Pre-Budget 2018 Statement

September 2017

Irish Fiscal Advisory Council

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Key Messages

Substantial progress has been made in moving the public finances to a safer position with a likely return to a budget balance in 2018, but risks remain. With the government's budget returning to balance, debt ratios on a downward trajectory and near-term interest and growth prospects relatively favourable, Ireland is in a good position to move the public finances to a safer position. The favourable short-term macroeconomic outlook means that there is no need for cyclical stimulus at this time, while risks of overheating could materialise in future years. Debt levels still remain very high, which leaves Ireland vulnerable to adverse shocks such as those from a harder-than-expected Brexit impact. On the basis that GNI* is a more appropriate measure of national income for Ireland than GDP, this suggests that Ireland's net debt burden ranks as the fourth highest in the OECD. Progress in moving the public finances to a safer position slowed in recent years following the introduction of within-year spending increases.

The Council assesses that it would be conducive to prudent economic and budgetary management for *Budget 2018* to stick to existing spending and tax plans within the available gross fiscal space for 2018 of around €1.7 billion. The Department's latest estimates show some €1.7 billion available for tax and spending changes in 2018 if the fiscal rules are fully met. This estimate of €1.7 billion is based on the required 0.6 percentage point of GDP improvement in the structural balance as Ireland moves to its medium-term budgetary objective. However, the cost of previously announced measures, as well as the yet-to-be approved public sector pay agreement (Public Service Stability Agreement 2018-2020), reduces the scope for new initiatives in *Budget 2018* to approximately €½ billion. If additional priorities are to be addressed, these should be funded by additional tax increases or through re-allocations of existing spending. Any unexpected increases in tax revenues or lower interest costs should not be used to fund permanent budgetary measures.

Additional in-year spending measures for 2017 would not be advisable. Considering that the rules already risk being breached this year, a further relaxation of the stance for 2017 would not be appropriate. Within-year expenditure increases, like those in 2015 and 2016, would result in a more expansionary stance than originally planned, unless they are offset by corresponding expenditure savings or new revenue measures elsewhere. Insufficiently ambitious budget plans combined with a number of within-year increases in expenditure contributed to limited compliance with the fiscal rules. This is visible in a lack of progress in improving the primary balance during 2016 and 2017, despite favourable economic conditions. Had unexpected corporation tax receipts and interest savings been used for deficit reduction, rather than for within-year spending increases in 2015 and 2016, the budget would have been in balance roughly two years earlier than is now projected.

The Government should commit to adhering to all elements of the fiscal framework, including the Expenditure Benchmark, even if the medium-term objective for a structural deficit of 0.5 per cent of GDP is exceeded. Once the objective for a structural deficit of 0.5 per cent of GDP is passed – as may happen next year under current plans – the other pillar of the rules, the Expenditure Benchmark, ceases to apply as strictly. However, continuing to adhere to this spending rule would help to avoid the boom-bust cycles that have proved costly in the past. The Expenditure Benchmark is designed to ensure that spending growth does not follow a procyclical pattern and is meant to be consistent with the structural balance rule, though differences in its calculation compared with the structural balance rule provide some safeguards around measurement issues. If current growth projections are realised, this would imply small budget surpluses in the coming years.

The Rainy Day Fund could make a useful contribution to more sustainable growth and to prudent management of the public finances, but details of how it is to operate should be published. It is not clear how the design of the Rainy Day Fund will ensure that it is truly countercyclical, given that allocations set out so far are fixed and appear to end in 2021 rather than responding to cyclical developments. How the fund is intended to operate in tandem with the fiscal rules should be clarified, particularly so that support can be provided to the economy in a downturn. Recognising these issues and the limited information that is currently available in relation to how the Rainy Day Fund is intended to operate, the Council urges the Government to publish a detailed proposal on the Rainy Day Fund before or as part of *Budget 2018*.

Public investment looks set to ramp up quite rapidly, while still complying with the fiscal rules. Following high levels of investment pre-crisis, the consolidation of the public finances saw public investment levels approximately halved. However, government plans show Exchequer capital spending set to ramp up again from €4.2 billion in 2016 to €7.8 billion in 2021, with some of these allocated resources still available to commit to new initiatives. As a share of either government spending or revenues, this would imply public investment in Ireland moving from relatively low levels to among the highest in the EU. The investment increase would be achieved while complying with the fiscal rules in future years. The recent experience in Ireland has seen a procyclical pattern to spending, and this has been a pronounced feature of public investment spending in particular. Adhering to all elements of the fiscal framework would help to prevent forced cuts in areas like investment spending in future downturns, and would help to smooth out spending on investment projects over future cycles.

1. Introduction

The Council's mandate includes assessing the prudence of the Government's fiscal stance. The basis for the Council's assessment is twofold: first, the Council conducts an economic analysis, which assesses the appropriateness of the fiscal stance in terms of the principles of sound economic and budgetary management; second, the Council assesses whether the Government's fiscal plans are in line with the requirements of the budgetary framework.[1]

This *Pre-Budget 2018 Statement* reviews the fiscal stance in advance of *Budget 2018* in line with these aspects of the Council's assessment. Since the Council's *Fiscal Assessment Report June 2017*, the Government has published its *Summer Economic Statement 2017* (*SES 2017*) and *Mid-Year Expenditure Report 2017*.

2. The Macroeconomic Context for the Budget

Recent data from the National Accounts confirm the Council's macroeconomic assessment in the *Fiscal Assessment Report June 2017* that the economy has undergone a rapid recovery. While near-term growth prospects continue to look favourable, longer term risks are posed by the possibility that the outcome of Brexit discussions has a more negative impact on the Irish economy than is currently assumed. Other risks stem from Ireland's reliance on a small range of specialised exporting activities, and from international tax policies.

Figure 1 examines a range of useful indicators of domestic activity. Starting with the new GNI* measure (Box A), as yet, only available in nominal terms, growth in economic activity has rebounded sharply in recent years. Nominal growth of GNI* was 11.9 per cent in 2015 and 9.4 per cent in 2016. Another useful measure, "Domestic GVA", tries to isolate domestic activity by ignoring sectors in the economy that are dominated by foreign-owned multinationals, and this is available in real terms (i.e., stripping out price inflation).[2] This measure shows real growth of 7.3 per cent in 2015 and 5.3 per cent in 2016.

