



**Irish Fiscal  
Advisory Council**

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# Fiscal Assessment Report

October 2011

# Introduction

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- The Fiscal Advisory Council
  - Background
  - Mandate
  
- First Fiscal Assessment Report



# Mandate

- To provide an assessment of the **soundness of the economic and budgetary projections and forecasts** set out by the Government in the annual Budget and the Stability Programme Update,
- To provide an assessment of the **appropriateness of the fiscal stance** set out by the Government in the Budget and Stability Programme Update, including, the Government's stated medium-term budgetary objective, with particular regard to whether they are conducive to prudent economic and budgetary management, including by reference to the provisions of the European Union Stability and Growth Pact,
- To provide an assessment of whether the budgetary plans set out in the Budget and Stability Programme Update are consistent with the fiscal rules - Fiscal Responsibility Bill by the end of the year, and
- To perform such other functions, including an assessment of the implications of budgetary plans for economic growth, investment and employment, as may be assigned by the Minister for Finance.

# Fiscal Assessment Report

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## 3 Broad Areas

1. Macroeconomic Assessment
2. Budgetary Assessment
3. Fiscal Stance

# Macroeconomic Assessment

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- Broadly appropriate at time of SPU
- Key post-SPU developments:
  - Recent softening of global growth prospects
  - Stronger than anticipated performance over first half of 2011



# Macroeconomic Assumptions

	2011	2012	2013	2014	2015
<b><u>SPU</u></b>					
Real GDP	0.8	2.5	3.0	3.0	3.0
Nominal GDP	1.4	3.1	4.0	4.3	4.6
<b><u>Update</u></b> Central Bank, 2011 & 2012; SPU, 2013-2015					
Real GDP	1.0	1.8	3.0	3.0	3.0
Nominal GDP	-0.2	2.2	4.0	4.3	4.6

# Budgetary Assessment

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- Broadly appropriate at time of SPU
- Exchequer returns close to profile
- Significant post-SPU developments
  - Reduction in interest rate on official loans
  - Lower than anticipated cost of bank recapitalisation
  - Nominal GDP - upward revision to 2010; downward revisions for 2011 & 2012



# SPU Key Projections

	2011	2012	2013	2014	2015
Gross Debt/GDP (%)	111.0	116.0	118.0	116.0	111.0
General Government Deficit/GDP (%)	10.0	8.6	7.2	4.6	2.8
Primary Deficit/GDP (%)	6.2	3.9	1.1	-1.7	-3.4
Nominal GDP Growth (%)	1.4	3.1	4.0	4.3	4.6
Average Interest Rate (%)	4.0	4.4	5.5	5.6	5.6
Assumed Discretionary Adjustment (Billions)	-6.0	-3.6	-3.1	-3.1	-2.0





# Allowing for Post-SPU Developments

	2011	2012	2013	2014	2015
Gross Debt/GDP (%)	109.1	115.4	117.7	116.9	112.9
General Government Deficit/GDP (%)	9.7	8.8	7.2	4.7	2.8
Primary Deficit/GDP (%)	6.2	4.4	1.6	-1.2	-2.9
Nominal GDP Growth (%)	-0.2	2.1	4.0	4.3	4.6
Average Interest Rate (%)	3.7	4.1	5.0	5.2	5.1
Assumed Discretionary Adjustment (Billions)	-6.0	-3.6	-3.1	-3.1	-2.0



# Additional Adjustments Required

	2012	2013	2014	2015
<b><u>General Government Deficit Target (GGD) (% of GDP)</u></b>				
Original GGD Targets in SPU	8.6	7.2	4.6	2.8
<b><u>Estimated Discretionary Adjustments (Billions of Euro)</u></b>				
Planned Adjustment in SPU	-3.6	-3.1	-3.1	-2.0
Additional Adjustment Required for Original Targets	-0.4	0.4	-0.1	0.0
<b><i>Total Adjustment Required</i></b>	<b><i>-4.0</i></b>	<b><i>-2.7</i></b>	<b><i>-3.2</i></b>	<b><i>-2.0</i></b>

