THE MALTA CHAMBER
OF COMMERCE,
ENTERPRISE AND INDUSTRY

REACTIONS TO THE
2018 BUDGET SPEECH
AND SUPPLEMENTARY DOCUMENTS

12TH OCTOBER 2016

Preamble

Further to its preliminary public reactions issued on the 9th of October 2017, the Malta Chamber of Commerce, Enterprise and Industry has undertaken an in-depth and fully comprehensive analysis of the 2018 Budget Speech within the broader parameters outlined in the Economic Survey and other documents presented with the budget. The reactions presented in this document are the result of an internal consultation process collecting feedback from committees and individual members. Hereunder are the Malta Chamber's detailed reactions.

1. Introduction

There is no doubt that the focus of the 2018 budget speech concentrated on further supporting low-income earners and pensioners through the redistributive role of Government. The Chamber already commented that this redistributive exercise must be made in full recognition of the private sector and its wealth generation role in the economy. In this context, it is also important to note that the 2018 Budget focused more on a string of small measures which in their totality can lead to positive results in the business community.

The Chamber is also cognisant of the fact that this was the first budget in many decades to be drafted in a situation where public finances are showing a surplus rather than a deficit. This indeed bodes well for the future, but nevertheless when one analyses the finer details of the fiscal situation, the Chamber immediately noticed that the surplus we speak of is related to the extended government rather than the consolidated fund. The extended government balance includes income from all other authorities and agencies outside the government's departmental structures which boosted the surplus even further in part due to the increased sale of passports under the Individual Investment Programme (IIP). According to the Ministry's estimates, the extended government balance for 2018, shows a surplus of €54 million which translates to 0.5% of Malta's GDP whilst the consolidated fund is showing a deficit of €21.4 million. The Chamber is therefore concerned that there is this over-reliance on the success of the IIP scheme which could become unsustainable in the long term in balancing public finances.

Indeed, the overall position of the consolidated fund will remain negative in 2017 and 2018 with marginal gains in 2019 and 2020. However, the overall deficit in the consolidated fund is expected to remain in the region of 100m over the period. This may be interpreted that Government is reinjecting the additional resources raised from taxation back into the economy in the process boosting personal and company incomes.

The Budget Speech, in fact, listed a number of measures that could help the competitiveness of Maltese enterprises. Some of the Malta Chamber's priority submissions were indeed heeded

As a result, wealth generation in the country continues to be hampered by uncompetitive industrial energy tariffs as well as by loss of productivity through the traffic situation. These hindrances are supplemented by a COLA increase which, although not unaffordable, exceeds the figure calculated by the established mechanism. Of further concern was the fact that shortly after the Budget, Government compromised discussions with the social partners on the minimum wage issue. Besides, the Budget Speech underlined Government's persistence in replacing Eco Contribution with Excise Duties on a wide range of essential products. This is a repressive and anti-social measure. The Chamber opposes this trend because companies were exempt from Eco-Contribution if they participated in a waste management scheme. With this measure, companies must pay the Excise Duty as well as the fee for the waste management scheme.

The fact that the collective adverse impacts of these measures were not neutralised by commensurate competitiveness enhancing ones to ensure a steady economic progress is of concern. The Chamber has stressed, time and time again, that resting on the laurels of recent economic success is strongly discouraged and that continued investment to achieve sustainable future economic growth is a must.

2. Macro Economy and Public Finances

The data for the Maltese economy as presented in the Budget 2017 document is encouraging and in line with one of the Chamber's objectives for the Budget, Convergence towards the Maastricht Criteria in terms of General Government Debt and Deficit is also positively noted.

The Chamber is encouraged by the rate of economic expansion over recent years and the manner in which Government is seriously tackling consolidation of public finances. General Government Debt is expected decrease to 61.9% in 2017, while forecasts for General Government Deficit were further improved to 0.7% ratio for 2016, from a previous forecast of 1.1%.

It is pertinent to note that previous forecasts have been exceeded, driven by larger economic growth than anticipated. This, coupled with conservative previous estimates it is noted that the public finance consolidation was less due to any contraction in public recurrent expenditure which was up by almost €262 million in the year under review. Despite this increase in real terms, the growth in GDP outpaced recurrent public expenditure and hence resulted in declining general government debt and deficit percentages. This creates a delicate scenario that may be derailed with the slightest slip-up. Credit rating agencies have consistently remarked that this is indeed a reality that the country potentially faces without forceful reforms in the sustainability of pensions and public healthcare.

3. Reactions to most notable Budget Measures and effects on Competitiveness

National competitiveness must remain a priority and the country must endeavour to constantly enhance it. All efforts need to be directed at improving the country's cost competitiveness through measures that seek to enhance both cost and non-cost factors of Malta's businesses. For Budget 2017, the Malta Chamber proposed more competitive industrial energy rates, a more competitive company taxation framework, mitigation in the abuse of free movement of goods, transport related measures, modernisation of education and development of the labour market, better integration of foreign workers and a holistic focus on research, development and innovation amongst many other proposals.