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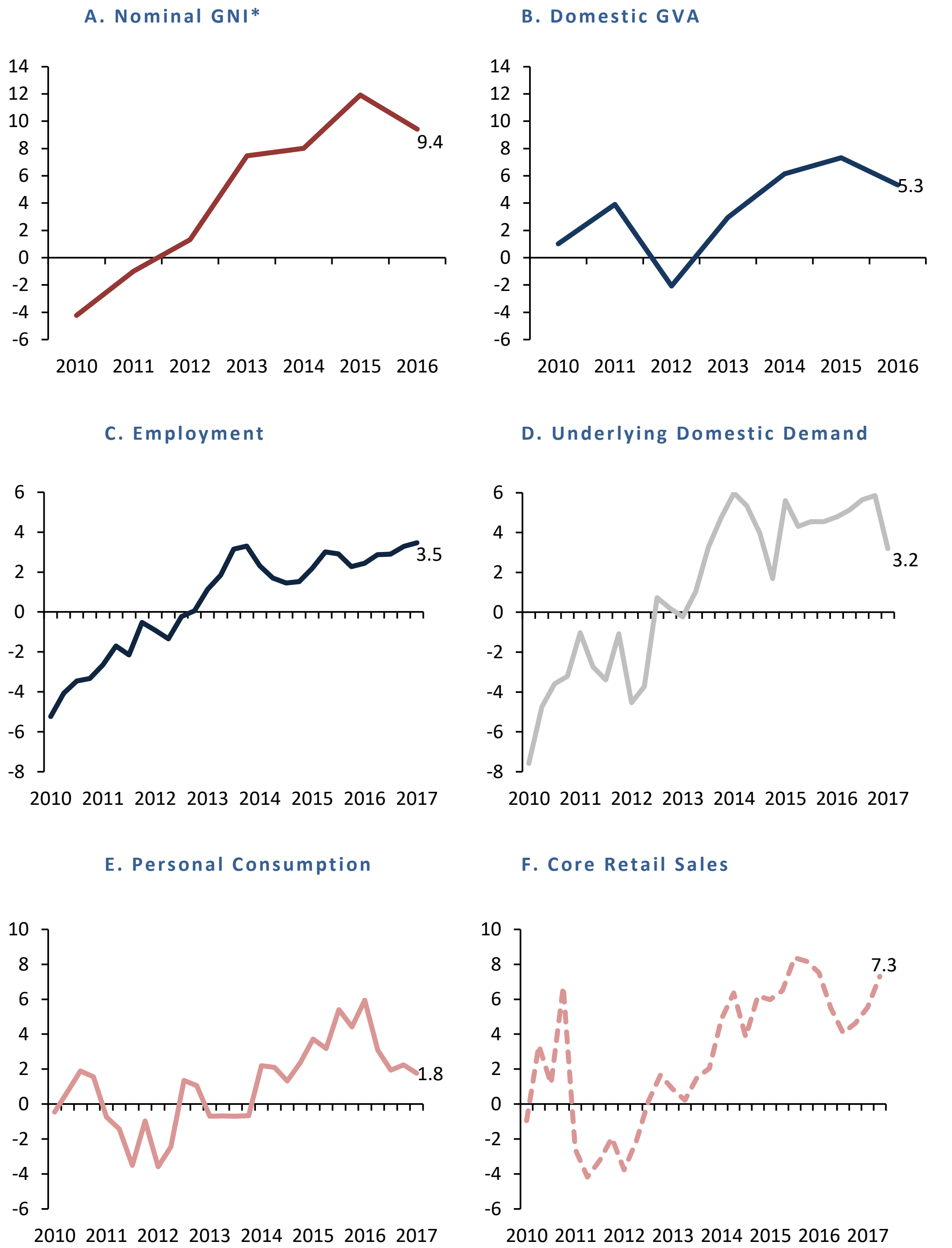
[1] The budgetary framework is a system of procedures and rules that are designed to set the public finances on a sustainable path. The framework includes the requirements outlined under the domestic Budgetary Rule (as set out in the Fiscal Responsibility Act 2012) as well as those covered by the EU's *Stability and Growth Pact* (*SGP*). The framework also gives an independent role in monitoring and assessment to the Council.

[2] Sectors are defined as being dominated by foreign owned-multinationals if they account for over 85% of turnover in that sector.

Figure 1: Indicators of Economic Activity

Volumes (unless stated), percentage change, year-on-year



Sources: CSO; and internal Irish Fiscal Advisory Council (IFAC) calculations.

Note: Underlying Domestic Demand strips out intangibles and aircraft investment in full as these are, in the main, imported, with little impact on real GDP. Core retail sales are total retail sales excluding motor trades.

Aggregate national accounts measures may still be prone to a variety of distortions, notwithstanding efforts to abstract from the effects of foreign-owned multinational enterprises. It is therefore useful to supplement this information with alternative indicators. Labour market data has proven a useful source of information on domestic activity, in particular, and reinforces the view of a rapid recovery. Employment growth in year-on-year terms has averaged close to 2.5 per cent since 2013 and has shown no let up through 2016 and early-2017. Underlying domestic demand, personal consumption and core retail sales similarly point to a sustained recovery over the last few years, bolstered by rising employment.[3]

As noted in the Council's *June 2017 Fiscal Assessment Report*, the rapid growth seen in the Irish economy in recent years is perhaps less surprising given the capacity for economies to bounce back sharply from severe downturns. As such, much of the recent growth may be considered cyclical, with the economy closing on its level of potential output.

Data for the year so far suggest that positive macroeconomic conditions appear set to continue in the near term. Real GDP growth for the first quarter is estimated at 6.1 per cent year-on-year, while the monthly unemployment rate has already fallen to 6.4 per cent as of July. Core retail sales data (i.e., excluding motors) and purchasing managers indices both point towards further growth in the first half of 2017. The recent momentum would suggest that the economy can be expected to grow strongly again through 2017 and into 2018.

The Department currently forecasts growth in real GDP of 3 per cent on average over 2018-2021. Their central scenario is a hard Brexit (i.e. a WTO style trading relationship between the UK and EU from 2019). There are upside and downside risks to this scenario. On the upside, domestic demand could grow faster than is currently envisaged. On the downside, the impact of a hard Brexit could be more severe than conventional models would suggest.[4]

[3] Underlying domestic demand is an aggregate measure comprising consumer spending plus investment plus government consumption, which also excludes investment in intangibles and aircraft, both of which have a high import content.

