



Assessment of the Macroeconomic Forecasts Underlying the Annual Progress Report 2026

June 08, 2026

Assessment Report

No. 01/2026

Malta Fiscal Advisory Council
New Street in Regional Road, Msida, Malta
Phone: +356 21312442 | Website: www.mfac.org.mt

The Malta Fiscal Advisory Council is an independent institution established under the Fiscal Responsibility Act (2014), which aims to contribute to stronger fiscal governance in Malta and offer assurance about the quality of the official economic and fiscal projections and fiscal sustainability through independent analysis and advice.

This assessment of the macroeconomic projections is undertaken in terms of Article 13, point 3(a), which states that the Fiscal Council shall “*endorse, as it considers appropriate, the macroeconomic and fiscal forecasts prepared by the Ministry for Finance and provide an assessment of the official forecasts*”.

This Report was prepared based on the information available until April 16, 2026

INTRODUCTION

- 1. Every year, Member States are required to submit an Annual Progress Report outlining progress in the implementation of the commitments set out in their Medium-Term Fiscal Structural Plan (MTFSP) for assessment by the European Commission.** Malta submitted its first [MTFSP on September 20, 2024](#), setting an average annual growth limit of 5.9% for net nationally financed primary expenditure over the 2025 – 2028 period.
- 2. The Ministry for Finance (MFIN) submitted this year's Annual Progress Report (APR26) on 30 April 2026. In this Report, the Malta Fiscal Advisory Council (hereinafter referred to as 'Council' or 'MFAC') presents its assessment and endorsement of the official macroeconomic projections within the APR26 for the year 2026.** These forecasts update the macroeconomic outlook previously published by the MFIN in the [Draft Budgetary Plan 2026](#) (DBP26), endorsed by the Council in October 2025, and the projections underpinning the [Medium-Term Fiscal Strategy 2025-2028](#), endorsed in January 2026. The initial draft of the macroeconomic projections was submitted to the Council on 17 April 2026, followed by the transmission of finalised figures on 27 April 2026. Potential output and output gap estimates were submitted on 28 April 2026. The cut-off date for the underlying data and assumptions of these macroeconomic projections is 16 April 2026.
- 3. The legal basis for this Assessment is [Directive 2024/1265](#) Article 8a(5) and Article 13(3)(a) of the [Fiscal Responsibility Act](#) (Cap. 534 of the Laws of Malta).** The Directive mandates Member States to empower independent fiscal institutions to produce, assess or endorse annual and multiannual macroeconomic forecasts. Furthermore, the Fiscal Responsibility Act prescribes that the MFAC shall “endorse, as it considers appropriate, the macroeconomic and fiscal forecasts prepared by the Ministry for Finance and provide an assessment of the official forecasts.” The forecasts included in the APR26 are considered official forecasts within the meaning of the Fiscal Responsibility Act.

- 4. The methodology used by the MFIN to generate macroeconomic estimates and fiscal projections remained broadly unchanged from previous forecast rounds.** The MFIN relies primarily on [STEMM \(Short-Term Quarterly Economic Forecasting Model\)](#) to produce its macroeconomic projections. The MFIN routinely revises the model equations to ensure they reflect the latest macroeconomic underpinnings and relationship developments that impact the Maltese economy and the external sector. The model forecasts are based on several exogenous assumptions about the external economy produced by Consensus Economics and the European Central Bank (ECB). The model also enables expert judgement based on ad-hoc data and routine discussions with key stakeholders. These are particularly useful when forecasting volatile economic drivers like gross fixed capital formation and specific industries such as tourism.

MACROECONOMIC SCENARIO UNDERLYING THE ANNUAL PROGRESS REPORT 2026

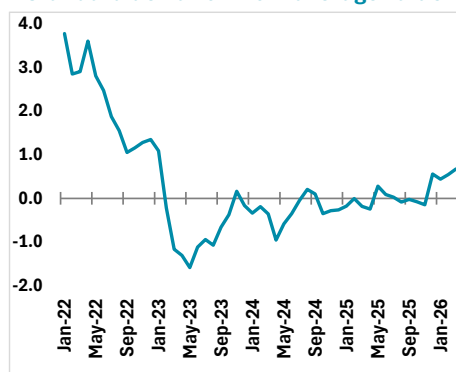
- 5. The global economy exceeded expectations in 2025, proving more resilient than anticipated to shifts in US trade policy and rising trade frictions. At the start of 2026, this momentum was expected to continue.** The near-term outlook was supported by lower effective tariff rates, reflecting new regional trade arrangements and tariff exemptions, while global trade and investment were expected to remain robust, underpinned by continued spending on AI-related technologies. In Europe, a more expansionary fiscal stance in Germany, centred on infrastructure and defence spending, together with resilient labour market conditions, supported activity in 2025 and was expected to provide further impetus in 2026. Real GDP growth in the European Union strengthened in the second half of 2025, and high-frequency indicators suggested that this momentum carried into 2026. In particular, the European Commission's Economic Sentiment Indicator for January and February 2026 rose to its highest level since the post-pandemic recovery in 2022, with improvements recorded across most sectors, especially in industry, where export order books improved.
- 6. However, the economic outlook changed materially following the outbreak of war in the Middle East at the end of February.** The

conflict disrupted energy infrastructure in the region and impaired maritime transport through the Strait of Hormuz, one of the world's most important energy trade routes, through which around a quarter of the world's seaborne oil and liquefied natural gas exports normally pass.¹ As a result, the average daily price of Brent crude oil rose to USD108.5 per barrel after the onset of the conflict, more than 50% above the level prevailing at the end of February. European natural gas prices also increased sharply, rising by almost 60%.

Chart 1: Global Supply Chain

Pressure Index

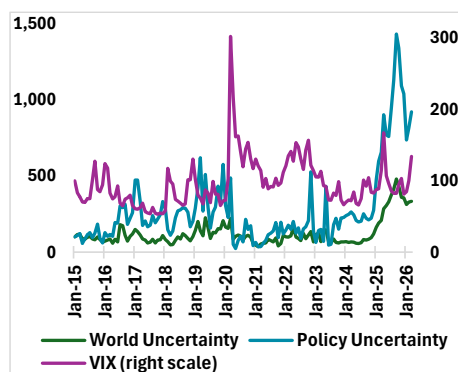
Standard deviation from average value



Source: New York FED

Chart 2: Uncertainty Indicators

Index, January 2015 = 100



Source: FRED; Ahir, Bloom, and Furceri 2022^{2,3}

Note: Last observation is March 2026

Given the region's key exporting role in fertilisers and other agricultural inputs, the conflict also entails downside risks to global food production and upward pressures on food prices. These developments are expected to renew supply chain pressures, leading to higher transport and production costs, weighing down on global economic activity. The Global Supply Chain Pressure Index increased to +0.68 in March 2026, the highest level since January 2023 (**Chart 1**), as pressures stemming from recent geopolitical tensions are compounded to earlier pressures from tariff volatility and import frontloading. Higher prices are set to reduce household purchasing power, which coupled with elevated uncertainty (see **Chart 2**) are likely to restrain global consumption and investment.

¹ In this report, the terms "war" and "conflict" are used interchangeably for ease of reference, in line with the IMF's [World Economic Outlook](#).

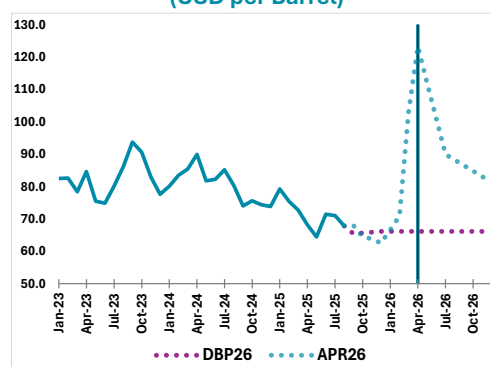
² World uncertainty indicators are sourced from: Ahir, H., Bloom, N. and Furceri, D. (2022) 'The world uncertainty index', NBER Working Paper Series.

³ The VIX index measures volatility in the US equity market

Moreover, the increase in inflationary pressures has contributed to a tightening in financial conditions, with bond yields rising across most economies as markets now expect central banks to take a more restrictive monetary policy stance. Against this backdrop, major international institutions have revised down their growth projections while marking up their inflation forecasts (see [Box A: The impact of the conflict in the Middle East on Malta's economic outlook](#)).

7. Within this international context, the MFIN incorporates specific exogenous assumptions into its modelling framework (see [Table 1 for the macroeconomic forecasts underpinning the APR26](#)). For 2026, real GDP among Malta's main trading partners is assumed to increase by 1.3%, representing a downward revision of 0.1 percentage points (pp) compared to the Autumn forecast round. In contrast, world prices are assumed to increase by 2.9% in 2026, an upward revision of 1.8 pp. The euro is expected to appreciate further against both the United States Dollar (USD) and the British Pound (GBP) over the forecast horizon. However, the projected appreciation against the USD is more moderate than that envisaged in the Autumn forecast round, reflecting safe haven flows into the dollar amid heightened uncertainty.

**Chart 3: Brent Crude Oil Price Assumption
(USD per Barrel)**



Source: US Energy Information Administration, Consensus Economics

Note: The data for the dotted blue line (APR26) reflect the assumption from the April issue of the Consensus Forecasts.

Meanwhile, global oil prices are assumed to remain at a relatively high level in the near term due to the supply shock from ongoing geopolitical tensions, averaging \$93.8 per barrel in 2026. Overall, the oil price assumption for 2026 has been revised upwards by 41.8% from the assumptions underpinning the DBP26 projections (see [Chart 3](#)).

Although gas prices are not incorporated into the forecast assumptions, recent developments remain noteworthy. European natural gas prices rose sharply following attacks on key energy infrastructure in the Persian Gulf, with prices increasing by 57.9% in March as supply disruptions intensified. However, futures markets suggest that gas prices are expected to moderate by the end of 2026 as supply volumes are expected to recover.

