



Irish Fiscal Advisory Council

Economic Outlook: Growth, Risks, and Sustainability

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Irish Fiscal Advisory Council

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Hotel, Sutton



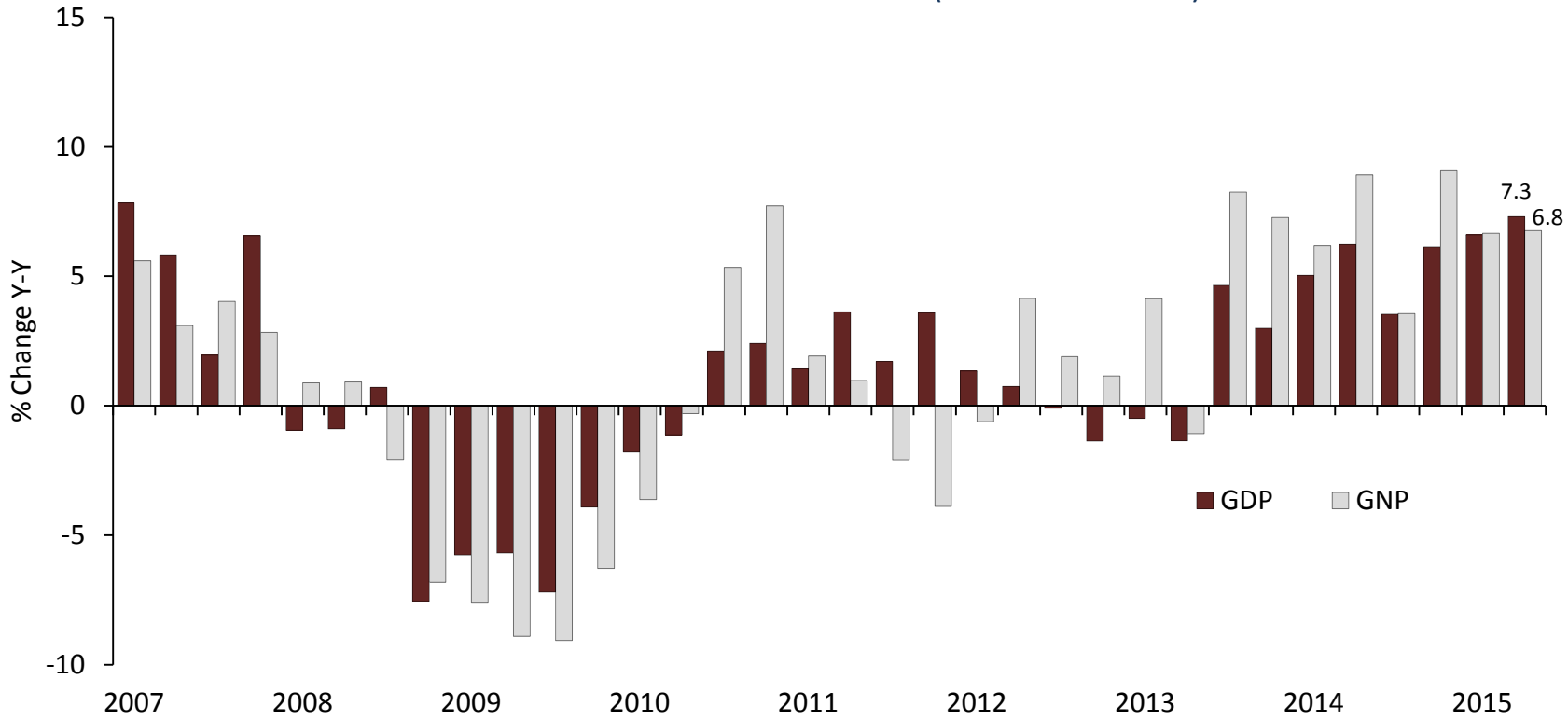
Overview

- Recent macroeconomic performance and outlook
- Risks to the outlook
 - Internal
 - External
- Sustaining growth
 - Value of the new fiscal framework



Strong recent growth performance

Real GDP and GNP Growth (% Year-on-Year)

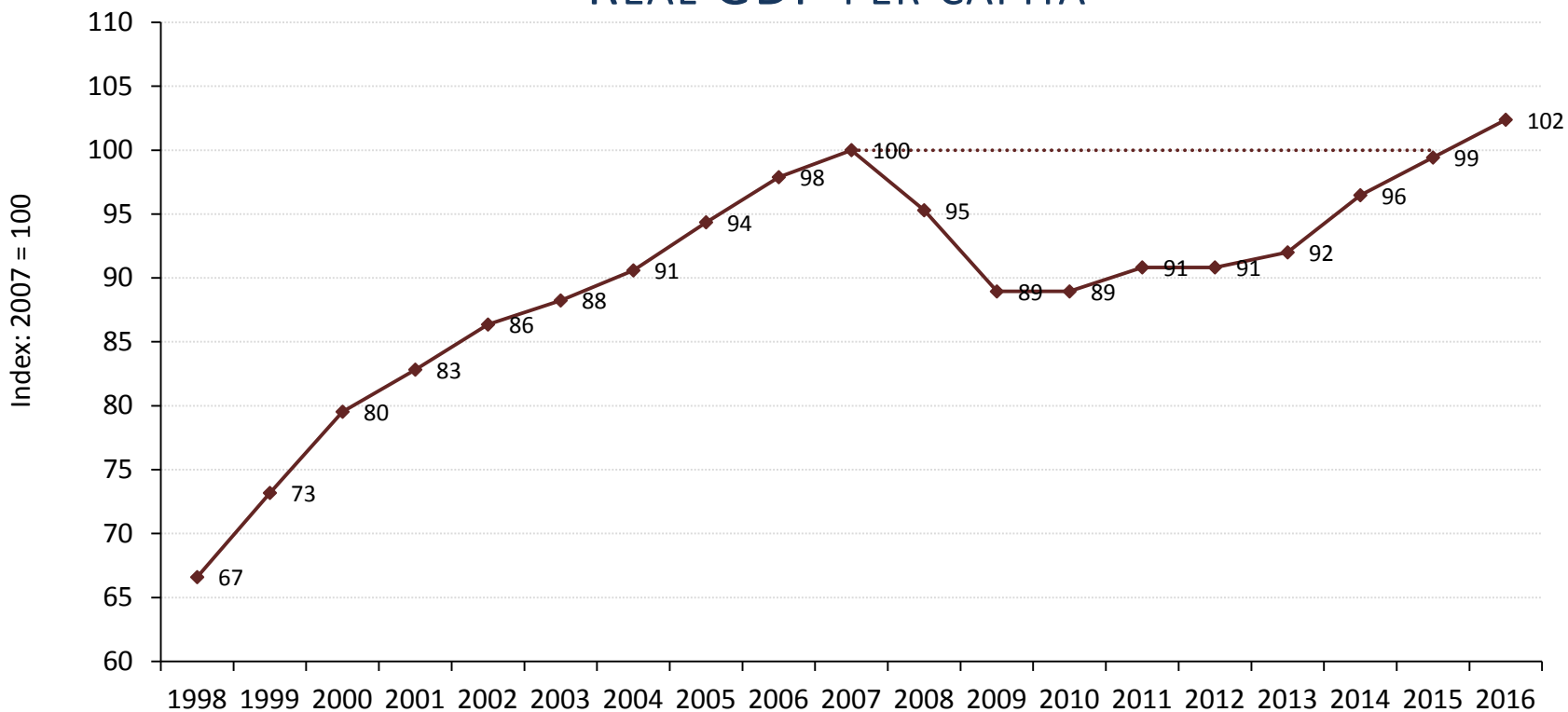


Source: CSO.



Near return to pre-crisis peak

REAL GDP PER CAPITA

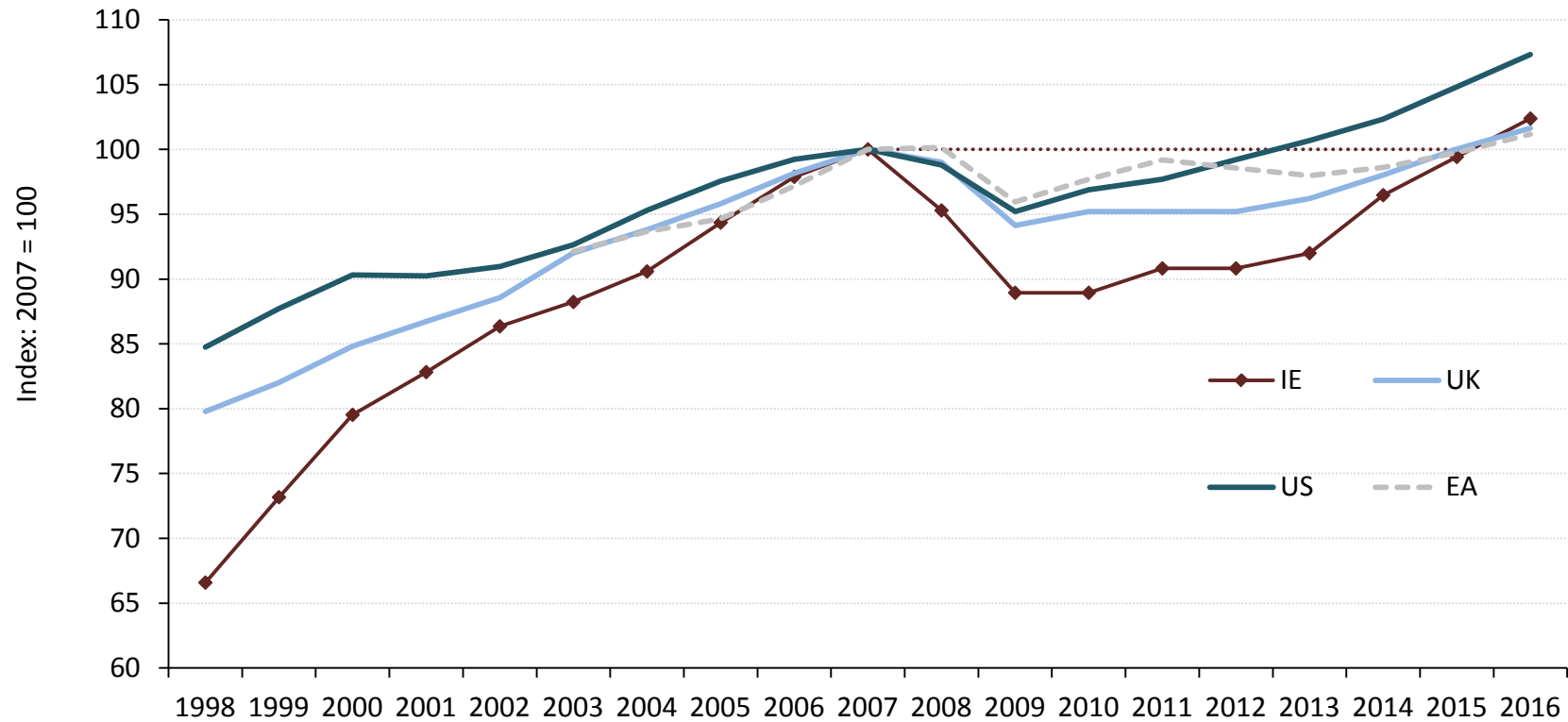


Source: CSO; internal calculations.



Sharper downturn + recovery than trading partners

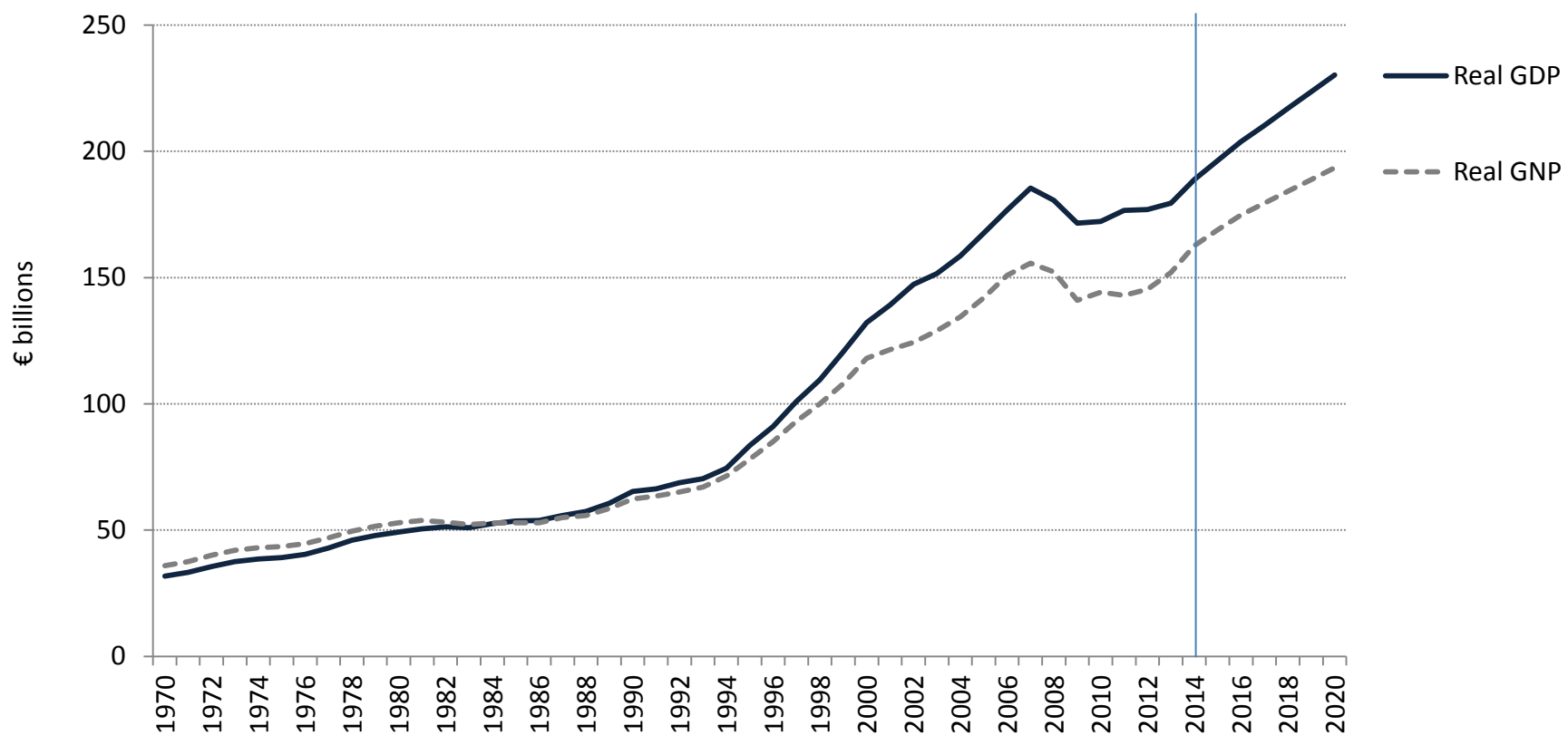
REAL GDP PER CAPITA



Sources: CSO; IMF and internal calculations.