[4] As noted in the *June 2017 Fiscal Assessment Report*, simulations which inform the Department's views on the medium-term impact on the Irish economy (Bergin et al., 2016) assume that the impact on the Irish labour market from a shock to UK output is equivalent to a shock to an average trading partner. However, UK destined exports tend to attract a relatively high labour intensity and so the impact of a trade disruption related to UK developments may be more adverse than is estimated.

With the recovery appearing set to continue, it is worth considering what this means for the cycle. While measures of the output gap (i.e., the gap between the economy's level of output and its full potential) are uncertain, a range of measures suggest that the output gap for Ireland is either almost closed or rapidly closing. Were the recent strong growth rates to continue over the coming years, there is a realistic possibility of the economy beginning to overheat, with wage and price pressures becoming stronger.

Box A: The New Modified Measures GNI* and Current Account*

Two new economic measures were published by the CSO in June 2017 as part of the national accounts release: a modified measure of Gross National Income (GNI) called GNI* and a modified measure of the current account balance called Current Account*.

Adjustments

Both GNI* and Current Account* use the same adjustments to the simple current account balance and GNI to arrive at the modified measures. These adjustments are intended to capture certain distortions related to foreign-owned enterprises, particularly multinational enterprises. The adjustments comprise: (i) the estimated factor income of re-domiciled companies; and (ii) the estimated depreciation related to aircraft leasing activities and research and development from imported intellectual property.

Better Measures of Economic Activity and External Balances?

While GDP is typically used as the standard measure of economic activity and as the base for assessing fiscal metrics, this has traditionally been well understood to be a poor measure for Ireland. This reflects the unusual gap between GDP and GNP arising from a relatively high level of multinational activity and subsequent repatriation of profits (Box A, IFAC 2017). Recent developments, both methodological and economic, have led to further distortions that have effected both GDP and GNP, so that both measures are now subject to large distortions.

In 2015, a level shift in both GDP and GNP was observed, as both measures were boosted by a dramatic rise in net exports that resulted from corporate restructuring (Box A, IFAC, 2016b). Many of the activities causing these distortions do not contribute significantly to the tax base; their presence is large by international standards; and they are predominantly conducted by foreign-owned multinationals. As such, there is a good case for disregarding them when assessing economic activity and debt sustainability. These innovations have recently had the effect of making growth rates and fiscal measures appear more favourable.

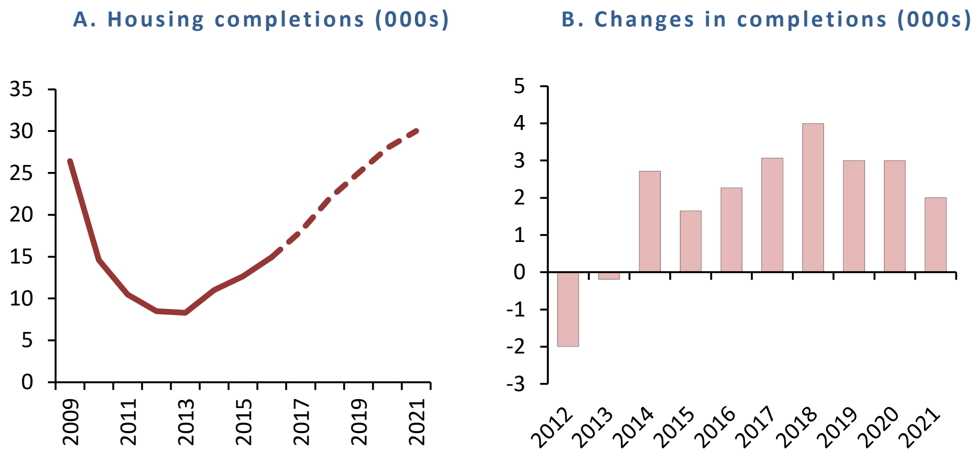
Although the new GNI* and Current Account* measures achieve the intended aim of removing two key sources of distortion, it remains to be seen if they provide reliable signals of national income and external balance. In particular, the Current Account* measure shows a deficit of lower than 10 per cent of GDP in 2016, which does not appear to accurately reflect the underlying external balance of the Irish economy.[5]

One sector that could grow more rapidly in the coming years is the housing sector, a development which would be welcomed given emerging supply shortfalls. Current forecasts from the Department imply that housing output will

[5] Adjusting for imports of intellectual property and aircraft gives a current account surplus of 4.4 per cent of GNI* for 2015 and 7.1 per cent for 2016.

increase steadily over the medium term (Figure 2). However, it is possible that a much faster response could take hold reflecting the possible significant pent-up demand for housing that may have emerged in recent years as completions have been running at levels well below estimated demand. Prices have also risen sharply in recent years – though are still short of pre-crisis peak levels. These pressures could prompt a faster and more pronounced increase in housing output than is currently envisaged.

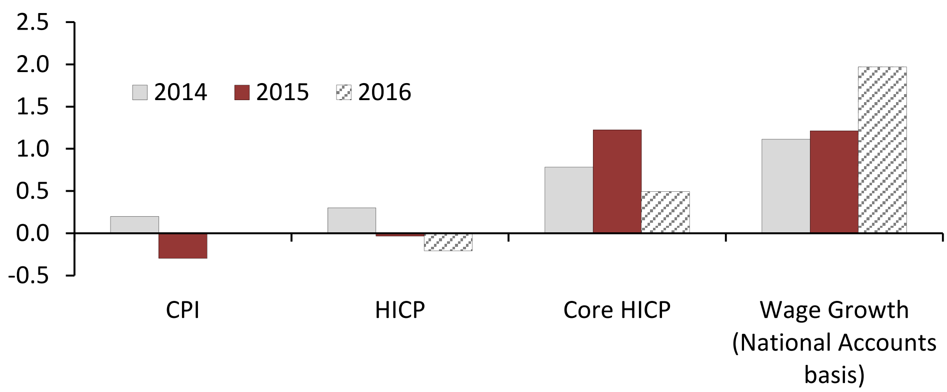
Figure 2: Housing completions



Sources: Department of Housing, Planning & Local Government; and *SPU 2017*.
Note: 2017-2021 estimates are based on *SPU 2017* forecasts.