Table 1: Macroeconomic Forecasts underlying the Annual Progress Report 2026

	Actual		Forecast
	2024	2025	2026
Real economic activity (% change)			
Private final consumption expenditure*	5.8	3.3	3.9
Public consumption expenditure	4.8	5.9	5.7
Investment	4.0	-0.1	6.5
Exports of goods and services	6.3	4.5	2.9
Imports of goods and services	5.2	4.4	3.6
GDP	6.2	4.0	3.7
Contribution to real GDP growth (in pps.)			
Final domestic demand	4.2	2.5	3.8
Inventories	-0.2	0.4	0.0
Net exports	2.2	1.0	-0.1
Labour market			
Total employment (% change)	5.1	3.9	3.6
Unemployment rate (% of labour supply)	3.2	3.1	3.2
Prices and costs (% change)			
GDP deflator	4.1	2.2	2.3
HICP	2.4	2.4	2.9
Nominal compensation per employee	7.6	4.2	4.4
Labour productivity (real GDP per person employed)	1.2	0.0	0.1
Real Unit labour costs	2.1	1.9	1.9
Business cycle			
Potential GDP (% change)	5.5	5.1	4.7
Output Gap (as a % of potential GDP)	1.0	-0.1	-1.1
Exogenous assumptions (% change)			
Weighted WGDP by trading activity	0.7	0.9	1.3
Oil prices (USD per barrel)	80.5	69.1	93.8
EUR/USD exchange rate	1.0821	1.1293	1.1603
EUR/STG exchange rate	0.8466	0.8566	0.8662

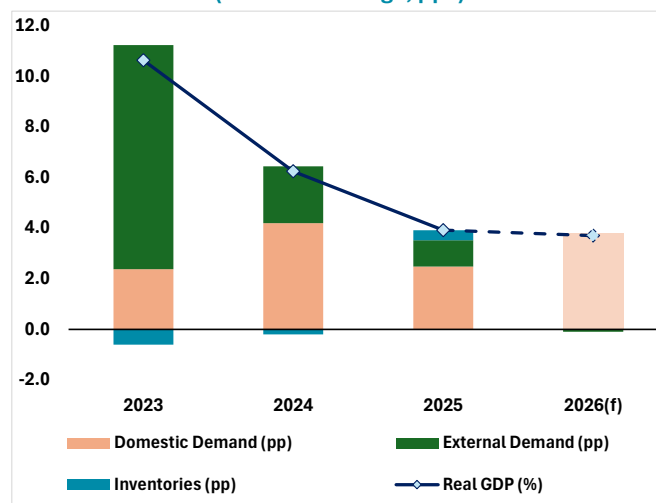
Source: Ministry for Finance & NSO

Note: GDP Data for 2024 and 2025 are based on statistics published by the National Statistics Office on February 26, 2026 (News Release 033/2026), while figures for 2026 represent the macroeconomic forecasts prepared by the Ministry for Finance. The exogenous assumptions are based on the Consensus Forecast of April 2026. The potential output growth and output gap estimates are derived from estimates by the Ministry for Finance using the EU-CAM methodology.

*Includes Non-Profit Institutions Serving Households (NPISH).

8. According to the MFIN's macroeconomic forecasts, real GDP is projected to increase by 3.7% in 2026, entirely driven by domestic demand which is expected to make a positive contribution of 3.8 pp (Chart 4). Private consumption growth is projected to accelerate to 3.9%, supported by a strong labour market and higher incomes, particularly following recently concluded collective agreements in segments of the public sector. Revisions to parental income tax brackets, effective from the start of 2026, are also expected to positively impact households' disposable incomes.

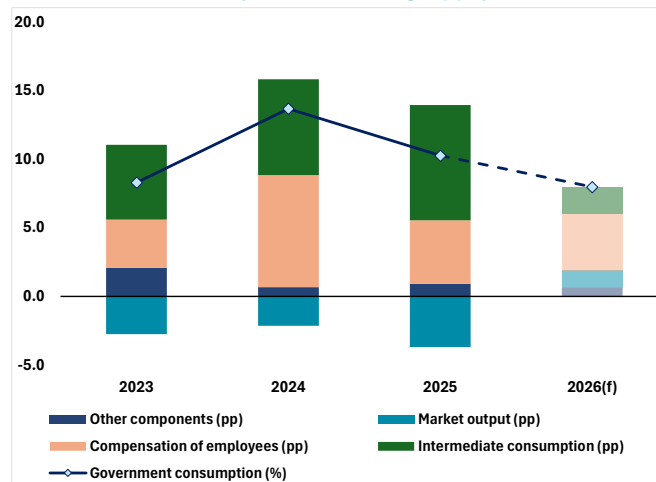
Chart 4: Real GDP growth and its main contributors
(% annual change, pps)



Source: NSO, MFIN

Government consumption expenditure, which grew by 5.9% in 2025, is expected to remain robust in 2026, albeit with a slight moderation. In real terms, it is projected to increase by 5.7%, reflecting an upward revision of 1.1 pp from the previous forecast round. In nominal terms, government consumption is set to increase by 8.0%, mostly driven by compensation of employees which is projected to contribute 4.1 pp, while the contribution of intermediate consumption is expected to ease to 1.9 pp in 2026 (Chart 5).

Chart 5: Breakdown of general government consumption
(% annual change, pps)



Source: NSO, MFIN

Gross fixed capital formation is projected to increase by 6.5% in 2026, marking a substantial upward revision from the Autumn forecast, which had anticipated a contraction of 0.9%. This revision is primarily driven by a stronger public investment profile, which is expected to increase by 18.6% in 2026 in nominal terms, while private investment is also projected to record robust growth of 7.0%.

9. **Net exports are projected to exert a small negative contribution to GDP growth, subtracting 0.1 pp, as imports are expected to outweigh exports.** Export growth is projected to moderate from 4.5% in 2025 to 2.9% in 2026, marking a significant downward revision from the Autumn forecast, which had anticipated growth of 4.5%. This revision reflects the impact of higher transport and production costs, as well as supply chain disruptions affecting disposable income and economic activity in Malta's main trading partners. The resulting slowdown in Malta's external markets is, in turn, expected to dampen foreign demand for Maltese exports. At the same time, the MFIN projections are underpinned by a recovery in goods exports, while services are expected to remain resilient, although to a lesser extent compared to the Autumn projections, supported in part by continued strength in tourism. Indeed, between January and February, inbound tourist had increased by 19.9% when compared to the same period in the previous year.

Imports are projected to increase by 3.6% in 2026, down from 4.4% in 2025. This marks a marginal upward revision of 0.1 pp from the Autumn forecast. Imports growth is expected to be mainly driven by importation of goods. The import profile reflects stronger domestic demand, particularly government consumption and investment, the latter being relatively import-intensive. Moreover, the assumed appreciation of the euro should also support imports over the forecast horizon, especially for industrial and consumer goods.

10. Inflation is projected to rise to 2.9% in 2026, representing an upward revision of 0.7 pp from the MFIN's Autumn forecast, primarily driven by stronger imported price pressures. Core inflation, which excludes energy and unprocessed food, is expected to increase to 2.8%. Consequently, the MFIN projections are underpinned by persistent underlying price pressures in services, consistent with the expected transmission of higher imported inflation, amidst strong domestic demand. Meanwhile, food prices are also expected to exert significant upward pressure. Despite upward pressure from rising international fuel prices, energy prices are expected to have a neutral impact on headline inflation, reflecting the government's commitment to maintaining fixed energy prices through energy subsidies.⁴

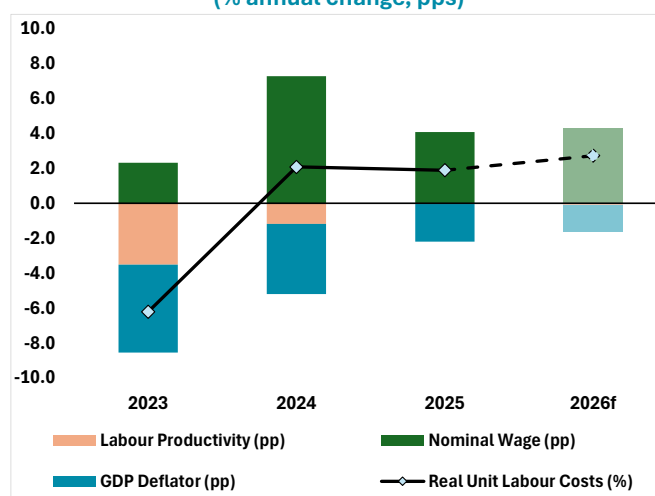
11. The labour market is expected to remain buoyant in 2025, with full-time equivalent employment projected to grow by 3.6%, corresponding to an increase of 12,326 workers. At the same time, the unemployment rate is forecast to remain low at 3.2%, rising by just 0.1 pp compared to 2025. Malta's labour force participation rate (persons aged 15-64 years) reached 82.6% in 2025, significantly exceeding the EU average of 75.7%. Given Malta's combination of low unemployment and high labour force participation, further employment growth in 2026 is likely to also depend on inward migration.

12. Although labour market conditions are expected to remain strong in 2026, labour productivity is projected to grow only marginally by 0.1%, falling short of the EU average productivity growth of 1.0% as

⁴ The fiscal implications of higher international fuel prices are further explored in the upcoming report of the MFAC on its assessment of the fiscal forecasts within the Annual Progress Report 2025

projected in the European Commission’s Autumn 2025 Forecast. Meanwhile, compensation per employee is expected to rise by 4.4%, contributing to an increase in real unit labour costs (ULCs) of 1.9%. In contrast, real ULCs in the EU are forecast to remain broadly stable. Although Malta’s GDP growth is projected to outpace the EU average, supporting continued wage increases, the absence of corresponding productivity gains raises concerns about Malta’s competitiveness. This comes after two successive years of increases in real unit labour costs (see [Chart 6](#)).