Following careful analysis, the Malta Chamber lays out its reactions to the most notable competitiveness-related measures included and overlooked in Budget 2017.

3.1 Excise Duties

The excise duties introduced in recent successive Budgets as a replacement for Eco-contribution has exacerbated the un-level playing field situation that exists amongst reputable, tax-abiding companies and others that are not. The Chamber, in face, perceives this as a knee-jerk reaction that imposes additional burdens on law-abiding operators and citizens in an attempt to make good for what others fail to contribute.

Responsible operators that self-complied or subscribed to private waste management schemes in order to recover or recycle their waste were exempt from eco-contribution. Yet, with the introduction of excise duties in this and previous budgets, the same operators are paying excise duties on top of the scheme fees, hence incurring additional tax burdens and administrative costs. This reality makes abuse of the system all the more attractive while bona fide operators will see market shares eroded in favour of non-compliant operators.

The Chamber is also concerned that once shifted to the Excise Duty regime, a window of opportunity to increase the prices of taxable goods is opened and frequently exercised. Excise duties also impose additional costs for operators as excise is paid on imports and not once the good sold, hence incurring a larger cost per unit of stock that remains unsold.

3.2 The Cost of Living Adjustment

While imposing additional costs for businesses, the €1.75 increase in the Cost of Living Adjustment figure for next year is not unaffordable figure in light of recent economic performances. It does, however, depart from the lower figure that should have applied using the standard calculation mechanism as it also includes an anticipated payment, hence highlighting the shortcomings of the COLA mechanism.

The Budget speech indicated that government opted to give a €0.59 increase in advance as had been done in the past. However, a precedent has been set this year because the speech also said that the 59 cents will only be deducted if next year's figure exceeds €1.75. This €1.75 benchmark figure for next year is entirely arbitrary and does not emerge from any calculation or discussion with a recognised structure or in which the Chamber was party.

3.3 Energy Tariffs

The Chamber is disappointed to note that there were no Budgetary measures that address further reductions in the energy tariffs for businesses – also one of the Chamber's primary pre-Budget proposals – despite the many factors that should make such a decrease possible such as the significantly lower price of crude oil and the highly competitive rates of energy supplied by the interconnector. It is feared that current commercial energy tariffs erode Malta's competitive position in cost-sensitive export sectors.

The Malta Chamber proposed a number of effective, easy to implement measures accompanied by workings depicting the feasibility of the proposals which included a widening of the tariff bands, a further 25% reduction across all bands, a decrease in the minimum threshold for applicability of night tariffs and an off-peak tariff rate discounted by 30%. The Chamber also proposed that multiple sites of the same entity and groups of companies should be charged as one customer to benefit from bulk discounts, the introduction of maximum demand for retail outlets and SMEs, maximum demand meter resets every quarter, discounts for customers with direct debit and prompt payments as well as the introduction of an off-peak tariff applicable between Friday at 22:00hrs and Monday at 06:00hrs.

Despite lengthy discussions with authorities and concerned entities, all of the above proposals were overlooked in the Budget 2017 speech. According to Eurostat's Industrial Energy Rates including all taxes and levies for the second half of 2015, the EU 28 average industrial energy tariffs remains below those available to Maltese businesses. Moreover, Malta's average rate as quoted by Eurostat is 36% higher than the average rate available in countries competing for foreign direct investment, namely Bulgaria, Czech Republic, Estonia, Croatia, Lithuania, Hungary, Poland Romania and Slovenia. In addition, it is also worth noting that Malta remains the only EU Member State where commercial rates are higher than domestic rates.

It is clear that the current structure behind energy tariffs policy differs from the principle that wealth is first created before it can be distributed. This does not bode well for continued economic expansion and wealth creation in a business-friendly environment.

3.4 Transport

Possibly the single largest issue straining businesses and society at present is the inefficiency of Malta's transportation infrastructure and the severe traffic congestion at virtually all hours of the day. This congestion is taking its toll on the cost-effectiveness of many businesses' operations that in some way involve transportation of goods, people or other resources.

With this issue featuring daily on the national media and coupled with Transport Malta's recent launch of the National Transport Strategy and Masterplan, the Malta Chamber expected the Budget to contain a plethora of measures that aim to alleviate traffic congestion and enhance the island's transport infrastructure. The Chamber is therefore compelled to express its disappointment and growing concerns on this issue. Despite Government being armed with the necessary tools, studies and plans, the concerns of citizens and businesses have not been addressed.

While the two transport related budget measures incentivising 18 year-olds to make use of public transportation and companies to arrange organised transport for employees are positive in their nature, they are far from sufficient and will have virtually no impact on traffic congestion. It is worrying that implementation of incentives aimed at tackling the real issues causing congestion remain elusive.

3.5 Minimum Wage and Parental Sick Leave

The Chamber acknowledges that there exists every intention to commence a consultation process on both the national minimum wage and the potential introduction of parental sick leave. The Chamber must stress that such delicate matters for both citizens and the economy must undergo careful yet exhaustive discussions including all social partners. The Chamber shall engage fully in such forthcoming discussions but must at the same time denounce the authorities for compromising these discussions before they have even commenced.