Central scenario is for solid growth to continue

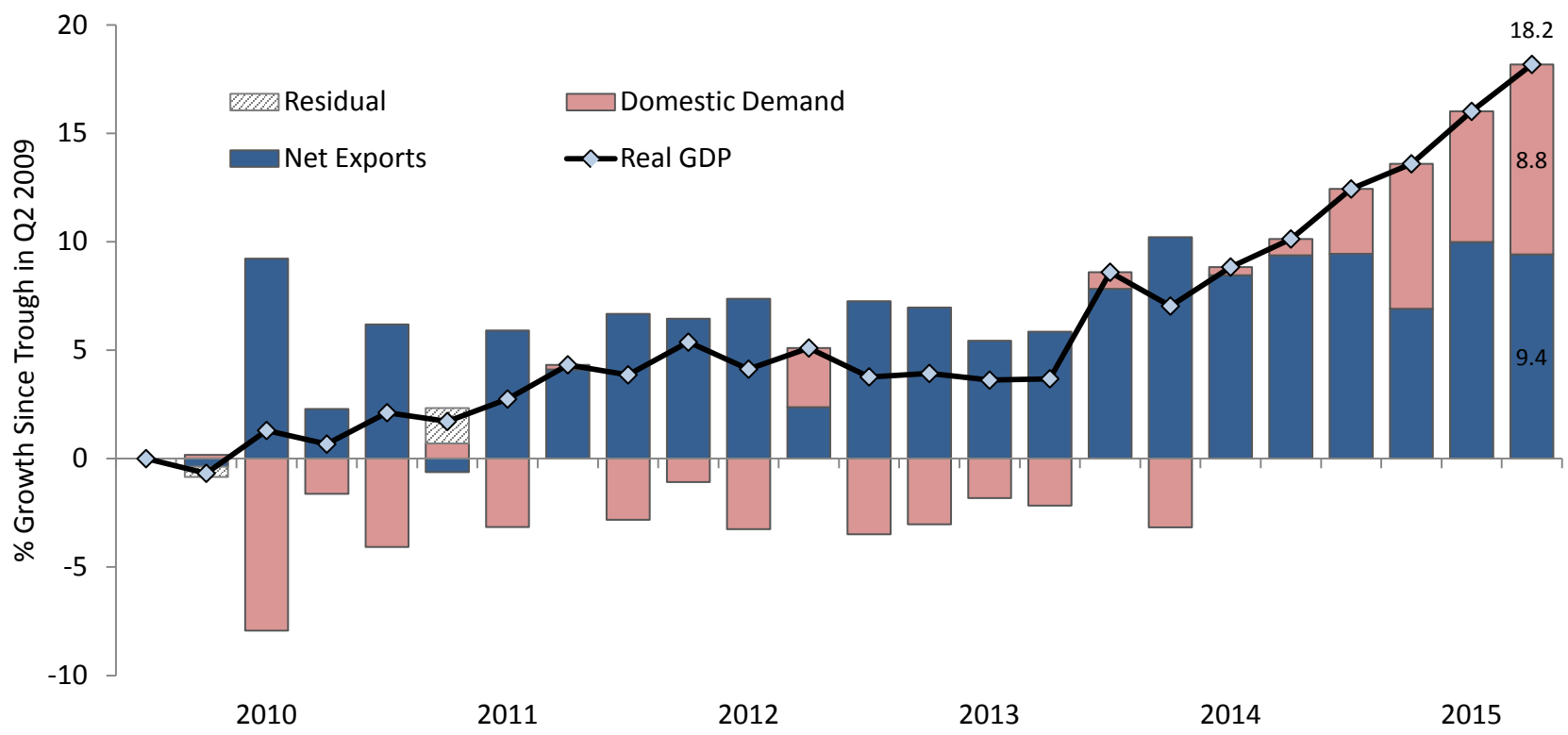


Sources: Department of Finance; CSO.



Increasing contribution of domestic demand to recovery

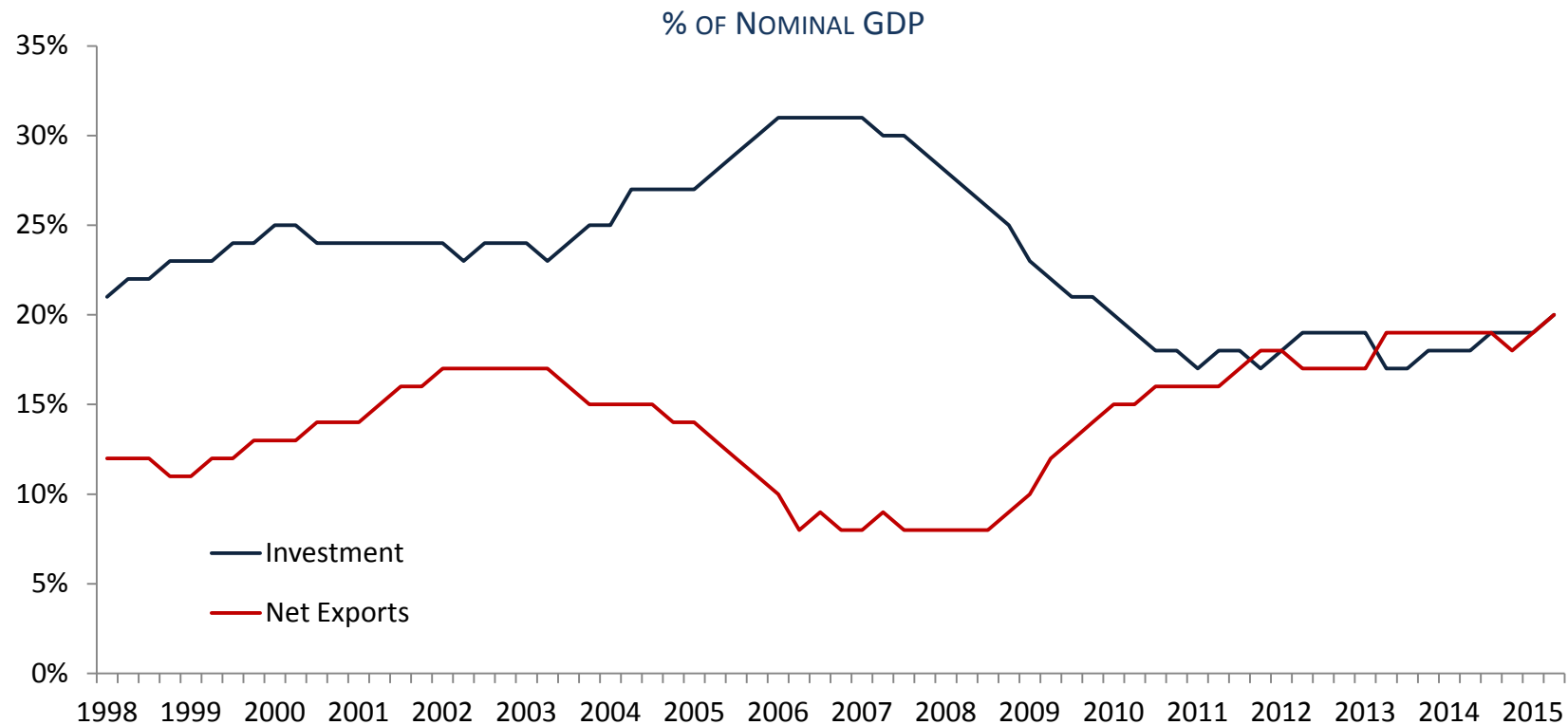
CUMULATIVE CONTRIBUTION TO REAL GDP GROWTH SINCE TROUGH



Source: CSO.



Evidence of rebalancing



Source: CSO.



Challenges with interpreting the National Accounts

- Patent cliff
- Contract manufacturing
- Re-domiciled PLCs
- Treatment of profits in IT sector
- Aircraft leasing

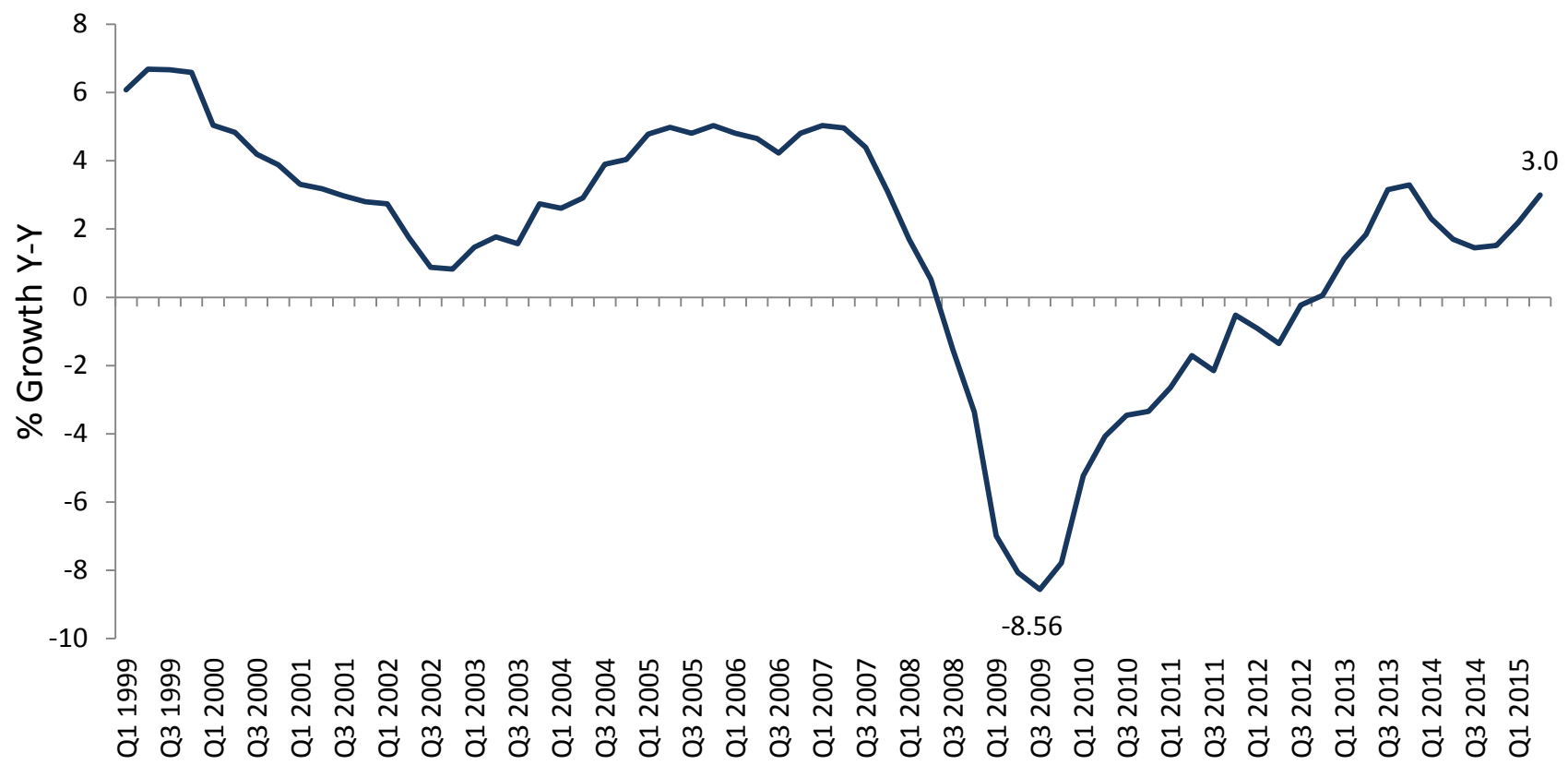


But high-frequency data confirm strong growth

- Employment
- Unemployment
- Industrial production
- Retail sales / consumer confidence
- Exchequer returns



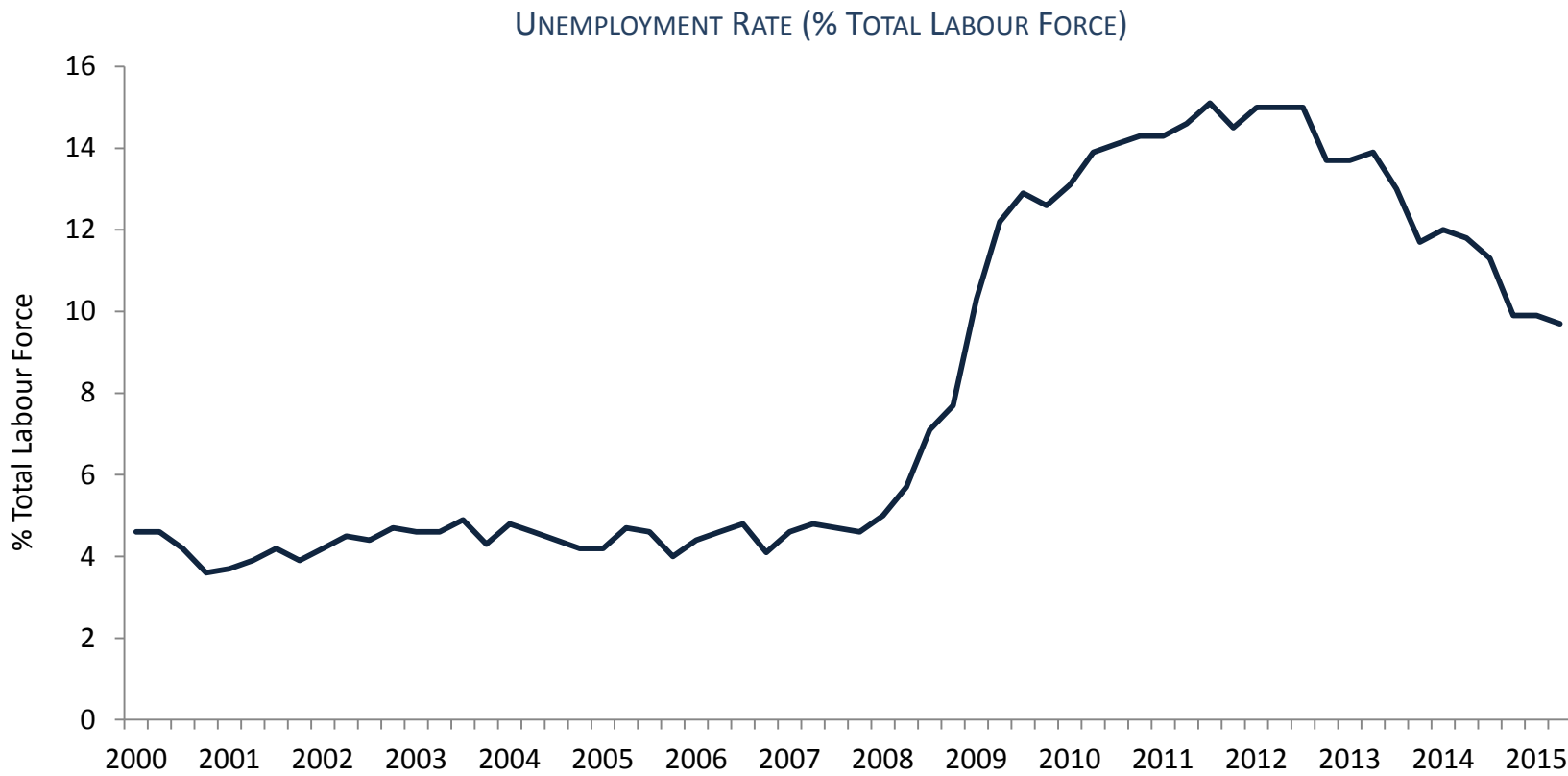
Encouraging employment growth



Source: CSO.



