stability, extending its remit to the entire financial sector.

In June 2021, Malta made a high-level political commitment to work with the FATF and MONEYVAL to strengthen the effectiveness of its AML/CFT regime and to continue to work on implementing its action plan to address its strategic deficiencies, including by: (1) continuing to demonstrate that beneficial ownership information is accurate and that, where appropriate, effective, proportionate, and dissuasive sanctions, commensurate with the ML/TF risks, are applied to legal persons if information provided is found to be inaccurate; and ensuring that effective, proportionate, and dissuasive sanctions are applied to gatekeepers when they do not comply with their obligations to obtain accurate and up-to-date beneficial ownership information; (2) enhancing the use of the FIU's financial intelligence to support authorities pursuing criminal tax and related money laundering cases, including by clarifying the roles and responsibilities of the Commissioner for Revenue and the FIU; and (3) increasing the focus of the FIU's analysis on these types of offences, to produce intelligence that helps Maltese law enforcement detect and investigate cases in line with Malta's identified ML risks related to tax evasion.

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