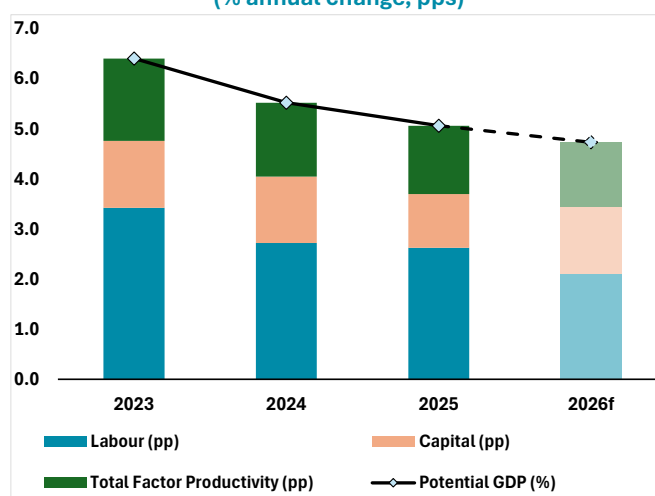
Chart 6: Contributions to Real Unit Labour Costs
(% annual change, pps)



Source: NSO, MFIN, MFAC estimates

Note: The chart shows the decomposition of real unit labour costs, approximated using log differences. Higher real unit labour costs can result from higher nominal wages, weaker labour productivity, or lower producer prices measured by the GDP deflator. Therefore, negative values for labour productivity in the chart reflect productivity gains and therefore imply downward pressure on real unit labour costs.

Chart 7: Drivers of potential output growth
(% annual change, pps)



Source: MFIN

13. The MFIN is anticipating a negative output gap of -1.1% in 2026, as potential output growth is projected at 4.7%, exceeding real GDP growth of 3.7%. The expected slowdown in potential output growth from 5.1% in 2025, is primarily driven by a weaker contribution from labour, which is forecast to decline from 2.6 pp in 2025 to 2.1 pp in 2026. The contribution from total factor productivity (TFP) is projected to remain broadly stable, contributing 1.3 pp in 2026. Meanwhile, the contribution from capital is expected to increase from 1.1 pp in 2025 to 1.3 pp in 2026. This reflects stronger capital accumulation, driven by investment growth (see [Chart 7](#)).

COUNCIL'S RISK ASSESSMENT

14. After considering the inherent risks and prevailing uncertainties surrounding the macroeconomic outlook, the Council considers that the macroeconomic forecasts for 2026, prepared by the MFIN in the context of the APR26, fall within the range deemed endorsable by the Council. In reaching this assessment, the Council also evaluated the forecasts in light of the MFIN's historical forecast performance (see [Box B: Assessing Macroeconomic Forecast Uncertainty Using Past Forecast Errors](#)) and against the projections produced by other reputable institutions (see [Box E: A Comparison of the MFIN's Macroeconomic Forecasts with Other Institutions](#)). Also, in reaching its assessment, the Council has made use of its recently developed heatmap tool to assess the forecasts in relation to the recent data (see [Box D: Updating the Heatmap for the Maltese Economy](#)). Whilst the macroeconomic forecasts have been deemed as plausible, the Council's assessment differs from that of the MFIN regarding certain elements of the growth composition, particularly the projections for investment and general government consumption expenditure. The Council also holds differing views regarding the estimates of potential output and the resulting output gap.

15. The Council considers that the investment targets for 2026 are subject to downside risks, particularly those surrounding the public investment outlook. This assessment is based on developments observed over the past three years, during which actual public investment consistently fell short of projected levels by an average of around €200 million annually. In addition, government

investment expenditure has remained broadly stable over this period, averaging around €750 million per year. Against this background, the projected level of €900 million for 2026 appears relatively ambitious. The recurring nature of these shortfalls points to persistent implementation challenges, particularly capacity constraints, which continue to weigh on the timely execution of the projected public investment targets.

Conversely, the Council assesses the risks surrounding the private investment outlook for 2026 to be broadly balanced. Although the prevailing geopolitical uncertainty may lead to the postponement of certain investment decisions, this is expected to be partly offset by the investment support measures announced in the latest Budget aimed at promoting digitalisation and business investment. These measures, which include accelerated tax depreciation and investment tax credits for expenditure related to digital technologies, machinery, IT equipment, and cybersecurity, are expected to support additional investment over the coming two years.

16. With respect to government consumption, the Council identifies upside risks to the 2026 projections. This assessment primarily reflects the relatively modest projected increase of 4.1% in intermediate consumption, which over the past three years, recorded an average growth of 16.2%. While the downside risks identified in relation to public investment could partially dampen expenditure growth in some investment-related contractual services classified within intermediate consumption, the Council considers that this effect would not be sufficient to contain growth to the level currently projected. This assessment is further reinforced by persistent demand pressures, particularly in the areas of health and infrastructure, together with continued cost increases associated with general government service contracts.

17. In conclusion, the Council assesses the risks to GDP growth in 2026 as broadly neutral, as the downside risk to gross fixed capital formation is broadly offset by the upside risk to government consumption. The downside risk identified in relation to gross fixed capital formation may also adversely affect the import content associated with such investment activity, which is typically relatively elevated in the Maltese economy.

18. In terms of potential output, the projected widening of the negative output gap from -0.1% in 2025 to -1.1% in 2026 appears to reflect a cyclical slowdown rather than a deterioration in underlying economic fundamentals. Nevertheless, the magnitude of the projected widening appears relatively pronounced. Core inflation (headline inflation excluding energy and unprocessed food) is expected to increase to 2.8%, representing an upward revision of 0.6 pp compared with the previous forecast round. While this revision reflects the passthrough of external supply-side pressures arising from the conflict in the Middle East, domestic conditions also point to firm domestic demand. Labour market dynamics are projected to remain resilient, with employment growth projected at 3.6% in 2026, the unemployment rate remaining close to historical lows, and nominal wages growth remaining solid. Taken together, these developments point to continued tightness in the economy, which appears difficult to reconcile with such a pronounced negative output gap.

CONCLUSION

19. The Council endorses the macroeconomic forecasts for 2026 prepared by the MFIN, as presented in the APR26, while noting certain differences in the composition of growth, particularly with respect to projections for gross fixed capital formation, government consumption. Notwithstanding these differences, the Council considers the forecasts to fall within its endorsable range. The Council also highlights the elevated level of uncertainty surrounding the current international environment, which may bear on the outlook. In its assessment, the Council envisages a somewhat weaker trajectory for investment growth, partly offset by stronger growth in government consumption expenditure. The Council also notes a divergence in its assessment of the projected output gap for the current year. While a cyclical moderation in activity, and consequently some deterioration in the output gap, appears plausible given the weaker external environment, domestic indicators continue to point to resilient underlying demand. This appears difficult to reconcile with the projected sizeable widening of the negative output gap.

20. In view of the growth dynamics projected in the APR26, the Council wishes to put forward the following recommendations to the Ministry for Finance:

Recommendation No. 1: Strengthening the Role of Productivity in Sustaining Economic Growth

The Council favourably notes that, in recent years, Malta has recorded one of the highest rates of economic growth within the European Union, though this has been supported primarily by robust domestic demand. Indeed, this expansion has been supported by a sustained increase in labour demand, which, in the context of historically low unemployment rates and high participation levels, has been increasingly met through inward migration. As a result, Malta's population has grown by approximately 10.4% between 2022 and 2025, equivalent to around 54,000 persons.

While these developments have supported economic activity, including through stronger domestic consumption, they have also contributed to rising pressures on infrastructure, public services, and natural resources. Continued reliance on demographic expansion as a driver of growth will therefore give rise to capacity constraints and exacerbate existing structural pressures. At the same time, labour productivity performance has remained relatively subdued. Notably, in certain periods, including 2016, 2018 and 2019, productivity declined despite strong overall economic growth, pointing to an increasing reliance on labour input which is not reflected in efficiency gains or higher productivity. In this context, the Council emphasises that Malta's economic growth should not continue to rely predominantly on increases in labour supply. A shift towards productivity-led growth is essential to sustain economic performance while alleviating pressures on infrastructure and public resources (see **Box C: Population Increases versus Improvements in Labour Productivity. Who did the heavy lifting?**).

Recommendation No. 2: Reinforcing Productive Investment as a key enabler of Labour Productivity

A key determinant of labour productivity is capital intensity, that is, the amount of capital available per worker. Evidence suggests that Malta's capital intensity remains comparatively low relative to peer economies, limiting the scope for efficiency gains and constraining productivity growth. This highlights the importance of relying less on short-term expenditure, such as consumption, and strengthening the capital base of the economy as a central pillar of a sustainable growth strategy.

Accordingly, the Council recommends that policy efforts be directed towards enhancing labour productivity through a comprehensive and coordinated strategy. In this regard, it is important to distinguish between overall investment levels and the composition of investment. Priority should be given to productive investment, namely investment that directly enhances the economy's productive capacity and efficiency, including in human capital, digital technologies, research and innovation, and advanced infrastructure. While Malta performs relatively well in investment in computer software and databases, investment in research and development remains exceptionally low, with an investment-to-GDP ratio of just 0.3%. Recent policy initiatives aimed at supporting firms' digital uptake, including fiscal incentives for capital investments in digital technologies, move in the right direction and should help broaden the diffusion of productivity-enhancing technologies across the economy.

Complementary measures should also focus on addressing skills mismatches through targeted education and training initiatives, fostering innovation and research activity, and advancing the twin transition towards digitalisation and environmental sustainability. Together, these measures would support a more sustainable, resilient, and productivity-driven growth model.

Box A: The Impact of the Conflict in the Middle East on Malta's Economic Outlook

The escalation of the conflict in the Middle East into direct military confrontation, which started on 28 February 2026, has increased downside risks to the global economic outlook. The shock is concentrated in a region that is central to global energy supply and to the production of key industrial inputs. Importantly, this has led to the effective closure of the Strait of Hormuz, a critical global energy transit route through which around 25% of global seaborne oil trade normally flows. Moreover, almost 20% of the total global volume of liquefied natural gas exports transit the Strait, with limited alternatives to divert energy flows.⁵ Meanwhile, prospects of a rapid recovery in gas production after the end of the conflict has declined, following direct strikes on key energy facilities in Qatar.