The Chamber shall not lack its social conscience during discussions on a minimum wage increase. However, it must be stressed that is unrealistic to assume that the minimum wage can be altered in isolation without triggering a realignment of salaries across the whole economy. The benefit of any increases will be short-lived and similar calls will be repeated in a few years' times once inflation consumer price inflation absorbs the sudden increase in disposable income. Such a measure is not the solution the 5.7% of workers and their dependents who are at risk of poverty require. The Chamber wishes to propose measures which further reduce the number of workers on minimum wage whilst safeguarding our country's cost competitiveness. Besides, there are other means to support the spending power of disadvantaged sectors of society, such as social benefits, in-work supplementary payments and education. Such means will have the desired effect on this small sector of society without the negative impacts of wage increases across the board.

The provision parental sick leave must be designed and implemented carefully as it may lead to further abuse of sick leave provisions. Such abuse may result from the institutionalisation of an injustice against employers and contribute to erode Malta's competitiveness and potential for growth

3.6 Education and Labour Market

European Commission and EUROCHAMBRES Surveys of Malta's business sector carried out over the last 36 months have shown that availability and recruitment of skilled human resources has steadily grown to become the largest hindrance to the continued growth of enterprises in all economic sectors. Companies are encountering ever-increasing difficulties to recruit personnel with adequate technical qualifications and soft skills such as written and spoken English language skills, critical and independent thinking as well customer-focused orientation - skills that are desperately required in order to meet the demands and expectations of the market. The national skills-gap has rapidly become a very real issue resulting from the lack of foresight and adaptation of the country's educational institutions.

The recently approved establishment of a National Skills Council tasked with aligning educational institutions and national curriculum with the needs of the economy is an encouraging step to mitigate the growing skills gap. It is now pertinent that the establishment and effective operation of the Council is rapid. The country stands to lose out on a number of potential growth opportunities if the present trends continue in the near-future.

With the prominence and severity of the skills gap and lack of labour supply, the Malta Chamber remains concerned that, as evidenced by the overall lack of Budget measures, Government has not recognised this issue as one that can seriously dampen the country's continued economic growth. Budget measures proposed by the Malta Chamber focusing on modernising education, curricula and career guidance, minimising the rate of early school leavers and incentivising young adults to focus on Science, Technology, Engineering and Mathematics were worryingly omitted.

In its Pre-Budget proposals document, the Malta Chamber proposed that

- lifelong learning must be encouraged through the permanent continuation of the Training Aid Framework schemes, notwithstanding the availability of European Social Funds,
- the teaching profession should also be tied to Continues Professional Education programmes so as ensure the country's educators are always up to date with advances and opportunities in their respective fields
- stipends must be used as an instrument to narrow skills gaps by linking it to an employability index while not provided gratuitously.
- integration of foreign workers must be simplified and facilitated by the respective authorities.

3.7 Concessions for Transfers of Family Businesses

Family Businesses are the backbone of Maltese society. The tax implications involved in inter-family transfers of family business have the undesired effect of disincentivising the transfer and survival of a family business into its third generation. The Budget measure introducing a lowered stamp duty rate on the transfer of family businesses from a parent to children for a year is positive in its intentions to overcome present issues but is not near enough to ensure that a majority of family business continue to thrive past the third generation of ownership.

Family business transfers, particularly in the case of family businesses owned by large families, present a very lengthy and delicate transfer process that is not possible to commence and complete within 12 months.

In order to ensure the effectiveness of this Budget measure, the Malta Chamber urges authorities to extend this measure indefinitely. A lengthier time window provides families and businesses with a more reasonable period during which to carry out the necessary succession planning, execute the planned delegation, ensure seamless continuation of business practices and navigate the legal aspects of said business transfer.

It is also vitally important for the authorities to understand that the transfers of family business are not exclusive to the structure where a business is transferring from a parent to a child, as is specified in the Budget speech. This measure must also cater for inter-family transfers in a wider sense as transfers may be from owner to a partner, to a sibling, to a parent, to a cousin, to a nephew or niece, aunt or uncle, from owner to grandchild and many other possibilities. Restricting this measure to transfers from parent to child is automatically disqualifying and discriminating against many other family structure within which a transfer from a parent to a child is not possible.

4. Conclusions

In the days since the Budget 2017 speech, the Chamber has endeavoured to perform an analysis of both the measures introduced by the Budget as well as those that have been overlooked.

As it has stated on numerous occasions, in times of unprecedented economic growth and notable improvements in the standings of public finances, the Chamber strongly discourages complacency and such performances being taken for granted. The present prosperity is the result of an improving business environment established over a number of years. While the intentions of this Budget – to distribute portions of the country's prosperity to the categories of society whom have benefitted least – are understandable, timely and just, the Chamber must continue to advocate the need to continuously stimulate the private sector by investing the proceeds of today's prosperity in ways that shall ensure Malta's continued and sustainable economic growth and competitiveness.

That said, the Chamber remains willing to participate in discussions aimed at the successful implementation of this year's Budget measures.

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