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The Economy

# Malta

July 1973

NATIONAL INTELLIGENCE SURVEY

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# Malta

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*This chapter supersedes the economic coverage in the General Survey dated May 1967 which should be destroyed.*

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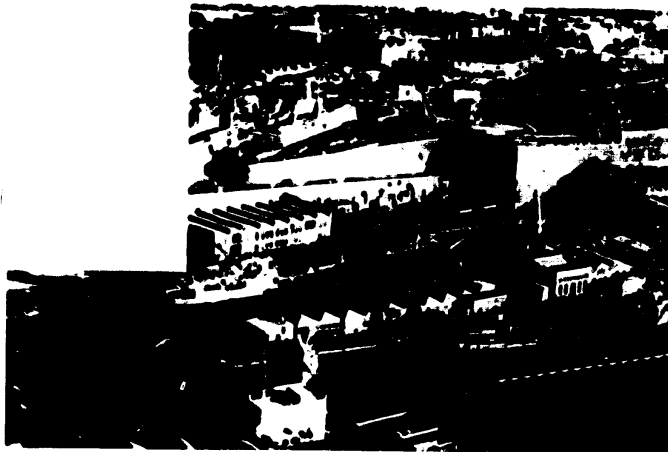
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**A. Economic appraisal (C)**

Although one of the world's smallest countries and one of the most poorly endowed in natural resources, Malta has parlayed its island location in the Mediterranean and its special relationship with the United Kingdom into a rapidly rising level of living. In 1971, Malta's gross national product (GNP) amounted to \$280 million in current market prices, the per capita GNP of \$800 was almost double that recorded at the time that Malta became independent from British colonial rule in 1964 (Figure 1). Although much lower than the level prevailing in the developed West, per capita GNP is higher than in Portugal and far exceeds that in Turkey and its Middle Eastern neighbors.

Economic growth accelerated after independence, averaging 9 1/2% annually in real terms in 1965-70. Investment in manufacturing and tourism provided the main impetus to development. The government encouraged the growth of industry through incentives such as tax remissions and loans provided for in Malta's 5-year plans and promoted tourism through advertising in northern Europe. The increased activity in manufacturing and tourism, along with a steady inflow of British settlers attracted by the pleasant climate, low taxes, and a low cost of living, sparked a construction boom that further boosted employment and incomes.

Except for balance of payments data, all Maltese pound values throughout this chapter have been converted into U.S. dollars at the central rate of £M1 = US\$2.65, the rate established in December 1971. The Maltese pound began floating in June 1972, with the rate being determined between that of sterling and that of the currencies of Malta's major trading partners. February 1972's average market rate, £M1 = US\$2.63. From 1967 through November 1971, the rate of exchange was £M1 = US\$2.40.

Industrial expansion has enabled Malta to expand its exports considerably, particularly sales of manufactured goods. Total exports, which accounted for 13% of GNP in 1964, amounted to about 18% of GNP by 1971. However, since economic growth has depended heavily on imported capital goods and rising incomes have increased the demand for

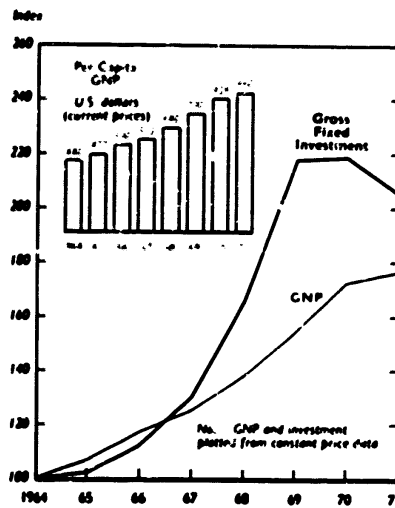


FIGURE 1. Gross national product and gross fixed investment, 1964-71 (U/OU)

consumer goods that are not produced locally. Malta's trade account remains in chronic deficit; the deficit was \$124 million in 1971.

The United Kingdom has played a dominant and pervasive role in Malta's economic life. Although Malta was given independence in 1964, the United Kingdom signed aid and defense agreements and continued to maintain a sizable presence on the island through the stationing of military troops and their dependents. U.K. economic aid substantially financed the Maltese Government's investment expenditures and provided foreign exchange to support Malta's high level of imports. British military expenditures accounted for 9% of GNP in 1964-69, and expenditures of dependents bolstered domestic trade and services. Furthermore, for several years British companies operated the drydocks, and Barclays Bank was the bank of the Maltese Government, which even today turns to British experts for counseling. British influence is still apparent in the British-run airport and in Malta Airlines, run by British European Airlines. In the business community, English is spoken as often as, if not more frequently than, Maltese, and retail stores in downtown Valletta are branches of London companies.

In 1969, the special relationship between the United Kingdom and Malta began to deteriorate. The U.K. Government insisted that the terms of the aid extended to Malta be changed, claiming that Malta's economic prosperity justified more stringent terms. The Maltese Government refused to accept aid under those conditions. The United Kingdom yielded in late 1970, in anticipation of the Maltese elections and the possibility of a Maltese Labor Party (MLP) victory. British economic aid at the old terms flowed into Malta to bolster the chances of the incumbent Nationalist government. The MLP, however, was victorious, and Don Mintoff, the new Prime Minister, quickly abrogated the defense and aid agreements and demanded rental payments for the British bases on the island. The controversy, which lasted 9 months, resulted in the evacuation of British dependents and most of the troops. Ultimately, Mintoff successfully negotiated an agreement for cash payments from the United Kingdom and its NATO allies, but the break had a pronounced negative effect on the economy that ultimately affected not only Maltese Government operations but tourism and trade as well.

In 1971 the growth rate of the Maltese economy fell to 2.5% (the rate was 11.9% in 1970), and fixed investment actually declined. The unemployment rate rose from 4.7% at the end of 1970 to 5.4% by the end of 1971. The controversy with the United Kingdom

was the major element in the slump, but there were other problems as well. The MLP government canceled government projects planned by the Nationalists, frightened prospective investors with price and profit controls, and canceled the investment incentive program. Tourism, which depends primarily on British visitors, fell off sharply. Imports and domestic commerce were adversely affected by rising levels of unemployment and the departure of British dependents. The foreign trade deficit fell for the first time in years, and many small store owners experienced financial losses. The construction sector, affected by the falling demand in other sectors, was marked by considerable unemployment.