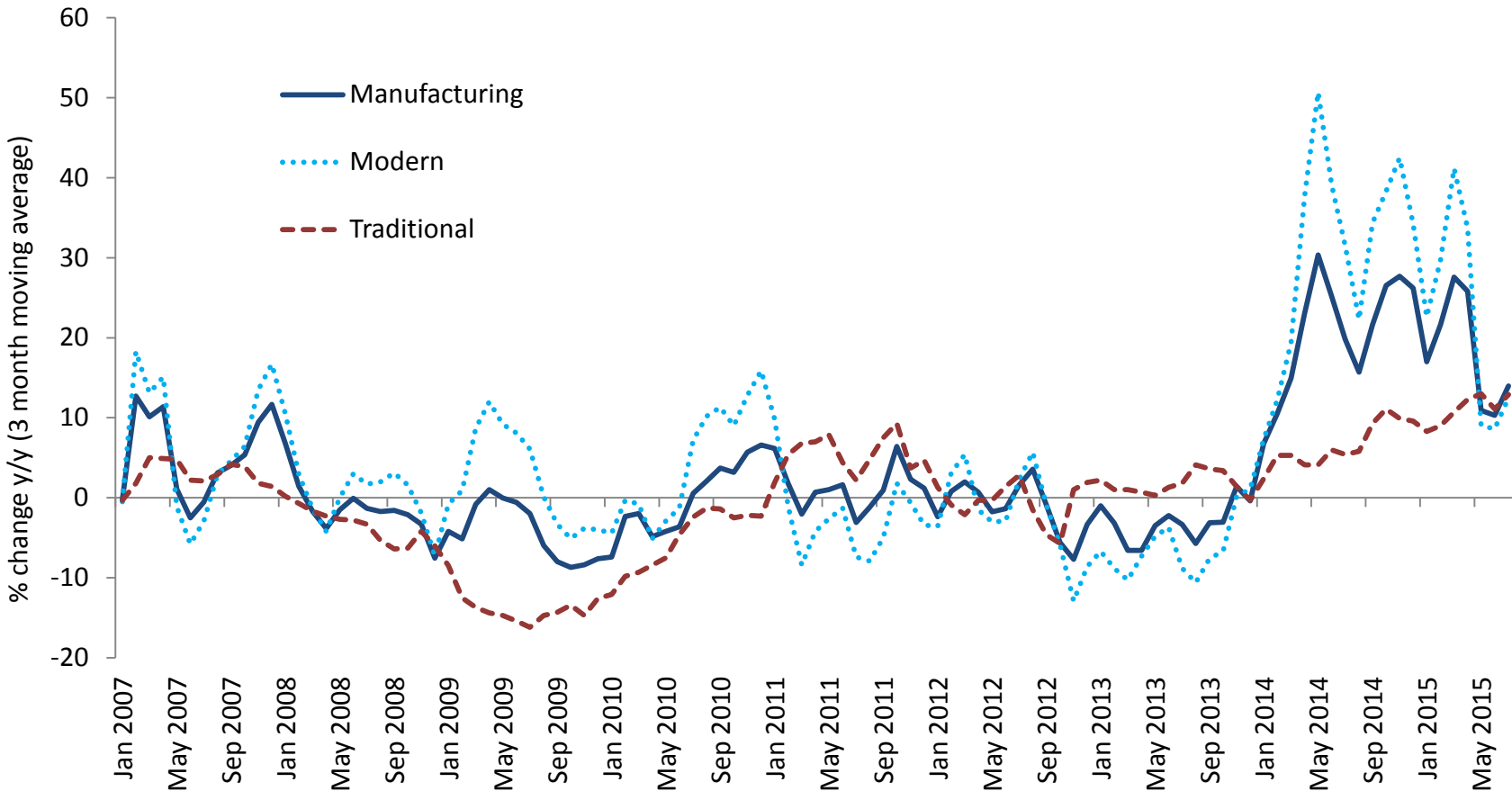
Unemployment rate falling, but well above pre-crisis lows



Sources: CSO



Industrial production volumes strong, including traditional sector

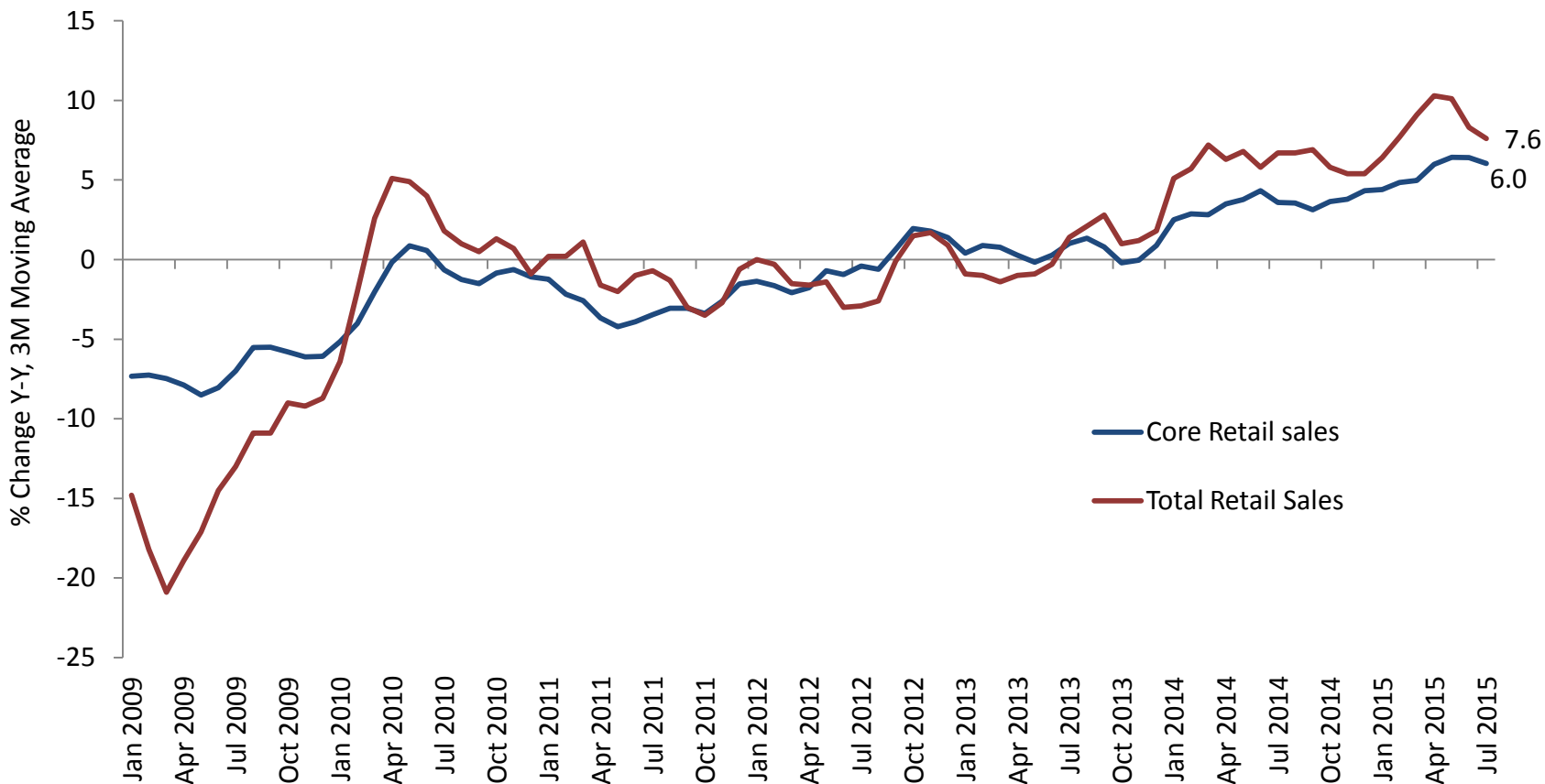


Source: CSO.

Notes: Traditional sector excludes all modern sectors (i.e. Chemicals and pharmaceuticals; Computer, electronic, optical and electrical equipment; Reproduction of recorded media; and Medical and dental instruments and supplies) but may still include activities with a high concentration of MNCs.



Good growth in retail sales augers well for consumption

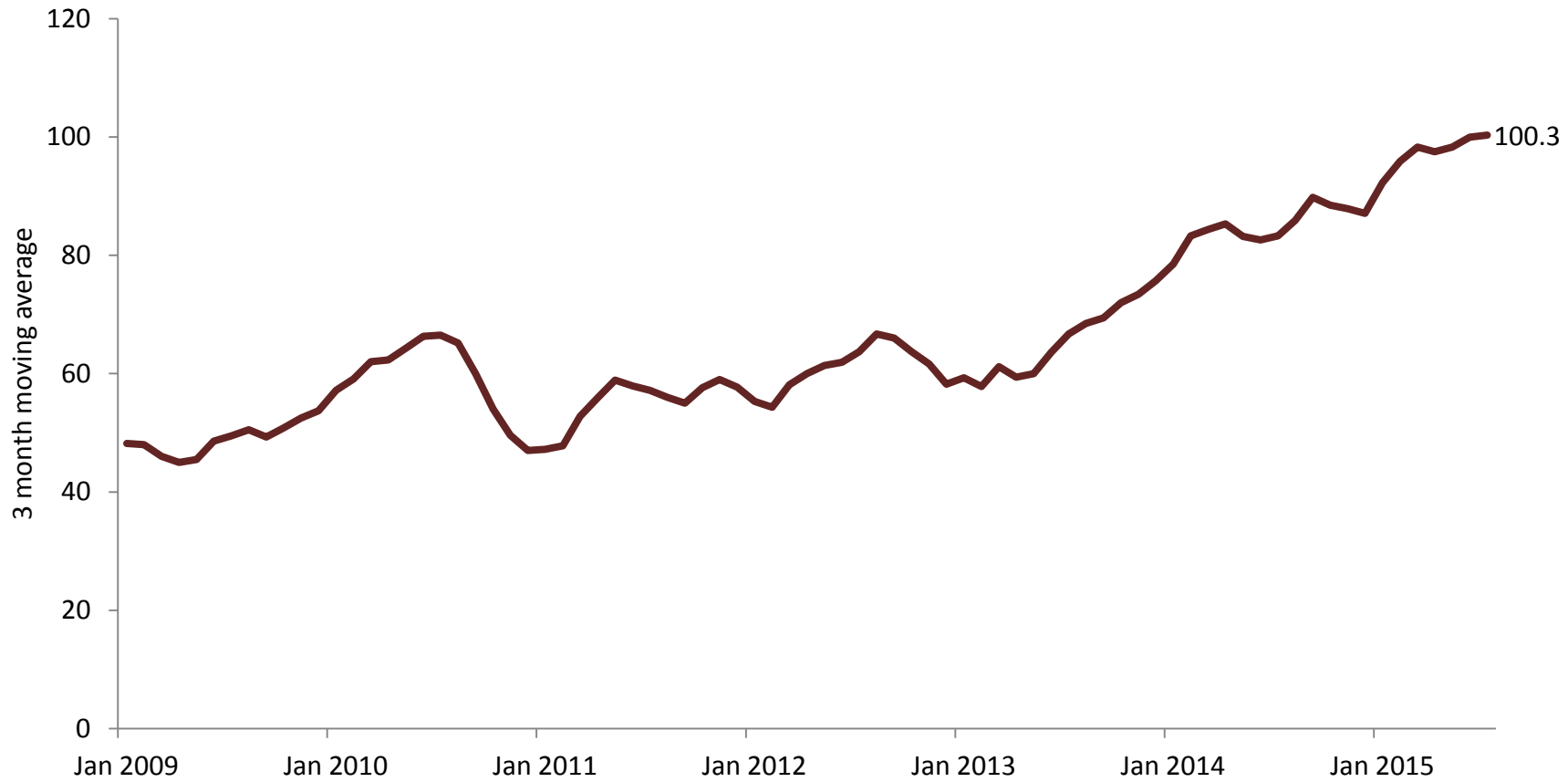


Source: CSO.

Note: Core retail sales excludes motor trades.