While the bulk of these flows is directed to Asian markets, the disruption is having a significant impact on global commodity prices and supply-chains. Market conditions have already tightened, with higher prices and volatility in energy markets. The Brent crude oil price surged from \$71.32 per barrel on February 27 to \$116.63 on April 16. European gas prices (Dutch TTF Gas) also increased markedly, from €32/Mwh to levels closer to €50/Mwh. Moreover, the Gulf region is also a major exporter of key agricultural inputs, including fertilizers, and any restriction in shipments of such products is expected to adversely impact global food supply. At the same time, the closure or restriction of regional airspace and reduced operations at major Gulf aviation hubs could disrupt international passenger and cargo flows, with potential spillovers to tourism, logistics and business travel.

For Malta, the macroeconomic impact is expected to materialise mainly through indirect channels rather than through direct trade exposure. Direct goods exports to the affected region account for a limited share of Malta's total exports. However, the Maltese economy remains exposed to second-round effects. Against this background, this box assesses Malta's direct export exposure to the affected region, identifies the main sectors involved, and discusses the broader indirect channels through which the conflict could affect the domestic economy. The analysis of direct trade exposure is

⁵ International Energy Agency (2026). Strait of Hormuz: Factsheet. Retrieved from <https://www.iea.org/about/oil-security-and-emergency-response/strait-of-hormuz>

limited to goods trade flows, primarily owing to data availability, as bilateral trade data for services are not available for the countries considered.

Direct Trade Exposure

For the purpose of this analysis, the affected region is defined as the countries with direct geographic exposure to the Persian Gulf and the Strait of Hormuz. The core sample comprises the Gulf Cooperation Council (GCC) economies, namely the United Arab Emirates (UAE), Saudi Arabia, Oman, Kuwait, Bahrain, and Qatar, and is extended to include Iraq and Iran. This selection provides a broader regional coverage of countries most directly exposed to the closure of the Strait of Hormuz through their geographic location and energy-export infrastructure. Accordingly, references to the affected region in this box pertain specifically to this group of Gulf-region economies, rather than to the Middle East as a whole.

Malta's direct goods exports exposure to the affected region is limited. In 2025, goods exports to these economies amounted to €84.6 million, accounting for just 2.5% of total goods exports.⁶ This is broadly in line with historical patterns, as over the past decade, exports to the region averaged €68.4 million annually, and generally accounted between 2% and 3% of Malta's total goods exports. Export flows are mainly concentrated to the UAE and Saudi Arabia, which together represent the largest destination within the group. Import exposure is even more limited, with imports from the affected region averaging 0.7% of Malta's goods imports over the past decade. In 2025, imports from the region amounted to €69.9 million, slightly above the decade average of €51.2 million.

At the product level, exports are concentrated in a narrow set of categories ([Table A1](#)). Food and live animals account for the largest share of Malta's exports to the region, amounting to €43.7 million in 2025. This represents 13.6% of total exports in this category, indicating a relatively higher sector-specific exposure despite the limited aggregate impact. Other notable export categories include miscellaneous manufactured articles, valued at €18.6 million and mainly related to exports of printing matter, and chemicals and related products, totalling €12.6 million. However, these made up only

⁶ Even after excluding fuel exports, which largely reflect re-export activity, exports to the selected group of Middle Eastern countries remain lower than 3% of Malta's total goods exports.

2.8% and 1.9% of Malta's total exports in their respective categories, suggesting that the broader export exposure remains contained.

Table A1. Malta: Goods exports to selected Gulf economies in 2025, by product group

	Value (€ millions)	Share of Malta's total exports (%)
Food and live animals	43.7	13.6
<i>Miscellaneous edible products and preparations</i>	37.9	32.9
<i>Cereals and cereal preparations</i>	5.3	44.4
Miscellaneous manufactured articles	18.6	2.8
<i>Printed matter</i>	11.8	3.4
Chemicals and related products	12.6	1.9
<i>Essential oils, perfume and flavour materials</i>	4.3	55.7
<i>Medicinal and pharmaceutical products</i>	4.1	0.8
Machinery and transport equipment	6.8	0.6
Other	2.1	0.4
Beverages and tobacco	0.7	5.9
Total	84.6	2.5

Note: The 'share of Malta's total exports (%)' column reports exports to the selected region as a percentage of Malta's total exports in each product group. Data by product-group is in line with the Standard International Trade Classification (SITC). The "other" category includes: Crude materials, inedible, except fuels; Mineral fuels, lubricants and related materials; Animal and vegetable oils, fats and waxes; Manufactured goods classified chiefly by material; Commodities and transactions not classified elsewhere in the SITC.

Exports within the food and live animals category are highly concentrated in miscellaneous edible products and preparations, which account for almost 87% of food exports to the affected region. More disaggregated data indicate that these exports mainly consist of processed food inputs and additives, including yeast and other micro-organisms, as well as malt extract and food preparations derived from flour, starch, and related ingredients. These products are commonly used in wider food manufacturing processes. Moreover, there is also a high degree of regional exposure in other selected food-related categories, with the selected Gulf economies absorbing 44.4% of Malta's cereal-related exports.

Indirect Channels

Overall, the direct trade channel appears limited at the aggregate level. Malta's exposure is further mitigated by the structure of its export base, with services accounting for around 85% of total real exports. Compared to goods trade, services exports are generally less sensitive to geopolitical tensions and physical disruptions to trade flows. This is particularly the case for "modern services", including financial, information technology, and business services, which are becoming less constrained by geographical barriers and re-alignments, and have benefitted from advances in

technology and digital delivery.⁷ Moreover, 64.2% of Malta's services exports are directed towards the European market.

Malta's main trading partners are Germany, United Kingdom, Italy, the Netherlands, and France.⁸ These economies also appear to have relatively limited direct trade exposure to the affected Gulf region with goods exposure ranging from 1.6% for the least exposed among them to 4.5% for the most exposed. This suggests that indirect spillovers to Malta through direct third-country trade linkages should be contained. However, the broader macroeconomic effects could be more material. Higher energy costs and increased uncertainty, coupled with weaker economic sentiment, are expected to weigh on Malta's main export markets, particularly those with larger energy-intensive manufacturing sectors. At a time when European households are still adjusting to earlier energy price shocks, renewed increases in energy and transport costs could reduce real disposable income and dampen consumer spending. Forecast revisions already point to a weakening outlook in some of Malta's main trading partners. According to Consensus Economics, growth forecasts for 2026 have been revised down for several key export markets, with the adjustment particularly pronounced for Germany. Consensus forecasts for Germany were lowered by 0.4 pp between February and April 2026. This is relevant for Malta, given that Germany accounts for around 20% of Malta's goods and services exports.

Tourism could also be adversely affected by the conflict in the Middle East. Lower real income in key source markets may weigh on discretionary spending, including travel demand. At the same time, Malta could benefit from some tourism diversion if war-related risks reduce demand for competing destinations in the Eastern Mediterranean. However, on balance, risks remain tilted to the downside, especially if the conflict is prolonged, with sustained disruptions to jet fuel availability in Europe.

Another important transmission channel is likely to be imported inflation. The increase in fuel costs, insurance premia, and risk-related shipping charges is already translating into higher freight rates (see [Chart A1](#)). The Baltic Dry Index increased by more than 20% between February and mid-

⁷ For more information see: International Monetary Fund (2026). Services trade: An emerging engine for global growth. World Economic Outlook, April 2026.

⁸ Based on export trade data of goods and services from balance of payments statistics.

April, and pressures could intensify further as higher bunker fuel cost are gradually incorporated into annual shipping contracts. Given Malta's dependence on imported goods and maritime transportation, this is expected to feed into imported inflation of consumer goods.

Chart A1: Freight Cost – Baltic Dry Index
(Index)

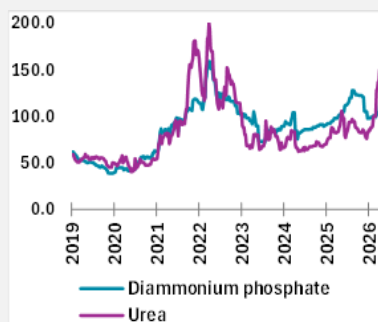


Source: UN Trade and Development

Note: The Baltic dry index is a shipping and trade index that tracks the cost of transporting raw materials, representing different sizes of dry bulk carriers.

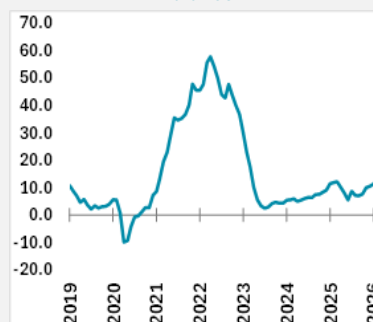
Moreover, higher energy costs are expected to pass through the global economy, pervading along industrial processes and supply-chains. Energy is a key input in transport, manufacturing and food production. If disruptions persist and energy prices remain elevated, higher input costs could gradually be transmitted to producer and consumer prices. Meanwhile, fertiliser prices have also increased sharply, by as much as 50%, as supply disruptions in the Gulf region continue to intensify pressures on agricultural production costs and global food prices ([Chart A2](#)). Price pressures in the European industry have already started to re-emerge, although they remain muted compared to the shock in 2022-2023. Producer prices increased by 1.6% in March, compared with increases of over 20% recorded during 2022. Selling price expectations have also ticked up in April but remain short of the levels seen during the supply-shock from the war in Ukraine ([Chart A3](#)). Consequently, even though Malta's fixed energy-price policy is expected to shield households and firms from direct exposure to higher international energy costs, the fact that Malta sources around 60% of its goods imports from EU countries, higher pipeline pressures in Europe are likely to spill over into Malta through imported inflation.

