

7. Foreign Trade and Payments

7. Foreign Trade and Payments

During the first nine months of 2004, a significant increase in the current account deficit was recorded. A variety of factors underpinned this deterioration in the current account balance. In particular, a substantial increase in profits by foreign owned companies, particularly in the banking sector, led to a significant outflow in the investment income account. Most of these earnings were however re-invested in the Maltese economy and will feature as an inflow of foreign direct investment in the capital and financial account of the balance of payments. In addition, lower net interest receipts from abroad were recorded during the Survey period.

Besides, developments in the merchandise account have also contributed towards a high current account imbalance. Imports of goods registered a substantial increase. In fact, higher imports of consumer and capital goods were recorded. Imports of fuel also increased as a result of the significant increase in international oil prices registered during the Survey period. Meanwhile, export performance remained modest. Sectors which typically generate high value added per capita, recorded a significant increase in exports. Such sectors included the machinery and transport equipment sector and the chemical and pharmaceutical sector. This positive development made up for the fall in exports by the clothing sector and the food, beverages and tobacco category. Moreover, tourist earnings increased over the Survey period. This was partly offset by higher payments on transportation, partly reflecting the increase in imports and higher transport costs due to the increase in international oil prices.

Foreign Trade

The first nine months of 2004 were characterised by a marginal increase of 0.3 per cent in export activity and an increase of 4.7 per cent in total imports. As a result, the trade deficit deteriorated by Lm43.1 million to Lm318.9 million. The rate of import cover declined further to 68.3 per cent during the Survey period. This is illustrated in Chart 7.2. The developments in international trade are highlighted in Table 7.1 and Chart 7.1. Following the introduction of the Intrastat Supplementary Declaration as the source of trade statistics relating to EU Member States, the subdivision between domestic exports and re-exports was discontinued. As a result, data in the Economic Survey now refers to total exports and is thus not directly comparable with previous publications.

Box 7.1

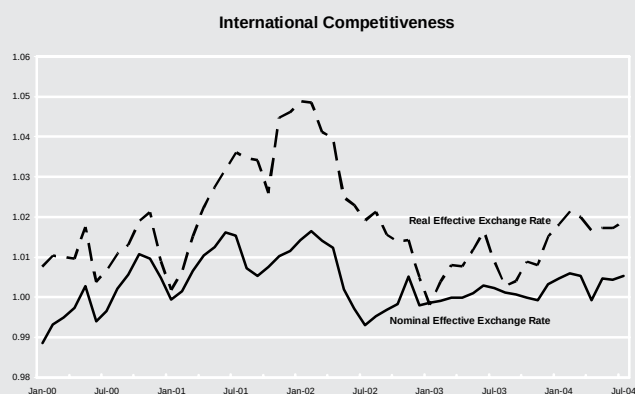
International Competitiveness

An indicator of a country's international price competitiveness is provided by the real effective exchange rate. The real effective exchange rate is calculated as the product of the nominal effective exchange rate and the relative foreign to domestic prices. In turn, the nominal effective exchange rate is an average of exchange rates weighted by bilateral trade shares. A decline in the real effective exchange rate is indicative of improved international competitiveness

Data published by the IMF for the first six months of 2004 indicate that the real effective exchange rate has increased marginally by 0.2 per cent on the level recorded in December 2003. Meanwhile, the nominal effective exchange rate has increased by 0.1 per cent over the same period. This indicates that the inflationary developments recorded in the first six months of 2004 contributed to a marginal deterioration in the price competitiveness of Maltese products and services on the international markets. This reflects higher domestic inflation relative to inflation abroad, particularly in relation to Malta's major trading partners within the EU.

A note of caution on the interpretation of real effective exchange rates is however warranted. In deriving the real effective exchange rate, the IMF uses the consumer price index as a measure of prices. This index does not necessarily reflect Malta's export prices in the short-term. In fact, the deflator for exports shows a substantial decline over the period under review.

In the long term, the inflation in consumer prices may be reflected in the costs of production and possibly in export prices, depending on whether the country is a price taker. In this case, the use of real effective exchange rates based on the consumer price index may be a relatively good indication of international price competitiveness. In any case, the real effective exchange rate should ideally be considered as one of a myriad of possible measures used to objectively measure trends in competitiveness.



Foreign Trade							
Table 7.1	Lm million						
	2001		2002		2003		2004
	Jan/Sep	Oct/Dec	Jan/Sep	Oct/Dec	Jan/Sep	Oct/Dec	Jan/Sep
Imports (c.i.f.)	918.8	306.4	906.3	321.2	960.4	320.8	1,005.4
Total Exports (f.o.b.)	668.3	212.3	719.9	248.5	684.6	243.7	686.5
Trade Gap	-250.5	-94.1	-186.4	-72.7	-275.8	-77.1	-318.9
of which:							
Exceptional Item (Exports)	-	-	50.1	-	-	-	-
Exceptional Item (Imports)	-	-	-	-	2.1	-	-

Source: National Statistics Office

Chart 7.1

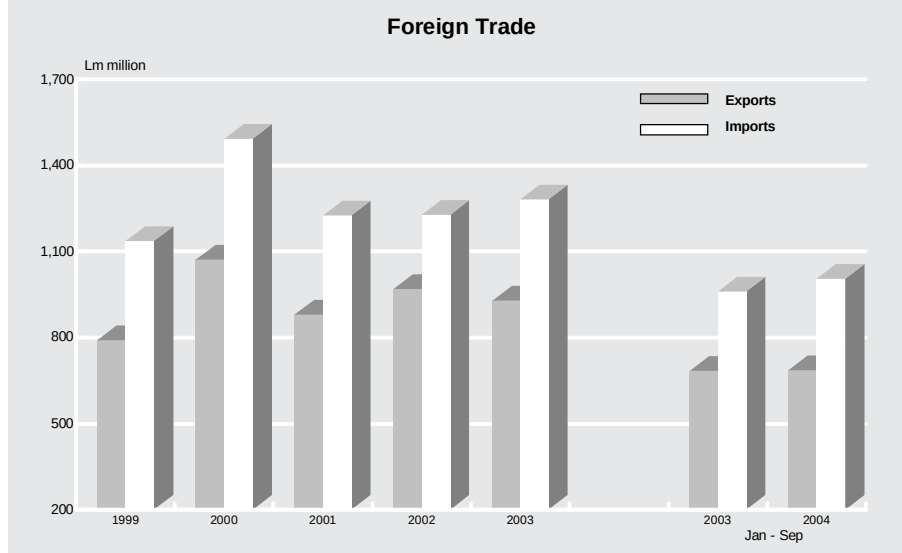
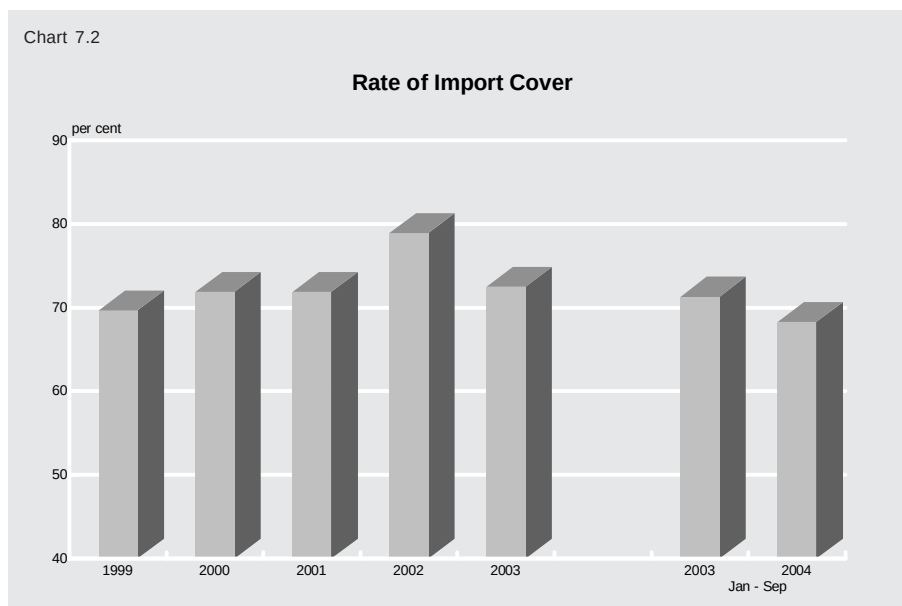