# Assessment of Fiscal Stance

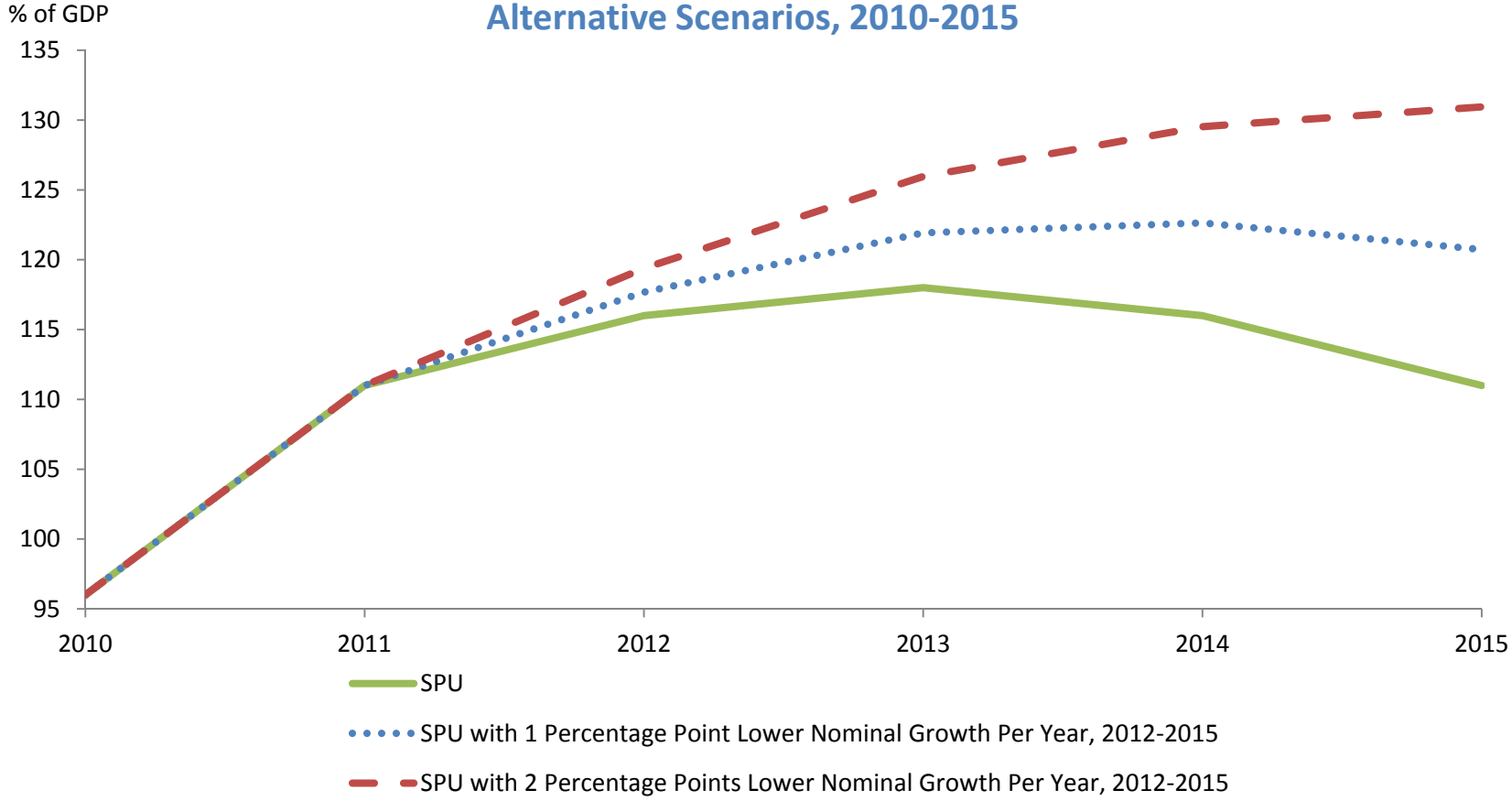
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- A difficult balancing act . . .
  - Rebuilding public finances
  - Funding vulnerabilities
  - Effects on domestic demand
  
- Is there a case for more ambitious targets?