Consumer sentiment now above long-run average

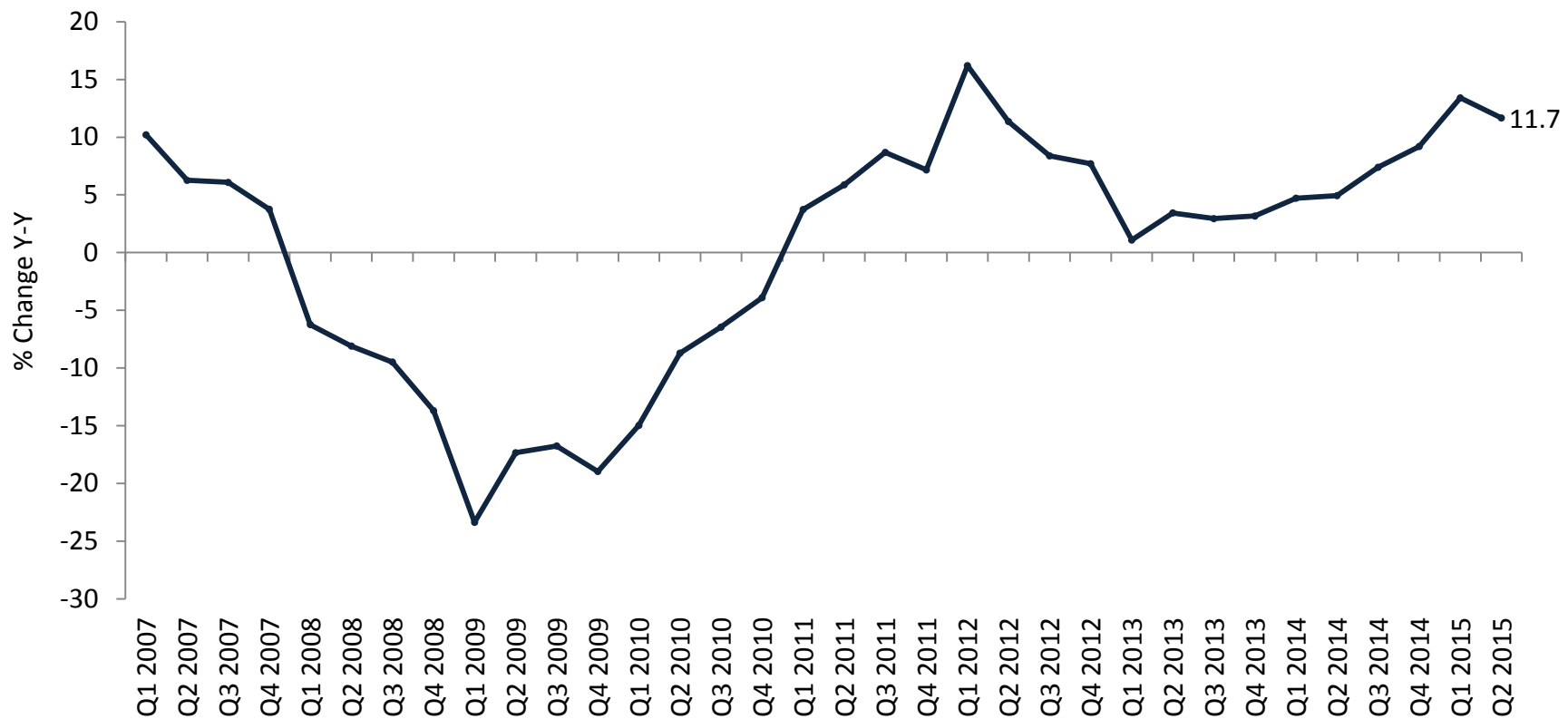


Source: KBC/ESRI

Note: Long-run average of consumer sentiment index = 85.5.



Strong year-on-year growth in exchequer revenues



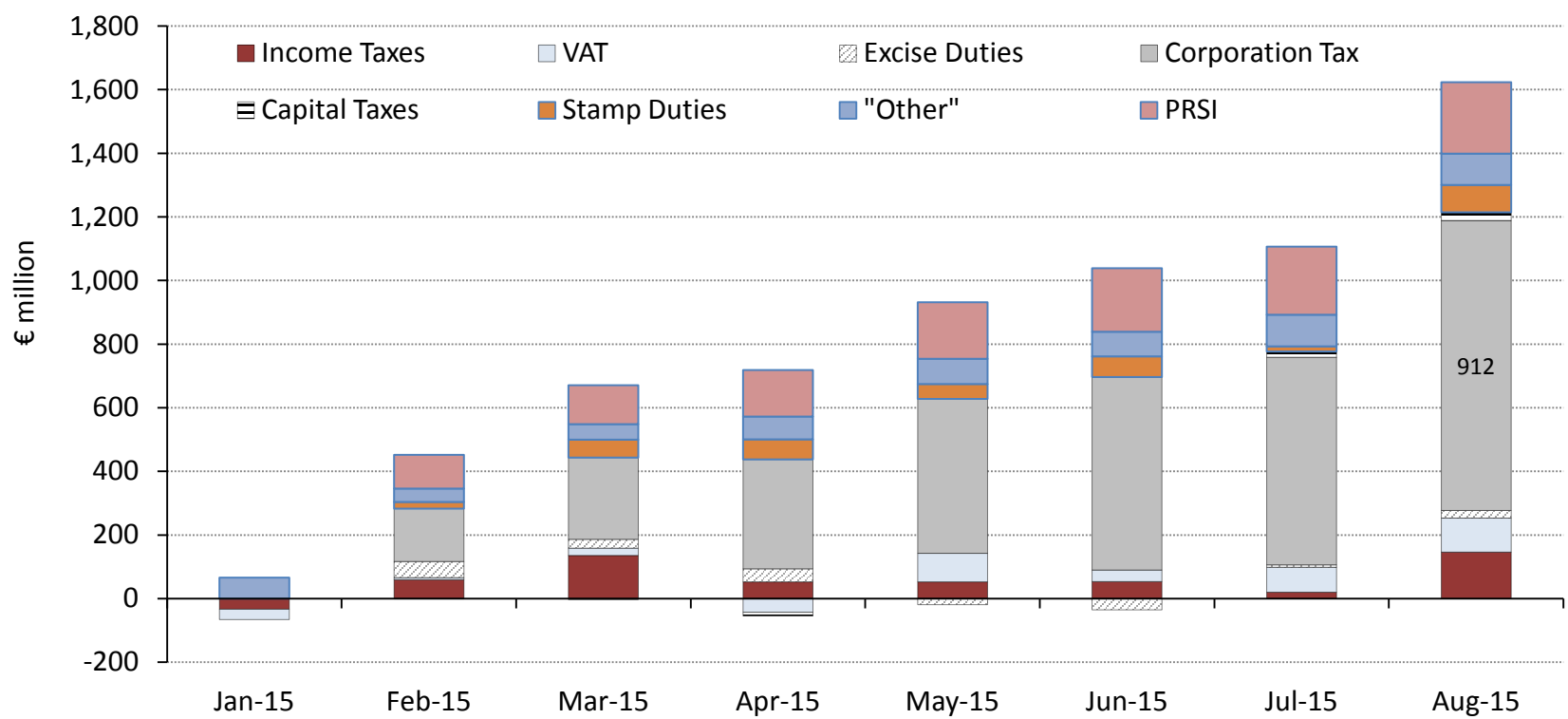
Source: Department of Finance.

Note: Based on in-year cumulative figures to end of quarter specified (e.g., Q2 2015 shows y/y % change for first six months of 2015 compared to same period in 2014).



Revenues above Budget-day expectations

FIGURE 3: TAXES AND PRSI RELATIVE TO CUMULATIVE PROFILE



Source: Department of Finance.



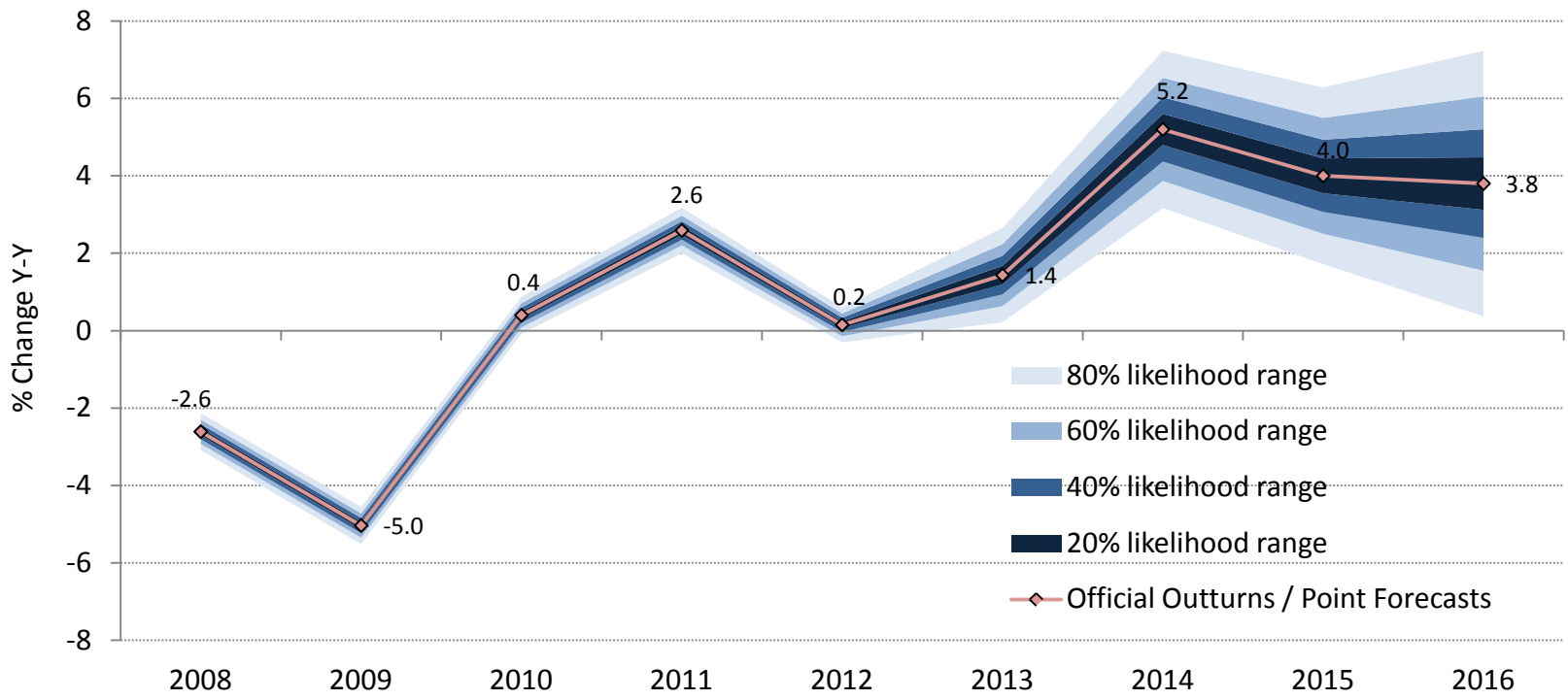
But significant risks

- Encouraging central growth scenario
- But significant risks surround that scenario
- Internal risks
 - Domestic imbalances
 - Requires ongoing monitoring
- External risks
 - Volatile external environment



Large margins of error surround growth forecasts

REAL GDP FAN CHART BASED ON SPU 2015 PROJECTIONS (TO 2016)



Sources: CSO; Department of Finance; internal IFAC calculations.

Note: Distributions or 'fans' around historical growth estimates are based on previous revisions to real GDP data. Both forecast errors and revisions are based on 1999-05 sample.

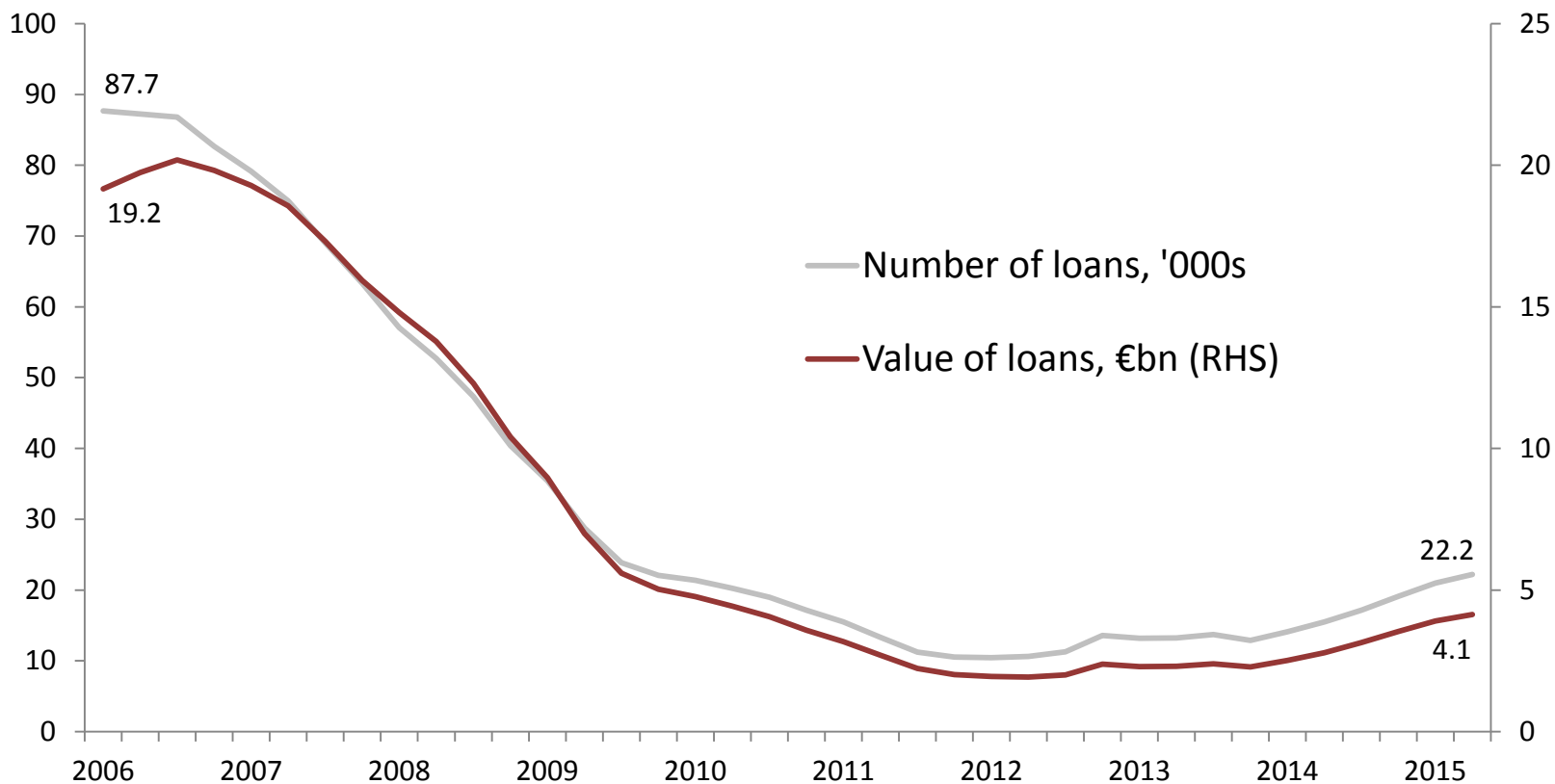


Monitoring internal imbalances

- Credit growth
- Property prices / construction
- Competitiveness
- Current account balance