Chart 7.2



It is pertinent to note that imports registered during the Survey period include Lm23 million worth of sea-craft. This followed the one-off concession granted last year on the VAT payable on registration of sea-craft, which in turn resulted in a substantial increase in yachts and pleasure boats registered in Malta. Although this figure is included in the data for foreign trade, it is excluded from figures for imports of goods and services in both the balance of payments and the national accounts data. In this sense, a significant amount of the aggregate increase in imports is due to the implementation of one-off measure by Government to increase its revenue. A significant part of the increase in imports can be safely considered of an exceptional nature which, in itself, does not reflect negatively upon Malta's ability to restore to a healthy trade gap position. Figures for 2003 also include the importation of a patrol boat worth Lm2.1 million. The net effect of these one-off items accounts for more than half the increase in the trade deficit. Excluding these one-off items, imports would have recorded an increase of 2.5 per cent.

Exports registered a marginal increase during the period under review. Export activity during the first nine months of 2004 was influenced by the restructuring process currently taking place as a result of increased competitive pressures from abroad. This involved export sectors such as the clothing sector. On the other hand, high value added sectors such as chemicals and scientific instruments recorded improvements. It is encouraging to note that export-oriented activity in Malta is gradually adjusting to increased price competition in international

markets. It further accentuates the need to upgrade the skills of the labour force in a bid to increase Malta's competitive edge by increasing productivity levels.

The analysis of Malta's export and import flows by geographical areas has been adjusted to account also for trade flows with the nine new Member States which, together with Malta, have joined the European Union in May 2004. At the same time, reference to Malta's trade flows with the EU 15 has been retained to allow comparability in trade data for the time-frame under review. In addition, trade data for EU countries is considered by country of consignment as from 2004.

Exports

Against the background of a consolidation of global economic recovery and increased pressure for the achievement of higher productivity levels, total exports were marginally higher than the corresponding nine months of 2003. Data on the composition of exports indicates that the manufacturing base of the Maltese economy is still undergoing structural change. Thus one notes a decline in exports of clothing, and the food, beverages and tobacco category, and a compensating increase in exports of chemicals and machinery and transport equipment. Table 7.2 shows the commodity breakdown of exports since 2001 whilst Chart 7.3 highlights the contribution of semi-manufacturing, machinery and transport equipment, and other manufacturing towards total exports. Chart 7.4 illustrates

Commodity Breakdown of Exports							
Table 7.2	Lm million						
	2001		2002		2003		2004
	Jan/Sep	Oct/Dec	Jan/Sep	Oct/Dec	Jan/Sep	Oct/Dec	Jan/Sep
Total Exports							
Food, Beverages and Tobacco	25.9	8.3	31.4	25.2	31.3	19.4	29.5
Chemicals	15.3	4.6	14.4	4.2	13.1	5.9	18.2
Semi-manufactures	39.5	13.9	36.5	12.5	36.0	12.8	35.8
Machinery and Transport							
Equipment	427.9	127.6	455.5	146.3	427.4	149.3	441.7
Clothing	46.6	16.4	51.9	17.1	47.4	14.6	36.0
Fuels	34.5	13.7	39.0	13.2	38.8	12.8	32.4
Printed Matter	13.4	5.4	19.5	8.3	24.3	7.5	24.1
Toys and Games	16.1	4.0	22.2	7.2	21.1	7.1	22.3
Scientific Instruments	20.7	6.7	19.9	5.4	20.1	7.8	19.9
Other Manufactures	28.4	11.7	29.6	9.1	25.1	6.5	26.6
Total Exports	668.3	212.3	719.9	248.5	684.6	243.7	686.5
Source: National Statistics Office							

Chart 7.3

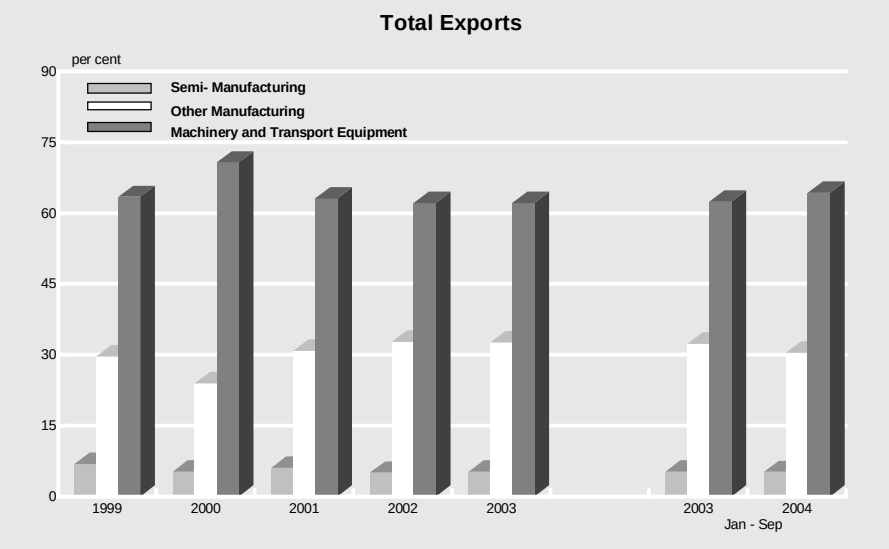
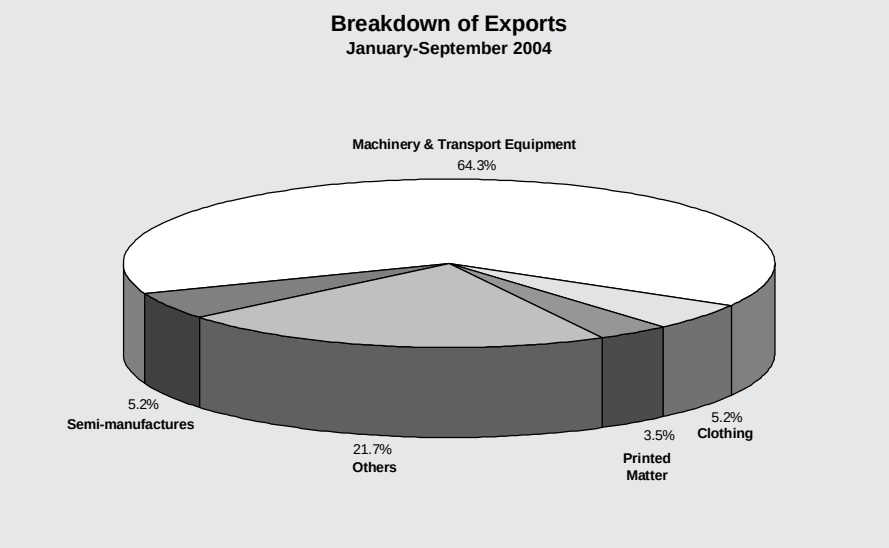


Chart 7.4



the contribution of different categories to total Maltese exports during the Survey period. During the period under review, total exports increased marginally by Lm1.9 million to Lm686.5 million.

