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INTERVIEW

Renowned hotelier and former Island Hotels Group CEO Winston J. Zahra confirms that he is set to head a new international hospitality start-up.

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PRIME MINISTER JOSEPH MUSCAT IN A MEETING WITH THE MDB'S BOARD OF DIRECTORS AND CEO. PHOTO: DOI



ANALYSIS

The changes instituted by the new MiFID II rules have raised concerns among some industry bodies who say the cost of implementation will be shouldered by investors.

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STOCK MARKET REVIEW

Which types of investors are really set to benefit from the introduction of MiFID II?

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Malta Development Bank aims to staunch capital funding gap costing billions

Martina Said

Malta risks losing between €2.3 billion and €3.1 billion in potential capital over the course of five years due to the surfeit of projects that are considered to be market failures, according to Professor Josef Bonnici, Chairman of the newly-established Malta Development Bank (MDB).

"According to a study by a private consultancy firm, market failures in Malta have been estimated to range between €2.3 billion and €3.1 billion over five years, equivalent to between 29 and 39 per cent of Malta's 2014 GDP," Prof.

Bonnici said, stating that there are a number of situations that can be defined as market failures. "There may be a shortage of suitable collateral that can be provided by borrowers (especially in the case of SMEs), a higher element of risk - as in the case of start-ups - or that the size of the loan is too large, for example in infrastructural projects, or the duration is too long because the gestation period of the project extends over a longer timeframe than banks are normally comfortable with."

The establishment of the Malta Development Bank, which marked the start of its operations in December 2017, aims to sup-

plement the lending activities of commercial banks. It's the first of its kind in Malta - a fully Government-owned bank with a specific remit that is aimed at supplementing the lending activities of commercial banks.

In this first interview since the bank's launch, Prof. Bonnici said that while the banking system in Malta has been servicing the borrowing needs of investors and industry very effectively over the years, there are cases where investors come up with viable investment projects and yet, commercial banks might be unwilling or unable to provide them with loan facilities.

"This problem has long been in existence, but it has become even more acute in the wake of the international financial crisis which led to a significant reduction in the risk appetite of banks worldwide and a marked tightening of the banking prudential regulatory framework to ensure that the commercial banks' capital position can withstand shocks and is not exposed to undue risks," said Prof. Bonnici. "The MDB's overriding objective is to address such market failures by offering financing facilities to support productive and viable

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INDUSTRY FOCUS

Key players discuss Valletta's transformation, and the European Capital of Culture's impact on Valletta and beyond.

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NEWS

Putting Malta at par with other EU member states

Continued from page 1

operations where the market is unable or unwilling to accommodate such activities on its own, in whole or part."

He added that the MDB's vision is to make a significant contribution towards sustainable economic development by encouraging inclusive and environmentally-sustainable economic growth and infrastructure development. "It will do this by linking entrepreneurship, investment and economic growth to improved living conditions, a higher quality of life, and better social inclusion." The MDB will be opening up numerous opportunities, he stated, primarily by filling an institutional gap, putting Malta at par with the other EU member states, virtually all of which have one or more promotional bank. "The MDB will be helping to stimulate new investment, job creation and social welfare, through collaborative arrangements that will be negotiated with strategic partners, both locally and abroad." He said that the MDB can also facilitate the blending of EFSI (European Fund for Strategic Investments) with ESIF (European Structural and Investment Funds) at project level, and will be able to borrow from international institutions or local sources for on-lending to smaller projects under an umbrella fund. "The list is endless and the opportunities are many."

A pertinent question in light of the bank's establishment is whether it will compete with private commercial banks, but Prof. Bonnici insists that the MDB will be complementing and supplementing the operations of market players, rather than competing with them. "In fact, the larger portion of the MDB's operations will take the form of so-called second-tier lending, that is, offering facilities primarily through financial institutions. These intermediaries will be responsible for the client due diligence process and project appraisal, and they will select and assess loan applications of end-cus-

"The MDB's overriding objective is to address market failures by offering financing facilities to support productive and viable operations where the market is unable or unwilling to accommodate such activities on its own."

tomers under promotional financing schemes which will be pre-agreed between the MDB and the intermediaries. This process will ensure a complementary relationship between the MDB and the intermediary banks, and will also enable the MDB to assume a leaner structure, thereby fulfilling its public policy role in a more cost-effective manner. Under such schemes, the focus will be on SMEs that cannot otherwise be accommodated by private financial institutions in spite of having feasible projects."