New mortgage lending rising from low base

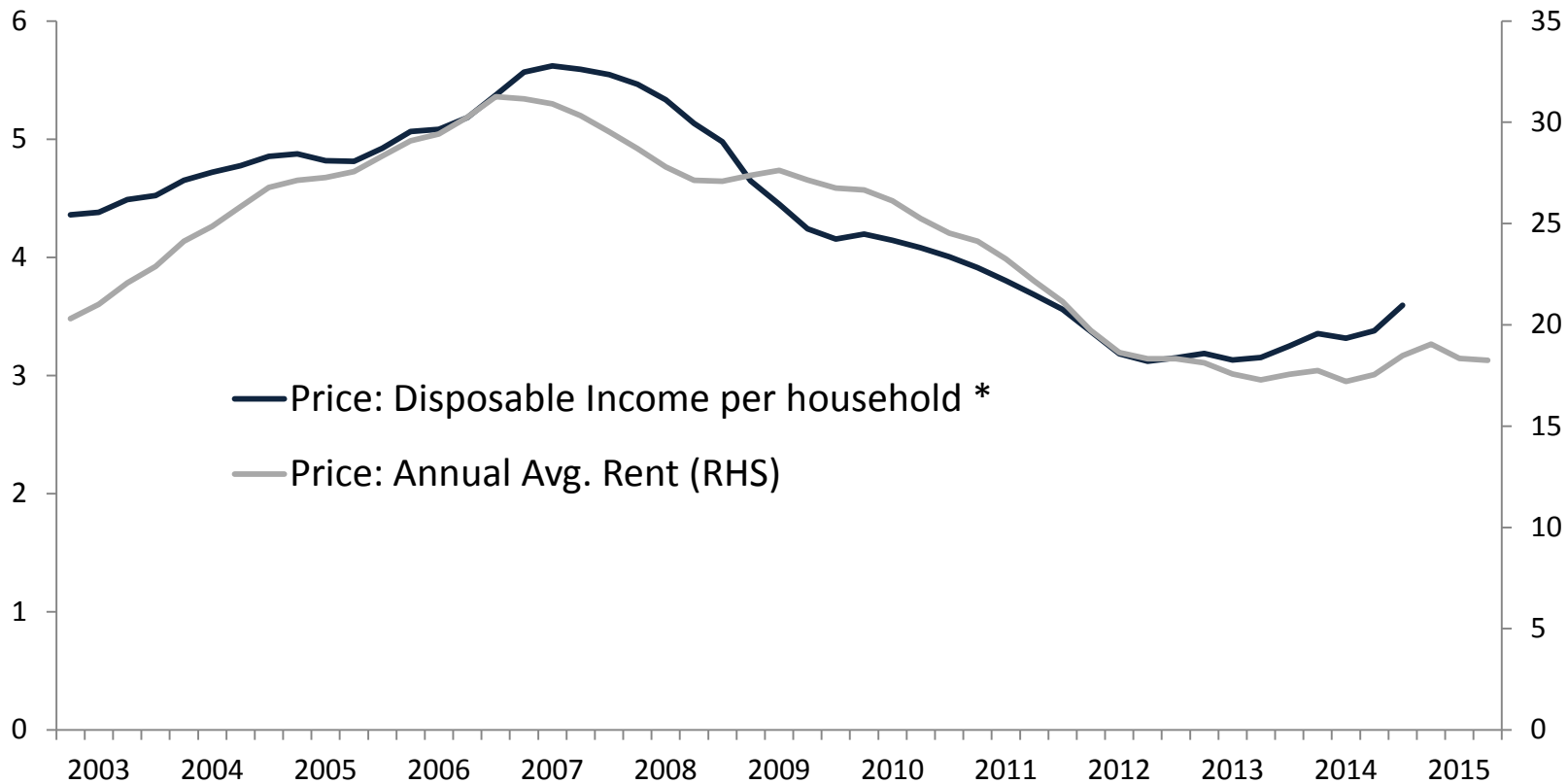


Source: IBF/PwC Mortgage Market Profile.

Notes: Both series cover first-time buyer and mover purchaser loans (moving 4-quarter sum).



Monitoring for signs of overvaluation



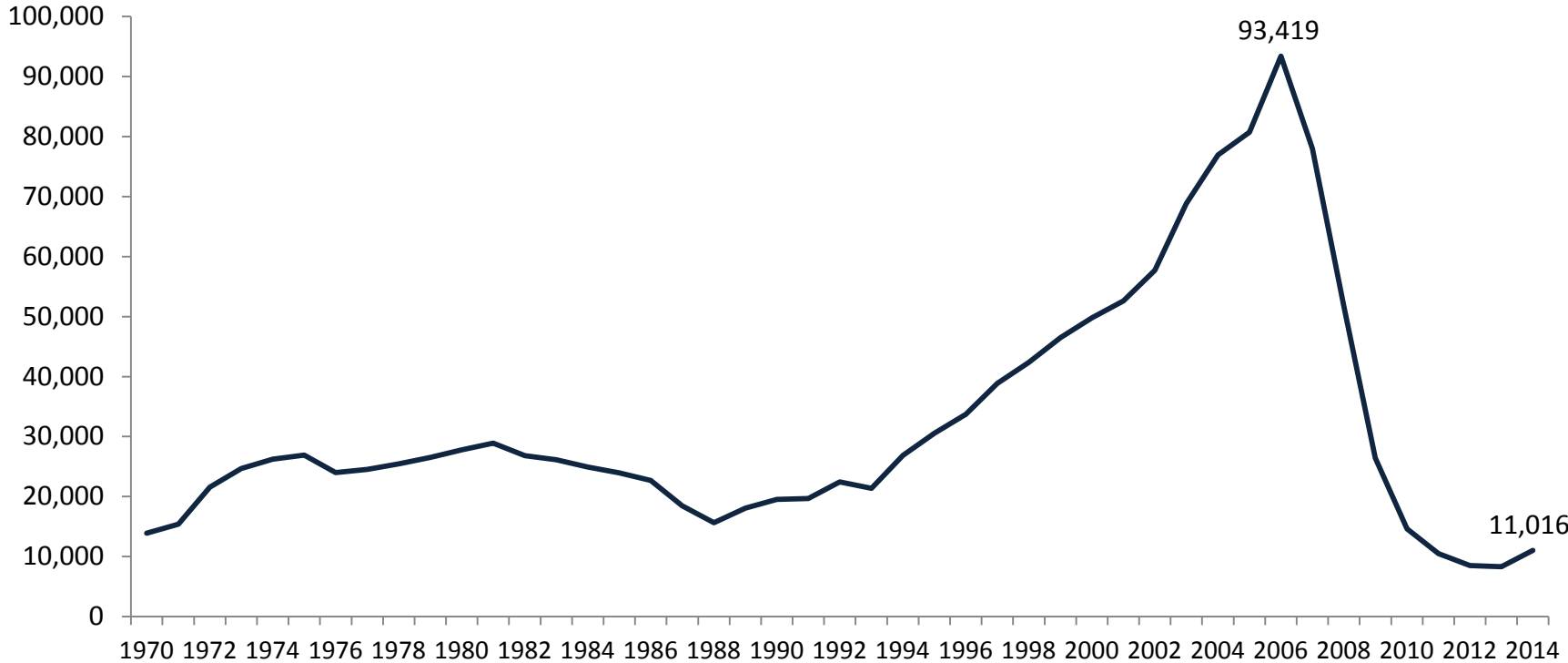
Sources: ESRI/PTSB; CSO.

*Average house prices divided by moving 4-quarter sum of adjusted personal disposable income per household.



House completions low but increasing

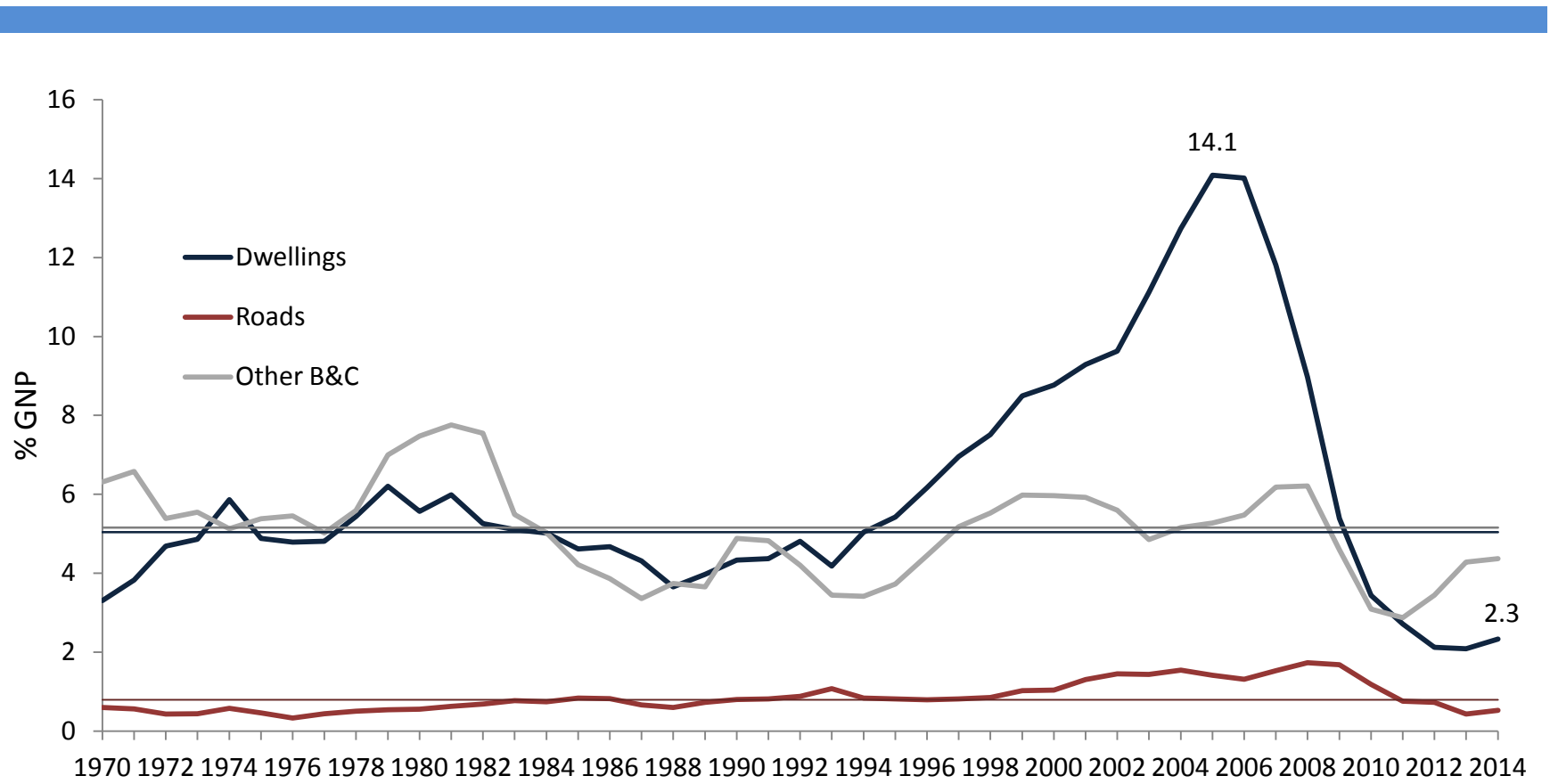
Total Housing Completions



Source: DOECLG



Construction shares of GNP below long-run averages



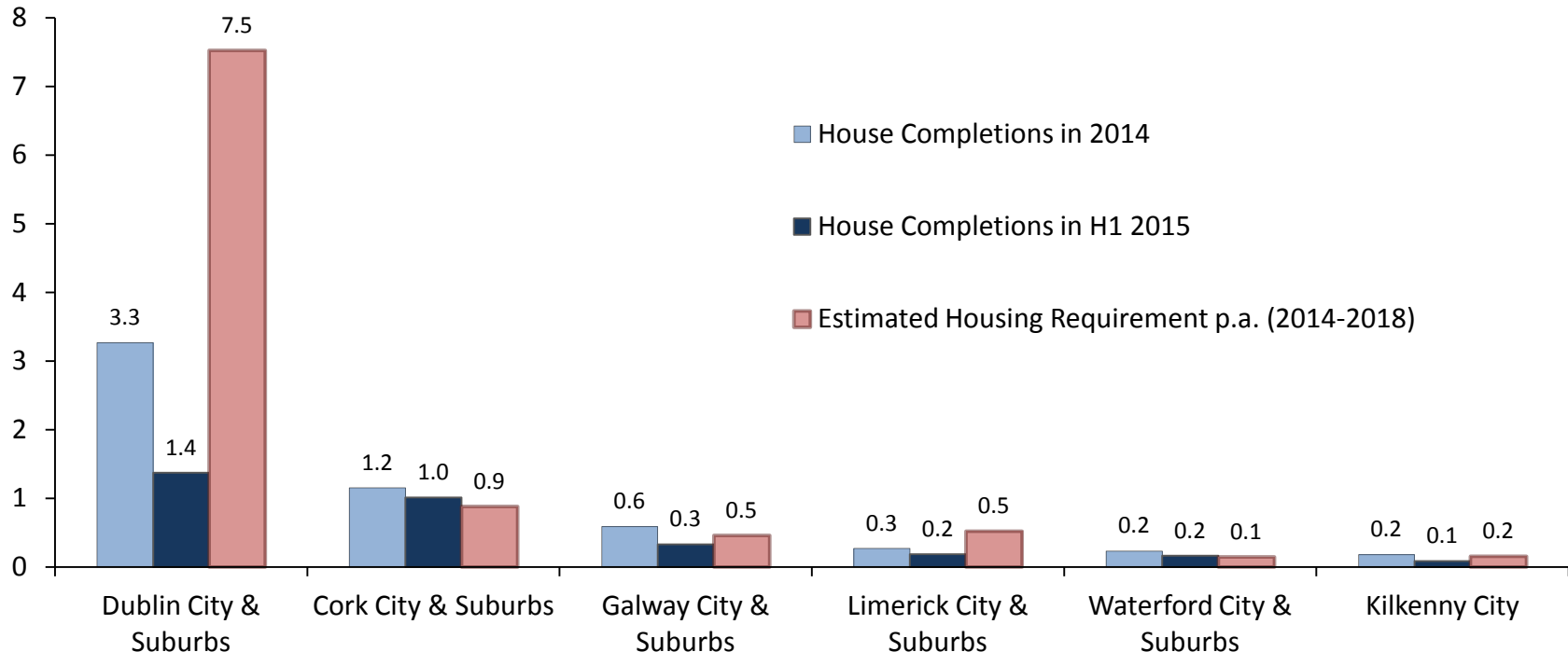
Source: CSO

Note: Respective long-run median (in same colours) of each series shown in horizontal lines.