Since 2002, the aggregate share of traditional export sectors, including the clothing category and food, beverages and tobacco category, has declined to 9.5 per cent of total exports in the first nine months of 2004. The clothing sector alone recorded a decline of 8.7 per cent and 24.1 per cent in the first three quarters of 2003 and 2004 respectively. During the Survey period total exports of clothing declined by Lm11.4 million to Lm36.0 million. The food, beverages and tobacco category also recorded a decline of Lm1.8 million, or 5.8 per cent, to Lm29.5 million.

During the January-September period, exports of chemical products recorded a substantial increase of Lm5.1 million, or 38.9 per cent, to Lm18.2 million. The machinery and transport equipment category, which includes exports of semi-conductors, also registered an increase of Lm14.3 million, or 3.3 per cent. The increase in international demand for semi-conductors may have contributed to this positive outcome in one of the most important sectors of manufacturing activity. This improvement should also be considered in the wider picture of price competition on the international markets for semiconductors, which has led to a constant decline in prices of semiconductors. This suggests that the domestic performance of this sector was also characterised by lower prices and higher export volumes.

Trade activity in 2004 was also characterised by the significant increase in oil prices. Despite this increase, however, exports of fuel declined by Lm6.4 million between the January-September period of 2003 and 2004. This followed the termination of services by a major bunkering operator in the third quarter of 2004.

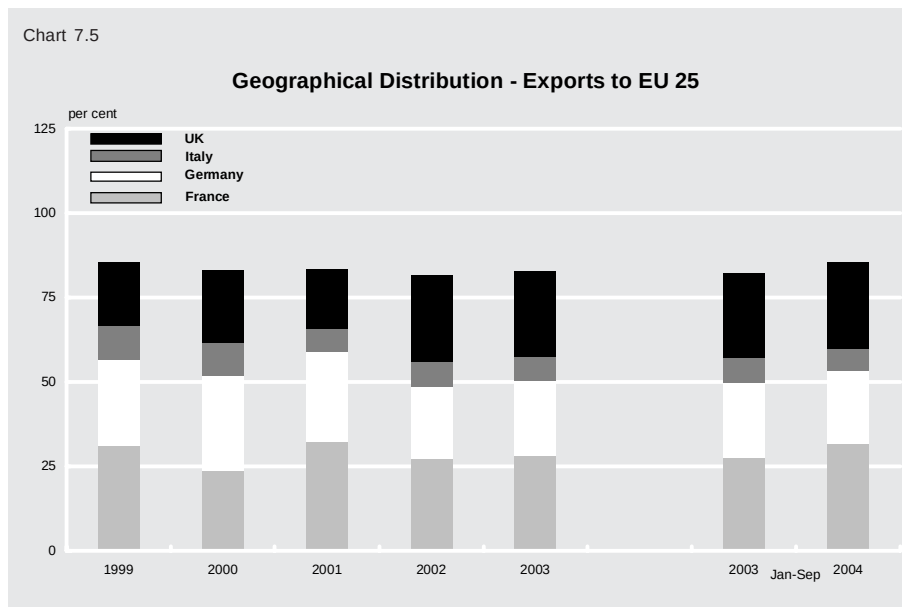
Exports of toys and games increased by Lm1.2 million. Following the increasing trend in exports since 2000, the share of exports of printed matter in total exports remained at the same level as the comparable nine months of 2003. Exports of semi-manufactures declined marginally to Lm35.8 million. An increase of Lm1.5 million, or 6.0 per cent, in exports of other manufactures was also recorded during the Survey period.

Geographical Distribution – Exports

The first nine months of 2004 were characterised by an increase in exports to the EU 25 and the American continent, whilst exports to Asia declined. Table 7.3 highlights these developments in more detail. Despite the marginal appreciation of the Maltese lira against the Euro, exports to the Euro Area have increased by Lm12.3 million, or 5.5 per cent, to Lm236.5 million. The higher exports to the EU 25 and North America reflect, in part, the improved economic performance recorded in 2004 by these two continents.

The EU 25 Member States account for 48.2 per cent of total exports compared to 47.2 per cent a year earlier, thus consolidating their position as Malta's major export market. Total exports to the EU 25 increased by Lm7.3 million during the period under review. Chart 7.5 shows the share of Maltese exports to France, Germany, Italy and the UK in total exports to the EU 25 Member States. During the Survey period, exports to France increased by Lm15.2 million to Lm104.6 million and exports to the UK increased by Lm3.6 million to Lm84.3 million. A marginal increase of Lm1.2 million in exports to Germany was recorded, whilst

Total Exports by Main Geographical Areas							
Table 7.3							
Lm million							
	2001		2002		2003		2004
	Jan/Sep	Oct/Dec	Jan/Sep	Oct/Dec	Jan/Sep	Oct/Dec	Jan/Sep
Europe	331.6	105.6	332.8	116.1	327.3	108.2	336.6
EU 15*	321.5	99.8	320.3	109.2	309.5	101.5	325.8
EU 25*	329.3	104.6	327.4	113.4	323.3	106.7	330.6
Italy	21.9	8.3	25.1	7.6	24.5	7.0	21.3
Germany	87.4	27.4	70.3	23.3	70.8	24.4	72.0
France	113.3	26.9	87.6	32.4	89.4	30.8	104.6
U.K.	53.7	22.5	82.1	30.1	80.7	28.3	84.3
Netherlands	9.7	2.8	8.4	1.9	5.6	1.2	4.0
Belgium	20.4	7.0	23.7	7.0	21.6	4.0	14.6
Others	22.9	9.7	30.2	11.2	30.6	11.0	29.8
Euro Area	265.4	76.0	235.6	77.8	224.2	71.9	236.5
Other European countries	2.3	1.0	5.4	2.6	4.0	1.5	6.0
Africa	24.0	9.1	34.2	10.6	25.2	9.9	32.2
America	141.3	36.9	131.4	32.3	98.6	44.6	113.9
USA	138.0	36.3	128.3	31.1	92.1	42.1	108.4
Others	3.3	0.6	3.0	1.3	6.5	2.5	5.5
Oceania	0.5	0.1	0.5	0.1	0.4	0.1	0.7
Asia	129.1	45.1	174.8	72.9	189.1	66.1	170.7
Japan	21.3	5.0	20.1	21.5	20.5	16.6	14.2
Singapore	76.1	27.7	116.0	35.9	121.9	34.0	101.5
Others	31.7	12.3	38.7	15.5	46.7	15.5	55.0
Ships & Aircraft	41.8	15.5	46.3	16.5	44.0	14.8	32.4
Total Exports	668.3	212.3	719.9	248.5	684.6	243.7	686.5
EU 25 Exports as % of Total	49.3	49.3	45.5	45.7	47.2	43.8	48.2
*As from 2004 considered by country of consignment							
Source: National Statistics Office							



exports to Italy were Lm3.2 million less during the Survey period of 2004. Further declines were registered in exports to Netherlands and Belgium.