The controversy with the United Kingdom was settled in March 1972, and Malta was guaranteed substantial annual aid payments to finance economic development for 7 years. The Prime Minister stated that these funds, along with other aid already agreed to, would be used to develop the economy so that it would no longer be dependent on military bases after the 7-year period of the agreement. In the 9 months following the agreement, however, little was done to increase the level of economic activity. The government has operated under a deflationary budget, with an absolute decrease in capital spending. Unemployment, however, has been reduced by recruiting idle workers into an emergency labor corps for public works projects. Prospects for renewed rapid growth depend heavily on the use eventually made of foreign aid inflows to stimulate investment and employment. A new 7-year development plan is scheduled to be released in 1973, at which time the government's policies for achieving the aim of economic independence are to be revealed. Preliminary indications are that the role of the government in economic activities will increase significantly.

## B. Structure of the economy

In some respects, Malta's economy differs markedly from those of other countries at a generally similar level of development. Agriculture is relatively much less important, and services are much more important than in Greece or Portugal, for example. The unusual prominence of services stems from the traditional use of the public payroll to absorb some of the unemployed, as well as from activities directly and indirectly related to the British military presence. Public administration and military services in Malta together employ one-quarter of the labor force and produce some 30% of the gross domestic product



(GDP), compared with less than 10% in Greece or Portugal. (U/OU)

During 1964-71, the share of public administration and military services in the GDP remained nearly constant, but the shares of certain other sectors changed significantly, as shown in the following tabulation (in percent of GDP):

	1964	1971 (est)
Agriculture, forestry, fishing	7.3	6.3
Mining, quarrying, and construction	3.3	6.9
Manufacturing	18.0	20.1
Electric power, gas, water	3.3	4.7
Public administration and military services	20.7	21.2
Wholesale and retail trade	21.0	16.8
Transport and communications	4.7	3.8
Banking, insurance, and real estate	2.9	3.6
Other services (including ownership of dwellings)	10.8	11.5

Manufacturing, generally recognized as the key to the development of Malta's economy, increased in relative importance. New manufacturing plants, many of them situated in industrial parks outside Valletta, and new tourist facilities provided the stimulus for most of the rise in the shares of GDP shown under mining, quarrying, and construction and under banking, insurance, and real estate. (U/OU)

**1. Agriculture and fishing (U/OU)**

**a. Agriculture**

Malta produces only one-fifth of the food required by its densely populated urban areas. Less than half the land area is classified as agricultural, and the available cropland area (Figure 2) is wholly

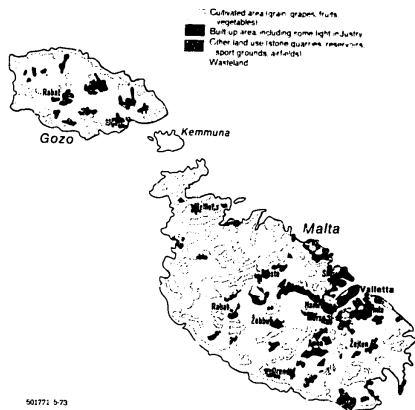


FIGURE 2. Land use (U/OU)

inadequate—amounting to about one-twentieth hectare (one-eighth acre) per inhabitant. Moreover, shallow soils and a dry climate that is ill-suited to agriculture severely limit productivity. A wide variety of crops, including cereals, is grown, but only potatoes and onions are produced in quantities adequate to meet domestic demand and provide sizable surpluses for export although wine produced from domestic grapes is also exported (Figure 3). Tomato production supplies the domestic market and may eventually become an important source of export earnings. Nearly all of the needed grains, however, must be imported. Although various vegetables and fruits are produced, imports supply about 30% of the green vegetables, 85% of the citrus, and 10% of the other fruits consumed. In addition, large amounts of meat and dairy products are imported to supplement local production.

About 45% of the agricultural area is planted in grains and fodder crops (Figure 4). The only grains of importance are wheat and barley, grown primarily for use as feed for livestock. The principal fodder crops include sulla, green barley, vetch, alfalfa, chickpeas, broad beans, and locust beans. Sulla, a perennial legume indigenous to the Mediterranean area, is grown extensively; the acreage used for sulla is about the same as that for cereal grains. Water requirements for sulla are low, and its extensive root system helps to prevent erosion.

The main vegetable crops are potatoes, onions, and tomatoes. Potato yields are generally below those of other Mediterranean countries because of the dry climate, soil deficiencies, and inadequate use of fertilizer. Potatoes, nevertheless, have been Malta's most important agricultural export for many years. Onions are also an important export crop. Since 1960,

FIGURE 3. Selected agricultural commodities: production, imports, and exports, 1969 (U/OU) (Metric tons)

	PRODUCTION	IMPORTS	EXPORTS
Wheat.....	1,700	*57,300	**
Barley.....	1,700	24,100	**
Corn.....	0	20,700	0
Potatoes.....	22,200	5,800	13,900
Tomatoes.....	9,600	0	**
Onions.....	4,700	0	2,400
Other vegetables.....	26,400	11,300	**
Grapes.....	4,300	0	(100,000 hd. of wine)
Citrus.....	600	4,000	0
Other fruits.....	3,300	7,900	0

\*Wheat and wheat flour in wheat equivalent.  
\*\*Less than 100 tons.

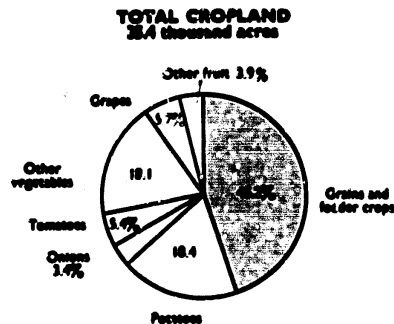


FIGURE 4. Distribution of cropland, 1969 (U OU)

the average production of onions has been lower than in the 1950's, acreage and output vary widely from year to year. In the past decade, there has been little change in acreage and output of field-grown tomatoes, which are sold mainly to canneries for conversion into paste for domestic consumption. Greenhouse production of tomatoes out-of-season is being subsidized by the government, and Malta has attempted to expand production and develop an export market for tomatoes.

Grapes, the principal fruit crop, are used mostly for making wines, exports of which are significant. Other fruits are grown, but the acreage devoted to them has declined continuously since 1955.

Malta does not produce enough livestock and dairy products to supply its domestic consumption requirements; considerable amounts of meat and 90% of the milk consumed are imported. Although the average annual rate of growth of meat output has changed little in the past decade, there has been a shift in the composition of animal holdings, as indicated in the following tabulation (in thousand head):

	1963	1971
Cattle	0.7	0.6
Pigs	15.8	23.4
Sheep	11.1	7.5
Goats	30.3	16.7
Poultry	170.2	258.1

Milk output has increased somewhat, and there is greater use of cow milk, as opposed to that of sheep and goats.

Poultry and pig farming are the most important livestock industries in terms of export potential. Poultry raising has shown such rapid growth that

Malta not only has become self-sufficient in poultry, meat, and eggs but faces the problem of disposing of surpluses.