Significant supply shortfall in Dublin

Housing Completions and Requirements ('000s)



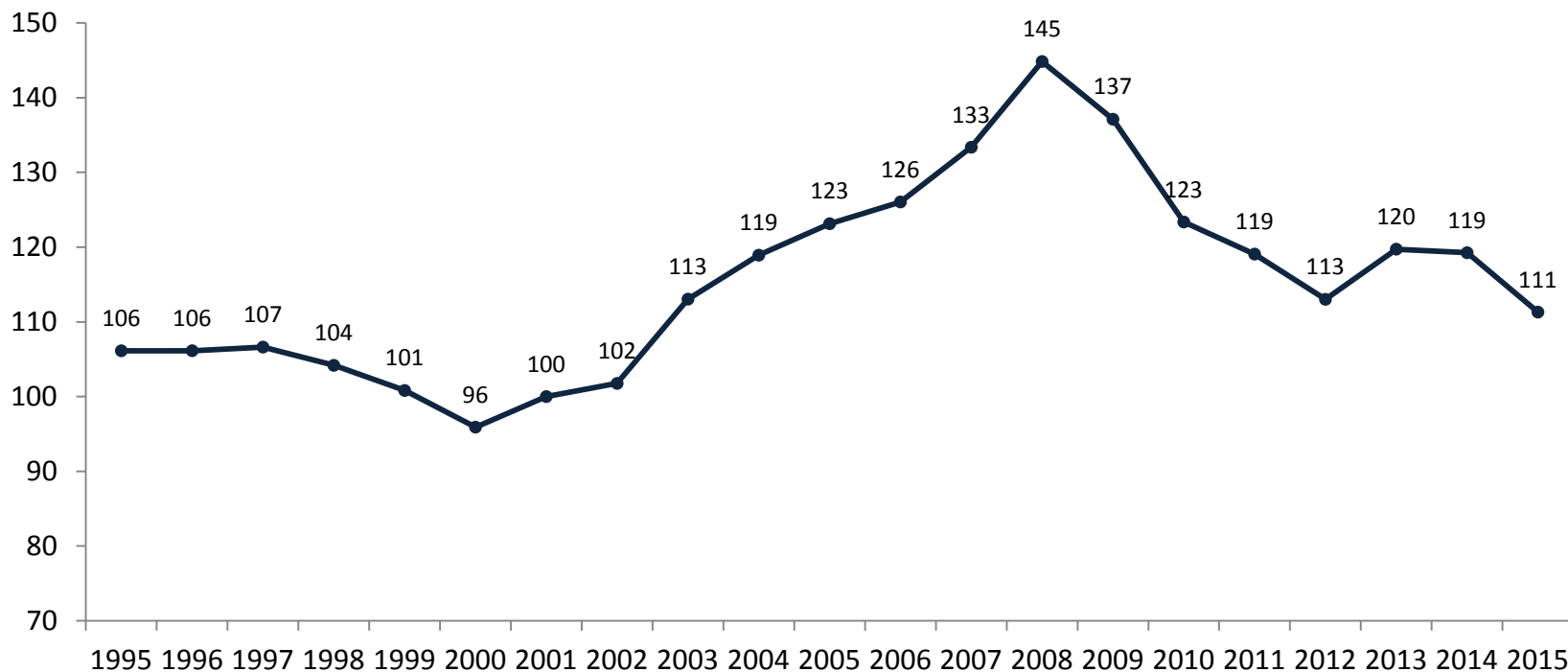
Source: Housing Agency; DoECLG.

Note: Completions cover rural + urban settlements (private and social); requirements only cover urban settlements of 1,000+ persons.



Improvement in competitiveness

RELATIVE REAL EFFECTIVE EXCHANGE RATE (BASE: 2001 = 100)

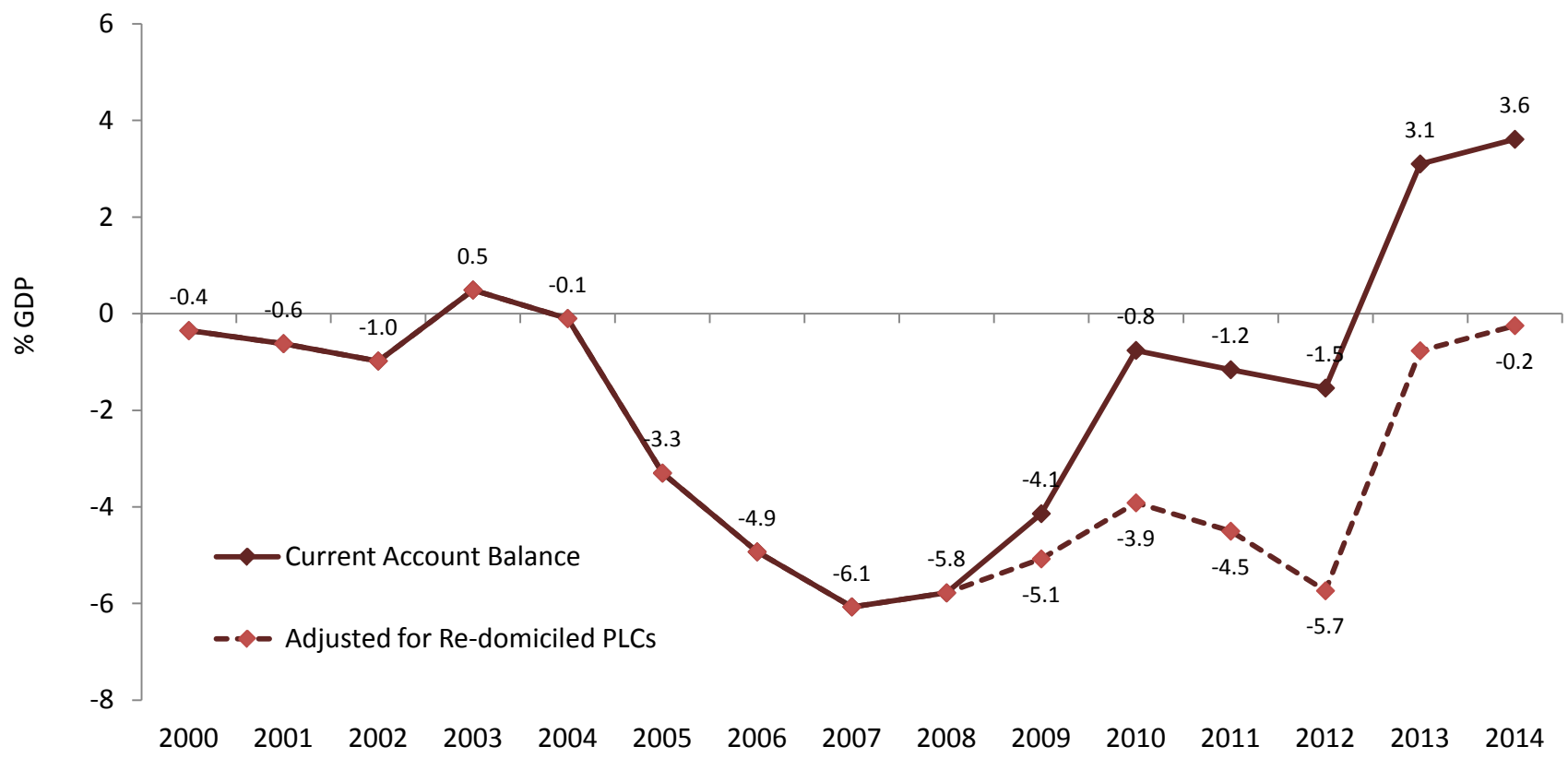


Sources: AMECO; Central Bank of Ireland.

Note: Relative Real Effective Exchange Rates (REER) are based on unit labour costs and are benchmarked against the performance of 24 industrialised economies.



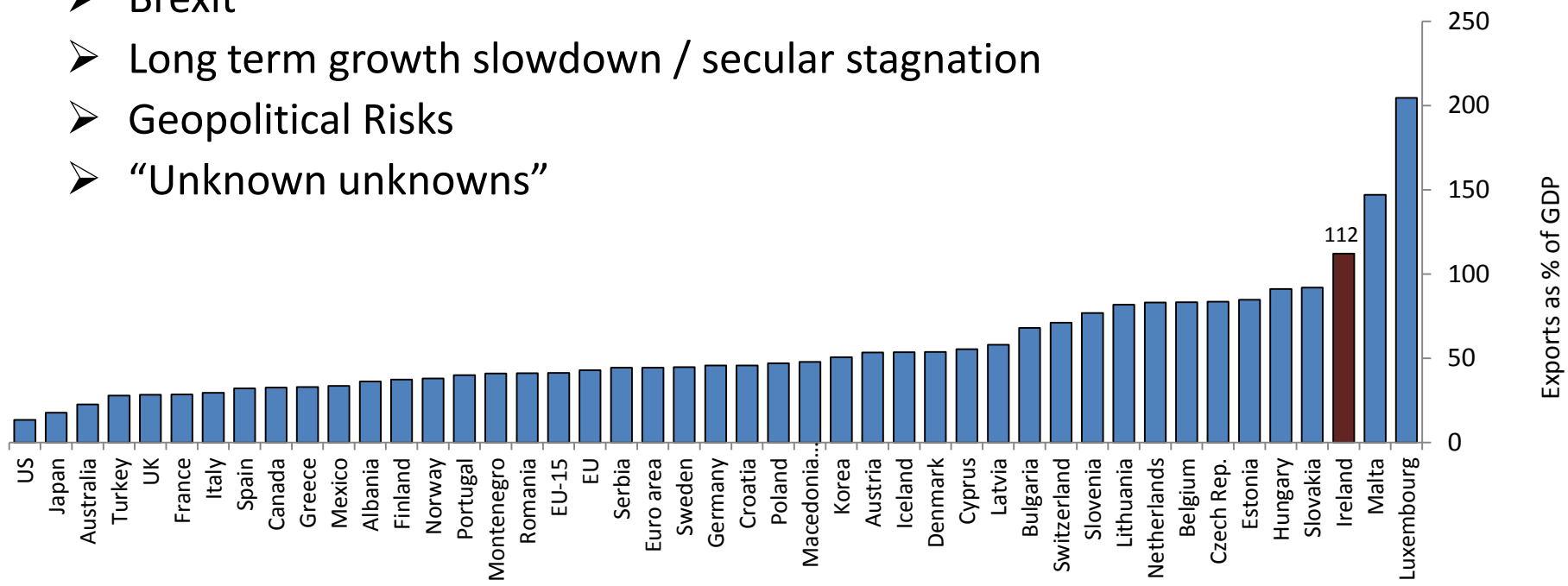
Current account near balance excluding re-domiciled PLCs





Openness makes the economy vulnerable to external shocks

- China / Emerging Markets
- US monetary policy normalization
- Euro Area stagnation
- Brexit
- Long term growth slowdown / secular stagnation
- Geopolitical Risks
- “Unknown unknowns”

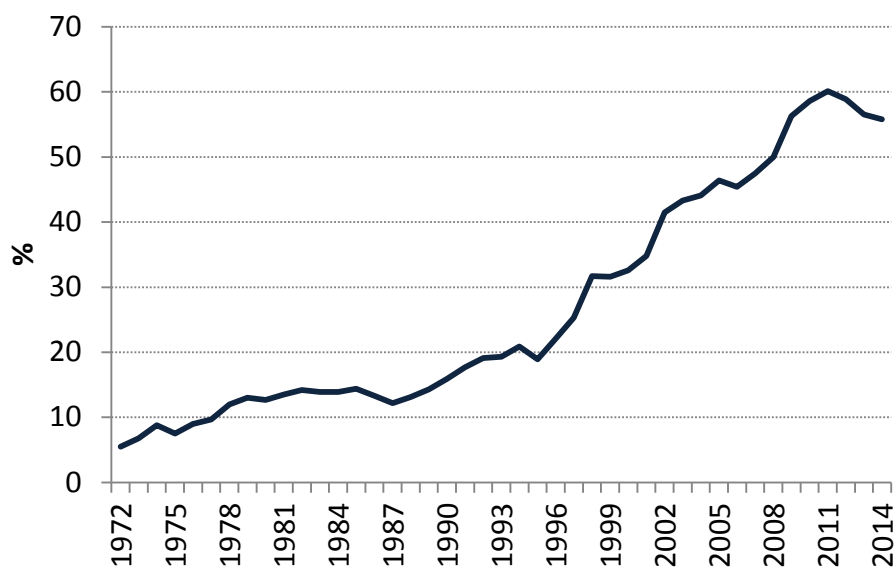


Source: AMECO.

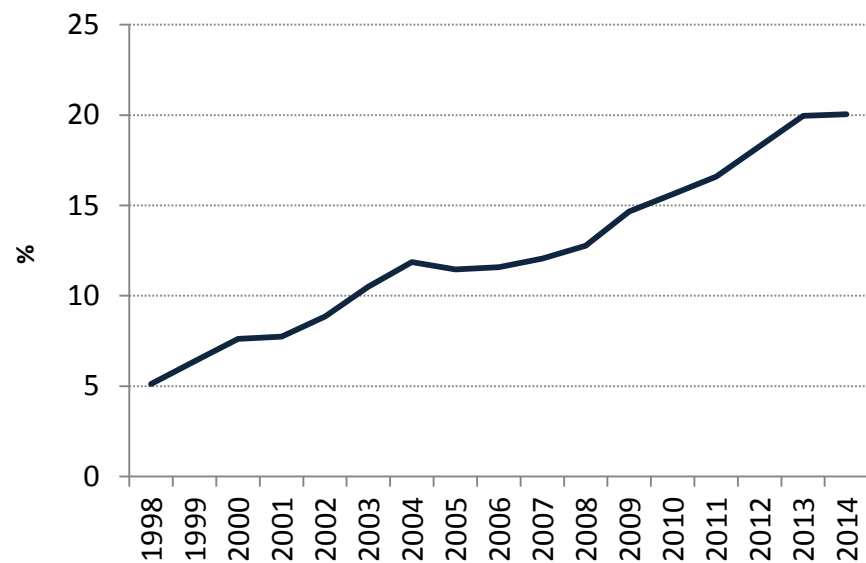


Growing dependence on certain sectors

CHEMICAL AND RELATED PRODUCTS AS % TOTAL GOODS EXPORTS



COMPUTER & FINANCIAL SERVICES AS % TOTAL SERVICES EXPORTS



Sources: CSO.