Chart A2: Fertilizer Prices
Index, 27 Feb = 100



Source: UN Trade and Development

Chart A3: Selling price expectations for the months ahead - Industry Balance



Source: European Commission

Elevated uncertainty may also weigh on domestic demand. Firms with greater exposure to global trade and energy-intensive activities may postpone investment decisions until supply conditions and cost pressures become clearer. Households may also respond by increasing precautionary savings and reducing discretionary spending. At the same time, stable energy prices through government subsidies help in alleviating some of this uncertainty on businesses and households, while limiting second-round effects. However, such support comes at a fiscal cost or re-prioritisation of expenditure, especially if international energy prices remain elevated for a prolonged period. These fiscal implications are considered in more detail in the MFAC's fiscal assessment, presented in the forthcoming report.

Conclusion

Overall, Malta's direct trade exposure to the affected region is limited, both in terms of goods exports and imports. However, the concentration of exports in some food-related categories suggests that some firms may be more exposed to disruptions in regional demand and logistics. The broader macroeconomic impact is therefore expected to arise mainly through indirect channels, including higher energy and food commodity prices, imported inflation, weaker demand in key European export markets, and increased uncertainty affecting tourism, investment and consumption. While government support measures may cushion the immediate pass-through of energy prices to households and firms, a prolonged conflict would increase fiscal costs and could weigh more materially on the economic outlook if expenditure is shifted away from more productive spending, particularly investment.

Box B: Assessing Macroeconomic Forecast Uncertainty Using Past Forecast Errors

Forecasting inherently involves uncertainty. Macroeconomic projections are based on a set of underlying assumptions and are subject to a range of both upside and downside risks, which may at times be asymmetrically distributed. This is particularly relevant in the context of a small and open economy such as Malta, where developments in the external environment can have a disproportionate impact on domestic outcomes. As a result, predicting future economic developments is subject to a relatively high degree of uncertainty, and it is not possible to fully characterise the distribution of possible outcomes *ex ante*.

Despite this, macroeconomic projections are typically presented as single, or “point”, estimates. However, it is highly unlikely that realised outcomes coincide exactly with these point forecasts, except by chance. It is therefore essential to complement such estimates with an assessment of the uncertainty surrounding them, both qualitatively and quantitatively. This allows policymakers to better understand the risks to the baseline scenario and the likelihood of alternative economic outcomes.

A commonly used tool to convey such uncertainty is the fan chart, which provides a visual representation of the probability distribution around a central forecast. By presenting a range of possible outcomes with associated probabilities, fan charts illustrate not only the degree of uncertainty surrounding projections, but also the balance of risks. As such, they have become an established communication device among central banks and international institutions, including the European Central Bank and the International Monetary Fund, to enhance transparency and inform policy discussions.

The construction of fan charts in this analysis builds on and updates with recent data, the empirical assessment of forecast performance presented in the MFAC’s working paper “Evaluating the Macroeconomic Forecasting Performance of the Ministry for Finance and Employment”.⁹ That study finds

⁹ Davison, K., Camilleri, G., & Spiteri, K. (2024). Evaluating the Macroeconomic Forecasting Performance of the Ministry for Finance and Employment. *Malta Fiscal Advisory Council*, (Working Paper 01/2024), Working Paper 01/2024.

that, while the Ministry's forecasts are generally unbiased over the medium term, forecast errors exhibit non-negligible variability and, in certain cases, asymmetries. In particular, the analysis highlights that forecast errors tend to widen with the forecast horizon and may display skewness, reflecting the presence of asymmetric risks around the baseline projections.

Building on these findings, the present analysis uses historical forecast errors to quantify the uncertainty surrounding GDP projections. Forecast errors (computed as Forecast – Actual) are computed on the basis of the MFIN's Spring forecasts for year t , covering a sample period spanning from the first Convergence Programme (2004–2007) up to the most recent Annual Progress Report. Actual real GDP data from 2004 to 2025 is sourced from the latest GDP release by the National Statistics Office (NR 033/2026). Following the computation of forecast errors, observations corresponding to the COVID-19 period are excluded from the sample to avoid distortions arising from exceptional shocks. The statistical properties of the resulting distribution are then analysed, with particular focus on the variance and the Pearson coefficient of skewness. In this context, the variance of past forecast errors is used to gauge the dispersion of possible outcomes, while skewness serves to capture potential asymmetries in the distribution of risks. These statistical measures provide the key inputs required for the construction of the fan chart.

The methodological approach draws on earlier work by the Economic Policy Department, which applied similar techniques to the Maltese context using historical forecast errors to derive probability distributions around GDP projections.¹⁰ To capture the balance of risks surrounding GDP projections, a two-piece normal distribution is employed. Following the approach outlined in Elekdag and Kannan (2009)¹¹, the fan chart is constructed through the following steps:

1. The central projection for GDP growth is set equal to the baseline forecast for 2026 as published by the Ministry for Finance in the latest Annual Progress Report.

¹⁰ Camilleri, G., & Vella, K. (2015). Interpolating Forecast Errors for Assessing Uncertainty in Macroeconomic Forecasts: An Analysis for Malta. Economic Policy Department, Working Paper Series (WP 01/2015).

¹¹ Elekdag, S., and Kannan, P. (2009). Incorporating Market Information into the Construction of the Fan Chart. IMF Working Paper No. 09/178.

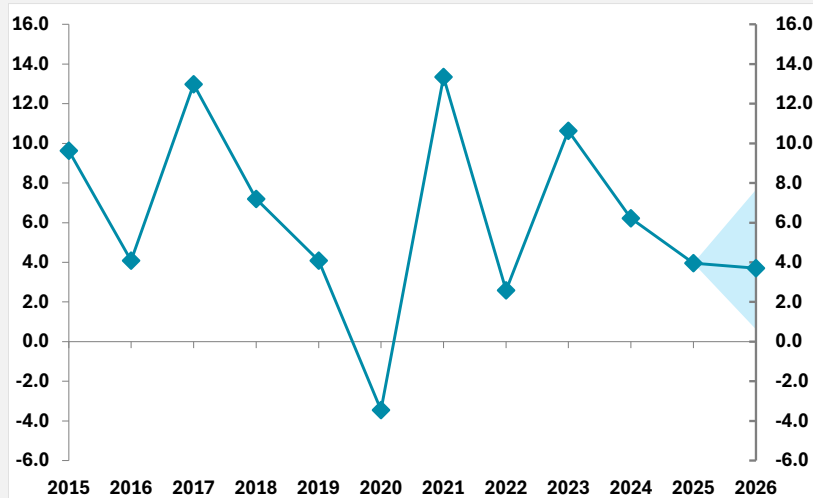
2. The degree of uncertainty is quantified using the historical variance of forecast errors. Where appropriate, this measure may be adjusted to reflect periods of heightened uncertainty.
3. To capture potential asymmetries in the distribution of risks, the Pearson coefficient of skewness is computed based on historical forecast errors. This is defined as three times the difference between the mean and the mode, divided by the standard deviation.
4. A confidence level is selected for the construction of the fan chart. In this analysis, a confidence interval of 70 per cent is adopted.
5. Given the estimated variance and skewness, the distribution of forecast outcomes is characterised using a two-piece normal distribution. This distribution is defined by a common mode, and distinct standard deviations on the left (σ_1) and right (σ_2) sides, thereby allowing for asymmetry.

The two-piece normal distribution can be interpreted as a combination of two normal distributions with identical central tendency but differing dispersion on either side. When $\sigma_1 \neq \sigma_2$, the distribution is skewed, and the central parameter corresponds to the mode. The variance and skewness parameters are then used to derive closed-form expressions for σ_1 and σ_2 .

6. Finally, confidence intervals around the central GDP growth projection are constructed for the chosen confidence level. These intervals are derived using the cumulative distribution function of the normal distribution, allowing for asymmetric bounds that reflect the estimated balance of risks.

By following this methodology, a skewed fan chart is constructed around the spring 2026 GDP growth forecast published in the Annual Progress Report 2026 ([Chart B1](#)). The fan chart constructed around the Spring 2026 GDP growth projection highlights a moderate degree of uncertainty surrounding the baseline forecast, as captured by the estimated variance of forecast errors (3.1). This suggests that historical forecast deviations have been non-negligible, implying a relatively wide distribution of possible outcomes around the central projection.