Agricultural productivity in Malta generally is low. The dry climate, the limited extent of irrigation, poor soil, and the inadequate use of fertilizers and pesticides are contributing factors. More important, however, are the small size of agricultural holdings and the fragmentation of plots—factors which hinder the use of machinery and make cultivation laborious and time-consuming. In 1969, for example, the average holding was under 1 acre, and some 60% of all holdings were under 3 acres.

The total acreage devoted to crops decreased steadily from 41,000 acres in 1963 to about 35,000 acres in 1969. The decrease in acreage planted in wheat and barley has been most notable, but vegetable and fruit acreage has also declined. The only crop acreages showing increases were for onion and citrus fruit. The 20% decrease in the number of full-time farmers accompanying the decrease in cultivated land area since 1963 reflects, in part, the lure of more lucrative jobs in industry and tourism. The economic slump that began in late 1970 checked the movement of labor out of agriculture, but a resumption of more rapid growth and a substantial decline in unemployment may be expected to revive the exodus of labor from the farms.

Governmental policy toward agriculture encourages the improvement and modernization of methods, greater investment in machinery and equipment, and concentration on more profitable crops that will provide small farmers with a reasonable living without tariff protection or subsidy. Other objectives are to increase agricultural exports and to supply fruits and vegetables of domestic origin for the tourist industry. Government assistance to agriculture in the form of grants and loans has contributed to the mechanization and modernization of farming. From 1965 to 1969, the number of two-wheeled tractors (2 hp. to over 10 hp.) in use rose from about 1,400 to about 1,900, and the number of other tractors (three- and four-wheeled and tracked units) rose from 86 to 129. The government has also helped the agricultural sector by increasing the availability of irrigation water by damming streams, constructing water storage reservoirs, and purchasing irrigation equipment. Continued emphasis is also being placed on greenhouse horticulture and hydroponic farming.

**b. Fishing**

Fishing is only marginally significant to the economy. Between 1961 and 1971 the weight of the local catch declined somewhat, but the value of the

catch increased, as follows (in metric tons and thousands of U.S. dollars):

	WEIGHT	VALUE
1961	1,372	632
1966	1,296	853
1967	1,504	924
1968	1,204	910
1969	1,159	855
1970	1,184	1,010
1971	1,245	1,149

The local catch constitutes about 40% of the value of Malta's total fish consumption. The remainder is provided by imports of fresh, frozen, dried, and preserved fish. To encourage fishing, the government conducts a training and information program for fishermen, provides grants and loans for the purchase of larger boats and equipment, and is constructing breakwaters and ship channels. In 1969, the fishing fleet consisted of 924 small fishing craft and nine trawlers.

Maltese fishermen exploit mainly the migration of pelagic fish in the central Mediterranean, up to a range of 100 miles from the Maltese Islands. Dolphin and pilotfish, caught between September and November, constitute about one-fourth of the total catch, and mackerel, scad, and bogue, caught mainly between May and July, account for another 45%. The supply of fish in the waters surrounding Malta has been declining, and if the fishing industry is to reverse the declining trend in catches, it will have to employ more oceangoing trawlers and exploit richer fishing areas outside the Mediterranean. In spite of the apparent decline in local fishery resources, the Maltese Government, in 1972, formed a joint company with the Libyan and Japanese Governments to survey the fishery resources of the Libyan and Maltese coastal waters and to study the feasibility of constructing a fish cannery on Malta.

## 2. Fuels and power (C)

### a. Fuels

Malta has no known indigenous resources of fossil fuels and no hydroelectric potential. Imported fuels supply the energy required. The total value of fuel imports remained relatively stable during the 1960's, although the commodity composition changed, as follows (in thousands of U.S. dollars):

	1961	1969
Total fuels	8,010	7,922
Of which: Petroleum products	5,639	7,527
Of which:		
Gasoline and aviation gasoline	2,176	1,727
Jet fuel	844	550
Kerosene	975	972
Gas oil	537	1,282
Fuel oil	732	2,013
Lubricating oil and grease	256	433

Nearly 95% of total fuel imports consisted of petroleum products in 1969, compared with 70% in 1961. A large share of total fuel imports for domestic consumption is used for the generation of electricity, and substantial quantities of the imported bunker oil and aviation fuels are reexported in servicing foreign ships and aircraft. Italy is the principal supplier of fuels, followed by the Netherlands and France.

Gas is manufactured locally from imported fuel oil; in the past it was made from imported coal. The gas is distributed to consumers in the Valletta area, including the Malta Drydocks. Gas output expanded 41% from 1965 to 1969.

Malta's geographic proximity to Libya, where oil has been found in abundance, has raised hopes that oil might be discovered in the country. Three offshore drilling concessions were granted in 1972 to French, Dutch, and Canadian oil companies. Preliminary drilling results were not encouraging, but efforts are continuing.

### b. Electric power

Electric power is the major form of energy available for industrial, commercial, and household consumption in Malta. Since 1962 consumption of electricity has increased 17% yearly. In 1971, gross production of electric power was about 505 million kilowatt hours (kw.-hr.), and per capita consumption (excluding generating-plant use and transmission losses) averaged 720 kw.-hr. Installed capacity was 115,000 kilowatts (kw.) at the end of 1971.

The generation of electricity occurs primarily in two petroleum-fueled powerplants. One is a modern, 85,000-kw. installation at Marsa, serving the dual purposes of power production and water desalinization. The second is an older, 30,000-kw. station built underground about 1 mile to the south-southwest. Fuel for operation of these plants is imported from Italy on a contract basis. In addition to the two powerplants, there are a number of small generating units serving wharves and a few commercial installations in the Valletta port area.

Electricity is transmitted from Marsa throughout the Maltese Islands by more than 120 miles of overhead lines and underground cables at 11 kilovolts (kv), and 33 kv. Gozo and Kemma are connected to the Malta grid by a submarine cable. Electricity is distributed mainly as 1- and 3-phase, 50-cycle alternating current at 220/440 and 240/415 volts.

Plans for further expansion of Malta's electric power capacity were scrapped in 1971, along with the 5-year development plan. The government also canceled a contract with a U.S. firm to provide the equipment for a fifth stage at the Marsa electric power and

desalinization plant. Prime Minister Mintoff has indicated, however, that the Marsa plant will be expanded to a capacity of 145,000 kw. and has requested U.S. aid for the project.

### 3. Metals and minerals (U/OU)

Quarrying accounts for less than 2% of the gross output of the industrial sector. Although employment has dropped and the number of quarrying establishments on Malta declined to 82 in 1968, output has been increasing, reflecting more efficient operations. In 1968, stone quarries, clay and sand pits, and saltpan operations together had a gross output valued at \$1,580,000. Stone quarrying accounts for the bulk of this output.