It is important to stress that there is not significant evidence of overheating in the economy at present. Looking at Figure 3, while wage growth has increased recently, core HICP inflation and other price pressures remain relatively subdued.

Figure 3: Inflation measures
Percentage change, year-on-year



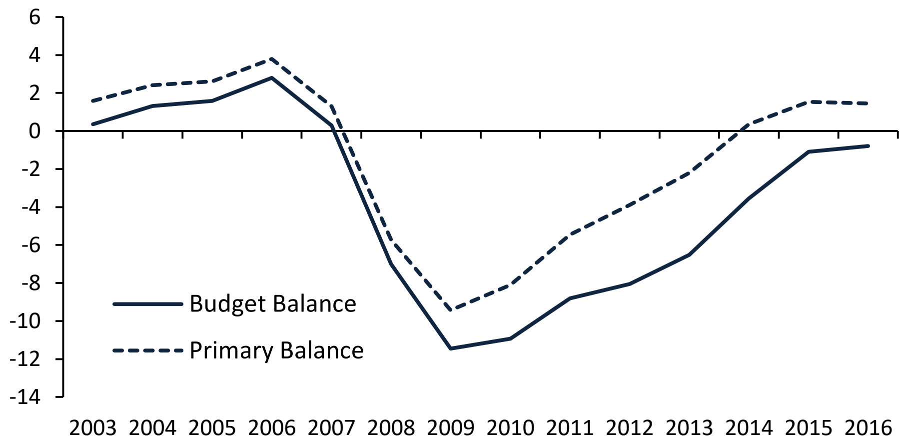
Sources: CSO; and internal Irish Fiscal Advisory Council (IFAC) calculations.
Note: Wages are defined as remuneration of employees (NIE) divided by total hours worked derived from the QNHS and EHECS data.

Though short-term prospects for the Irish economy look positive, significant risks surround future growth prospects. As a small open economy, Ireland remains exposed to changes in external conditions. Exchange rates, the monetary policy stance of the ECB and trading partner growth are all key inputs into Irish growth prospects. While risks to the forecasts may be balanced in the short term, with upside risks stemming from the response of the housing market in particular, there are clear downside risks for the much longer term. As noted above it is possible that the impact of a hard Brexit may be underestimated. The impact of Brexit is a key consideration for Ireland's trend growth rate, which informs the setting of appropriate fiscal policy.

3. The Fiscal Context for the Budget

Since 2008, successive governments have achieved a sizeable correction in the deficit that emerged in the public finances during the crisis with a likely return to a balanced budget in 2018. These improvements are also visible in the general government primary balance excluding one-offs (i.e., the budget balance excluding interest costs and any temporary items), which moved from a deficit of 9.4 per cent of GDP in 2009 to a surplus of 1.5 per cent in 2015 (Figure 4).[6]

Figure 4: Government Balances Excluding One-Offs
% GDP, general government basis



Sources: CSO; Department of Finance; and internal IFAC calculations.
Note: Data are adjusted to exclude one-offs assessed as applicable by the Council for 2016 and earlier years.

[6] The primary balance excluding one-offs is a useful measure and is close to the definition of the fiscal stance as outlined in the Fiscal Responsibility Act 2012, except that it does not account for the effects of the cycle. The Act specifies the "fiscal stance" as the change in the annual structural balance of the general government, excluding interest payments.

The correction in the deficit was achieved through a mixture of discretionary increases in revenues and expenditure reductions, a rebound in economy activity, lower interest costs and increased non-tax revenues. This combination of substantial consolidation efforts, successful implementation and good fortune elsewhere succeeded in stabilising the rising debt ratio and, finally, in putting it on a downward path.

Table 1: Summary of Key Aggregates for the Public Finances
% GDP unless stated, general government basis

Date Source	2015 CSO	2016 CSO	2016 DoF	2017 DoF	2018 DoF	2019 DoF	2020 DoF	2021 DoF
Revenue [1]	27.0	26.1	27.3	26.8	26.5	26.2	26.2	26.1
Expenditure [1]	28.0	26.9	28.0	27.2	26.6	26.3	25.8	25.3
Balance [1]	-1.1	-0.8	-0.7	-0.5	-0.1	-0.1	0.4	0.8
Interest Expenditure	2.6	2.3	2.3	2.1	2.0	1.9	1.7	1.6
Primary Expenditure [1]	25.4	24.7	25.7	25.1	24.6	24.4	24.0	23.7
Primary Balance [1]	1.5	1.5	1.6	1.7	1.9	1.8	2.1	2.4
CAM Structural Balance [2]			-1.4	-1.2	-0.5	-0.3	0.3	0.8
Change in CAM Structural Balance (pp) [2]			0.3	0.2	0.6	0.2	0.6	0.6
CAM Structural Primary Balance [2]			1.0	1.0	1.5	1.6	2.0	2.4
Change in CAM Structural Primary Balance (p.p.) [2]			0.0	0.0	0.5	0.1	0.4	0.4
Gross Debt	76.9	72.8	75.4	72.7	70.6	68.5	64.3	62.1
Net Debt	65.6	63.7	66.0	63.4	60.9	58.8	57.1	55.2
Gross Debt (% GNI*)	116.5	106.0	106.0					
Net Debt (% GNI*)	99.4	92.8	92.7					
Gross Debt (% Revenue)	285.2	276.4	274.4	271.3	266.6	261.3	245.7	238.0
Net Debt (% Revenue)	243.4	241.8	240.3	236.7	230.1	224.3	218.4	211.6
Real GDP Growth (% change)	25.6	5.1	5.2	4.3	3.7	3.1	2.7	2.5
Nominal GDP Growth (% change)	34.7	5.2	3.9	5.5	5.0	4.6	4.4	4.2
CAM Potential Output (% change) [2]			5.1	4.2	4.3	3.5	3.0	2.8
CAM Output Gap (% potential GDP) [2]			1.2	1.4	0.8	0.5	0.3	0.0