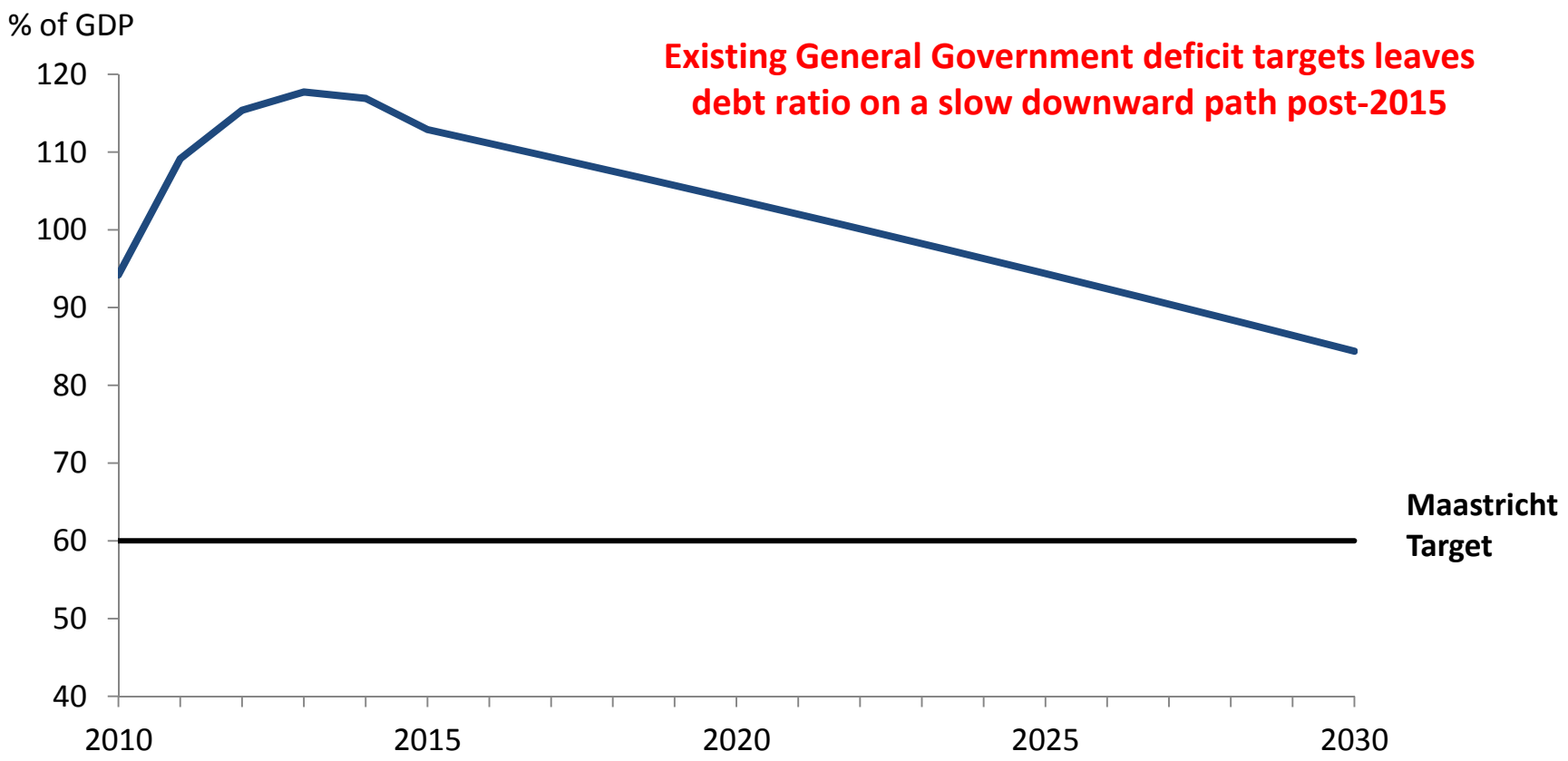
# Fragility of Debt Sustainability

**Medium-Term Evolution of Debt/GDP Ratio  
Alternative Scenarios, 2010-2015**





# Slow Rate of Improvement in Debt/GDP Ratio



Assumptions:

- 1. 1 percentage gap between nominal interest rate and nominal growth rate, 2016-2030
- 2. Primary surplus as a share of GDP is held constant at 2015 level, 2016-2030

# Funding Vulnerabilities

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- Uncertain external environment
  - Market funding vulnerability
  - Official funding vulnerability
- European crisis-resolution policies → Distinction between illiquid and insolvent countries
- Importance of being on the “right list”

# Effects on Domestic Demand

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- Uncertainty about size of multipliers
- Review of literature suggests deficit multiplier positive but relatively small under current Irish conditions
- Unlikely that fiscal adjustment is “self defeating”
  - Deficit is falling despite weak domestic demand and output

# Basic Assessments

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- Current General Government deficit (GGD) targets within the range of appropriate fiscal policy stances
- Council sees no case for relaxing targets
- On balance, the Council sees a strong case for more ambitious targets – notably a GGD target of 1% of GDP by 2015



# Arguments for more ambitious targets

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- Debt ratio on a strong downward path post-2015
- Insurance against shocks
- Timely signal of political capacity