Chart B1: Fan Chart based on MFIN's Spring Forecast Errors for Year t



Source: NSO, MFAC Calculations, MFIN

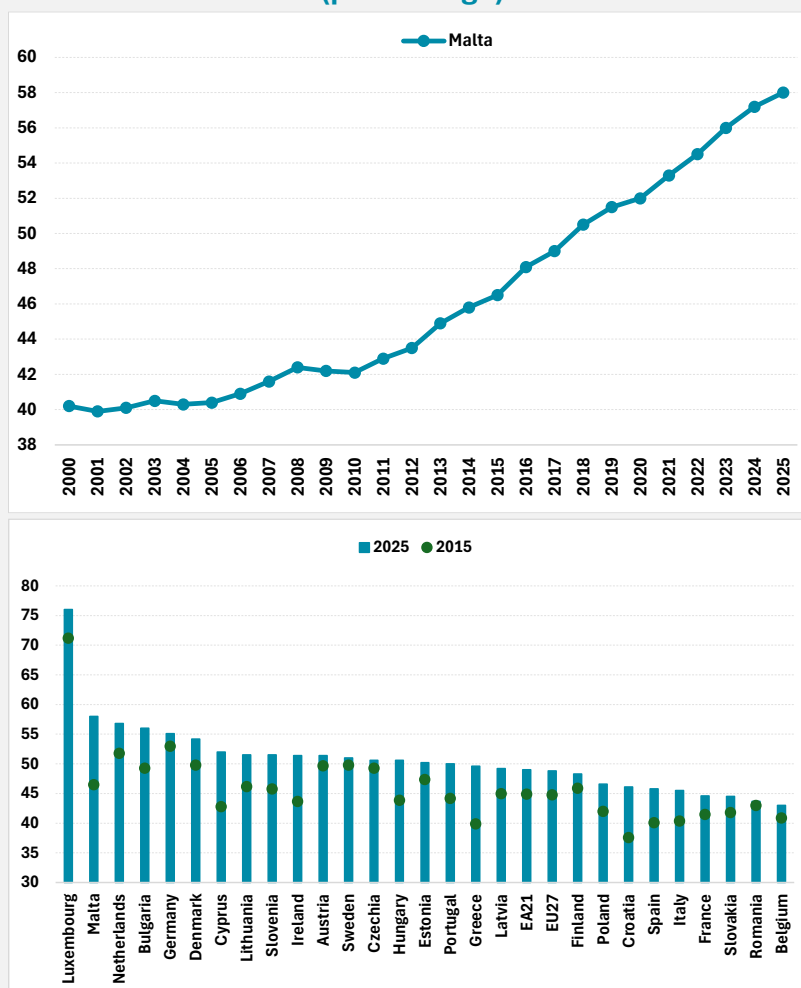
Importantly, the distribution of risks is found to be asymmetric, as indicated by the positive Pearson coefficient of skewness (0.2). In deriving this measure, expert judgment was incorporated by assigning greater weight to more recent forecast errors, relative to those observed in earlier periods. This implies that upside risks marginally dominate, with the probability distribution exhibiting a longer tail on the upper end. In practical terms, this suggests that favourable outcomes, where growth turns out stronger than projected, are more likely, or potentially more pronounced, than downside surprises.

At the chosen 70 per cent confidence interval, the fan chart illustrates a range of plausible GDP growth outcomes around the baseline forecast. While the central projection remains the most likely outcome, there is a meaningful probability that actual growth could deviate from this estimate, particularly on the upside. This asymmetry suggests that risks to the outlook are not evenly balanced.

Box C: Population Increases versus Improvements in Labour Productivity. Who did the heavy lifting?

Over the past decade, Malta has experienced a remarkable economic expansion, consistently outpacing average growth in the European Union. During this period, real GDP growth averaged 6.5%, driven primarily by domestic demand, which contributed 4.9 percentage points (pp) to overall growth, while net exports contributed a further 1.4 pp. Real GDP per capita (in 2020 prices) doubled over the last 20 years, reaching approximately €35,000 per capita in 2025, and surpassing the EU average when adjusting for purchasing power standards. Malta thus moved from a position close to the middle of the EU income distribution to one of the leading European economies, reflecting a significant process of real convergence within the European Union.

Charts C1 & C2: Total Employment per Capita in Malta (percentage)

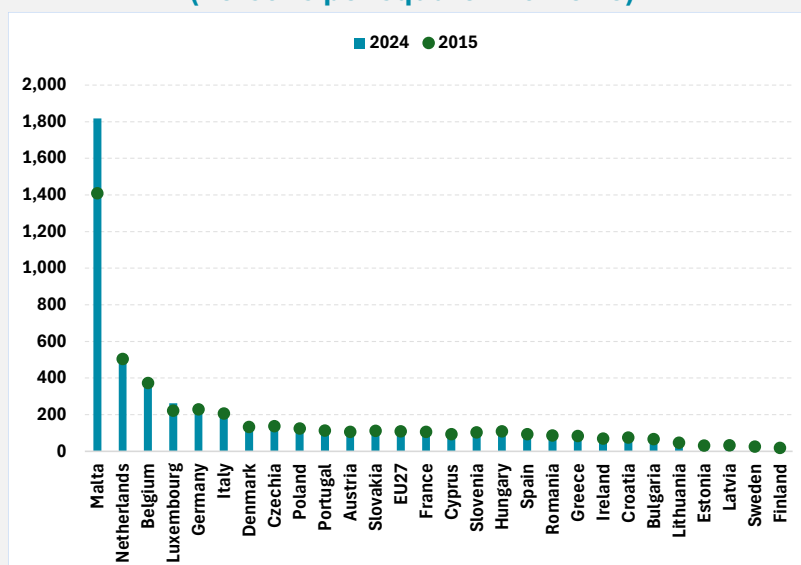


Source: Eurostat

Economic activity was mainly supported by the expansion of services sectors, particularly tourism, information and communication, professional and administrative services, and remote gaming. Growth in these sectors contributed to an increase in labour demand and sustained job creation.

During the last years, Malta recorded a substantial increase in employment per capita over time, with the share of the population in employment rising more markedly than in many other EU Member States (see [Charts C1 and C2](#)). Malta's employment-to-population ratio is now among the highest in the EU. This suggests that labour market expansion, both through increases in participation rates, in particular the female participation rate, and net migration, played an important role in supporting economic growth. In fact, in 2025, Malta's population stood at 583,000 from around 455,000 in 2016, an increase of close to 30.0%, or an average of 14,000 persons each year. This rapid population growth has contributed to a substantial increase in population density, with Malta now recording the highest population density in the European Union by a considerable margin. Indeed, Malta's population density is more than three times higher than that of the Netherlands, the second most densely populated Member State, highlighting the growing pressures associated with accommodating further population growth within a geographically constrained territory (see [Chart C3](#)). This expansion was driven primarily by net inward migration, with the share of foreign residents rising from around 11.0% of total population in 2016, to 29.4% in 2025.

**Chart C3: Population Density
(Persons per square kilometre)**



Source: Eurostat

At the same time, labour market participation also increased markedly, from 70.6% to 82.6%, with the female participation rate increasing from 58.0% to 75.5%, mainly supported by government measures aimed at supporting workers with dependent children to remain in the labour market. Notably, the female participation rate now exceeds the EU average of 71.1%, suggesting that Malta has largely closed the historical participation gap and that the scope for further gains from this source may be more limited going forward.

While labour inputs increased significantly, productivity gains were more moderate. Between 2016 and 2025, output per hour worked increased by an annual average of 1.6%, translating to an absolute increase of 16.1% over the period.

Given the strong interaction between economic activity and labour market developments, this box decomposes Malta's recent economic growth into the contribution of labour input and productivity. In this framework, labour productivity is measured as output per hour worked, while labour input is captured through total hours worked. This supply-side accounting approach provides clear distinction between growth generated by increased labour utilisation and growth supported by productivity gains. Labour utilisation is further decomposed between average hours worked, changes in the employment rate, labour force participation, demographic developments, and population growth, such that:

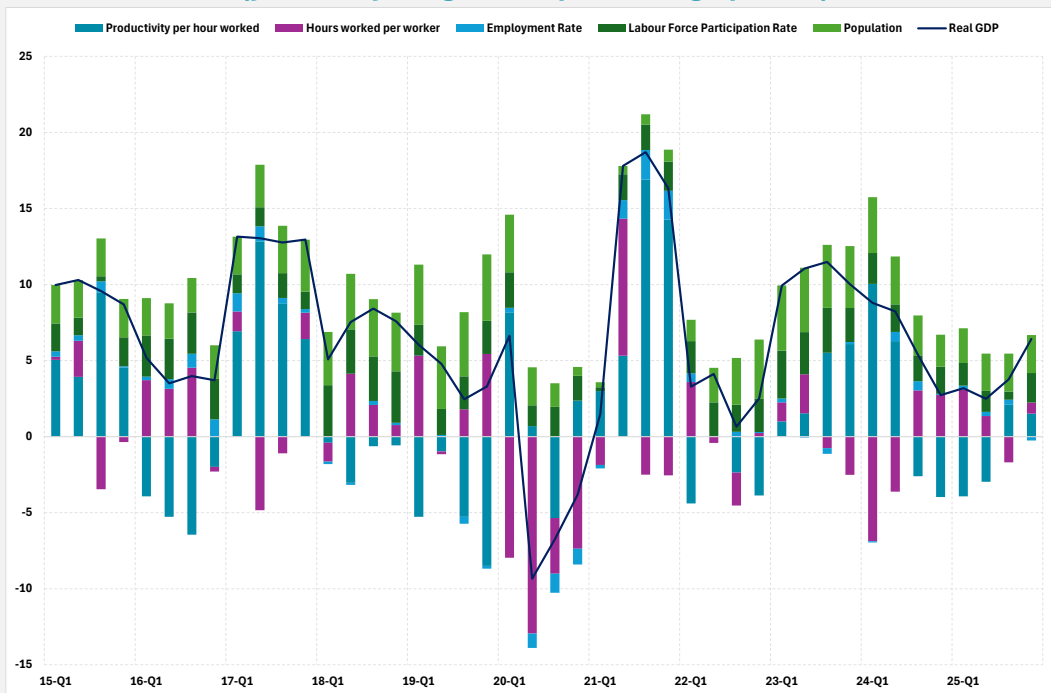
$$\Delta \ln Y = \underbrace{\Delta \ln (Y/H)}_{\text{Contribution of labour productivity per hour worked}} + \underbrace{\Delta \ln (H/E) + \Delta \ln (E/LF) + \Delta \ln (LF/P)}_{\text{Contribution of total hours worked}} + \Delta \ln P$$

where: Y is real GDP, H is hours worked, E is employment, LF is labour force, and P is population. Consequently, Y/H is output per hour worked, H/E is hours worked per employed person, E/LF is the employment rate, and LF/P is the participation rate.

The decomposition suggests that Malta's strong economic growth over the past decade was driven primarily by labour market expansion rather than sustained productivity gains (see [Chart C4](#)). In particular, increases in labour force participation and population growth made consistently positive

contributions to real GDP growth, underscoring the importance of labour supply dynamics in supporting economic activity. Between 2015-2025, the increase in labour force participation accounted for 2.0 pp of real GDP growth, while population contributed 2.8 pp. This reflects, to a significant extent, the role played by inward migration and rising labour market participation in sustaining output growth.