During the Survey period, the American continent accounted for 16.6 per cent of total Maltese exports compared to 14.4 per cent in the first three quarters of 2003. Indeed, exports to the USA exceeded Lm108 million, Lm16.3 million higher than in 2003. This partly reflects the positive economic performance registered by the US economy in the first nine months of 2004.

The Asian continent accounts for 24.9 per cent of the total Maltese export market. During the Survey period, exports to Asia were Lm18.4 million less, representing a decline of 9.7 per cent over the comparable period of 2003. This includes a fall of Lm20.4 million and Lm6.3 million in exports to Singapore and Japan, respectively. Meanwhile, exports to other Asian countries registered an increase.

Other developments registered during the first nine months of 2004 include an increase of Lm7.0 million, or 27.8 per cent, in exports to Africa and a marginal increase in exports to Oceania. The fall of Lm11.6 million in exports to ships and aircraft reflects, in part, the termination of services provided by a major oil-bunkering operator.

Imports

Imports of goods during the first nine months of 2004 registered an increase of Lm45.0 million to Lm1,005.4 million. This was mainly driven by imports of capital goods, consumer goods and fuel. Imports of industrial supplies declined. Table 7.4 highlights developments in imports by broad economic category.

The removal of the remaining levies on imports in May 2004, partly explains the higher imports of food, beverages and tobacco products. It may have led to a shift in demand, away from locally produced goods in the food and beverages sector, towards imported goods. Indeed, imports of food and beverages increased by Lm8.9 million in the first nine months of 2004. During the period under review, imports of durable consumer goods also recorded an increase of Lm6.7 million. Likewise, imports of other consumer goods rose by a further Lm8.7 million. A breakdown of consumer imports is portrayed in Chart 7.6.

Imports of capital goods registered a substantial increase of Lm32.8 million, or 21.0 per cent, over the first nine months of 2003. Included in this figure is Lm23.0 million worth of sea-craft registered in the first quarter of 2004, following the temporary reduction in the VAT rate on yachts and other vessels for pleasure or sport. This led to a substantial increase in newly registered sea-craft. Even

Imports by Broad Economic Category							
Table 7.4							
	2001		2002		2003		2004
	Jan/Sep	Oct/Dec	Jan/Sep	Oct/Dec	Jan/Sep	Oct/Dec	Jan/Sep
Consumer Goods							
Food and Beverages	69.8	27.2	72.6	27.0	75.4	28.7	84.3
Durable Goods	86.1	31.7	85.4	34.8	90.3	37.0	97.0
Others	47.4	16.9	55.6	18.7	59.4	20.3	68.1
Total	203.3	75.8	213.6	80.4	225.1	86.0	249.4
Industrial Supplies							
Primary	13.1	4.6	18.3	5.2	14.5	3.0	10.3
Semi-finished	452.3	149.4	432.7	147.2	459.7	152.6	449.8
Finished	11.2	3.9	11.1	6.8	14.3	6.8	16.1
Total	476.6	157.9	462.1	159.2	488.5	162.4	476.2
Capital and Others							
Capital Goods	151.6	47.8	148.7	49.9	156.4	49.5	189.2
Fuel	78.7	22.0	73.8	29.0	81.8	20.1	84.0
Non-specified and Gold	8.7	2.8	8.1	2.6	8.6	2.8	6.6
Total	239.0	72.6	230.6	81.5	246.8	72.4	279.8
Total Imports	918.9	306.3	906.3	321.2	960.4	320.8	1,005.4
Source: National Statistics Office							

Chart 7.6

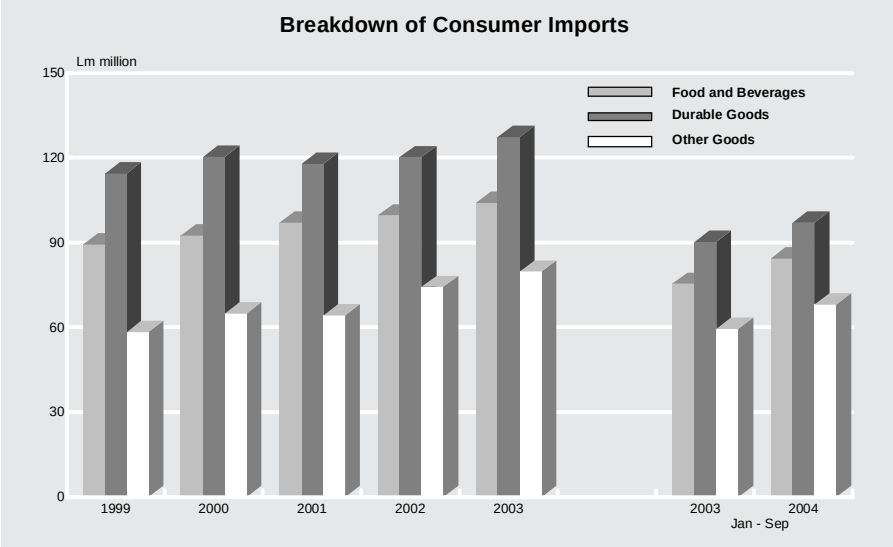
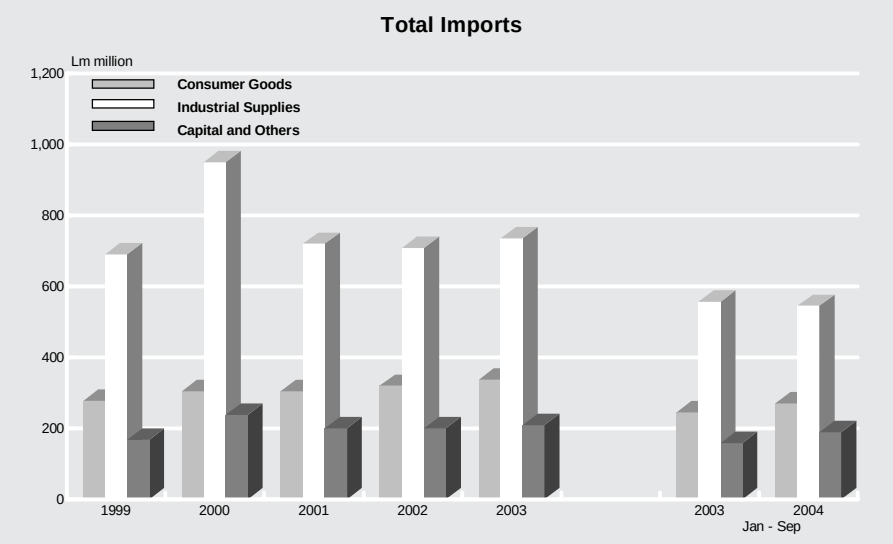


Chart 7.7



after accounting for this one-off item, imports of capital goods advanced by Lm9.8 million or 6.3 per cent.