Malta has no proven mineral resources other than limestone and salt. The coralline and globigerine limestone are quarried for local use as building materials. All other minerals and construction materials, principally cement, some marble, and asbestos, must be imported.

### 4. Manufacturing and construction (U/OU)

#### a. Manufacturing

The share of manufacturing in the GDP was about 20% in 1971. One key facility, the Malta Drydocks, commonly referred to as the dockyard, dominates the manufacturing sector of the economy. The dockyard employs about one-sixth of the manufacturing labor force and is a major earner of foreign exchange. The strategic importance of the dockyard, a key Royal Navy repair facility since the beginning of the 19th century, diminished after World War II. In 1957, the U.K. Government decided to convert the yard from naval to commercial ship repair work. Subsequently, the dockyard was run on a contract basis by a succession of British shipyard firms. In 1968, the Maltese Parliament enacted the transfer of the facility to a Maltese government entity, the Malta Drydocks Corporation (MDC). In 1972, with the appointment of a Maltese national as Chairman of the Board of Directors of the MDC, the dockyard finally became a Maltese institution.

The dockyard has lost money every year since becoming a commercial operation, mainly because of the strike-prone, indolent labor force. Labor problems reached a critical stage in 1970 and the first half of 1971, during which time the labor force was either striking or engaging in slowdown tactics. The Labor government, elected in June 1971, settled the strike, but productivity remains low and customers have been slow to return. The financial result of the labor turmoil

was a negative value added by the drydocks in 1971, which reduced value added by the manufacturing sector from an estimated \$53.4 million to \$46.2 million.

Other manufacturing firms are generally small, averaging only nine employees per plant, and produce primarily consumer goods for domestic consumption. The domestic market is small, a factor that precludes the development of plants capable of realizing the benefits of large-scale operation or the external economies possible in diversified industry. The overall export market is also small. Although some progress was made in developing export markets during the 1960's, progress was slow, and the prospects for further expansion are limited by the fact that Malta has to compete with countries having greater advantages in resources, skilled labor, and experience.

The food processing, beverage, and tobacco industries together accounted for 40% of gross output of manufacturing (excluding the dockyard) in 1968 (Figure 5). Among the food processors, the most important are the bakeries, followed by the flour mills. The beverage-producing firms generally operate on a larger scale than the food processors. Productivity in the beverage industry, as measured by value added per worker, is the highest among the industries shown in Figure 4. Tobacco manufacturers produce both cigars and cigarettes; their productivity ranks second to that of the beverage industry.

The production of textiles has expanded rapidly. In 1968, 45 establishments (compared to 15 in 1963) were producing cotton thread and yarns for weaving and knitting, woolen yarns and fabrics, manmade fibers for spinning, and a variety of other products such as lace, carpets, hosiery, rope, and twine. The manufacture of textiles is important not only in terms of output but also as a major earner of foreign exchange.

Other rapidly growing industries include paper products and quarry products (to support the construction boom). Since 1959, rebuilt and retreaded tires and inner tubes have become important as exports, and several plants producing electronic components and clothing for export have been established on Malta by foreign firms.

Under the Nationalist government of Borg Olivier, an incentive program was developed to attract industry. The program included tax holidays, grants, loans, and subsidized rental of factory space in government-owned industrial parks. Firms established under this program employ 11,000 workers, or 11% of total employment, and are concentrated in the textile, wearing apparel, and rubber products industries, and are predominantly foreign owned.

FIGURE 5. Survey of manufacturing,\* 1968 (U./OU)  
(Output in millions of U.S. dollars)

	NUMBER OF FIRMS	NUMBER OF EMPLOYEES	GROSS OUTPUT
Food processing.....	167	2,785	16.6
Beverages.....	51	1,119	8.8
Tobacco.....	11	311	6.1
Textiles.....	15	2,775	11.2
Clothing.....	200	1,219	2.9
Footwear.....	108	157	0.8
Wood, cork, and furniture.....	285	1,358	2.9
Printing and publishing.....	62	1,167	2.9
Leather and leather goods.....	12	99	0.3
Chemicals.....	28	798	1.1
Nonmetallic minerals.....	87	1,071	1.5
Metal products not elsewhere specified.....	112	771	2.9
Machinery.....	12	565	1.9
Rubber products and transportation equipment.....	213	1,921	7.7
Other manufacturing.....	121	1,135	3.6
Total manufacturing.....	1,910	17,861	79.6

\*Associated repair services generally are included in the respective manufacturing categories; data exclude the Malta Drydocks, for which data are not available.

**b. Construction**

The construction industry boomed during the latter half of the 1960's under the impetus of steady economic growth. Political problems, however, resulted in a slowdown in the economic growth rate and a cutback in government contracting in 1971. With new governmental projects near a standstill and demand for housing slack, building activity slowed abruptly, and the value added by construction rose by only 3.2% in 1971, compared with 17.2% in 1970.

Almost all construction materials must be imported, but some processing plants on Malta manufacture lime and a limited range of precast concrete products. There is no basic steel industry, but reinforcing bars and wire mesh are produced locally from remelted scrap. Millwork, hardware, paints, electric cables, and pipes are all manufactured in Malta, and a number of workshops and foundries fabricate structural steelwork, sheet metal work, and castings from imported materials.

**5. Tourism (U./OU)**

Tourism is becoming increasingly important to Malta's economy. Up to 1960, expenditures by residents of Malta traveling abroad exceeded foreign tourist expenditures in Malta. The government paid little attention to tourism, and the military image of the island discouraged visitors. Following a decision by the government in 1959 to encourage tourism, an

extensive campaign was started under the auspices of the Malta Government Tourist Board to establish Malta as a holiday resort. Government funds and tax incentives were provided to encourage the improvement of facilities for tourists, and funds were allocated to carry out an extensive advertising campaign in Europe. The success of these measures is shown by the rapid increase in the number of foreign tourists from 10,000 in 1958 to 179,000 in 1971. In the latter year, tourist expenditures amounted to almost \$20 million, accounting for one-quarter of Malta's foreign exchange receipts from services.

Although the proportion of British tourists dropped from 76% of total visitors in 1968 to 61% in 1971, the British still dominate Malta's tourist scene. Italian and Scandinavian arrivals have been increasing rapidly, however, and they now account for almost 20% of the tourist trade. Visitors from the United States account for less than 6% of tourist arrivals.