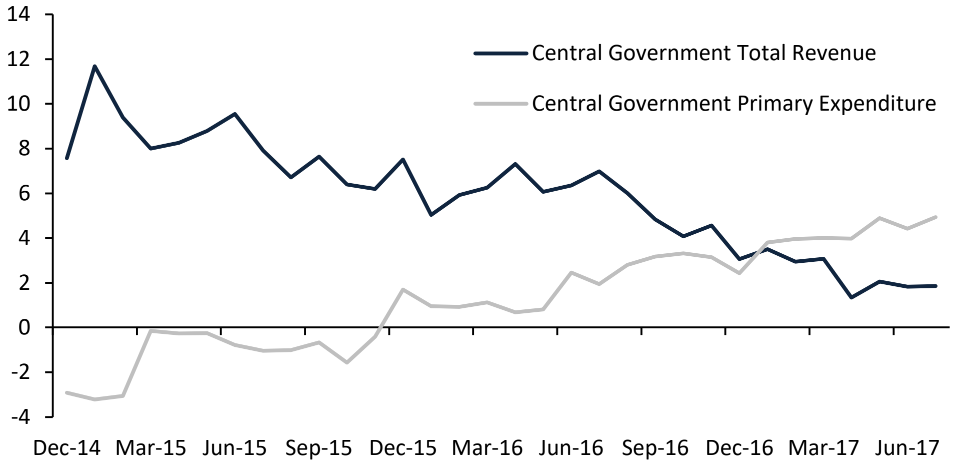
Sources: CSO (National Accounts 2017; and latest Government Finance Statistics); Department of Finance (*SPU 2017* and *SES 2017*); and internal IFAC calculations.
[1] One-offs/temporary measures are removed from fiscal aggregates to get a sense of the underlying fiscal position (IFAC 2017) and are as assessed by the Council to be applicable for 2015-2016, with Department of Finance one-offs used thereafter.
[2] Figures are based on Commonly Agreed Methodology (CAM)-based potential output estimates and are those published in *SPU 2017*. One offs used are same as above.

However, the pace of improvement in the budget position slowed has slowed since a deficit of less than 3 per cent of GDP was achieved in 2015.This has been, in part, due to within-year spending increases introduced during 2015 and 2016 which – though individually small – are cumulative and long-lasting. For 2016 and 2017, it is likely that government non-interest spending will have risen at a pace only slightly below that of revenue growth excluding one-offs (2.8 per cent as compared to 3.2 per cent, when using annual average growth rates).

These developments have led to the slowdown in improvements to the primary balance (excluding one-offs), which has barely improved despite the favourable economic conditions (Table 1).[7]

The near-term fiscal context is broadly favourable, supported by strong growth prospects and low effective interest rates on government debt. Yet, recent data (Figure 5) would also suggest that the pace of growth in non-interest spending (4.9 per cent for the twelve months to June 2017) has begun to outpace revenue growth (1.9 per cent).

Figure 5: Central Government Revenue and Primary Expenditure
% change year-on-year (12-month moving sum)



Sources: Department of Finance; Analytical Exchequer Statements and internal IFAC calculations.
Note: Transactions that do not impact the general government position are excluded. Total Revenue is Exchequer tax plus non-tax revenue plus appropriations-in-aid and excess capital resources. Primary Spending is gross Exchequer expenditure minus national debt interest. Receipt of Central Bank Surplus moved from April to May in 2016 for consistency with other years.

Latest Budgetary Data

In the run up to *Budget 2018*, the performance in overall revenues has been broadly as expected. Exchequer and other central government revenues are short of expectations by just €34 million for the year-to-end-July. Income taxes have fallen below expectations for the year-to-end-July by €208 million, yet this has

[7] Note that historical data have been updated since the publication of the *SES 2017* to reflect revised national accounts and public finances data. This should lead to revisions to *SES 2017* forecasts for *Budget 2018*.

been offset by an over-performance in PRSI receipts of €162 million. PRSI receipts have been relatively strong in the year-to-July; with the average twelve-month rolling growth rate some 8 per cent reflecting the improvements seen in the labour market. The under-performance in income tax is a little surprising, though it seems that part of the reason for the shortfall in income tax may be related to a misallocation of the *Budget 2017* package between PAYE and schedule D payers giving rise to timing issues.[8]

Table 2: Government Revenue Performance

Performance against profile (i.e., *Budget 2017* forecasts) for Jan-July 2017

	Profile	Outturn	Difference (Outturn – Profile)	
	€m	€m	€m	%
Income Tax	10,928	10,720	-208	-1.9%
VAT	8,719	8,793	74	0.8%
Corporation Tax	3,620	3,606	-14	-0.4%
Excise Duty	3,365	3,322	-43	-1.3%
Other Taxes	1,410	1,371	-39	-2.8%
Exchequer Tax Revenue[1]	**28,042**	**27,812**	**-230**	**-0.8%**
PRSI Receipts[2]	5,374	5,536	162	3.0%
National Training Fund Levy[2]	247	243	-4	-1.6%
Other Appropriations in Aid[3]	1,270	1,305	35	2.8%
Non-Tax Revenue	1,332	1,335	3	0.2%
Capital Resources	14	14	0	0.0%
Other Revenue[4]	**8,237**	**8,433**	196	2.4%
Exchequer and Other Central Government Revenues[4]	**36,279**	**36,245**	**-34**	**-0.1%**

Source: Department of Finance Analytical Exchequer Statement
Notes: Revenues with no general government impact are excluded
[1] Excludes Motor Tax, Commercial Rates and other items
[2] Includes excess of fund receipts over expenditure
[3] Reflects Departmental expenditure covered by Departmental receipts and balances
[4] Excludes Certain Investment Income, Broadcasting License Fee, Local Government Receipts and other items

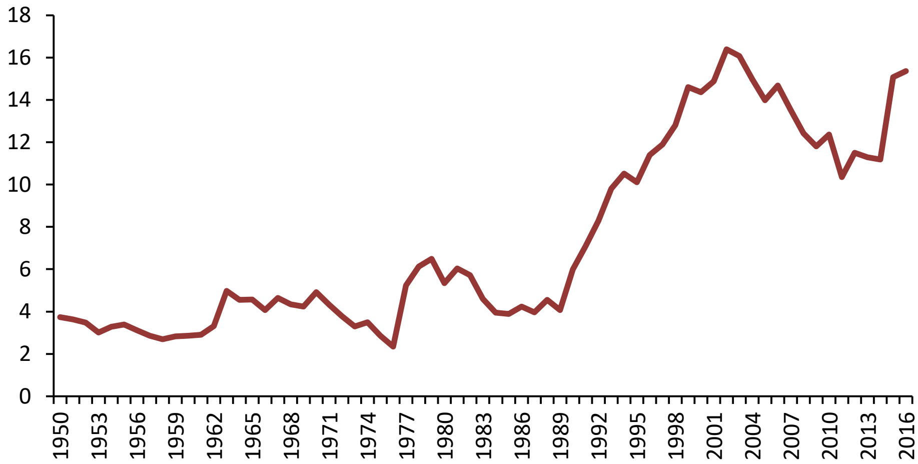
Corporation tax receipts are performing in line with expectations, unlike in previous years when the rise in receipts outpaced forecast growth rates. The Council has in the past emphasised that there are risks in using surprise gains

