

THE IMPORTANCE OF THE GROWING KNOWLEDGE ECONOMY IN MALTA¹

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The knowledge economy is also growing in Malta with a fast pace because our economy has no choice but to adapt and become more flexible in relation to the growing economic sectors that depend on knowledge creation and high value added industries.

The University of Malta is at the forefront of this knowledge creation in Malta. From its humble beginnings in 1592 as a Jesuit College, the University was re-founded under the Knights of Malta in 1769, and continued to grow under the British rule. The University educated the important professions in law, medicine, theology, architecture, humanities, arts and sciences during the 20th century, and was crucial towards providing the needed professionals that worked for our self-government in 1921 and succeeded to bring independence from Britain in 1964.

Tuition at the University was made free during the 1970s and this allowed more students from humble families to be able to attend tertiary education in Malta. In late 1980s, the “*numerus clausus*” entrance requirements were lifted, allowing the students numbers to mushroom into large proportions. Today the University is composed of fourteen Faculties and 27 Institutes and caters for almost 11,000 students in a wide area of subjects, including the modern areas of business, banking and finance, ICT, engineering, digital media, pharmacy, health and social sciences. These new areas have become the back bone of our modern economy.

Knowledge creation is the foundation of the modern tertiary services industries. The primary sector of agriculture, and the traditional secondary sector of manufacturing, required workers to mainly utilize their hands in a repetitive manner. The industrial revolution lifted the standard of living of the masses through the more efficient use of technology. Technological innovation allowed the productivity of labour to drastically increase from the medieval agriculture era, allowing real wages to constantly rise, lifting the overall standard of living of the whole economy.

When the British took over the island of Malta from Napoleon in 1800, the economy was basically dependent on agriculture and ship pirating practiced under the Knights of Malta. The British made Malta a strategic maritime location, basing the head quarters of their Mediterranean navy in the Grand Harbour. The dry-docks offered important job opportunities to many skilled workers, who were paid higher wages than other agricultural or commercial workers in the 19th century. The dry-docks was a university of skills, training workers in several skilled areas, and offering them attractively highly paid comparative salaries.

The invention of the steam engine transformed the sailing ships entering our Grand Harbour into faster steam engine cargo and military ships. More trade was transacted through Malta (Falzon and Lanzon, 2011) which remained a strategic location during the First World War (Falzon, 2012). During the second World War, Malta was more heavily bombed than London

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by the German and Italian air force powers, but was never captured. Malta was awarded the George Cross in April 1942 for its bravery, hardship and resilience during these heavy bombings.

After the War, Malta began its long road for reconstruction and rebuilding of its economy. Malta succeeded to gain independence from Britain in 1964 but its economy remained heavily dependent on servicing the British troops that remained stationed here. In the 1960's the modern foundations of the economy were built on manufacturing and tourism. The free trade association agreement signed with the European Union in 1970, allowed the attraction of many German manufacturing companies leaving Bavaria to relocate to Malta. Export manufacturing flourished during the 1970s, as did the growth of the tourism industry. Although the British troops were downsizing and finally left in 1979, British tourists formed the highest proportion of all incoming tourists. In some way, the local economic dependence on Britain was switched from servicing the military forces, to serving the British holiday makers.

In the late 1980s import trade restrictions were completely lifted while capital controls started to be slowly eliminated. In the 1990s, the structure of the Maltese economy started to be slowly transformed into one embracing more knowledge sectors like financial services, ICT companies and e-gaming. This transformation intensified into the beginning of the 21st century (Ernst and Young, 2013). These new sectors have provided comparatively high paying jobs for our new university graduates in banking and finance, financial services law and compliance, information computer technology engineers and e-gaming professionals.

The structure of the Maltese economy has changed considerably in the last 20 years (Falzon, 2011) :

- The number of Full Time Equivalent jobs in Financial Intermediation, Business Activities and Personal Services almost doubled in 15 years between 1995 to 2010.
- The number of people working in the Manufacturing sector, however, declined by 30 % in the same period.
- Manufacturing was the largest sector by gross value added in 1995. It was replaced by Business Activities by 2010.
- Manufacturing was also the largest sector by employment in 1995. However, Wholesale and Retail became the largest employer by 2010.
- Moreover, Personal services (which includes I-gaming), Business activities, and Financial Intermediation became the three sectors with the highest gross value added per Full Time Equivalent by 2010.
- However, in 2012, manufacturing was still a large sector with 12.5 % of gross value added, while financial and insurance activities accounted for another 8.1 % of gross value added generated in the whole economy.

In the 1970s the German manufacturing companies relocated here because they were seeking comparatively cheap and productive labour force and no customs duties on their re-exports to the European Union. The British tourists took their holidays in Malta mainly participating in the major tour operator packages that were organized in all Mediterranean countries. The restructuring of the Maltese economy in the 1970s from one based on a military base

servicing the British forces in Malta, was done through the servicing of export manufacturing companies through productive and relatively cheap labour force, and through relatively cheap holidays offering a lot of sun, sea and sand.