The first nine months of 2004 were characterised by a significant increase in crude oil prices. As pointed out in Chapter 1 of the Economic Survey, a number of factors contributed to a significant rise in the international price of oil. As a result of these developments, Malta's fuel imports bill increased during the period under review. The impact on the fuel import bill of higher international oil prices was partly mitigated by lower imports of fuel intended for bunkering activities, after a major operator in the oil-bunkering sector ceased its operations in the third quarter of 2004. This explains why the fuel import bill for the January-September period of 2004 was only Lm2.2 million higher than the corresponding period in 2003.

Imports of industrial supplies stood at Lm476.2 million during the first three quarters of 2004, a decline of Lm12.3 million, or 2.5 per cent. This reflects the modest export performance registered during the Survey period. Primary supplies declined by Lm4.2 million whilst semi-finished supplies fell by Lm9.9 million. Meanwhile, finished industrial supplies registered a marginal increase of Lm1.8 million. The composition of imports is illustrated in Chart 7.7.

Geographical Distribution – Imports

Imports from the Euro Area, increased by Lm21.9 million, or 4.0 per cent, to Lm562.8 million during the first nine months of 2004. Higher imports from Asia were also registered during the Survey period whilst imports from America declined. Further details are provided in Table 7.5.

Imports from the EU 25 Member States increased significantly by Lm51.8 million during the Survey period. Almost 70 per cent of Maltese imports originate from the EU 25, up from around 68 per cent in the Survey period of 2003. Significant increases in imports from Malta's major trading partners within the EU were recorded. The share of France, Germany, Italy and the UK of total imports from the EU 25 is illustrated in Chart 7.8. Imports from Italy, U.K. and Germany increased by Lm22.9 million, Lm28.4 million, and Lm10.7 million, respectively. On the other hand, imports from France registered a significant fall of Lm30.4 million. A rise of Lm12.4 million in imports from the Netherlands was recorded in the first nine months of 2004.

Imports from America continued on a downward trend during January-September 2004 falling by Lm30.7 million. As a result, the share of imports

Table 7.5 Imports by Main Geographical Areas Lm million

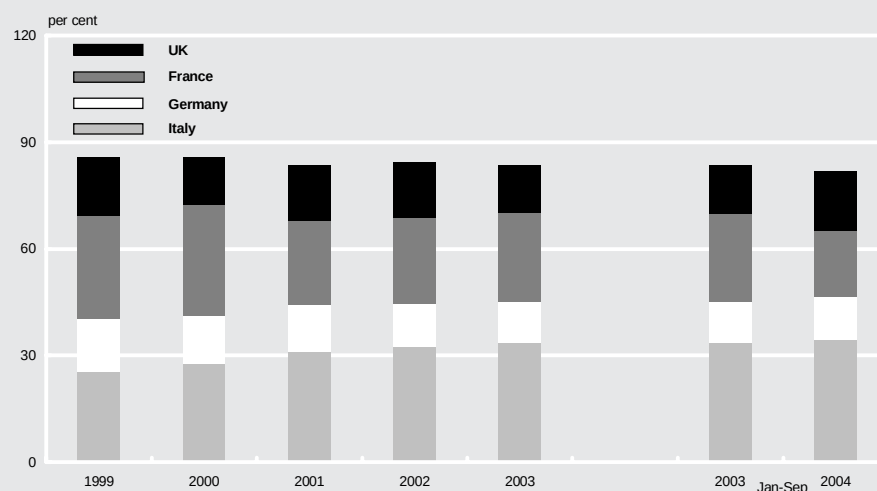
	2001		2002		2003		2004
	Jan/Sep	Oct/Dec	Jan/Sep	Oct/Dec	Jan/Sep	Oct/Dec	Jan/Sep
Europe	622.7	212.4	661.6	230.0	700.1	237.4	737.4
EU 15*	581.6	197.5	610.4	214.5	642.6	224.7	694.6
EU 25*	588.3	200.1	616.4	216.9	649.6	227.4	701.4
Italy	182.1	61.3	197.7	74.0	218.1	76.3	241.0
U.K.	89.4	33.7	93.8	33.9	89.7	28.9	118.1
Germany	79.8	27.6	74.3	24.2	75.7	25.3	86.4
France	138.5	45.6	155.3	49.8	159.6	59.3	129.2
Netherlands	21.0	7.4	20.8	7.7	22.2	7.5	34.6
Others	77.5	24.5	74.4	27.2	84.3	30.1	92.1
Euro Area	480.9	159.9	504.9	176.0	540.9	191.6	562.8
Other European Countries	34.3	12.3	45.1	13.1	50.5	10.0	36.0
Africa	20.7	7.9	12.3	5.0	9.1	1.7	17.6
America	113.7	43.7	94.0	33.4	91.2	24.7	60.5
USA	101.7	40.0	84.7	30.6	81.7	22.2	47.0
Others	12.0	3.6	9.3	2.8	9.5	2.5	13.5
Oceania	5.5	1.3	4.9	1.3	5.6	1.2	2.5
Asia	156.2	41.1	133.5	51.5	154.4	55.8	187.4
Japan	19.7	6.5	21.0	6.9	21.1	8.2	25.3
Singapore	71.2	10.8	37.2	14.6	47.5	12.1	75.7
Others	65.4	23.8	75.3	30.0	85.8	35.5	86.4
Total Imports	918.8	306.4	906.3	321.2	960.4	320.8	1,005.4
EU 25 Imports as % of Total	64.0	65.3	68.0	67.5	67.6	70.9	69.8

*As from 2004 considered by country of consignment

Source: National Statistics Office

Chart 7.8

Geographical Distribution - Imports from EU 25



from the American continent declined from 10.9 per cent in 2000 to 6.0 per cent in 2004. At Lm47.0 million, imports from the USA were at their lowest level in the last five years.

The fall in imports from America was compensated by an increase in imports from the Asian continent, which advanced by Lm33.0 million in 2004. Asia now represents more than 18 per cent of Maltese imports. Imports from Singapore increased by a further Lm28.2 million to Lm75.7 million during the Survey period. An additional Lm4.2 million in imports from Japan was also recorded. Higher imports from Africa and lower imports from Oceania were also registered.