[8] As noted in the June 2017 Fiscal Assessment Report.

under this tax head, considering the uncertainties over the sustainability of unexpected increases.[9] The Government has indicated that, "while Corporation Taxes are now expected to account for around just 15½ per cent of all Exchequer tax revenues, this is within the previous pre-crisis range from such receipts".[10] However, the share of total tax receipts is close to historical peaks and is the highest level in absolute terms on record, albeit different tax regimes prevailed over earlier periods (Figure 6).

Figure 6: Irish Corporation Tax Receipts

% total Exchequer tax revenues



Sources: Department of Finance databank and finance accounts.

Expenditure is also broadly as expected for the year-to-July, with total voted expenditure 0.8 per cent (€254 million) below forecast. The majority of Departments (13 of 16) currently remain below expectations in terms of current expenditure. The Department of Health has seen large deviations from spending plans in past years but spending for the first seven months of 2017 is still broadly as forecast.

Capital expenditure is below expectations for the year-to-date (4.1 per cent below profile), though this may be related to timing. Reflecting the stage in the cycle of the *Capital and Investment Plan 2016 to 2021,* capital projects are likely to begin to ramp up gradually and budgetary projections suggest that gross voted capital expenditure is to increase by some 7.7 percent in 2017. Most departments are

[9] Corporation Tax represents the most volatile of the main Irish tax heads; is difficult to forecast accurately; is especially concentrated; and is acutely prone to exogenous risk factors such as international tax policy developments (Casey and Hannon, 2016).

[10] See the Response of the Minister for Finance and Public Expenditure & Reform to the Fiscal Assessment Report, June 2017.

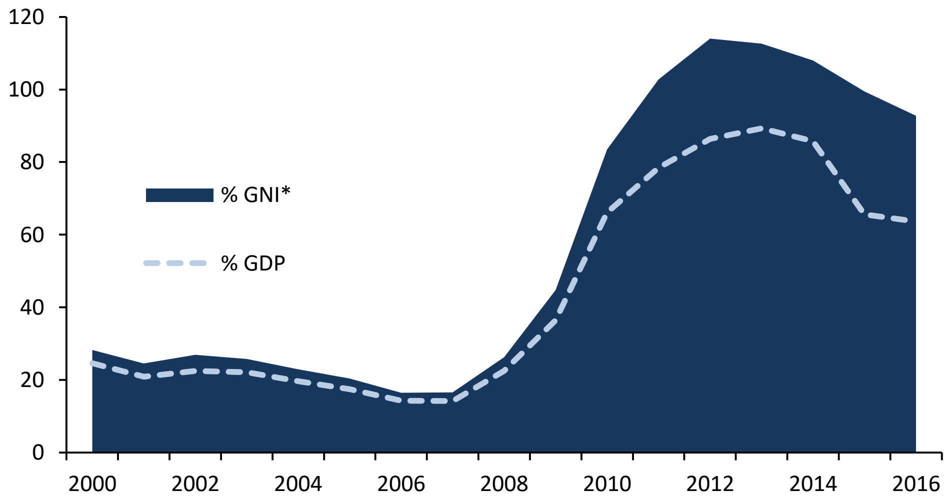
behind expectations thus far in terms of capital spending. An exception is the Department of Housing, Planning, Community and Local Government, which is €111 million (+42.2 per cent) ahead of its gross voted capital expenditure forecast for the year-to-date.

4. Assessment of the Fiscal Stance in Advance of the Budget

The Council's approach to assessing the prudence of the overall fiscal stance involves: (i) a broad economic assessment that considers appropriate management of the cycle as well as the sustainability of the public finances; and (ii) an assessment of compliance with the legislated domestic and EU fiscal rules.

Based on official forecasts for 2017-2021, Ireland's debt dynamics are expected to remain relatively favourable by historical standards. Notwithstanding the considerable progress made in recent years (Section 3), challenges remain. Debt levels remain high following the crisis (Figure 7) and are set to decline at a gradual pace under current plans.

Figure 7: Government Net Debt Levels
% GNI* and % GDP



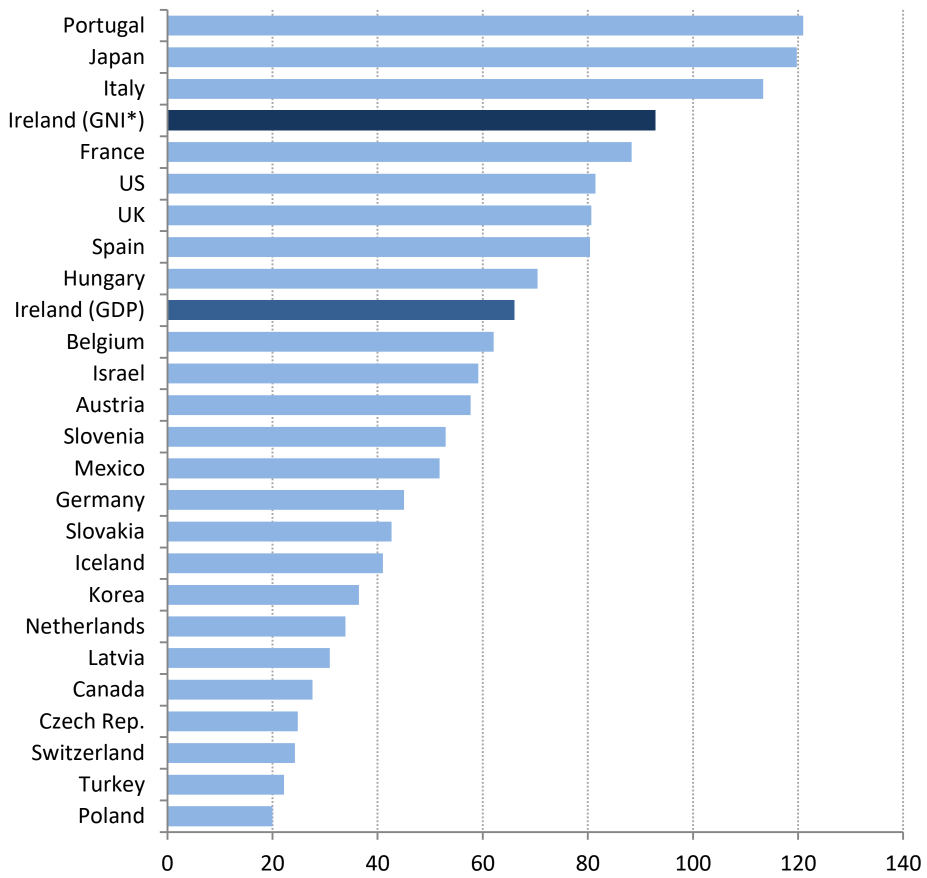
Sources: CSO; Department of Finance; and internal IFAC calculations.