In the last 20 years, manufacturing lost a third of its workers because the low value added textile factories could no longer compete with rising wages in Malta and comparatively cheaper wages in Asia and Eastern Europe (Bezzina, Falzon and Zammit, 2012). The manufacturing companies that remained however, have introduced more automation and computerized systems and robotic technology. This enabled the productivity of labour to be increased, allowing a proportionate increase in real wages to be offered.

Similarly, tourism has recently reached record highs in the number of tourist arrivals. This has been due to the introduction of low cost airlines in Malta in 2006 and the continuous marketing financial support offered by the Malta Tourism Authority to these low cost airlines. The low cost airlines have developed an alternative model in Europe that fly from secondary airports while tapping the financial support of the local governments in return for stimulating more incoming tourists. The young travellers have especially liked this model, attracted by cheap flights, internet connections and wider hotel selection online.

The financial services industry has provided much growth to the local economy especially since 2004 when Malta became full member of the European Union. This was further intensified after 2008 when Malta adopted the Euro as its currency. Malta has attracted several international banks (like HSBC, Deutsche Bank, Akbank and Turkeye Garanti Bankasi), a good number of captive insurance companies of large European companies, and a large number of hedge funds. Assets under management reported through these hedge funds branches in Malta have mushroomed, attracting several fund administration companies, together with the respective legal, tax, accounting and advisory servicing companies.

Malta has become an attractive and emerging financial centre in the middle of the Mediterranean, offering a diversified economic climate, a stable political democracy within the European Union, capable and talented workers, comparatively low costs, very favourable corporate tax regime, and a sunny and moderate climate. Malta also did not suffer any banking crisis, and its core domestic banks remain conservatively managed, very liquid, and with a strong capital base. In this respect, the World Economic Forum's October 2008 report on global competitiveness **ranked Malta amongst the top ten countries in regards to the soundness of its banking system.**

ICT and IGaming have also been a growing and important sector, employing several local and foreign nationals specialized in this sector. Gross value added per hour worked in this sector was Euro 35 in 2007. Malta has the second highest gross value added among all EU countries in this sector, and stands second only to Luxembourg with Euro 51 per hour worked. These figures show the importance of this new sector for the Maltese economy and the necessity to protect and continue to help this sector to flourish and grow without any unnecessary constraints.

In spite of these economic achievements, Malta still enjoys almost half the productivity per hour of that enjoyed on average in the Euro zone countries (Falzon, 2011). In 2007, the gross value added per hour worked in the whole economy in Malta was 15 Euro, compared to 29 Euro of gross value added per hour produced on average in the Euro zone 17 countries. Similarly, the compensation of employees per hour worked in Malta in 2007 was 7.54 Euro, compared to 16 Euro enjoyed on average by workers in the Eurozone 17 countries.

The EU 27 Member States can be grouped into three categories: the Core group (composed of the northern industrialized countries like Germany, France, UK, Netherlands and Sweden), the Mediterranean periphery (composed of Spain, Italy, Portugal, Malta, Greece and Cyprus), and the Eastern countries (that left the Soviet Block in 1989).

The northern industrialized countries produce the highest gross value added per hour worked, and so enjoy the highest compensation of employees per hour in the whole European Union. The Mediterranean countries fall in the middle, while the Eastern and Central European countries have the lowest productivity per hour and the lowest wages per hour.

The challenge of the Maltese economy in the near future is to hasten its economic development and increase its gross value added per hour faster than the EU average. Only in this way can Malta improve its standard of living and converge to the EU average. In 2007, Malta ranked the fifth among the six Mediterranean countries in terms of gross value added per hour worked, and ranked in the last place in terms of compensation of employees per hour worked among the other six Mediterranean countries in the European Union (Camilleri and Falzon, 2013).

The Global Competitiveness Report 2013-2014 (World Economic Forum, 2013) assesses the competitiveness landscape of 148 economies, providing insight into the drivers of their productivity and prosperity. In this Report, which remains the most comprehensive assessment of national competitiveness worldwide, Malta has been placed in the 41st place, or among the top 28 % of all countries in the world. Malta was ranked ahead of Italy (49th), Portugal (51th), Cyprus (58th) and Greece (91th), but below Germany (4th), Luxembourg (22nd), Ireland (28th) and Spain (35th).

Herein lies the economic challenge for the Maltese economy in the next decade. A national effort needs to be made to help Malta achieve a higher ranking, in terms of productivity, competitiveness and gross value added per hour worked (Bonnici, 2013). Malta needs to constantly improve its position among the Mediterranean and the other EU countries, and not fall behind the fast growing Eastern and Central EU countries.

This will not be an easy task. All the other EU countries will continue to grow, some at a very fast pace. To go up in the standard of living ranking, Malta needs to grow faster than the other EU countries. However given his history of survival and resilience, its strategic place in the Mediterranean, its flexible and talented work force, and its recent membership in the European Union and the Euro zone, many believe that Malta will continue to rise to the future economic challenges, and remain a free country where its citizens can continue to enjoy ever growing economic benefits and rising standards of living.

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