Geographical Distribution – Trade Balances

Table 7.6 shows Malta's trade balances with a number of countries. The trade balance with the EU 25 Member States deteriorated by Lm44.5 million. Within the EU 25 higher trade gaps were registered with Germany, Italy, the UK, Belgium and the Netherlands. This was partly compensated by an improvement in the negative balance with France. Outside the EU, a significant improvement of Lm49.0 million in the positive trade balance with the USA was registered

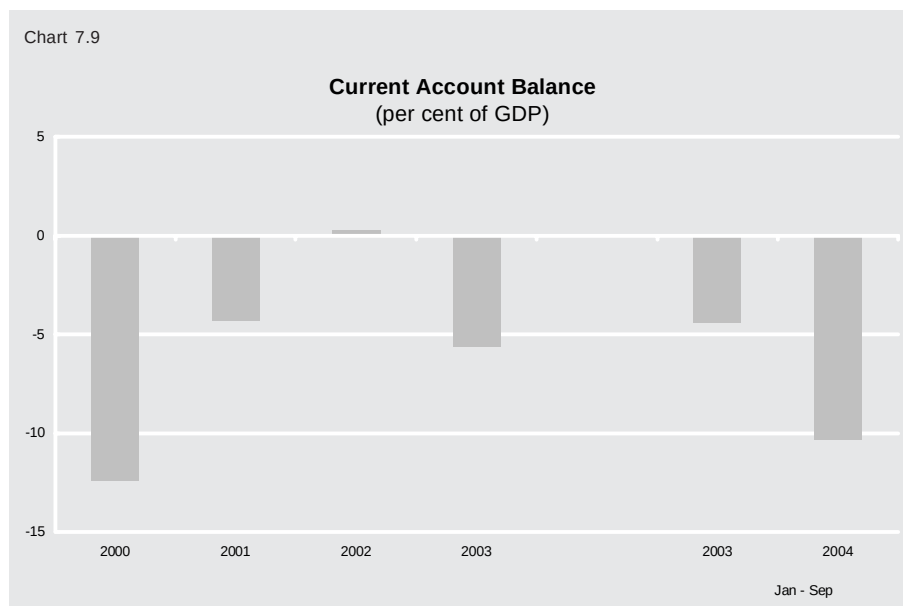
Trade Balances with Various Countries					
Table 7.6	Lm million				
	2001	2002	2003	2003 Jan/Sep	2004 Jan/Sep
EU 15*	-357.6	-395.3	-456.3	-333.5	-368.8
EU 25*	-354.5	-392.5	-447.1	-326.3	-370.8
Belgium	12.1	-10.4	3.8	5.5	-6.2
France	-43.9	-85.1	-98.7	-70.2	-24.6
Germany	7.4	-5.0	-5.8	-4.1	-14.3
Italy	-213.2	-239.1	-262.9	-193.2	-219.7
Netherlands	-15.9	-18.3	-22.9	-16.4	-29.0
United Kingdom	-46.9	-15.5	-96.2	-10.6	-33.7
Other EU	-54.1	-19.0	35.6	-37.3	-43.3
Other Countries					
USA	32.6	44.1	30.3	12.4	61.4
Japan	0.1	13.6	7.8	-0.6	-11.1
Singapore	21.9	100.2	96.3	74.4	25.8
Libya	2.2	24.0	20.9	15.8	20.0
China	-24.0	-25.2	-33.5	-23.6	-16.3
*As from 2004 considered by country of consignment					
Source: National Statistics Office					

during the Survey period. However, the positive trade balance with Singapore deteriorated by Lm48.6 million.

Balance of Payments

The widening of the current account deficit during the first nine months of 2004 suggests that domestic absorption continued to exceed national income. In turn, the high level of domestic absorption relative to the income level is also indicative of low national savings relative to investment. Chart 7.9 shows the current account balance as a percentage of GDP since 1999. The deficit in the first nine months of 2004 stood at 10.3 per cent of GDP. A deficit in the current account has been registered throughout this period with the exception of a surplus in the January-September period of 2002, which was related to an exceptional export item.

During 2002 the NSO revised the data related to the conversion of the merchandise trade data for imports which is at c.i.f. values into the methodology used for balance of payments purposes, that is, at f.o.b. This revision has affected the merchandise, transport and other services components. Since the data have been revised as from 1995 onwards, the figures shown in this Chapter are internally comparable. However, such figures are not comparable to those in Economic Surveys published prior to 2002.



The Current Account

In the period under review the current account deficit stood at Lm144.4 million. This represents an increase in the deficit of Lm83.4 million over the comparable level of 2003. However, around 43 per cent of this deterioration was attributable to net re-invested earnings, particularly in the banking sector. Meanwhile, lower net interest earnings from abroad represented a further 29 per cent of the increase in the deficit on the current account. Another 22 per cent of the deterioration in the current account was attributable to higher imports of goods. Also, net current transfers abroad increased, causing the current account deficit to widen by a further 12 per cent. On the other hand, higher net inflows of services, mostly related to tourist earnings, contributed to a narrowing of the current account deficit by about 6 per cent. Developments in the goods, services and income account are presented in Table 7.7.

The Goods and Services Account

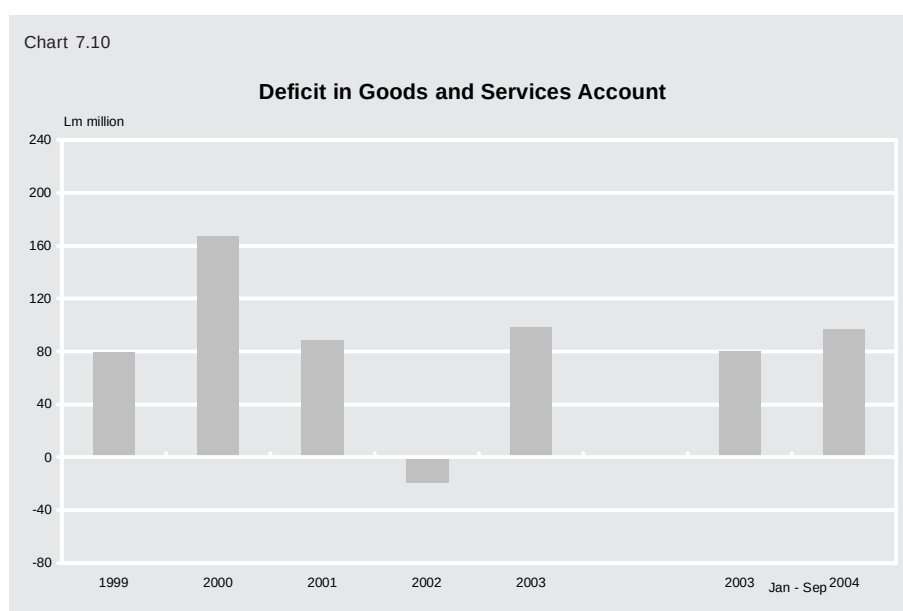
The negative balance on the goods and services account deteriorated by Lm16.9 million during the first nine months of 2004. This was underpinned by a significant increase in imports of goods. The increase in imports of goods registered in the Survey period has already been analysed in the section on foreign trade. It is

