FOREWORD

During the fourth quarter of 2024, real gross domestic product (GDP) rose by 2.8% on an annual basis. Domestic demand remained the main engine of economic growth, as net exports had a limited contribution. When adjusting for imports, domestic demand still remained the main contributor to GDP growth.

Potential output growth is estimated to have stood at 4.6% in the fourth quarter of 2024, slightly below that of 4.9% estimated for the third quarter. On a four-quarter moving average basis, the level increase in potential output relative to the previous quarter exceeded that in GDP. As a result, the output gap is estimated to have narrowed to 1.2% from 1.7%. This implies some moderation in the degree of over-utilisation of the economy's productive capacity.

The Bank's Business Conditions Index (BCI) improved slightly in the fourth quarter indicating that economic growth stood above its long-run average. This partly reflected above average growth in residential permits, tax receipts and industrial production, which offset below average growth in GDP.

The Bank's Economic Policy Uncertainty (EPU) Index, which monitors economic policy uncertainty by synthesising information gleaned from Maltese news portals, rose to 95.1 in the fourth quarter, up from 69.6 in the preceding quarter but nonetheless remained slightly below its historical average. The latest increase primarily reflected heightened economic and political uncertainty overseas.

Developments in the labour market remained positive. Although employment growth moderated compared to the previous quarter, it remained strong, at 4.2% according to the Labour Force Survey (LFS). The unemployment rate remained low and well below that in the euro area. Meanwhile, the job vacancy rate and the labour tightness indicator remained high from a historical perspective.

Consumer price pressures eased further during the quarter under review. Annual inflation, as measured by the Harmonised Index of Consumer Prices (HICP), stood at 1.8% in December, down from 2.1% in September. This was mainly driven by a smaller contribution from unprocessed food inflation. Meanwhile, annual inflation based on the Retail Price Index (RPI), which only considers expenditure by Maltese residents, was unchanged at 1.2%.

Non-labour cost indicators regularly monitored by the Bank continued to signal moderate price pressures, albeit with different dynamics. Annual inflation according to the industrial producer price index remained negative but rose to -0.4% on average in the fourth quarter of 2024, from -0.9% in the previous quarter. Other indicators moved sideways. The domestic producer price index rose at a slightly faster pace but remained subdued at 0.6%, while the imports of goods deflator showed somewhat weaker growth but stood relatively higher at 3.0%. Meanwhile, the construction cost index (CCI) for new residential buildings increased at a slightly higher rate than before, at 1.8%.

Meanwhile, Malta's unit labour cost (ULC) index, measured on a four-quarter moving average basis, rose at an annual rate of 5.0%, following a rise of 2.3% in the previous quarter, largely reflecting an acceleration in compensation per employee. On a four-quarter moving average basis, the latter increased by 5.8%.

In the fourth quarter of 2024, the current account surplus narrowed compared with a year earlier. This was mainly due to higher net outflows on the primary and secondary income accounts. By contrast, the merchandise trade deficit narrowed and net receipts from services increased. On a four-quarter moving sum basis, the current account surplus was equivalent to 5.7% of GDP.

When measured on a four-quarter moving sum basis, the general government deficit ratio stood at 3.7% of GDP; it stood higher than in the third quarter of 2024, but below the 4.7% registered at end-2023. The general government debt-to-GDP ratio reached 47.4% at the end of December, higher than in September, but slightly lower than the 47.9% posted at end-2023.

In December, Maltese residents' deposits with monetary financial institutions (MFIs) in Malta increased from their year-ago level, reflecting higher balances belonging to both households and non-financial corporations (NFCs). The annual rate of change exceeded that recorded in September. Meanwhile, credit to Maltese residents also grew at a faster pace compared with the previous quarter, driven by faster growth in credit to general government. The Bank's Financial Conditions Index (FCI), in fact, suggests that financing conditions remained loose from a historical perspective and were marginally more favourable when compared with the third quarter of 2024.

The weighted average interest rate offered to households and NFCs on their outstanding deposits closed the year 9 basis points above its year-ago level, reaching 0.39%. The corresponding lending rate decreased by 22 basis points, to 3.36%. The spread between the two rates amounted to 297 basis points, from 328 basis points a year earlier.

Data on new business show an increase in both the weighted average deposit rate and the weighted average lending rate over the year to December, but decreased somewhat since September. The spread between the two rates stood at 75 basis points at the end of the year. Overall, these rates on new business continue to signal a modest degree of pass-through of the recent policy rate cuts by the European Central Bank (ECB).

The primary market yield on Treasury bills increased between September and December. The secondary market yields on five-year and ten-year Malta Government Stocks (MGS) also rose over this period, while the Malta Stock Exchange (MSE) Equity Price Index declined.

In October and December, the Governing Council of the ECB lowered the deposit facility rate (DFR), the rate on the main refinancing operations (MROs) and the marginal lending facility rate to 3.00%, 3.15% and 3.40%, respectively. At the December meeting, whilst reiterating that it was not pre-committing to a particular rate path, the Governing Council dropped its restrictive bias with regard to policy rates. The Council noted that the disinflation process was well on track and most measures of underlying inflation suggested that inflation would settle around the 2% medium-term target on a sustained basis. The Governing Council restated that it would continue to follow a data-dependent and meeting-by-meeting approach in determining the appropriate monetary policy stance.

Meanwhile, securities held under the asset purchase programme (APP) continue to decline at a measured and predictable pace, as the Eurosystem no longer reinvests the principal payments from maturing securities. Securities under the pandemic emergency purchase programme (PEPP) portfolio are also decreasing, as the related reinvestments ended at the end of 2024.

In January, and again in March and April 2025, the Governing Council cut its policy rates further. Accordingly, the interest rates on the deposit facility, the MROs and the marginal lending facility were decreased to 2.25%, 2.40% and 2.65%, respectively. Especially in current conditions of exceptional uncertainty, the Council will continue to follow a data-dependent and meeting-by-meeting approach in determining the appropriate monetary policy stance.