**6. Domestic trade (U./OU)**

Wholesale and retail trade establishments are typically small, privately owned, and owner operated—72% had no salaried employees in 1969 (Figure 6). Only 25 trade firms had more than 20 salaried employees that year. Wholesalers are generally importers as well. On occasion, the government directly imports and distributes certain "essential" products to increase supplies and stabilize prices; milk and butter are recent examples. Few

FIGURE 6. Wholesale and retail trade establishments, 1969 (U/OU)

	TOTAL NUMBER OF FIRMS	DISTRIBUTION BY NUMBER OF SALARIED EMPLOYEES				
		0	1	2 to 9	10 to 49	50 or more
Wholesale merchants.....	126	133	46	189	36	2
Food retailers.....	2,115	2,056	280	72	7	0
Pharmacies.....	120	36	35	48	1	0
Other nonfood retailers.....	2,511	1,697	454	334	26	3
Total.....	5,475	3,922	835	643	70	5

foreign firms maintain their own sales outlets in Malta; instead, they conduct business through Maltese agents.

## C. Economic policy and development

### 1. Governmental economic policies (C)

The Nationalist government of Borg Olivier, which lasted from 1959 until June 1971, followed conservative economic policies, balancing the budget or running a surplus in most years and limiting the economic role of the government to providing incentives for the private sector. In 1971, the Maltese Labor Party came into power on a platform of stimulating economic development—through a program based on “democratic socialism”—to the extent that Malta would be free of its dependence on British military bases. The Labor government inherited an economy that had begun to falter under the pressure of disagreements with the United Kingdom over the terms of aid, problems in the tourist industry, and uncertainties engendered during the election campaign. In its first year and a half, the Mintoff government continued a conservative course in fiscal policy, in spite of the deteriorating economic situation. Mintoff has opposed deficit financing and offered an austere rather than an expansionary budget.

The Labor government, however, has not hesitated to become directly involved in the economy to achieve specific goals. This involvement so far has included importation of milk and butter to maintain low prices, imposition of price and profit controls, and establishment of an emergency labor corps to absorb excess labor. The investment incentive program for new industries has been canceled, although previous commitments apparently will be met. Because Mintoff's first year in office was spent in negotiations to secure economic aid abroad, the government has had few resources to devote to developing a

comprehensive domestic economic program. The policies that have been implemented, however, suggest that the Labor government will be much more active than the Nationalists in controlling and directing economic activity.

#### a. Fiscal policy and the budget

The government's budget is divided into two parts: the ordinary budget and the capital budget. Until fiscal year 1972 (1 April 1971-31 March 1972), total expenditures exceeded ordinary revenues in every year since independence; in the latter year, however, the inclusion of new sources of revenue raised total ordinary revenues above total expenditures. Ordinary revenues, largely from taxes, have financed ordinary expenditures, mostly for social services; capital expenditures have accounted for the government's annual deficits. Financing for investment expenditures has come primarily from the United Kingdom under a financial aid agreement signed in 1964. The share of the annual deficit covered by U.K. funds has varied from 50% to 96% since FY64, except for FY70, when Malta refused to accept aid due to a disagreement with the United Kingdom over the amount of aid to be extended in the form of grants, and Malta covered the entire budget deficit that year through domestic bond issues and other local borrowing. The disagreement was settled in 1970, but in 1971, the new Labor government abrogated the financial agreement and negotiated a rental arrangement with the United Kingdom and its NATO allies for base rights on Malta. The new agreement will provide Malta with \$33 million annually in cash payments, which will be used to finance the budget deficits arising from capital spending during the 7 years beginning in 1972. In addition to foreign aid, domestic resources are also available to finance government projects.

The initial receipt in FY72 of base rental payments from the United Kingdom, transfers from the sinking fund surplus to the ordinary revenue account, and bilateral aid from Italy significantly altered the

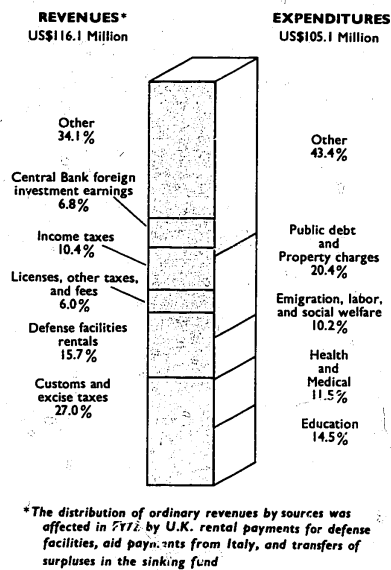


FIGURE 7. Ordinary budget revenues and expenditures, fiscal year 1972 (U/OU)

traditional distribution of ordinary receipts. The largest source of ordinary revenues is customs and excise taxes, which accounted for 27% of the total in FY72 (Figure 7). These payments are supplemented by income taxes and licenses and fees. Earnings on foreign investments made by the Central Bank of Malta account for 6.8% of the government's ordinary revenues. Reflecting rapidly rising incomes since 1964, personal and corporate income taxes have increased rapidly, but their share of total ordinary revenues was only 10.4% in FY72. Thus, the government's traditional dependence on customs and excise taxes has decreased as new sources of revenue have become available.

Ordinary budget expenditures in FY72 were mainly for public debt and property charges and for social services. Expenditures for education, health, and social welfare accounted for approximately 36% of the total in FY72. Public works and utilities, including water, telephone, telegraph, and electricity, account for another 30% of ordinary government expenditures. Ordinary expenditures have been increasing at about

the same annual rate (slightly over 11%) as ordinary revenues since independence.

Nominal capital expenditures have been increasing steadily since independence—from \$11.8 million in FY65 to \$33 million in FY72. However, the greater part of these expenditures has been in the form of subsidies to industry and to the drydocks, thereby overstating actual government investment. Nevertheless, government programs have greatly improved Malta's infrastructure over the period, especially communications, power, housing, sewers, and public buildings.

Under the Labor government capital expenditures are budgeted to decrease in FY73, as follows (in millions of U.S. dollars):

	ACTUAL	BUDGETED
Basic services	3.47	4.01
Economic services	21.09	17.36
Social services	8.54	10.41
Total	33.10	31.78

Expenditures for economic services will continue to absorb the majority of capital resources. These funds will be used to meet previous commitments under the investment incentives program for industry, to absorb drydock losses, and for capital improvements to the drydocks and Luqa Airport. The basic services expenditures will be used for roads and telephones. Over half of social services expenditures will go for housing, with much of the remainder being spent on improving health facilities.

Under the Labor government, certain taxes have been increased and reforms initiated. The numerous foreign residents (mostly British retirees), who formerly enjoyed a low income tax rate of 2.5%, have had their taxes increased to a minimum of 10% of income. Corporate income tax rates also have been increased, from 25% to 37.5%. In September 1972 the Maltese Government announced that a "pay as you earn (PAYE)" system of income tax collection would become effective on 1 January 1973. Although none of these measures has been popular, PAYE has caused particular concern among the Maltese, who are well aware of the difficulties of recovering overpayments from the Ministry of Finance.