**Chart C4: Labour market decomposition of real GDP growth
(year-on-year growth, percentage points)**



Source: Eurostat, Authors' calculations

Notes: Following the productivity accounting framework widely used by the OECD and the European Central Bank, real GDP can be expressed as the product of labour productivity (GDP per hour worked), average hours worked per employee, the employment rate (total employment / total labour force), the labour force participation rate (total labour force / total population) and total population. Employment is measured on a domestic concept basis, consistent with national accounts and GDP measurement. This includes all persons employed within the Maltese economy irrespective of their nationality or residence, ensuring consistency between labour input and domestic production (ESA 2010 methodology). The labour force is defined as the sum of employed and unemployed workers. The contribution of total hours worked to the growth rate of real GDP can be obtained by adding together the contributions of average hours worked, employment rate, labour force participation and total population.

By contrast, labour productivity per hour worked displayed greater volatility and, in several years, contributed negatively to growth despite robust economic performance. This was particularly evident in 2016, 2018 and 2019, when real GDP growth remained strong while productivity growth weakened, indicating that output expansion was largely supported by increases in labour input and total hours worked. On average, over the last decade, output per

hour worked accounted for 1.6 pp of real GDP growth, which is considerably lower than the contribution from labour utilisation.

The decomposition also highlights the relatively flexible adjustment of hours worked over the economic cycle. During the COVID-19 pandemic, average hours worked declined sharply due to containment measures and weaker economic activity, making a strongly negative contribution to GDP growth. Employment, however, remained comparatively resilient, suggesting that firms adjusted primarily through reductions in hours worked rather than through large-scale job losses. This pattern is consistent with labour hoarding behaviour and aligns with previous findings reported by the Malta Fiscal Advisory Council (MFAC, 2024)¹², as well as government measures aimed at cushioning the impact on the labour market, especially through the wage supplement scheme which guaranteed a basic wage cover to employers and engaged employees.

Overall, the analysis indicates that Malta's growth model during the period under review relied heavily on factor accumulation, particularly labour market expansion, while productivity improvements provided a less stable contribution to growth. These findings highlight the importance of strengthening productivity growth over the medium- to long-term, especially given the constraints associated with continued population expansion.

Alternative growth simulations

Malta already has a population density far above the EU average, and rapid population growth has put pressures on infrastructure, housing and public services. As a result, the economy cannot rely indefinitely on population growth as a source of labour input and economic expansion. At the same time, with the unemployment rate at historically low levels and labour shortages persisting in several sectors, slower expansion in the labour force could intensify labour market tightness, adding to wage and inflationary pressures. Therefore, unless accompanied by stronger productivity gains, this would present challenges to Malta's competitiveness in the medium- to long-term.

Indeed, the supply-side accounting framework used in this analysis shows that, for the Maltese economy to sustain real GDP growth at around the rates recorded in 2025 (approximately 4%), while labour productivity continues to contribute in line with its average performance over the past decade, the

¹² The thematic research chapter published by the MFAC can be found [here](#).

labour force would need to continue expanding by around 14,000 persons annually. This estimate takes into account the limited scope for further increases in labour market participation, given that participation rates are already at historically high levels, as well as the assumption of broadly stable average hours worked per employee.

Nevertheless, it should be noted that there is still some scope for further increases in labour market participation rates amongst some demographic groups. For instance, Malta still has one of the lowest participation rates for persons aged 55 to 64 years, standing at 63.0% compared with the EU average of 69.5%. As an example, if participation rates for this cohort were to converge towards the higher levels observed in the EU, the labour force would increase by around 10,500 persons, without adding further strains associated with population growth. That said, achieving such gains is likely to prove challenging, as labour market participation decisions within this age group are often influenced by factors such as health conditions, skills obsolescence, caring responsibilities, and proximity to retirement. Furthermore, activating such cohorts may require significant efforts in upskilling and re-training.

Conversely, stronger productivity growth could substantially reduce the need for additional labour inputs. For example, if labour productivity growth were to accelerate to an average of 3.0% per annum, while maintaining real GDP growth of 4.0%, the required annual increase in the labour force would fall to around 6,000 persons. These simulations highlight the critical importance of productivity-enhancing reforms in supporting long-term economic growth while alleviating pressures associated with continued population expansion.

Conclusion

Overall, the supply-side decomposition of economic growth underscores the central importance of productivity for ensuring the sustainability of Malta's future economic growth. Over the past decade, labour productivity has made a positive contribution to economic activity, but its role was smaller and less stable than that of labour force expansion and labour utilisation. As demographic, spatial and infrastructural constraints become more binding, sustaining high growth through continued increases in labour input will become increasingly challenging. A stronger productivity performance is therefore essential to raise potential output, support higher wages without adding excessive cost pressures, and safeguard external competitiveness.

This shift to productivity-led growth requires a sustained and multifaceted agenda across human capital, infrastructure, regulation and digitalisation, amongst other areas. Strategic labour market policies are particularly important to address skills mismatches, support upskilling and re-training, while facilitating job mobility towards higher value-added activities.

Meanwhile, fiscal policy has a central role in supporting this transition. Creating and preserving fiscal space would allow Malta to prioritise and finance productivity-enhancing investments in education and infrastructure. Improving the quality and efficiency of public spending would help ease supply-side bottlenecks and improve the efficiency of the economy, including by crowding-in private investment.

Box D: Updating the Heatmap for the Maltese Economy

The macroeconomic heatmap, developed by the Council and presented in a thematic chapter in its 2025 Annual Report, has been updated to include the latest data, including national accounts data up to the fourth quarter of 2025. The latest data suggest that the momentum in economic activity remained strong in Q4, although some labour market and price indicators moderated. This easing is evident across several macroeconomic indicators, while survey-based indicators point towards sustained activity, with the overall economic performance remaining above its long-term average, calculated over the period from Q1 2010 to Q4 2025.

Overall, developments point to a gradual cooling in underlying economic conditions. In the Prices and Competitiveness block, inflationary pressures continued to ease following the post-pandemic surge and the induced price pressures from the terms-of-trade shock. While core inflation remained above its long-term average, it continued to decelerate. At the same time, the private consumption deflator fell below its historical average, reinforcing the moderation in price dynamics. Meanwhile, growth in the house price index remained broadly stable when compared with Q4 2025.

Labour market indicators, although still signalling tight conditions, also showed tentative signs of moderation. The unemployment rate edged up marginally in Q4, though remaining well below its long-term average. The employment rate declined slightly from 72.3% in Q3 to 71.3% in Q4 but continues to stand significantly above its long-term average. Meanwhile, average wages recorded no growth, largely reflecting base effects from strong public sector wage increases (including arrear payments) in the same quarter of 2024. As a result, nominal unit labour costs fell below their long-term norm.

The External Balances block presents a mixed picture. The real effective exchange rate increased further above its long-term average, pointing to a deterioration in price competitiveness. Malta's net investment position, while still positive, declined further below its historical norm, indicating some weakening in the external balance sheet. By contrast, both the current account and trade balances remained above their respective long-term averages, albeit moderating compared to the previous quarter.

Credit and financial indicators continue to suggest broadly accommodative conditions. The interest rate spread relative to the German Bund remained below its long-term average, largely driven by a rise in long-term German sovereign yields following fiscal expansion and increased borrowing expectations in Germany. The yield curve, while below its historical norm, remained positively sloped, typically associated with stable macroeconomic conditions and favourable growth expectations. Both indicators declined further relative to their long-term averages during this quarter.

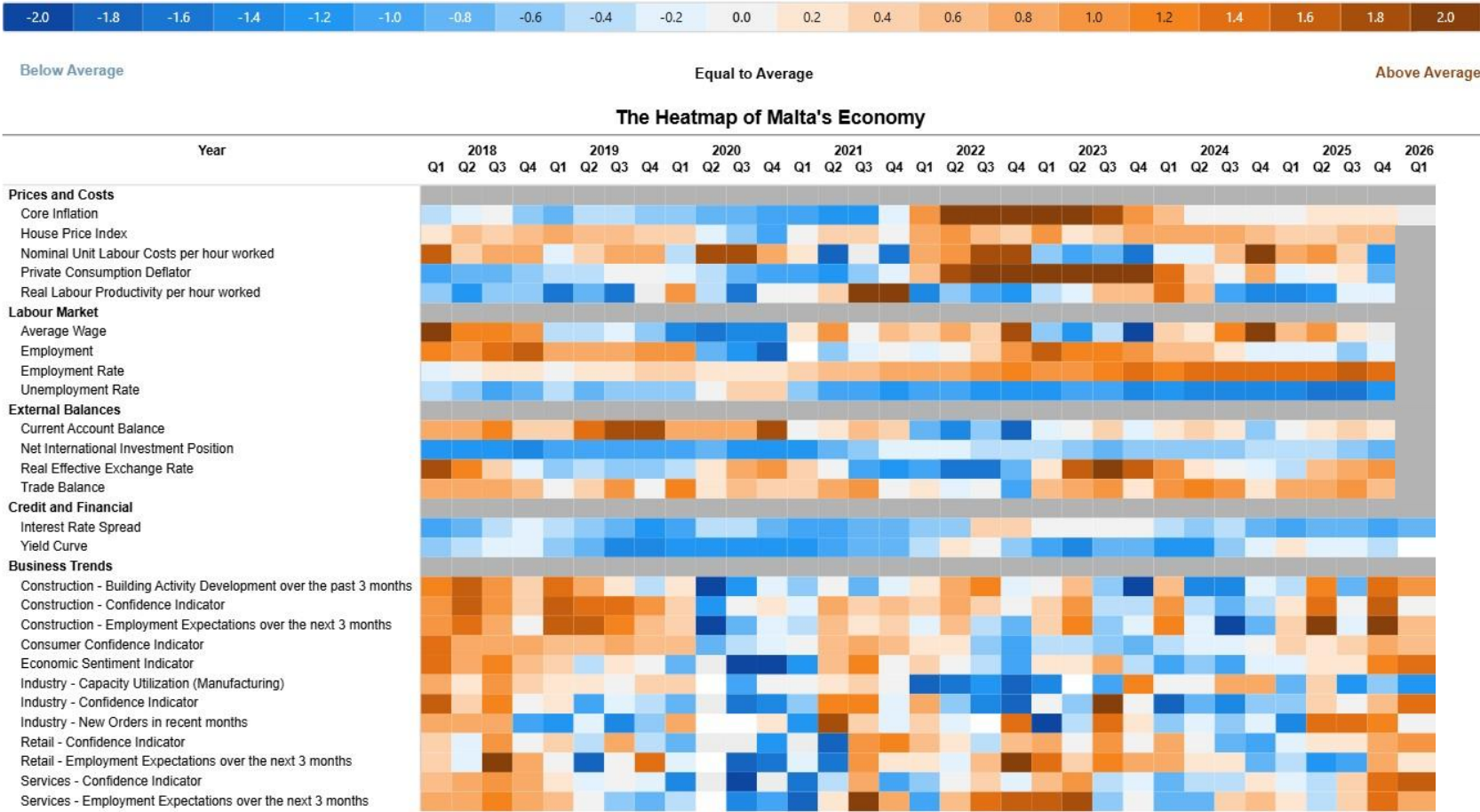
Taken together, these macroeconomic indicators point to a moderation in underlying economic activity during the final quarter of 2025. This stands in contrast to the stronger GDP outturn recorded over the same period. Nevertheless, it should be noted that the acceleration in GDP during the final quarter was primarily supported by robust growth in wholesale and retail trade, partly reflecting base effects and re-export activity in fuels. At the same time, key services sectors, including tourism, information and communication, and professional and administrative services, also continued to support economic expansion.

