Memorandum to Cabinet by the
Hon Minister of Finance, Customs and Port

As Hon. Members are aware the fact that no agreement has been reached with the British Government on the terms of aid during the quinquennium ending March, 1974 implies that no payments are being made to Malta in terms of the Financial Agreement. It follows that all disbursements which are currently being made have to be financed out of current revenue and out of the Floating Debt arrangements (Treasury Bills, Ways and Means advances from the Central Bank and overdraft facilities). The Government, at the moment, has no legislative powers to float development loans as the enabling law to float "Local Development Loans" expired on the 31st March, 1969.

The projection of cash flows over the next few months reveals that if no funds are received from British sources there will not be enough cash available to cover all disbursements after September 1969 unless legislation is enacted to enable the Government to raise loans. Technical opinion is of the view that loans should be spread over a period to lessen the risk of a large amount of stock remaining in the hands of the Central Bank as underwriters. To enable this to be done the required legislation should be passed before Parliament goes into recess.

This situation poses a number of problems. If Hon Ministers agree that borrowing legislation should be passed through the House before the recess, - and there is no safe alternative to this course of action unless the Government is satisfied that an agreement is likely to be reached with the British Government before September - a decision will also have to be taken as to whether the borrowing legislation should be limited to a period of one year or to the full five years of the Plan as would have been done in normal circumstances. It is necessary to give an upper limit to the borrowing powers of the Government and whilst the House has an indication

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of the order of magnitude proposed for the first year of the next Five Year Plan, no indication has been given of the size of the Plan as a whole, nor can such an indication be given before the present controversy with the British Government is resolved.

As things stand, therefore, there appears to be no alternative but to go to the House with loan legislation covering only the current financial year. Here again, the estimates have been drawn up on the understanding that some £5million be found out of local loans and £6 million out of U.K. aid. If the present impasse remains unresolved the Government will have to borrow up to a limit of £11 million for the current year.

It is not difficult to envisage the sense of shock when it is realised that Government in one year will be raising by way of local loan more than double the amount raised over the full period of the last five year plan. Faced with such a large loan financing exercise the local private investor would tend to question the Government's judgement and control over the situation and to seek safer investment abroad. Such a state of affairs will naturally shake confidence and there appears to be a very limited chance of the Government being able to raise £11 million as local loans from the private sector. This would imply that the Central Bank as underwriters would have to purchase out of reserves, the balance which is not subscribed by the public. In other words our reserves would start falling and this would in turn aggravate the people's loss of confidence.

Such a situation is obviously dangerous both economically and politically. We do not know when the present controversy is likely to come to an end and clearly we cannot ask the House to approve a loan for £11 million without serious political and economic consequences. The amount required can only be reduced substantially by a drastic pruning exercise which would affect the whole basis of the Plan and could have adverse consequences on income and employment. All this points towards the need for an early conclusion to the present controversy over the terms of aid with the British Government.

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Once it is not possible to go to the House for a loan covering the total capital expenditure for this year a good alternative would be to introduce legislation giving the right to the Government to raise a local loan of £4.3 million as provided in the draft estimates. It is anticipated that such a loan, together with the floating debt, will provide the necessary cash to meet forseeable expenditure up to December of this year. This would give the Government a valuable breathing space during which the terms of aid could be negotiated. Such a course of action would imply that the Government is still hopeful of a satisfactory solution to the impasse thus maintaining public confidence. If, however, the matter is still unresolved by December, Government will have to ask the House for a further £6 million loan with the consequences described above, and in particular this would imply that a substantial part of this loan will have to be underwritten by the Central Bank and financed out of Malta's reserves.

One final point. We cannot foresee at this stage what the final outcome of the U.K. aid negotiations will be and for all we know we might have to settle for conditions which might necessitate a pruning of the Plan to ensure that the debt servicing charges could be borne by the recurrent budget. To forestall this eventuality it is imperative to explore the possibility of reducing this year's expenditure. It is recommended that an exercise be performed to assess what expenditure can be deferred and which schemes can be slowed down without affecting Malta's economic development.

Hon. Minister are requested to approve:-

(a) that a bill be introduced enabling the raising of £4.3 million local loans; and

(b) that the exercise referred to in the preceding paragraph be started straightaway.

18th June, 1969.