#### b. Monetary policy and the banking system

Prior to independence in 1964, Malta's banking system operated through local banks and their foreign correspondents. Between 1964 and 1967 the government, with the help of the Bank of England, the International Monetary Fund's technical

assistance program, and the Bank of International Settlements, planned the new Central Bank of Malta. Parliament approved the Central Bank of Malta Act in late 1967, and the bank was constituted on 17 April 1968. The Act assigned the following functions to the bank: Issuing legal-tender currency notes and coin, maintaining external reserves, controlling credit, developing a capital market, acting as banker to the government and commercial banks, and advising the government on financial matters, functions that were previously handled by independent and uncoordinated government offices.

Although creation of the Central Bank was the first step in the establishment of a modern banking mechanism responsive to monetary policy, the basic legislation controlling the commercial banks was not enacted until March 1970, when the Banking Act was approved by parliament. Covering all phases of banking activities, this act provided the framework for Central Bank supervision of commercial banks and financial institutions. Commercial banks are now subject to reserve requirements, regulation of their foreign currency assets, and control of interest rates.

The new monetary policy tools have not been very effective in influencing economic activity. The Central Bank's discount rate is ineffective, because local banks do not have to borrow from the Central Bank. The high liquidity of the banks also renders reserve requirements useless as a monetary tool.

The Central Bank is required to hold a reserve of gold or convertible foreign exchange equal to 60% of the note and coin circulation and its other demand liabilities. In mid-1972 Malta's currency was backed over 100% by external reserves. Traditionally, these reserves have been held in sterling, but the Labor government has been trying to diversify Malta's foreign exchange holdings, and in mid-1972 sterling comprised only 60% of Malta's foreign exchange.

The leading commercial bank is Barelays Bank D.C.O., which has 31 branches and agencies in Malta and was the bank for the government before establishment of the Central Bank. The largest Maltese-owned commercial bank, the National Bank of Malta, Ltd., has 23 branches. There are three other locally owned smaller banks, one of which is now wholly owned by the National Bank. There is also a Government Savings Bank, formed in 1833, which taps small savings and generally invests the proceeds in London. A small savings bank was founded by a religious order early this century; it is still very small and conservatively run by priests, who have been criticized by the Central Bank for not employing proper banking techniques. The bank is known for strictly respecting the secrecy of its customers' affairs.

Several additional financial institutions have been established since 1968. The Malta Development Corporation (MDC), an autonomous agency fully owned by the government, acts both as a development bank and as an agency for administering foreign aid. Four merchant banks also have been established. Barelays Finance Corporation, Ltd., provides medium- and long-term finance to industry and tourism. The Investment Bank of Malta, Singer and Friedlander, Ltd., and Brandt and Grindlay, Ltd., were also established to provide capital for industry.

## 2. Economic development (C)

### a. Government plans

Malta has been engaged in economic planning since 1959. The principal objective of its three plans has been to develop industry and tourism at a pace adequate to counterbalance the income and employment losses resulting from the anticipated and actual withdrawal of British forces. The core of each plan has been a program of public capital expenditure combined with substantial incentives to private industry.

The First Five-Year Plan (FY60-FY64) provided for the promotion of new export industries and tourism, the construction of a new plant to generate electric power and distill sea water, the extension of port and drydock facilities, and the provision of technical education. Actual capital expenditures by the government during this period, however, were \$53.1 million, considerably below the \$71.2 million anticipated in the plan. The results of the first plan were disappointing: annual growth of the real GDP averaged only 3% during the plan period.

Based largely on the work of a group of experts from the United Nations, the Second Five-Year Plan (FY65-FY69) recommended public development expenditure of \$102.5 million. The major investments were made in industry, tourism, and glasshouse horticulture. Actual expenditure under this plan amounted to \$89 million, almost 75% of which was financed by British aid. These outlays, combined with political stability and the momentum generated by previous efforts, yielded an 8% annual average growth rate, exceeding the modest plan target during the period.

Malta's ill-fated Third Development Plan (FY70-FY74) had the same broad objectives as the previous plans, but it set more ambitious target. The plan aimed for an average annual rate of real growth of 9.4%, which would raise real output by nearly 60% over the plan period. Because of a disagreement with the United Kingdom, which was to provide 55% of the financing, implementation of the third plan was



delayed until October 1970. In June 1971, the newly elected Labor government declared the plan unsuitable and began work on a 7-year plan, implementation of which was to begin in FY74.

In the formulation of its development strategy, Malta relied heavily on advice from the United Kingdom, the United Nations, and other foreign advisers, who unanimously recommended that Malta develop export-oriented industries and tourism to provide employment and raise the level of living. All three of the country's plans have reflected this recommendation, setting high growth rates for manufacturing and tourism.

**b. Incentive programs**

Since 1959, Malta has provided incentives for domestic and foreign investment, such as permission for 100% foreign ownership of companies and land in Malta, unlimited currency conversion, a 10-year tax holiday, duty-free importation of machinery and building materials, reduced duties on raw material imports, and antidumping and countervailing duties as measures of protection. Grants and loans at low interest rates were offered, along with factory space in industrial parks at subsidized rentals. In 1971, industries benefiting from these measures accounted for 43% of employment in manufacturing and 86% of total exports.

Prime Minister Mintoff strongly criticized the incentive programs for encouraging the establishment of uneconomic firms, and in 1971, he announced that

no further concessions would be granted. In lieu of subventions, Mintoff organized an Industries Promotion Council, composed of influential foreign economists and industrialists to advise him as to which industries were appropriate for Malta and what means should be used to attract them. Mintoff conceded that some incentives might be necessary, but they have not yet been defined.

**3. Manpower (U/OU)**

Only about a third of the total population are economically active (Figure 8), because of the small number of women in the labor force. As more industrial plants involving assembly-line techniques are established, more women are expected to join the labor pool.

