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Recommendation for a

COUNCIL RECOMMENDATION

with a view to bringing an end to the situation of an excessive government deficit in Malta

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with a view to bringing an end to the situation of an excessive government deficit in Malta

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 126(7) thereof,

Having regard to the recommendation from the Commission;

Whereas:

(1) According to Article 126 of the Treaty on the Functioning of the European Union (TFEU) Member States shall avoid excessive government deficits.

(2) The Stability and Growth Pact is based on the objective of sound government finances as a means of strengthening the conditions for price stability and for strong sustainable growth conducive to employment creation.

(3) On [21 June 2013], the Council decided, in accordance with Article 126(6) TFEU, that an excessive deficit existed in Malta.

(4) In accordance with Article 126(7) TFEU and Article 3 of Council Regulation (EC) No 1467/97 on speeding up and clarifying the implementation of the excessive deficit procedure[1], the Council is required to address recommendations to the Member State concerned with a view to bringing the situation of an excessive deficit to an end within a given period. The recommendation has to establish a maximum deadline of six months for effective action to be taken by the Member State concerned to correct the excessive deficit. Furthermore, in a recommendation to correct an excessive deficit the Council should request the achievement of annual budgetary targets which, on the basis of the forecast underpinning the recommendation, are consistent with a minimum annual improvement in the structural balance, i.e. the cyclically-adjusted balance excluding one-off and other temporary measures, of at least 0.5% of GDP as a benchmark. In addition, in accordance with Article 2 of Council Regulation (EC) No 1467/97 specifying the requirement under the debt criterion, the budgetary target recommended for the final year of the correction period must ensure that the required reduction in the differential between the debt-to-GDP level and the 60%-of-GDP Treaty reference value will occur over the two years following the correction of the excessive deficit, based on the Commission forecast.

(5) The Commission 2013 spring forecast projects that the deficit will continue to be above the reference value in 2013 and 2014, respectively at 3.7% and 3.6% of GDP. These budgetary projections are based on current policies, thus incorporating the 2013

[1] OJ L 209, 2.8.1997, p. 6.

budget that was endorsed by Parliament in April 2013, which includes expansionary measures on both the revenue and expenditure side as well as the already planned equity injection into Air Malta (0.6% of GDP), with a net deficit-increasing impact of 0.3% of GDP. The expansionary measures are only partially compensated by increases in excise duties, the collection of tax arrears as well as the expenditure savings and higher social contributions stemming from the 2006 pension reform. In addition, the contribution of net deficit-reducing one-offs, as identified by the Commission, to the consolidation effort would fall sharply after 2012. Due to the expected continued primary deficits in 2013 and 2014, the general government debt, according to the Commission 2013 spring forecast, is projected to rise further, to 73.9% of GDP in 2013 and to 74.9% of GDP in 2014. In 2015 and 2016, the general government deficit is projected to remain above the 3% of GDP reference value, and the debt-to-GDP ratio would increase to 75.6% of GDP by 2016.

(6) According to Regulation 1467/97, the correction of the excessive deficit should be completed in the year following its identification, unless there are special circumstances. In light of this, a correction of the excessive deficit by 2014 is warranted. In particular, a credible and sustainable adjustment path would require Malta to reach a headline general government target of 3.4% of GDP for 2013 and 2.7% of GDP in 2014, which is consistent with an annual improvement of the structural balance of 0.7% of GDP in 2013 and 0.7% of GDP in 2014. The 2014 target ensures that the required reduction in the differential between the debt-to-GDP level and the 60%-of-GDP Treaty reference value will occur over the two years following the correction of the EDP. To reach the above-mentioned structural targets, Malta would need to adopt additional consolidation measures of around 0.4% of GDP in 2013, on top of the measures already included in the baseline scenario, and around ¾% of GDP in 2014. These targets take into account the need to compensate for the negative second-round effects of fiscal consolidation on public finances, through its impact on GDP growth. The baseline scenario on which this adjustment path is built incorporates the Commission 2013 spring forecast and extends it up to 2016 relying on standard assumptions about the closure of the output gap and the sensitivity of the budget to the cycle; it does not include however the additional capital injection into Air Malta that is planned in 2015 according to the 2013 stability programme. It is thus assumed that the capital injection will not take place or be offset by measures in the opposite direction.

(7) Malta's fiscal framework is quite flexible, and its non-binding nature and the short horizon of fiscal planning are not supportive of a sound fiscal position. Directive 2011/85/EU on budgetary frameworks has not yet been transposed. Moreover, in accordance with Article 5 of Regulation No 473/2013 of the European Parliament and of the Council of 21 May 2013 on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member States in the euro area, Malta should put in place independent bodies for monitoring compliance with fiscal rules. While the stability programme states the intention of the government to set up a fiscal council, no concrete plans are laid out.

(8) In accordance with Article 9(1) of Regulation No 473/2013 of the European Parliament and of the Council of 21 May 2013 on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member States in the euro area, Malta should present to the Commission and to the Council an economic partnership programme, simultaneously with the report to be submitted in accordance with Article 3(4a) of Regulation (EC) No 1467/97.

(9) In the view of the Council, budgetary consolidation measures should secure a lasting improvement in the general government balance, while being geared towards enhancing the quality of the public finances and reinforcing the growth potential of the economy,

HEREBY RECOMMENDS:

(1) Malta should put an end to the present excessive deficit situation by 2014.

(2) Specifically, Malta should:

(a) reach a headline general government target of 3.4% of GDP for 2013 and 2.7% of GDP in 2014, which is consistent with an annual improvement of the structural balance of 0.7% of GDP in 2013, and 0.7% of GDP in 2014. This adjustment path would allow bringing the headline government deficit below the 3% of GDP reference value by 2014 while at the same time ensuring that the government gross debt ratio will approach the 60%-of-GDP reference value at a satisfactory pace;

(b) specify and rigorously implement the measures that are necessary to achieve the correction of the excessive deficit by 2014, and use all windfall gains for deficit reduction.

(3) The Council establishes the deadline of 1 October for Malta to take effective action and, in accordance with Article 3(4a) of Council Regulation (EC) No 1467/97, to report in detail the consolidation strategy that is envisaged to achieve the targets.

Following the correction of the excessive deficit, Malta is invited to continue making progress at an appropriate pace towards its medium-term objective of a balanced budget in strcutral terms, including by meeting the expenditure benchmark. To limit risks to budgetary execution, the Council invites Malta to strengthen the effectiveness of its budgetary framework and improve the monitoring of budget execution throughout the year. In particular, Malta is invited to put in place a more binding, rule-based multiannual fiscal framework. In addition, the role of independent bodies monitoring fiscal policy should be strengthend, in accordance with Article 5 of Regulation (EC) No 473/2013 of the European Parliament and of the Council of 21 May 2013 on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member States in the euro area.

Finally, to ensure the success of the fiscal consolidation strategy, the Maltese authorities are invited to back the fiscal consolidation with comprehensive structural reforms, in line with the Council recommendations addressed to Malta in the context of the European Semester and in particular those related to the preventive arm of the Macroeconomic Imbalances Procedure.

This recommendation is addressed to the Republic of Malta.

Done at Brussels,

For the Council
The President