Balance of Payments Goods, Services and Income Account (Net)							
Table 7.7							
Lm million							
	2001		2002		2003		2004
	Jan/Sep	Oct/Dec	Jan/Sep	Oct/Dec	Jan/Sep	Oct/Dec	Jan/Sep
GOODS							
General Merchandise Transactions	-207.5	-75.5	-133.0	-58.5	-231.0	-62.7	-237.7
Nonmonetary Gold	-7.9	-2.5	-7.0	-2.2	-6.7	-2.1	-5.9
Others	28.0	10.7	34.4	12.1	32.8	8.2	17.2
Total Goods	-187.4	-67.3	-105.6	-48.6	-204.9	-56.6	-226.4
SERVICES							
Transportation	8.3	-3.7	-1.2	-4.9	-12.3	-5.5	-15.7
Travel	146.3	33.2	133.2	46.2	137.3	43.3	144.1
Other Services	-13.6	-4.4	1.7	-1.8	-0.3	0.7	1.0
Total Services	141.0	25.1	133.7	39.5	124.7	38.4	129.3
Total Goods and Services	-46.4	-42.2	28.1	-9.1	-80.2	-18.2	-97.1
INCOME							
Compensation to employees	-0.5	-0.2	0.0	0.1	1.3	0.2	0.8
Investment Income	16.2	-4.4	30.1	-28.0	29.4	-15.5	-26.4
Total Income	15.7	-4.6	30.6	-28.1	30.7	-15.3	-25.6
Total Goods, Services and Income	-30.6	-46.8	58.7	-37.2	-49.5	-33.5	-122.6
Source: National Statistics Office							

important to note that imports of goods in the balance of payments have increased by Lm18.1 million. The discrepancy between this figure and the increase of Lm45.0 million recorded in the trade statistics is partly related to the different treatment of the transaction related to the imports of yachts and pleasure boats in the two sets of accounts. The latter is featured in the balance of payments as an adjustment. Chart 7.10 shows the deficit in the goods and services account since 1999.

The deficit in the merchandise account increased by Lm6.7 million. This was underpinned by higher merchandise imports. Higher payments for repairs on goods and lower receipts from bunkering activities led to a further fall in net receipts in the goods account. On the other hand outflows of non-monetary gold have declined marginally during the Survey period. As a result of these developments the deficit in the goods account increased by Lm21.5 million.

An improvement of Lm4.6 million in net receipts on the services account partly compensated for the deterioration in the goods account. This was underpinned by higher tourist earnings, which advanced by Lm6.8 million, or 3.4 per cent, to Lm203.5 million during the period under review. Meanwhile, payments by Maltese tourists abroad remained unchanged at Lm59.5 million, from the corresponding 2003 period.



The improvement in the travel account was partly offset by an increase of Lm3.6 million in payments overseas on transportation services, partly reflecting the increase in imports of goods. Meanwhile net flows from other services improved by Lm1.3 million. Lower net receipts on Government services were more than offset by higher receipts on communication services, other business services and lower payments on royalties and license fees.

The Income Account and Current Transfers

During the period under review, net income from abroad deteriorated by Lm56.3 million from a net inflow of Lm30.7 million in the first nine months of 2003 to a net outflow of Lm25.6 million. The net outflows in the investment income account was the result of higher reinvested earnings (i.e. earnings by foreign owned companies which were reinvested in Malta) and lower interest receipts.

The main item in the income account is the income from direct investments. During the Survey period, outflows in the form of re-invested earnings increased by Lm37.2 million reflecting the increase in profits, particularly in the banking sector. It is pertinent to note that although re-invested earnings do not constitute a physical outflow of funds abroad, they are recorded as an outflow of direct investment income and an offsetting inflow of direct investment in the capital and financial account of the balance of payments. Payments of dividends and

Balance of Payments Current Account							
Table 7.8	Lm million						
	2001		2002		2003		2004
	Jan/Sep	Oct/Dec	Jan/Sep	Oct/Dec	Jan/Sep	Oct/Dec	Jan/Sep
GOODS AND SERVICES							
Exports of Goods and Services	1,066.3	332.8	1,117.3	375.3	1,058.9	361.6	1,055.6
Imports of Goods and Services	1,112.6	375.0	1,089.2	384.4	1,139.1	379.8	1,152.7
Goods and Services Account	-46.3	-42.2	28.1	-9.1	-80.2	-18.2	-97.1
INCOME							
Income Received	291.8	81.1	281.9	79.3	245.3	86.1	225.9
Income Paid	276.1	85.7	251.3	107.3	214.5	101.4	251.5
Income Account	15.7	-4.6	30.6	-28.0	30.7	-15.3	-25.6
CURRENT TRANSFERS (Net)							
General Government Transfers	4.1	-0.5	1.8	1.4	7.3	1.6	10.7
Private Transfers	-1.5	1.7	-12.5	-6.8	-18.9	-10.4	-32.5
Total Net Current Transfers	2.6	1.2	-10.7	-5.4	-11.6	-8.8	-21.8
Balance on Current Account	-28.0	-45.6	48.0	-42.6	-61.0	-42.3	-144.4
Source: National Statistics Office							

distributed branch profits fell by Lm4.3 million. As a result, net outflows of income on equity investments increased by Lm31.6 million. Meanwhile, net receipts by way of interest income declined by Lm24.2 million. This was primarily attributable to a fall in interest receipts of Lm19.7 million which exceeded the increase in interest payments abroad of Lm4.6 million. On the other hand, net inflows by way of employee compensation fell by Lm0.5 million.

The negative balance on current transfers has continued to increase and in the first nine months of 2004 the deficit stood at Lm21.8 million, up from Lm11.6 million a year earlier. The developments in current transfers are shown in Table 7.8. Higher private transfers sent abroad caused the net outflow of private transfers to increase by Lm13.6 million. This was partly compensated by a fall of Lm1.4 million in Government transfers abroad and an increase of Lm2.0 million in Government transfers received.

The Capital and Financial Account

The excess of investment over national savings requires the flow of funds from abroad and/or the depletion of foreign exchange reserves. The following provides an analysis of capital flows and the composition of such flows in Malta, as reflected in the financial account of the balance of payments. The analysis relates to annual flows from 2000 till 2003. Data for the January-September period of 2004 were not yet available by the time of publication of this Economic Survey. Table 7.9 shows the capital and financial flows as a percentage of GDP.

Despite another consecutive current account deficit, the accumulation of reserves has generally continued, albeit at a lower rate. During 2003, the stock of reserve assets increased by 3.0 per cent of GDP at current market prices. This indicates that capital inflows continued to finance the excess investment over national savings. The flows recorded in 2002 and 2003 were partly influenced by the Investment Registration Scheme launched in January 2002 and extended in 2003. This affected mostly the value of portfolio investment assets and currencies and deposits held by Maltese residents.

Following the net outflow of direct investment in 2002 related to a loan repayment made by a foreign owned bank to its parent company overseas, a positive balance was recorded in 2003. Net foreign direct investment in 2003 stood at 5.4 per cent of GDP. This was mainly the result of Lm89.8 million in new equity capital and Lm15.8 million in re-invested earnings. Figures for 2003 partly reflected the opening of a subsidiary of a foreign bank in Malta as well as a loan taken by

Current, Capital and Financial Flows*
(per cent of GDP)

Table 7.9

	2000	2001	2002	2003
Current Account	-12.4	-4.3	0.3	-5.6
Capital Account	0.5	—	0.2	0.1
Financial Account excl. Reserves	5.4	3.7	4.8	3.2
Net Foreign Direct Investment	15.5	6.2	-10.2	5.4
Net Portfolio Investment Equity Flows	1.8	-4.2	1.5	-0.3
Net Portfolio Debt Flows	-21.0	-8.5	-10.5	-31.4
Net Financial Derivatives	...	...	...	0.5
Net Other Investment Flows	9.1	10.2	24.1	29.0
Reserve Assets	5.8	-6.7	-6.9	-3.0
Net Errors and Omissions	0.8	7.2	1.6	5.3

* A positive sign represents a decrease in assets or increase in liabilities.
A negative sign represents an increase in assets or a decrease in liabilities

Source: National Statistics Office

a resident non-bank firm from abroad. Moreover, inflows of direct investments during 2003 were sustained by the sale of shares to a foreign owned company in the telecommunications sector. Meanwhile around Lm11 million were invested by Maltese nationals abroad during 2003.