Manufacturing plants employ almost one-fourth of the labor force, and civil servants and U.K. military employees account for another quarter of total employment. Construction and quarrying provide jobs for 10% of the labor force, while the remainder are employed in various service occupations or agriculture and fishing. The share of workers employed in agriculture and trade has fallen, and this trend is expected to continue. As economic development proceeds, manufacturing and financial services are expected to continue to attract workers, increasing their relative share of the labor force. Employment by the Maltese Government has remained stable, while employment by the British forces has fallen sharply. The British are expected to continue to release labor,

FIGURE 8. Labor force (U/OU)

	1966		1971	
	Number of employees	Percent of total	Number of employees	Percent of total
Total labor force.....	97,364	100.0	109,005	100.0
Unemployed.....	6,584	6.7	5,925	5.4
Total gainfully occupied.....	90,780	93.3	103,080	94.6
Agriculture and fishing.....	6,970	7.2	6,160	5.7
Manufacturing.....	18,870	19.3	25,480	23.3
Construction and quarrying.....	9,700	10.1	11,010	10.0
Wholesale and retail trade.....	11,990	12.3	12,630	11.6
Banking, insurance, and real estate.....	790	0.8	1,590	1.5
Transport and communications.....	3,960	4.1	4,560	4.2
Private services.....	9,220	9.5	13,470	12.3
Electricity and gas.....	780	0.8	960	0.9
Malta Government.....	18,060	18.5	20,510	18.8
Military base departments and British forces.....	10,350	10.6	6,040	5.5
Malta Land Force.....	*	na	670	0.6

na Data not available.

\*Included in Malta Government.

and the Maltese Government hopes that growth in manufacturing will enable that sector to absorb both the workers released by the British and the natural increase in the labor force.

Unemployment has been increasing rapidly from the low level reached during the boom in 1969, as shown in the following tabulation of registered unemployed:

1969 (December)	3,813
1970 (December)	4,962
1971 (December)	5,925
1972 (February)	7,469

The construction industry was hit hardest by the uncertainties associated with the political change-over in 1971 and the subsequent dispute with the United Kingdom. For the same reasons banking, insurance, and real estate have been dismissing employees. At the same time, the British have continued to reduce employment of Maltese nationals. Unemployment reached 7% of the labor force in 1972 and was estimated at 8.5% in early 1973.

The government encourages workers dismissed by the British services to acquire new skills by offering a 6-month basic retraining course, and by financing other vocational training. Four technical secondary schools, four specialized technical institutes, and two industrial training centers provide courses in selected trades. In addition, training is offered to young people entering the tourist and catering industry.

Before 1968, wage increases were relatively moderate, averaging 6% in 1964, 2% in 1965, and 4% in 1967. In 1968, the economy began to experience a shortage of skilled workers, and minimum wages were increased through wage regulation orders issued by the Ministry of Labor on the recommendation of Wage Councils. The Wage Councils—set up for practically all sectors of private industry—are composed of representatives of unions, employers, and government and establish minimum wages enforceable by law. Even considering the minimum wage increases of 1968 and 1969, wages in Malta are substantially below those in western Europe, and recent increases in unemployment have discouraged additional wage increases.

Unions cover less than half the economically active population. The largest, the General Workers Union, controls the drydock labor force and is a politically powerful organization supporting the Malta Labor Party.

## D. International economic relations

### 1. Foreign trade (U/OU)

Malta's trade deficit, which was over \$70 million in 1964, rose rapidly in succeeding years (Figure 9). This

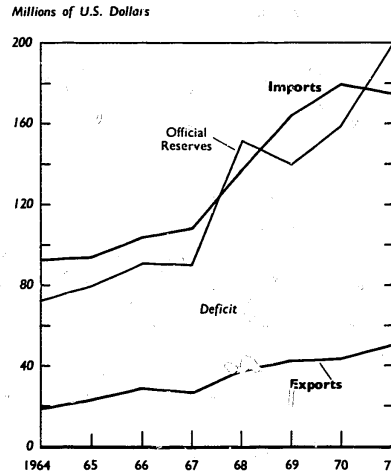


FIGURE 9. Foreign trade, 1964-71 (U/OU)

trend was reversed temporarily in 1971 because of the slowdown in economic activity, which reduced imports, while output increased in a few foreign-owned, export-oriented firms. Increasing imports resulting from rising incomes and industrial expansion, however, are expected to cause further deterioration in Malta's trade accounts over the next several years.

The composition of imports changed considerably during the 1960's (Figure 10). Imports of machinery and transport equipment, 15% of total imports in 1961, increased rapidly under the impetus of the

FIGURE 10. Imports, by commodity (U/OU)  
(Thousands of U.S. dollars)

	1961	1968	1969
Food and live animals	26,708	35,004	38,859
Beverages and tobacco	1,906	3,904	4,213
Crude materials except fuels	1,364	6,659	8,301
Lubricants and fuels	8,010	8,055	7,922
Oils and fats	902	1,028	1,642
Chemicals	4,777	9,129	11,062
Machinery and transport equipment	11,892	27,068	36,189
Other manufactures	23,819	45,334	54,866
Miscellaneous	1,343	1,057	1,196
Total	80,721	137,235	164,248

industrialization programs and accounted for 22% in 1969. The impact of rising levels of living was reflected in the growth of nonfood consumer goods imports, which were one-fourth of the total in 1969. These imports have been increasing at an annual rate of 21%; the overall annual rate of increase in imports since 1966 has been 15%. Food and beverages accounted for 34% in 1961 but constituted only about one-quarter of total imports in 1969.

As a result of the introduction of new industries during the 1960's, the composition of Malta's exports also has changed considerably since 1961 (Figure 11). Agricultural products, which accounted for nearly 40% of exports in 1961, provided about 15% in 1969, while exports of manufactured goods, barely 14% of exports in 1961, rose to 62%. The most important exports of manufactured goods were clothing, textiles and yarns, and rubber products such as retreaded and rebuilt tires and tubes; gloves, plastic goods, furniture, and innerspring mattresses were also significant.

Imports from west European countries accounted for more than 80% of Malta's imports in 1971 (Figure 12). The United Kingdom traditionally has been and still is Malta's principal source of imports, partly because under the U.K.-Malta financial agreement imports for projects financed by U.K. and were required to be purchased in the United Kingdom, and partly because of historical ties and the continued

FIGURE 11. Exports, by commodity\* (U/OU)  
(Thousands of U.S. dollars)

	1961	1968	1969
Food and live animals.....	1,231	3,831	3,984
Beverages and tobacco.....	662	1,573	1,100
Crude materials.....	1,911	1,288	1,552
Of which:			
Metal scrap.....	1,511	1,020	1,242
Seeds, plants, and cut flowers.....	232	900	651
Vegetable oil and fats.....	358	376	331
Chemicals.....	21	651	127
Of which:			
Detergents.....	na	579	371
Machinery and transport equipment.....	214	272	2,139
Manufactured goods.....	726	16,210	20,749
Of which:			
Rubber.....	19	2,103	3,207
Thread and yarn.....	na	3,749	1,777
Textile fabrics.....	54	1,519	1,340
Clothing.....	451	6,208	8,320
Miscellaneous.....	67	43	109
Total exports.....	5,196	27,247	33,391

na Data not available.

\*Excludes reexports.