In general, the MDB will be offering five main types of facilities, namely loans, guarantees, and, to a lesser extent, equity participations, underwriting and advisory services. "It is well known that the major cause of market failures in Malta is not a shortage of liquidity or loanable funds, but a shortage of adequate collateral that can be offered by prospective borrowers. Therefore, it is envisaged that the MDB's major contribution will be by way of providing guarantees," said the Chairman.

The MDB will be in a position to cover a wide range of operations where there is market failure. The main sectors that it is expected to be engaged in are: Private Sector Development, in particular financing the private sector through innovative financing, credit enhancement, venture capital and advisory function; Skills and Technology, specifically sustaining competitiveness by investment in innovation, skills,

knowledge-generation and technology; Infrastructure Development of regional or national importance; Green Economy, mainly supporting clean energy and energy efficiency projects, sustainable transport, and water resources; and Community Services, in particular supporting social enterprises operating community services in such sectors as education, health and housing.

Asked to elaborate on the criteria for businesses or entities to apply for funding, he explained that MDB lending may be on state-aided terms or on market terms. "Aided financing must be in accordance with the EU State Aid regulations, in particular the General Block Exemption Regulation, the de Minimis Regulation and other EU financial instruments and aid schemes approved by the Commission. MDB financing on market terms is also subject to certain conditions. For instance, in the case of infrastructure projects, participation by private investors must be at least 50 per cent of the projects' costs on a *pari passu* basis with the bank."

Once the MDB launches new schemes to enhance access to finance for SMEs, such firms will need to go to the participating financial intermediaries to present their request. "Furthermore, all requests for MDB financing must be bankable projects, that is, viable projects that have satisfactory revenue-generating potential. In fact, the MDB Act specifies that loan applications have

PROF. JOSEF BONNICI,
CHAIRMAN OF THE MALTA
DEVELOPMENT BANK (MDB).



to be assessed according to sound banking principles."

With Government being the only shareholder of the bank, it has been questioned what or who exactly the bank is accountable to. Prof. Bonnici said that the MDB Act obliges the MDB to present its Annual Report and Financial Statements to Parliament by not later than four months after the end of its financial year, and is subject to the prudential oversight, regulation and supervision of a Supervisory Board appointed in terms of the MDB Act. "The Supervisory Board is composed of very senior officials from the Malta Financial Services Authority, the Central Bank of Malta, the Ministry for Finance, as well as two independent professionals with banking or regulatory experience. The MDB may also be subject to inquiry by the Auditor General."

As the first of its kind in Malta, the MDB brings with it many mile-

stones, not least for Prof. Bonnici himself who will be the first Chairman of the bank. He has long been a firm believer in the need to establish a national development bank, and is convinced that the institution will have a lot to offer for the furthering of Malta's socio-economic development. "During my term as Central Bank Governor, I had made a number of public statements in favour of such an institution and had also presented a proposal to the Cabinet for the setting up of such a bank. I am very glad that this vision is now becoming a reality."

As for challenges, Prof. Bonnici said that the MDB still has to go through the capacity-building process. "It will be important for the bank to recruit the appropriate pool of personnel with the right skills and to continue to deepen the technical expertise in this new sphere of the financial services sector."



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EDITORIAL

Preventing the cost of market failures

It has been over a decade since the global financial crisis broke out, starting in late 2007 with a crisis in the subprime mortgage market in the US, and snowballing and plunging the world into a full-blown international banking crisis within a year. Excessive risk-taking by banks such as Lehman Brothers, which collapsed in September 2008, magnified the global impact of the crisis. Despite tremendous efforts, ranging from the bailing out of financial institutions at huge cost, to the introduction of analgesic financial policies designed to prevent the entire worldwide financial system from imploding, a chain of dismal events followed – the global economic downturn and the Great Recession which lasted five years, followed by the European debt crisis, which muffled economic growth within the Eurozone as well as the European Union overall.