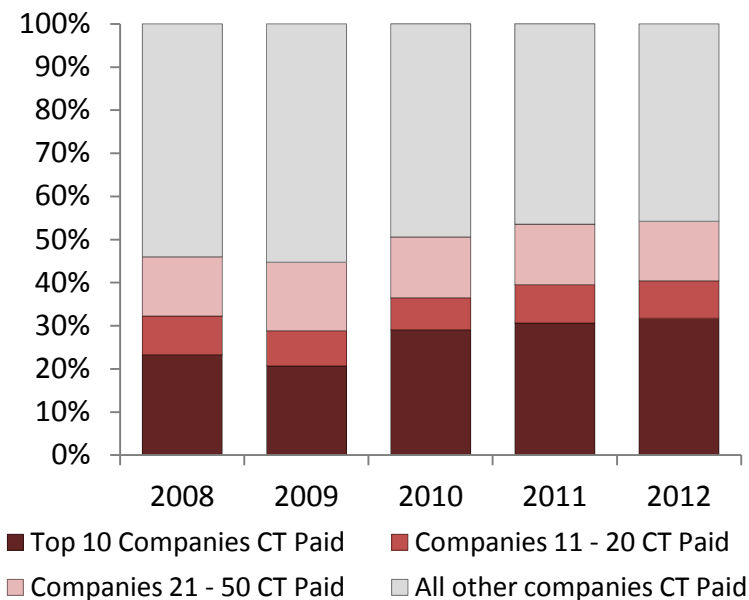


Corporation Tax: Top 10, 20 & 50 Companies

CORPORATION TAX PAYMENTS (ANNUAL AVG. 2008-2012)

	€bn unless stated	% of Total
Top 10, 20 and 50 Companies		
Total Corporation Tax	4.1	
Top 10 Companies CT Paid	1.0	24%
Top 20 Companies CT Paid	1.3	32%
Top 50 Companies CT Paid	1.9	46%

CORPORATION TAX PAYMENTS (% OF TOTAL)

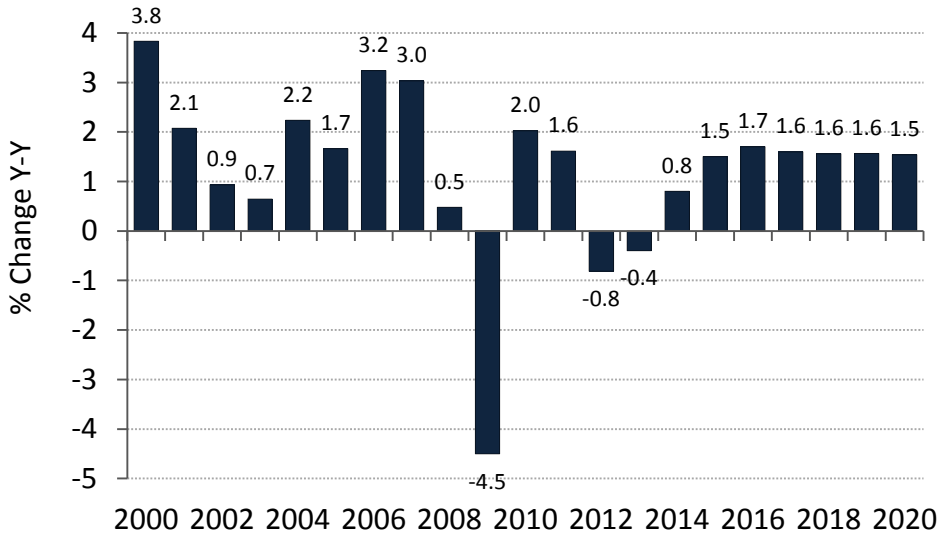


Source: [Pigott and Walsh \(2014\)](#); authors' analysis of Revenue data.

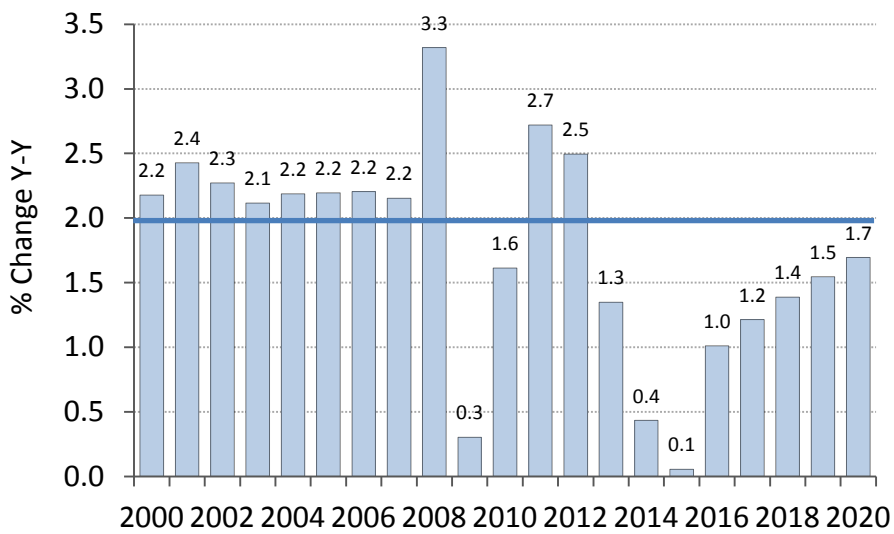


Euro Area challenges

Euro Area: Real GDP Growth (% Y-Y)



Euro Area: CPI Inflation

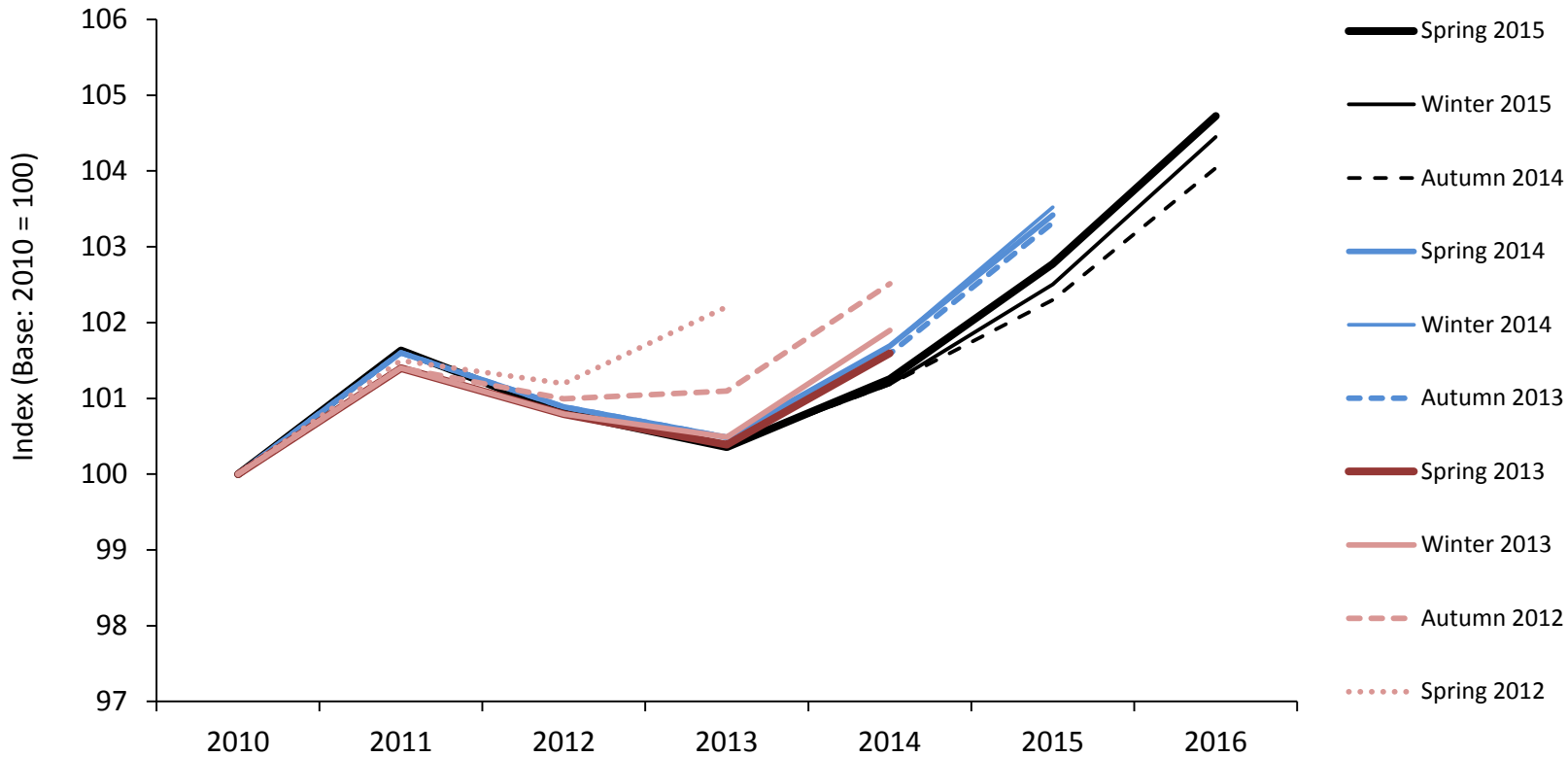


Source: IMF (Latest World Economic Outlook).



Pattern of Euro Area growth downgrades

Euro Area: Real GDP (European Commission Forecast Vintages)



Sources: European Commission Forecasts, Different Vintages.



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Sustaining growth

--Avoiding pro-cyclicality

--Preventing crises

Some emerging lessons from the banking inquiry

- Difficulty of avoiding pro-cyclical policies in times of strong economic growth
- Importance of risk management
 - Looking beyond central scenarios
- Significant crisis-induced institutional reforms
 - Banking
 - Fiscal



Value of a strong budgetary framework

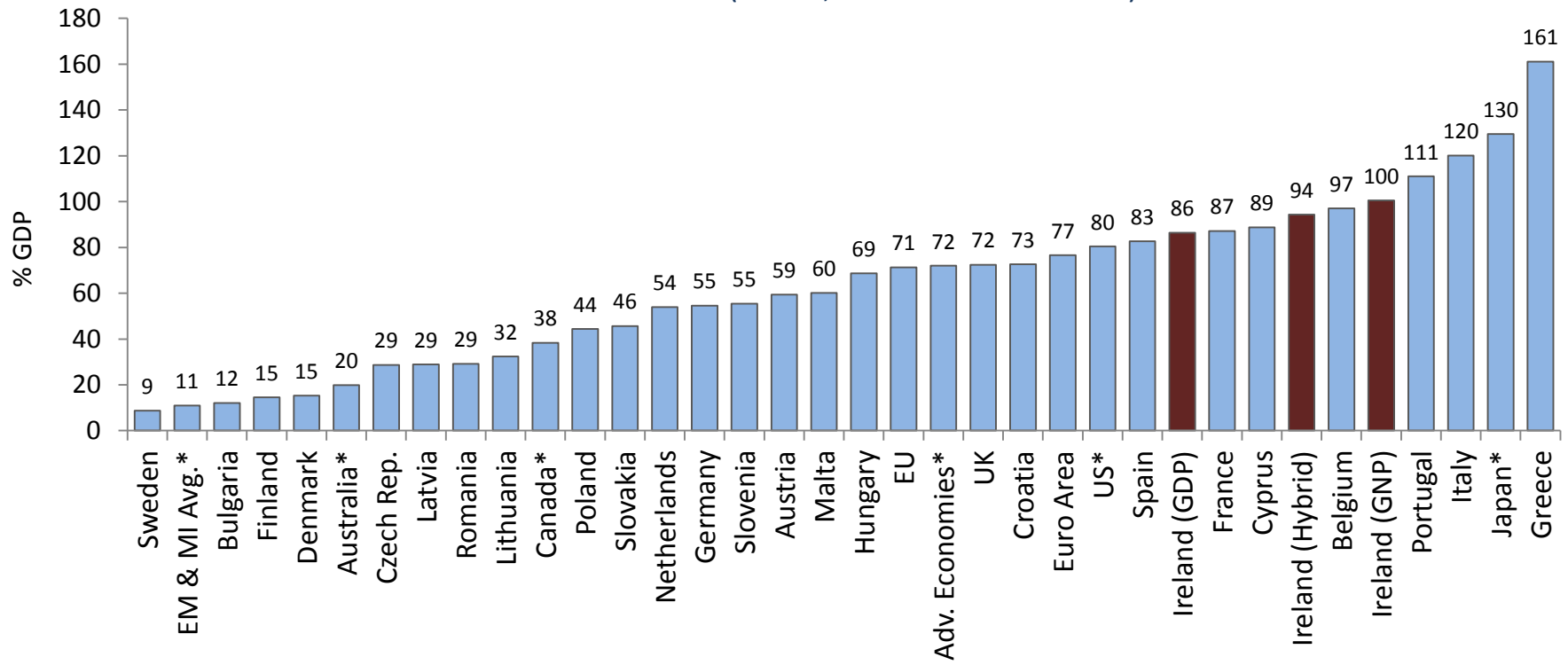
- European rationale
 - Spillovers across countries

- Domestic rationale
 - Avoid pro-cyclicality in good times
 - Avoid large forced adjustments in bad times



Risk: Net debt ratio among highest in the world

NET DEBT RATIOS (% GDP, Q1 2015 UNLESS STATED)



Sources: Eurostat; IMF Fiscal Monitor (April 2015); CSO and internal IFAC calculations.