The debt burden is still comparatively high for Ireland, but is understated by standard metrics like GDP. Figure 8 compares Ireland's end-2016 debt ratio using both GNI* and GDP against other OECD countries for which data are available. On the basis that GNI* is a more appropriate measure of national income than GDP, this suggests that Ireland's net debt burden ranks as the fourth highest in the

OECD, somewhat above France, Spain, the United Kingdom and the United States. Only Portugal, Japan and Italy have higher debt burdens.[11]

Figure 8: OECD Countries Net Government Debt (Top 25 Countries)

End-2016 net general government debt % GDP (incl. % GNI* for Ireland)



Sources: CSO; Eurostat; IMF World Economic Outlook (April 2017) and internal IFAC calculations.
Note: CSO data are used for Ireland; Eurostat data for Luxembourg, Czech Rep., Slovakia, Slovenia; and IMF data for remaining countries.

As Section 2 shows, the macroeconomic context for *Budget 2018* is one that is largely favourable for the short term, with real GDP growth forecast to average 3 per cent per annum over 2018-2021. In addition, near-term upside risks stem from pressures arising in the housing market. However, the hard Brexit assumed in the Department's forecasts could be more negative for Ireland's trend growth rates than is currently expected and further risks are posed by the concentration of Ireland's exporting base and potential changes to the international tax system. All else equal, such impacts could reduce the pace at which incomes and government revenues could sustainably grow. By extension, this would reduce the

[11] Note that net debt data are not available for Greece.

pace at which public spending can be increased sustainably in future, in the absence of new revenue sources.

Budget 2018 should seek to avoid for 2017 the within-year increases in spending that were introduced in 2015 and 2016 to ensure that mistakes of past cycles are not repeated. Had unexpected corporation tax receipts and interest savings been used for deficit reduction, rather than to part-fund within-year spending increases in 2015 and 2016, the budget would have been already in balance in 2016 (IFAC 2017). This would have been roughly two years earlier than now projected by the Government. In addition, the debt level would have been estimated to be just over €8 billion lower by 2021 (or €4 billion lower at end-2018, just in advance of the expected conclusion of Brexit negotiations). Furthermore, the structural balance would have been brought to its MTO this year (a year earlier than originally expected). Achieving the MTO a year earlier would have allowed expenditure to grow in line with the estimated pace of sustainable economic growth (without any convergence margin). Instead, by using various budgetary surprises to increase expenditure within-year, fiscal space that would have been available for 2018 has already been used, and further efforts are required to achieve the MTO.

Recognising the risks to long-term growth rates and from high debt levels, it is important that the Government underlines its commitment to adhering to the new fiscal framework that has been put in place as a valuable structure to guide Irish fiscal policy. There are a number of ways in which this can be achieved, which later parts of this section outline.

Sticking to Available Fiscal Space for *Budget 2018* and Subsequent Budgets

Under current plans, net primary spending can grow by 2.4 per cent in 2018 and by over 5 per cent on average per annum over 2019-2021.[12] The Council assesses that it would be conducive to prudent economic and budgetary management to stay within the currently estimated available fiscal space for *Budget 2018* as well as for later years. If additional priorities are to be addressed, these should be funded by additional tax increases or re-allocations of existing spending.

[12] This is the nominal growth rate that current estimates for the fiscal rules indicate that primary spending can grow by, in the absence of discretionary tax changes.

The *Summer Economic Statement 2017* shows that current estimates of "gross fiscal space", the amount available for tax and spending changes in 2018 if the fiscal rules are complied with at a minimum, suggest €1.7 billion is available for *Budget 2018*. Using this estimate as a basis for implementing the budget is a sensible approach – one that is calculated on the basis of both pillars of the fiscal rules – and this approach should serve as an anchor for future budgets.[13]

In addition to the €1.7 billion of gross fiscal space, there is a further €0.5 billion of scope for new initiatives created through non-indexation of the tax system. This non-indexation is treated as a discretionary revenue-raising measure, and it implies scope of €2.2 billion for tax and spending measures in 2018.

However, much of the available gross fiscal space is already pre-committed following a number of past government decisions as well as the cost of accommodating expected demographic changes:

First, *Budget 2017* included a number of new tax and spending measures that had additional carry-over costs of some €0.65 billion which are expected to arise in 2018. On the tax side, decisions made in *Budget 2017* whose costs are only realised in full during 2018 reduce gross fiscal space by €0.17 billion. On the expenditure side, similar carryover effects from the previous budget impact on fiscal space for 2018 by lowering it by €0.47 billion.[14]

Second, a number of spending plans have already been outlined by the Government, which further reduce fiscal space for 2018 by some €0.9 billion. This includes spending programmes already committed to such as the "*Action Plan for Housing and Homelessness*" launched by the Government in July 2016 as well as the cost of providing existing public services and benefits, while allowing for demographic changes.[15]

[13] The two pillars of the fiscal rules referred to here are the Expenditure Benchmark rule and the requirements for the Structural Budget Balance.

[14] For example, social protection measures introduced under *Budget 2017* have a gross carry-over cost of €0.17 billion for 2018. Similarly, education and health measures introduced in *Budget 2017* each have further carry-over costs of €0.1 billion for 2018.