In contrast to the moderation signalled by these indicators, forward-looking sentiment measures pointed to increased optimism towards the end of 2025. The European Commission's economic sentiment indicator rose further above its long-term average in Q4, while consumer confidence also remained elevated. All sectoral confidence indicators exceeded their historical norms, and although industry capacity utilisation remained below average, in line with trends in global manufacturing, it moved closer to its long-term trend. Overall, these suggest an improvement in expectations and a more positive outlook among economic agents heading into 2026.

Available data for the first quarter of 2026 appears to support this more favourable outlook. Inflation decelerated further to 2.2%, in line with its long-term average, while the economic sentiment indicator remained above its historical average, although moderating. Sectoral confidence indicators continued to exceed their long-term averages. However, these readings should be interpreted with caution. They largely predate the escalation in geopolitical tensions observed from March onwards, particularly the intensification of the conflict in the Middle East. As such, the earlier improvement in sentiment is likely to weaken as these developments feed

through to expectations and economic conditions over the remainder of 2026.

Chart D1: Heatmap of the Maltese Economy

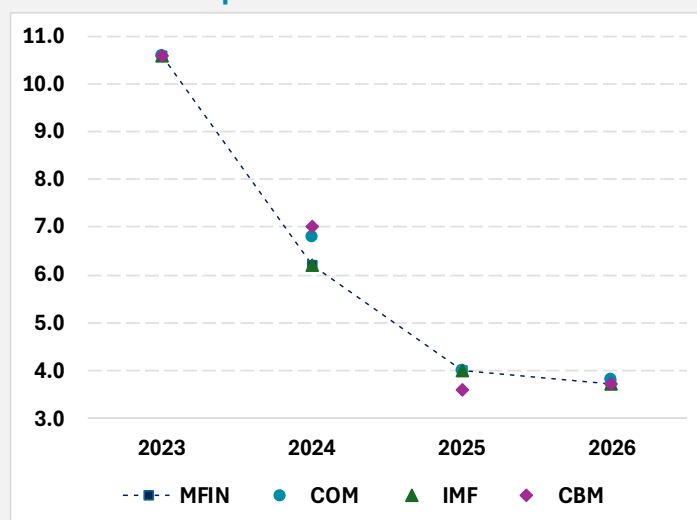


Box E: A Comparison of the MFIN's Macroeconomic Forecasts with Other Institutions

As part of its assessment, the MFAC also conducts a comparative evaluation with the macroeconomic forecasts issued by other reputable institutions including the European Commission (COM), the International Monetary Fund (IMF), and the Central Bank of (CBM). For this assessment, particular consideration is given to the IMF's April 2026 projections and the CBM's 2026 forecasts, both of which incorporate the most recent data published by the National Statistics Office (NSO) in release NR 033/2026. On the other hand, the most recent COM forecast by the cut-off date of this Report is that published in Autumn 2025.

The CBM projects real GDP growth of 3.7% for 2026, in line with the MFIN's forecast. The IMF anticipates the same rate of economic growth, while the COM projects a marginally higher growth rate of 3.8%. Hence, the MFIN's real GDP forecast for 2025 is consistent with those of other key institutions.

Chart E1: Comparison of Forecasts for Real GDP

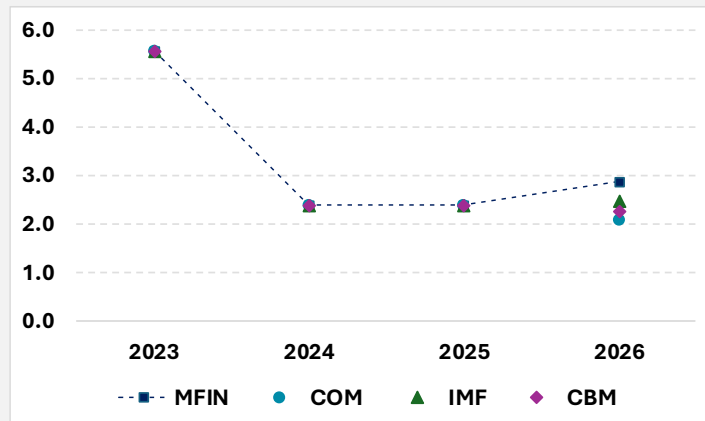


Source: MFIN, COM, IMF & CBM

Inflation forecasts for 2026 vary across institutions. The MFIN projects an acceleration in inflation from 2.4% in 2025 to 2.9% in 2026, while the IMF also anticipates inflation to rise, though more moderately, to 2.5%. In contrast, both the CBM and the COM anticipate a deceleration in inflation to 2.3% and 2.1%, respectively. However, these latter projections were formulated before the sharp rise in fuel prices following the outbreak of the

war in the Middle East, which is a key consideration in more recent forecasts.

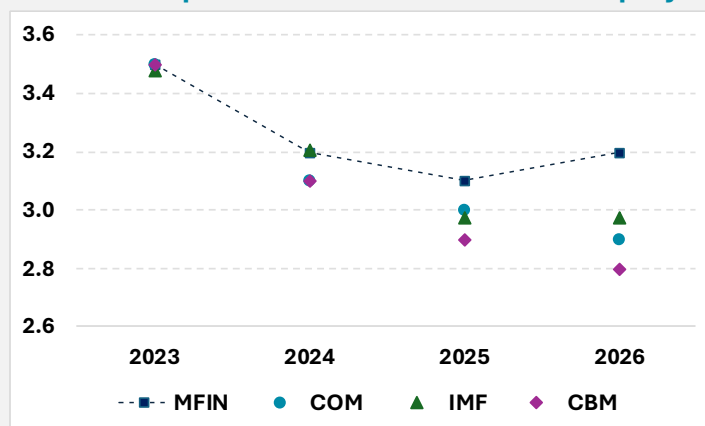
Chart E2: Comparison of Forecasts for HICP



Source: MFIN, COM, IMF & CBM

The MFIN's unemployment forecast for 2026 stands at 3.2%. The IMF forecasts an unemployment rate of 3.0%, while the CBM and COM forecast even lower rates of unemployment of 2.8% and 2.9%, respectively.

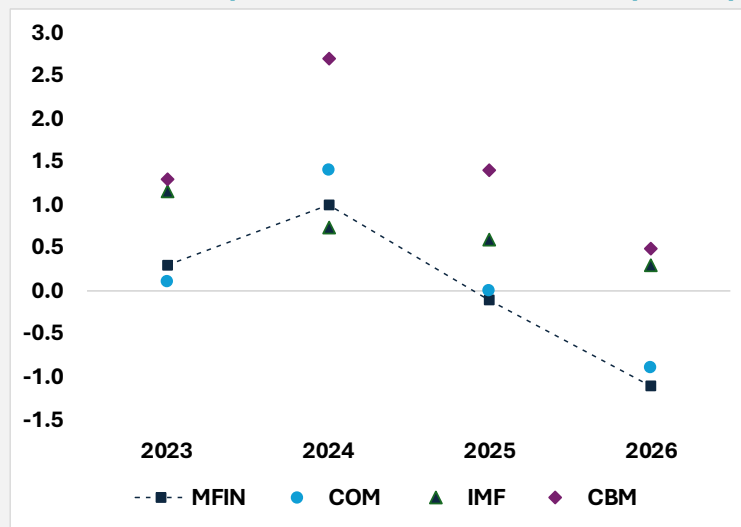
Chart E3: Comparison of Forecasts for Unemployment



Source: MFIN, COM, IMF & CBM

Both the MFIN and the COM anticipate that the output gap will remain negative in 2026. However, the MFIN projects a larger gap of -1.1% , compared to the COM's estimate of -0.9% . In contrast, the IMF and CBM forecast a positive output gap, at 0.3% and 0.5% , respectively.

Chart E4: Comparison of Forecasts for Output Gap



Source: MFIN, COM, IMF & CBM

Overall, the forecasts provided by the various institutions for real GDP growth, inflation, and unemployment exhibit broadly similar trajectories and are closely aligned. Since most of the MFIN's macroeconomic forecasts fall within the range projected by other institutions, this further supports the Council's endorsement. In contrast, projections for the output gap differ markedly across institutions, with some anticipating a positive gap, unlike the negative gap projected by the MFIN and the COM. Indeed, in its assessment, the Council expresses concern on MFIN's projected pronounced widening of the output gap.