The significant net outflow of funds abroad in the form of portfolio investment flows continued in 2003. Most of the outflow recorded is in the form of debt flows rather than equity flows. It mainly consists of holdings by Maltese banks of foreign assets typically in the form of bonds. In 2003 net outflows of portfolio debt were 31.4 per cent of GDP compared to 10.5 per cent in 2002. Net outflows of portfolio equity flows represented 0.3 per cent of GDP. Data for 2003 also includes, for the first time, a measure of financial derivatives. Net foreign liabilities in the form of financial derivatives represented 0.5 per cent of GDP.

During 2003, other investment assets held by domestic banks in the form of long term loans and advances to non-residents increased by Lm230.0 million. However, assets in the form of currency and deposits and other assets fell by Lm210.6 million. Meanwhile liabilities in the form of borrowings, mostly of a long-term nature, increased by Lm358.4 million in 2003. This was more than offset by a fall of Lm388.5 million in liabilities in the form of currency and deposits held by foreign residents with domestic banks. On the other hand, other short-term liabilities increased by Lm572.8 million. Transactions in the

other investment account typically reflect balance sheet transactions of the banking system and thus subject to significant fluctuations.

As a result of these developments, the net increase in liabilities which constitutes an inflow of funds (borrowings) from abroad exceeded the net increase in assets which constitutes an outflow of funds abroad. Net inflows of capital, excluding reserves and including the capital account, stood at 3.3 per cent of GDP in 2003 whilst errors and omissions represented a further net inflow of 5.3 per cent of GDP. The resulting total capital inflows of 8.6 per cent of GDP were used to finance the current account deficit, with the remaining balance constituting an increase in foreign reserves.

The International Investment Position

Table 7.10 shows Malta's international investment position, which represents the stock of external financial assets minus the stock of external liabilities. The position also includes valuation changes from movement in exchange rates and prices and other adjustments. Data for 2003 are provisional estimates and warrant caution in their use and interpretation.

International Investment Position								
Table 7.10								Lm million
	1996	1997	1998	1999	2000	2001	2002	2003*
Direct Investment Abroad	38.8	54.7	64.3	76.3	88.9	118.1	111.2	120.8
Direct Investment in Malta	303.6	335.3	443.2	771.6	1,044.3	1,157.7	973.4	1,074.2
Assets								
Portfolio Investment Equity	1.7	6.0	2.5	76.2	74.8	54.1	118.7	161.9
Portfolio Investment Debt	539.6	496.7	562.1	794.8	1,159.9	1,313.6	1,617.1	2,231.2
Liabilities								
Portfolio Investment Equity	...	...	2.7	79.9	114.9	17.8	21.0	19.8
Portfolio Investment Debt	82.3	110.2	144.6	132.9	134.4	137.0	126.2	123.8
Financial Derivatives Assets	...	...	...	...	...	...	...	1.8
Financial Derivatives Liabilities	...	...	...	...	...	...	...	10.8
Other Investment Assets	575.9	950.8	1,757.3	2,405.0	2,508.0	2,034.6	2,410.7	2,476.3
Other Investment Liabilities	1,008.6	1,339.7	2,138.9	2,827.1	3,077.1	2,736.4	3,376.8	3,923.5
Reserves	554.1	561.7	640.0	740.3	644.1	760.4	880.9	935.5
International Investment Position	315.6	284.6	296.7	281.0	105.2	231.9	641.2	784.5
* Provisional estimates								
Source: National Statistics Office								

The transactions that have taken place in 2003 have already been described in detail in relation to the flows in the capital and financial account. Meanwhile, the composition of portfolio assets of Maltese residents held abroad continues to be biased towards debt rather than equity investments. They are mostly made up of foreign bonds and notes held by the domestic banking system. However, the share of equities in total assets has increased from 0.3 per cent of total portfolio investment assets in 1996 to 6.8 per cent in 2003. Private investors hold most of these equity securities. Meanwhile, the share of portfolio investment liabilities that are equity securities has declined from a high of 46.1 per cent in 2000 to 13.8 per cent in 2003.

The stock of assets and liabilities in the form of other investments typically reflect transactions by foreign banks which take deposits from and lend to non-residents. Assets in the form of loans to non-residents and liabilities in the form of borrowings from abroad are typically of a long-term nature. However, whereas loans represented around 70 per cent of total other investment assets, borrowings represented only about 25 per cent of total other investment liabilities in 2003. Meanwhile, currency and deposits and other investment liabilities constituted around 75 per cent of other investment liabilities. On the other hand, the remaining 30 per cent of assets are mostly made up of currencies and deposits. Therefore, it is possible to conclude that other investment assets are more biased towards the holdings of long term foreign securities whereas other investment liabilities are more biased towards currencies and deposits.

Reserve Adequacy Ratios								
Table 7.11	1996	1997	1998	1999	2000	2001	2002	2003
Imports of Goods and Services (Lm million)	1,186.4	1,173.5	1,248.1	1,371.9	1,740.1	1,487.6	1,473.6	1,518.8
Monthly Import bill (Lm million)	98.9	97.8	104.0	114.3	145.0	124.0	122.8	126.6
Gross International Reserve Coverage (months)*	5.6	5.7	6.2	6.5	4.4	6.1	7.2	7.4
Monetary Base (Lm million)	451.9	485.2	506.1	543.3	564.5	567.6	612.8	623.3
Gross Reserves as a ratio of Monetary Base (per cent)*	122.6	115.8	126.5	136.3	114.1	134.0	143.8	150.1
* 2003 figures are based on estimates of the stock of exchange reserves as documented in Table 7.10								
Source: National Statistics Office Central Bank of Malta								

Foreign Reserves

The deficit registered in the current account of the balance of payments in recent years was generally more than offset by capital inflows and hence reserves tended to continue to accumulate. The stock of reserves increased from Lm554.1 million in 1996 to Lm935.5 million in 2003. Reserve accumulation is important in order to maintain confidence in the currency, particularly in the context of Malta's exchange rate peg and in light of the liberalised capital account regime which Malta is now operating in.

An indication of the adequacy of foreign reserves in Malta is provided by the ratio of reserves to the monthly value of total imports of goods and services as shown in Table 7.11. The stock of reserves covers more than 7 months of imports and is thus significantly in excess of the three-month import coverage typically used as a ratio of reserve adequacy. Another indicator of reserve adequacy is provided by the ratio of foreign reserves to the monetary base, which increased to 150.1 per cent in 2003.