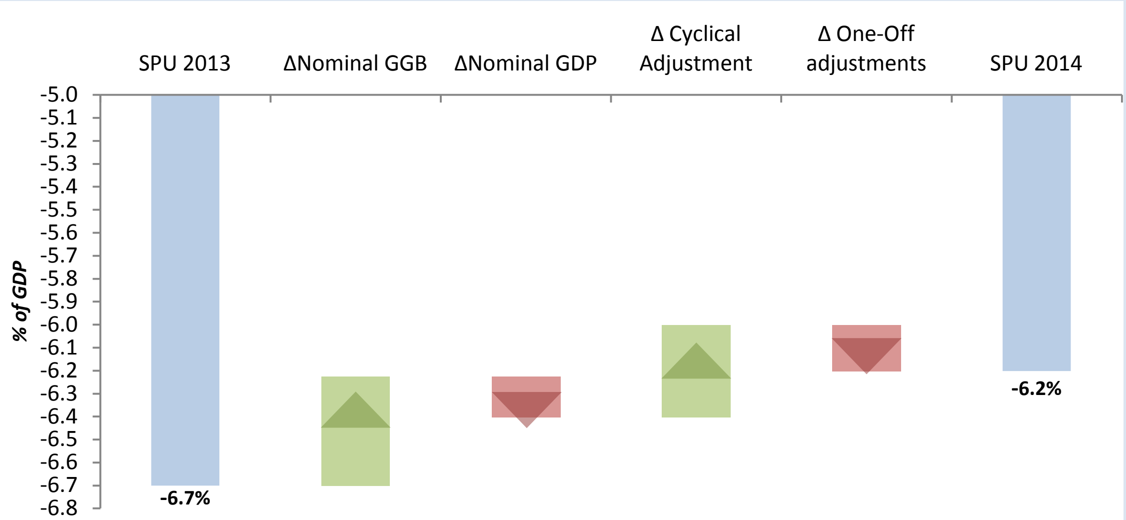
Box C: Revisions to Structural Balance Estimates for 2013

This Box examines the source of the 0.5 percentage point revision to the structural balance estimate for 2013 since *SPU 2013*. Broadly speaking such revisions can arise from three areas; (i) changes to the headline deficit ratio, (ii) changes to the estimated impact of the economic cycle or (iii) adjustment to the calculation of one-off and temporary measures.

Figure C: Decomposition of Changes to the Structural Balance Estimate for 2013



Source: Internal calculations. As the residual from this calculation is minor and does not materially impact on results it is omitted from the chart.

General Government Balance

The 2013 General Government balance as a percentage of GDP was forecast at 7.5 per cent in *SPU 2013* and the latest outturn figure is 7.2 per cent in *SPU 2014*. This change in the headline ratio masks the extent of the reduction in the nominal deficit estimate as it is offset in part by downward revisions to the nominal GDP level. (See Chapter 3).

Cyclical Adjustment

A revision of 0.4 percentage points arises from changes to the cyclical component of the budgetary balance. The cyclical component is calculated by multiplying the output gap by the estimated sensitivity of the budget balance to changes in the output gap.

The estimate of the output gap for 2013 was revised from -0.5 per cent of potential GDP in SPU 2013 to -1.3 per cent of potential GDP in *SPU 2014*. Over this period, real GDP growth was revised from 1.3 per cent to -0.3 per cent, while potential GDP growth was revised marginally from 0.3 per cent to 0.4 per cent. This arises not only from data and forecast revision but also from the change in the methodology for calculating the NAWRU (see Analytical Note 2).[1] In estimating the sensitivity of the budget

[1] The composition of potential growth over this period changed, with a labour contribution of -1.1 percentage points being revised up to 0.1 percentage points. This was offset by a downward reduction in the contribution of Total Factor Productivity (TFP) from 1.3 to 0.1 percentage points.

balance to changes in the output gap, the EC approach is based on a methodology devised by the OECD, which was recently updated.[2] This update gives a semi-elasticity of the budgetary balance for Ireland of 0.5, which was used for both *SPU 2013* and *SPU 2014*.

One-offs and Temporary Measures

The 'two-pack' Code of Conduct defines 'one-off and temporary measures' as measures having a transitory budgetary effect that do not lead to a sustained change in the inter-temporal budgetary position.[3] More detailed guidance from the EC identifies certain principles aimed at ensuring consistent treatment across countries but the interpretation remains relatively subjective.[4] This element of the structural balance estimation is typically the least technically complex but is also open to more subjectivity.[5] The one-off measures of -0.4 percentage points of GDP (€0.6 billion) for 2013 in *SPU 2014* arise predominantly from a combination of:

(i) €1.1 billion from the Eligible Liabilities Guarantee (ELG) call relating to the promissory note restructuring

(ii) -€0.7 billion in mobile license sales

(iii) €0.2 billion in promissory note interest.

The estimate of -0.4 per cent of GDP represents a downward revision from -0.6 percentage points of GDP in *SPU 2013*, while the latest EC estimate of -0.3 percentage points of GDP is somewhat lower.

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[2] See Mourre *et al* (2013).

[3] Examples of one-off and temporary measures are sales of non-financial assets; receipts of auctions of publicly owned licenses; short-term emergency costs emerging from natural disasters; tax amnesties; revenues resulting from the transfers of pension obligations and assets.

[4] The EC paper (Larch and Turrinni, 2009) specifies that items classified as one-off or temporary in their impact on the cyclically adjusted balance should: (i) have an impact of at least 0.1% of GDP; (ii) should be concentrated in a single year of very limited number of years; (iii) typically but not exclusively be classified as a capital transfer; and (iv) deficit increasing measures should not be regarded as one-off on the basis that expenditure measures initially regarded as one-off can become permanent.

[5] For example, work by the EC has shown that there are typically more and larger one-off adjustments when the deficit is closer to 3 per cent of GDP. (EC, 2009).