For better or for worse, the global financial crisis left deep scars on the banking landscape worldwide. Banks became far less open to risk, and the banking prudential regulatory framework was tightened to ensure that commercial banks' capital position would be able to withstand shocks if anything like that ever happened again, whilst preventing their exposure to undue risks. Objectively, this is not a negative development – indeed, the cavalier attitude to lending by the Lehman Brothers and similar made the global financial crisis the worst of its kind since the Great Depression in the 1930s. Caution would have served well in that case, as it did Malta, which emerged from the crisis with its economy and its financial standing relatively unscathed. However, this does mean that years later, there are several instances of investors who come to banks with sound investment projects and are rejected as candidates for a loan, either because they don't have enough collateral to fit the bank's criteria, or because they need too much money to carry out their vision, or because it will take the project too long to start turning a profit. In either case – the bank won't, or the bank can't – it yields the same result: the project fails to get off the ground.

These failed projects are described in our cover story by Prof. Josef Bonnici, Chairman of the newly-established Malta Development Bank (MDB),

as market failures. The MDB commissioned a study by a private consultancy firm, using 2014 as base year, which computed a forward-looking estimate of the market gap over a period of five years, as computed at the time of the estimation report (2015). In estimating the value of the projects or investments that risk failing to materialise, due to lack of sufficient access to financing from the market owing to market failures, the bank made the shocking discovery that Malta could be looking at losses of between €2.3 and €3.1 billion over the course of five years. At its most conservative, the figure amounts to 29 per cent of Malta's 2014 GDP, but it could be up to 39 per cent – almost two fifths of Malta's entire yearly GDP.

The MDB, which went through Parliament with full consensus from both sides of the House – “as has been the general pattern characterising financial services legislation over the past two decades,” Prof. Bonnici remarked – seeks to prevent these costly market failures by stepping in to offer financing facilities where commercial banks can't. Its creation is aimed at helping to stimulate new investments, new jobs and new ideas. Virtually all other EU member states have one or more such banks, and the founding of the MDB aims to put Malta at par with the other EU member states, allowing its innovators to bring to fruition new projects in areas ranging from technology, innovation and knowledge generation, to the green economy to education, health and housing. Never has it been as necessary as it is now. Europe has made a strong recovery from the worst ravages of the financial crisis, but it's not out of the woods yet – Brexit looms, still murky in its terms, but with the promise of greatly reduced funding from one of its most important contributors. On the other hand, Malta's economy keeps roaring forward, but despite the hefty cash injection it has received in the past few years that has electrified certain sectors of the economy, Malta still lags behind when it comes to research and innovation. What it really needs are bright, original ideas, and a way to let visionaries take their dreams from the clouds to the streets. If the MDB accomplishes what it has set out to do, it could be the catalyst that transforms the Maltese economy for years to come.

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BUSINESS OPINION

Culture that is accessible to all



Catherine Tabone

This year Valletta is holding the title of European Capital of Culture (ECOC), giving Malta a unique opportunity to celebrate its identity, heritage and aspirations, and to share our story as a nation around the world. Now in its 34th year, the European Capital of Culture experience is a remarkable one, and I am most glad to be at the helm of the organisation with the most exciting remit in Malta, contributing directly towards making Valletta and Malta take centre stage in 2018.

The Foundation has worked hard to ensure that culture is democratised and inclusive rather than elitist – accessible to all, not merely the few. We have created a strong cultural programme that invites people at grassroots level to become co-creators and participants. It sees the involvement of around a thousand local and international artists, curators, creative collectives, performers, workshop leaders, writers, designers, musicians and filmmakers. We want to encourage cultural practitioners, residents and visitors to engage with important