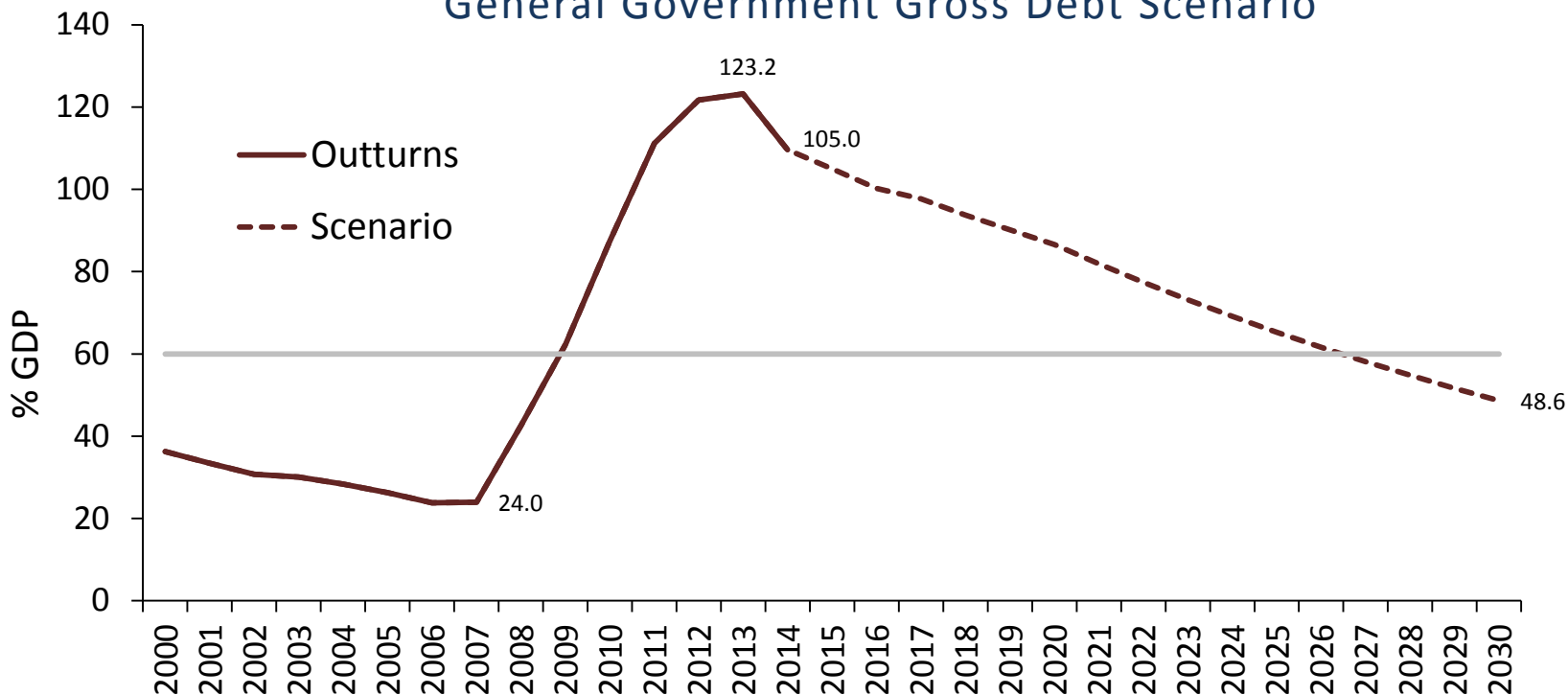
Notes: Other than those countries marked by an asterisk, all net debt ratios are based on Q1 2015 Government Finance Statistics from Eurostat or the CSO (for Ireland). Net debt is calculated as Gross Consolidated Debt less EDP debt instrument assets (F2: Currency and Deposits; F3: Debt securities; and F4: Loan assets).

* IMF 2015 estimates are reported for those countries not covered by Eurostat Q1 Government Finance Statistics. For cross-country comparability, net debt levels reported are those of national statistical agencies for countries that have adopted the 2008 System of National Accounts (Australia, Canada, United States) excluding unfunded pension liabilities of government employees' defined-benefit pension plans.



Fiscal rules should bring debt to safer levels

General Government Gross Debt Scenario

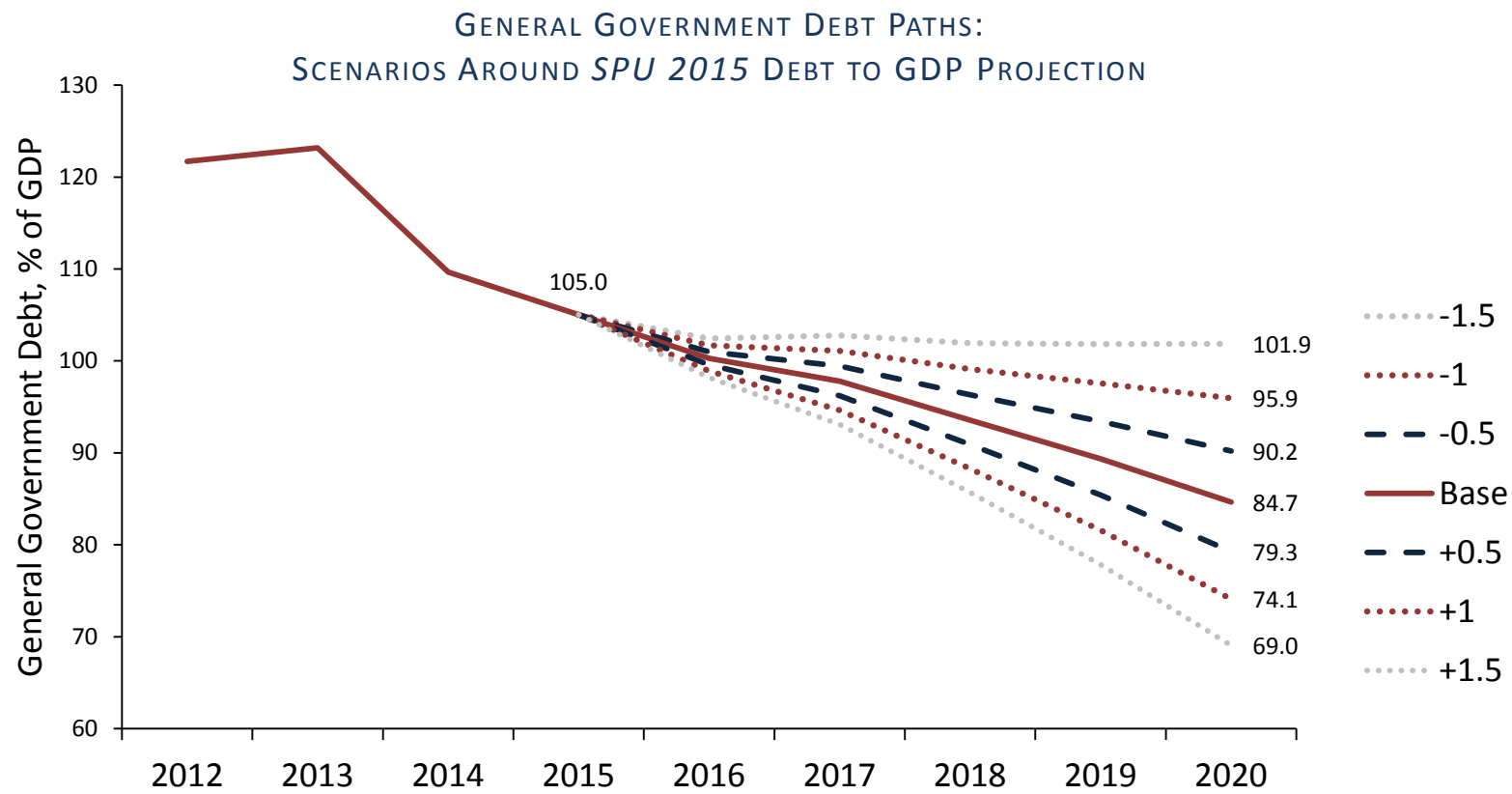


Source: Department of Finance; internal IFAC calculations.

Notes: Illustrative scenario assumes Department of Finance projections for 2016-2020 adjusted for minimum compliance with the Budgetary Rule; real GDP growth of 3% beyond 2020, with GDP deflator growth of 2% and marginal borrowing costs of 3.5%.



Debt path highly sensitive to growth shocks

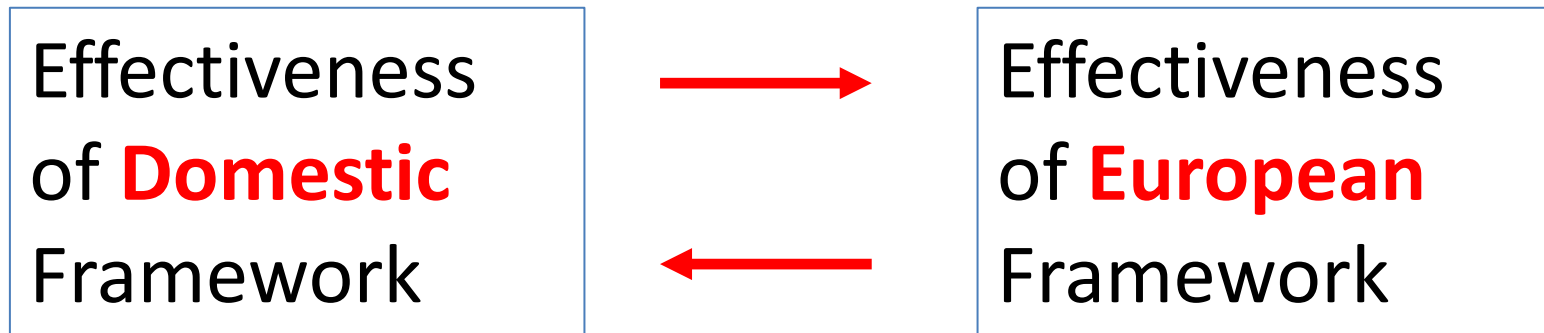


Source: Department of Finance, internal IFAC calculations based on the Council's Fiscal Feedbacks Model.
Note: The figure shows alternative projections of the balance ratio based on GDP growth forecasts that deviate from SPU projections by 0.5, 1.0 and 1.5 percentage points in either direction. The "Base" scenario corresponds to the central projection for the debt GDP ratio as published in *SPU 2015*.



Complementary domestic and European elements

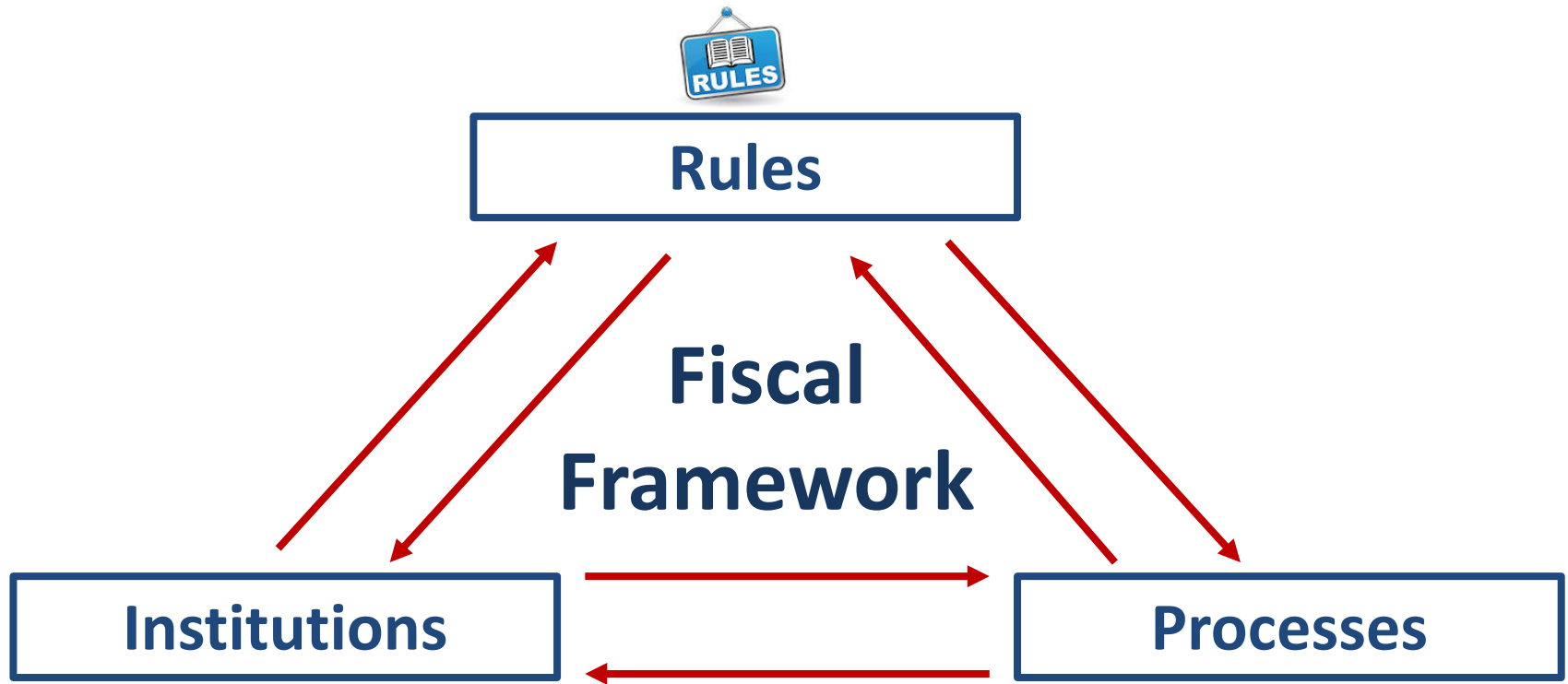
Domestic ownership adds legitimacy to the European rules



Monitoring, peer pressure and possible sanctions of the European framework enhances the effectiveness of the domestic framework



Synergies between rules, institutions and processes



European/Domestic fiscal rules



European

Domestic



Corrective Arm
of SGP

Preventive Arm
of SGP

Domestic Budgetary Rule
Consistent with Preventive
Arm of SGP

3% Deficit
Rule

1/20th
Debt Rule

MTO /
Adjustment
path to MTO

Expenditure
benchmark

Domestic
Expenditure
Ceilings

Domestic
Budgetary
Rule

Domestic Expenditure Ceilings Consistent
with Expenditure Benchmark



Summing up

- Strong recent economic performance
- Encouraging central scenario for projected growth
- But significant risks around that scenario
- Institutional reforms should help avoid repeat of past mistakes
- But now need to respect the new frameworks