# Amended SPU with Revised GGD Targets

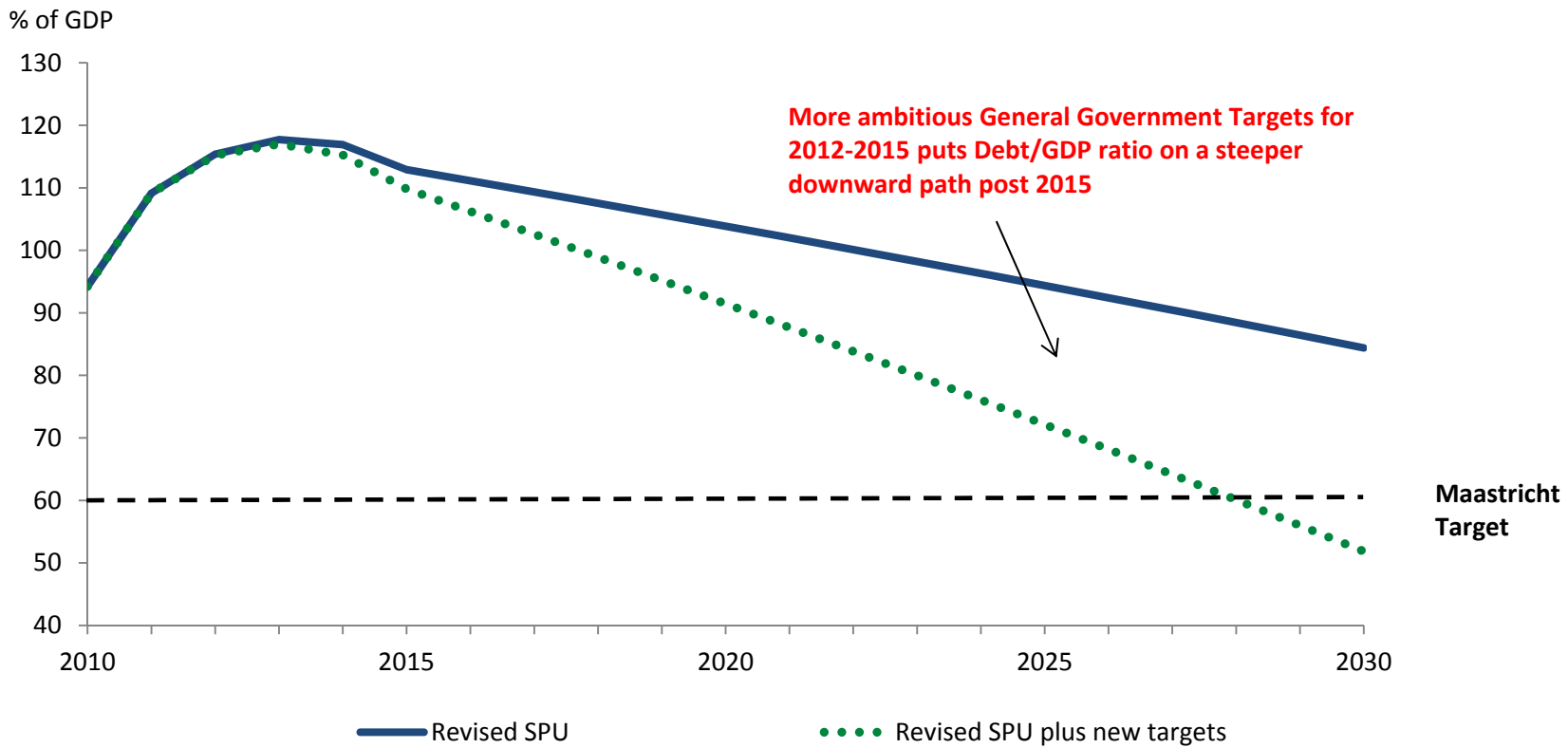
	2011	2012	2013	2014	2015
Gross Debt/GDP (%)	109.1	115.2	117.0	115.3	109.8
General Government Deficit/GDP (%)	9.7	8.4	6.4	3.6	1.0
Primary Deficit/GDP (%)	6.2	4.0	0.9	-2.2	-4.7
Nominal GDP Growth (%)	-0.2	1.9	3.8	4.1	4.2
Average Interest Rate (%)	3.7	4.1	5.0	5.2	5.1
Assumed Discretionary Adjustment (Billions)	-6.0	-4.4	-3.9	-3.8	-3.7

## Alternative GGD Targets and Discretionary Adjustments

	2012	2013	2014	2015
<b><u>General Government Deficit Target (GGD) (% of GDP)</u></b>				
Original GGD Targets in SPU	8.6	7.2	4.6	2.8
Alternative Targets to get to 1% GGD in 2015	8.4	6.4	3.6	1.0
<b><u>Estimated Discretionary Adjustments (Billions of Euro)</u></b>				
Planned adjustment in SPU	-3.6	-3.1	-3.1	-2.0
Additional Adjustment Required for Original Targets	-0.4	0.4	-0.1	0.0
Additional Adjustment Required for Alternative Targets	-0.4	-1.2	-0.6	-1.7
Total Additional Adjustment	-0.8	-0.8	-0.7	-1.7
<b><i>Total Adjustment Required to Reach 1% GGD Target in 2015</i></b>	<b>-4.4</b>	<b>-3.9</b>	<b>-3.8</b>	<b>-3.7</b>



## Impact of Revised Targets on the Path of Debt/GDP Ratio



Assumptions:

- 1. 1 percentage gap between nominal interest rate and nominal growth rate, 2016-2030
- 2. Primary surplus as a share of GDP is held constant at 2015 level, 2016-2030



# Summary

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- Macro forecasts and budgetary projections broadly appropriate at time of SPU
- Significant post-SPU developments
  - 2.8% GGD target for 2015 still achievable
  - 8.6% GGD target for 2012 challenging given own estimates
- Case for more ambitious GGD target for 2015 (3% → 1%)
  - Would require an estimated €4 billion of additional adjustments