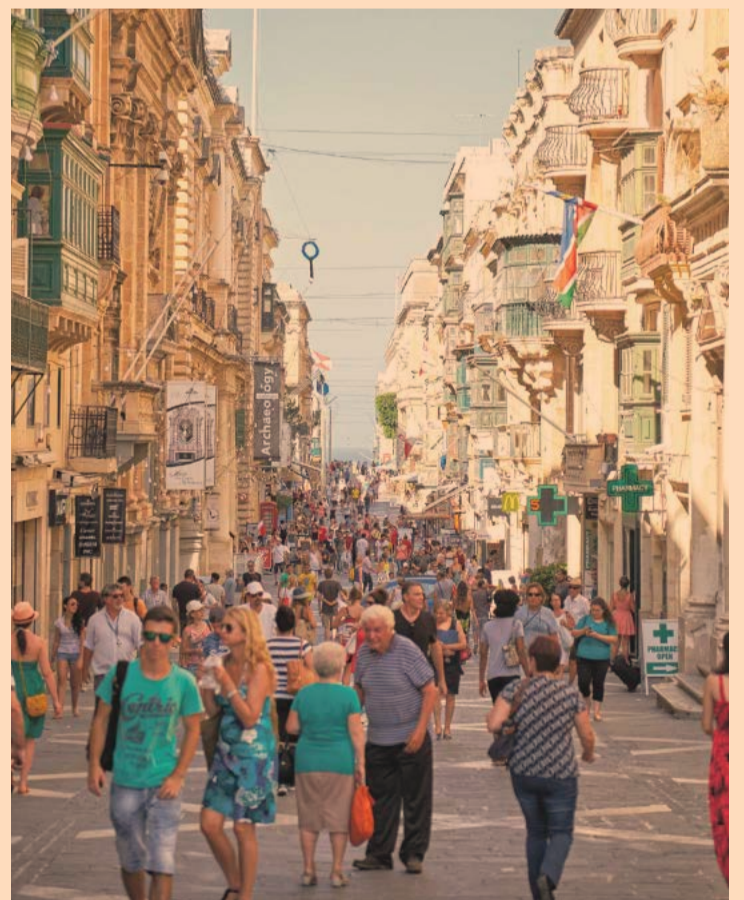
issues in diverse and immediate ways. With over 400 events in store, this year holds something for everyone. From participatory events and initiatives, festivals within the city, community workshops, interactive exhibitions, and platforms designed to support inventive production and debate, to extra-curricular activities, cultural initiatives for young people, creative residencies within the Euro-Mediterranean region and collaborations with countries as far as Japan. There's also a whole spectrum of innovative events involving film, music, theatre, opera, and much more, as well as talks and panels hosting some of the world's leading thinkers, movers and shakers.

Our vision has always been to act as a catalyst and provide opportunities for economic and cultural transformation. A huge effort was undertaken by the Foundation to analyse and understand the needs of our society and of the Valletta community. The realm of human experience is our priority. 'Quality of life', 'well-being', 'urban renaissance' and 'liveability' became central concepts which animated our discourse and helped shape our policies. People require cities to be connected, vibrant, safe, clean, sustainable, resilient places. We believe ours needs to be re-imagined in a way that makes street life engaging and inevitable. We always felt that we must do everything to encourage links that urge people to co-operate and strive towards the common good. The Foundation has worked ceaselessly to prepare Val-

letta for success and international excellence in the 21st century.

The ECOC title has added vigour to Government's efforts to give culture the importance it merits. I can say with considerable satisfaction that the arts are at the heart of this Government's agenda – and rightly so, for culture has always been Malta's strongest resource. In this context, it is important to stress that at the centre of the 2018 programme are several infrastructure projects designed to evolve and expand well beyond this year. Among these are MUŻA, the Valletta Design Cluster, Is-Suq tal-Belt and Strait Street. The Valletta 2018 Foundation has always been committed to providing opportunities and spaces that enable our creatives to express themselves to the fullest, even beyond 2018. For us, legacy is not just a buzz-word but a guiding principle. What we create today is tomorrow's inheritance. Building knowledge, capacity, infrastructure and internationalisation have been vital ingredients of our strategy for 2018 and the future.

Intentionally, the Cultural Programme is planned to have a significant, long-lasting effect on Valletta's cultural vibrancy, strengthening networks and opening up new possibilities. A staggering €40 million have been invested in the run-up to prepare our creatives to meet the European Capital of Culture challenge and equip them for the years ahead. All of this work will be taken up and built upon by the Valletta Cultural Agency – an entity that will be created in 2019 – which is one of the



commitments included in the Government's programme.

The Maltese islands are a combination of history nestled in cutting-edge contemporary innovation. Our culture is a construct of who we were, who we are, and who we shall be. This is why the Valletta 2018 Foundation is continuously

nurturing an environment that is vibrant, accessible, regenerative and sustainable, that will take Valletta and Malta beyond 2018 and into the future.

Catherine Tabone is the Executive Director of the Valletta 2018 Foundation.