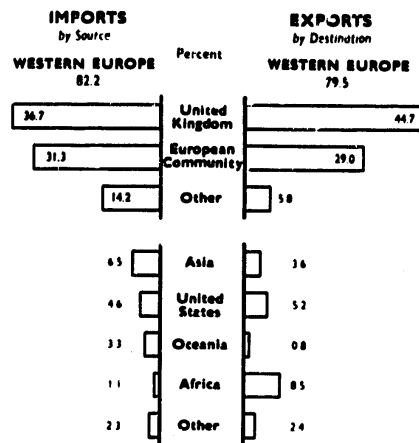


FIGURE 12. Direction of foreign trade, 1971 (U/OU)

presence of British personnel who preferred British products. Malta is a member of the sterling area, and it enjoys certain advantages in trade and payments with the members of that group. Italy is the second-ranking source of imports, supplying 17% of total imports in 1971; purchases from West Germany and the United States accounted for 5.3% and 4.6%, respectively, of total imports in 1971. The United Kingdom provides mostly motor vehicles, machinery, clothing, and fabrics; Italy supplies fuels and food; West Germany, consumer durables and machinery; and the United States, machinery, fabrics, and fibers.

The United Kingdom, Malta's biggest customer by far, purchases textiles; cotton, woolen, and synthetic yarns; knitted wear; vegetables; plants and cut flowers; and rubber products. Italy and West Germany are next in importance as export markets: Italy buys wines, hides and skins, scrap metal, and thread and yarn, and Germany imports scrap metal, flowers, and thread and yarn. The United States accounted for about the same share of Malta's exports in 1971 as in the mid-1960's.

Malta's trade with the U.S.S.R. and East European Communist countries is small and consists largely of imports of foodstuffs and clothing. Although still only about 1% of total trade, trade with the People's Republic of China has been increasing, and that country is now Malta's most important Communist trading partner.

**FIGURE 13. Balance of payments\* (U/OU)**  
(Millions of U.S. dollars)

	1964	1970	1971
Current account balance.....	-0.7	-5.5	5.3
Trade balance, f.o.b.....	-70.2	-109.9	-101.9
Net invisibles.....	69.5	104.4	107.2
Freight, insurance, and transportation.....	-0.5	-3.8	-8.4
Foreign travel.....	1.6	18.7	21.3
Investment income.....	11.5	16.5	18.4
Government, n.i.e.....	42.8	31.6	30.7
Other services.....	-1.6	-3.9	-4.7
Private transfers.....	4.6	27.7	25.7
Official transfers.....	11.1	17.6	24.2
Capital account balance.....	-2.2	**17.1	**1.9
Net errors and omissions.....	2.9	6.7	10.2
Change in official assets (minus sign indicates addition to reserves).....	0.0	-18.3	-17.4

\*These data, from IMF sources, were expressed in U.S. dollars derived by converting Maltese pounds at rates of exchange applicable in the respective years.

\*\*Including SDR's.

**2. Balance of payments (C)**

Malta's balance of payments (Figure 13) reflects the most salient features of the economy—the large, persistent trade deficit and heavy dependence on U.K. military expenditures and aid. In 1971, 71% of the trade deficit was covered by U.K. military expenditures and government aid, which together accounted for 30% of total foreign exchange earnings. In contrast, exports accounted for only 23% of foreign exchange earnings. The specific sources of foreign exchange earnings from U.K. military services and aid were as follows (in millions of U.S. dollars):

	1969	1970	1971
Sales to British servicemen and dependents.....	12.3	13.9	11.7
Material, contracts, etc.....	5.9	7.2	6.1
Payments to Maltese civilians and servicemen.....	14.7	15.2	16.3
Payments for public utility services.....	0.8	0.8	0.8
Pensions and gratuities.....	4.8	6.7	5.9
Grants under the 1964 Financial Agreement.....	4.5	17.4	12.0
Rent for use of military base.....	0.0	0.0	12.3
Loans under 1964 Financial Agreement.....	3.2	0.0	7.5
<b>Total receipts.....</b>	<b>46.2</b>	<b>61.2</b>	<b>72.6</b>

Among other earnings from services, gross receipts from tourism increased rapidly and in 1971 were 13% of foreign exchange earnings; investment income, growing much slower, accounted for another 15%; and ship repairs, ship and aircraft supplies, and bunker fuel, insurance claims, and other minor receipts accounted for the remainder.

The capital account generally shows substantial inflows of foreign direct investment capital. These inflows have offset outflows of Maltese funds, largely portfolio investment in the United Kingdom, and produced a small capital account surplus for Malta. The inflow of capital in part reflects the establishment of new ventures induced by incentives offered to industry under the 5-year plans, and in part the drawings against long-term loans to Malta by the United Kingdom and other aid donors.

With U.K. military expenditures and aid from various donors more than offsetting the trade deficit and capital outflows, Malta has had a surplus in its balance of payments since independence. These surpluses provided a continuous increase in foreign exchange reserves—from \$71.5 million in 1964 to \$198.1 million in 1971. At the end of 1971 foreign exchange reserves were equal to over 13 months of imports at the import level existing at that time.

**3. Foreign aid (C)**

In 1964, when Malta was granted independence, defense and financial agreements were signed with the United Kingdom, under which Malta was to receive \$140 million over a 10-year period ending in 1974. In early 1969, with \$55.2 million of the aid remaining to be drawn, the United Kingdom insisted that the terms of the aid be changed—from 75% grant and 25% loan to 50% grant and 50% loan. Malta refused to accept this proposal, and no funds were forthcoming under the agreement until October 1970, when the United Kingdom withdrew its demand. Through 1969, the

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United Kingdom was almost the sole supplier of economic aid to Malta. Italy provided small loans for electric power development, and some technical assistance came from other sources.

In June 1971, after the Maltese Labor Party victory, Prime Minister Mintoff abrogated the defense aid agreements with the United Kingdom and began negotiating with the United Kingdom and its NATO allies for rent to be paid for the British bases on Malta. In March 1972, a new agreement (backdated to October 1971) was finally reached, calling for U.K./NATO payments of \$36.5 million per year, the agreement to be in force until March 1979. Mintoff stated that he would use these funds to develop the Maltese economy to the extent that military bases would not be needed to sustain the economy by 1979.

In addition to the aid from U.K./NATO, the Prime Minister negotiated bilateral aid agreements with most countries of the industrialized West. Thus far, Western nations have extended approximately \$42 million in bilateral aid, mostly in the form of credits and grants. The major contributors have been West Germany, Italy, and the United States.

The Prime Minister has also signed an aid agreement with the People's Republic of China, in which an interest-free loan of about \$45 million was to be extended over a 6-year period beginning in May 1972. Most of these funds are to be used for development projects to build up light industry. Aid from other Communist countries has consisted only of increasing the number of their ships calling at the Malta drydocks for repairs.

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