[15] Rebuilding Ireland: Action Plan for Housing and Homelessness is available at: http://rebuildingireland.ie/Rebuilding%20Ireland_Action%20Plan.pdf

Once all of the carry-over costs from *Budget 2017* and other measures already committed to by Government are accounted for, the remaining scope for new measures in *Budget 2018* falls to an estimated €0.65 billion.[16]

Table 3: Fiscal Space for *Budget 2018*
€ billions

	2018
Gross Fiscal Space (*SES 2017 Estimate*)	**1.7**
Non-indexation	+0.5
Pre-Committed Spending (e.g., for demographics, etc.)	-0.9
Carry-over costs of *Budget 2017* Measures	-0.65
...of which tax	*-0.17*
...of which expenditure	*-0.47*
Nominal Resources for New Measures	**0.65**

Sources: Department of Finance; and internal IFAC calculations.
Note: Figures may not add due to rounding. Non-indexation amounts refer to additional revenue generated from not proceeding with indexation of income tax bands and rates. This is treated as a policy decision and is therefore included as a discretionary revenue-raising measure.

A number of additional policy changes are expected to be determined by budget day, many of which the Government has indicated will be met within existing resources. For 2017, there is the payment of the Christmas Bonus and a potential refund of water charges. For 2018, there is the cost of the new public sector pay agreement.[17] Such measures could reduce available fiscal space if they are not met within existing resources. Furthermore, it would not be appropriate, as in recent budgets, to introduce within-year spending increases.

In setting the Budget for 2018 and making commitments for future years, an important consideration in the context of fiscal space is the cost of providing today's level of public services over the forecast horizon. While there may be scope for efficiency savings or reallocation of spending, the setting of new

[16] To ensure that achieving the MTO in 2018 is not jeopardised, the Department has factored in a "margin of compliance" of €0.15 billion relative to minimum compliance with the Expenditure Benchmark. This leaves an estimated €0.5 billion in scope for new measures in *Budget 2018*.

[17] The proposed pay agreement (Public Service Stability Agreement 2018-2020) is estimated to cost €0.18 billion in 2018. This was recently agreed by Government, but is subject to approval by public service unions and staff associations. *SES 2017* notes water funding decisions will be made later in the year. An estimated cost of refunding water charges already paid was given to the Oireachtas Budgetary Oversight Committee 20 July 2017, with the costs of refunding charges estimated at a total cost of €178 million.

commitments should take into account the cost of meeting existing commitments.

The Council's Stand-Still scenario shows the estimated increases in current spending if demographic pressures were fully accommodated for and if spending moved in line with inflation as forecast in *SPU 2017* by the Department.[18] Table 4 compares the gross fiscal space available for 2019 to 2021 with the Council's Stand-Still scenario. In this scenario, gross voted current spending would increase by just over €1½ billion each year, whereas gross fiscal space of more than €3½ billion is available each year.

Table 4: Comparison of Estimated Gross Fiscal Space and Current Expenditure Increases under a Stand-Still Scenario
€ billions

	2019	2020	2021
Gross Fiscal Space (*SES 2017*)	3.6	3.9	4.0
Gross Voted Current Spending Increases (IFAC Stand-Still Scenario)	1.5	1.7	1.8

Sources: Department of Finance; Department of Public Expenditure and Reform; and internal IFAC calculations.

This scenario highlights the capacity for rising public spending, while complying with the fiscal rules. However, it also emphasises that such increases may leave limited scope for an additional expansion in services unless reallocations from investment spending, changes to existing tax plans, the introduction of new revenue-raising measures or efficiency gains in spending are realised elsewhere.[19]

A Clear Commitment to all Elements of the Fiscal Framework

Ireland's high debt position leaves it exposed to adverse shocks. Rebuilding the capacity to withstand these will take time. It is essential that policy mistakes,

[18] The Stand-Still Scenario estimates are attained using a bottom-up approach based on the latest expenditure estimates for 2016, a cohort component demographics model and the latest macroeconomic and inflation forecasts from the Department. For more details on the Stand-Still scenario see Box G in the June 2017 Fiscal Assessment Report. It is important to note that the Stand-Still scenario estimates do not take account of any other pre-committed expenditure increases included in *SPU 2017* and are only based on the estimated cost of fully accommodating demographic changes and price increases. Additionally, live register savings noted in the Expenditure Report 2017 could offset the pre-committed gross voted current expenditure increases noted should such savings be realised.

[19] Obviously, introducing spending increases like those outlined in the Stand-Still scenario would be a decision for the Government. The scenario is intended solely as an illustrative estimate of future spending pressures based on the calculation of the cost of providing today's level of public services over the forecast horizon.

which have contributed to multiple economic crises in recent decades, are not repeated. In particular, changes in spending and taxes should be managed carefully so as to ensure that the public finances do not provide unnecessary stimulus to the economy if it begins to overheat. This would also help to ensure that debt levels continue to be reduced to safer levels at a gradual pace, and to reduce the risk of sharp retrenchments being required in the event of a severe downturn.

The domestic and EU fiscal rules offer a reasonable framework to achieve both of these objectives. One of the pillars of the rules – the Expenditure Benchmark – seeks to limit growth in net primary expenditure (i.e., government spending less interest and taking into account any discretionary revenue measures or tax cuts) to a pace in line with sustainable growth in the economy and total government revenues.[20] This should allow scope for moderate changes to spending and taxes, while limiting risks that cyclical or other transitory revenue gains are used to fund any permanent increases in spending. Sticking to all elements of the framework (including the Expenditure Benchmark) when the budget is close to balance and when the economy is operating close to its potential level should help to prevent a return to the boom-bust cycles of the past.

The Council therefore considers it important that the Government commit to adhering to the Expenditure Benchmark even after the MTO of a 0.5 per cent of GDP structural deficit has been achieved. Official plans for the period 2018-2021 are consistent with this, and present an appropriate basis for anchoring future policy. Such a commitment to follow the Expenditure Benchmark, even when the MTO is exceeded, would go beyond the formal requirements of the rules. It would imply a small budget surplus in the coming years, but would allow for greater fiscal resources to be applied in the event of a downturn (such as that which may result from a harder-than-expected Brexit) than would otherwise be the case. Doing so helps to ensure that the rules work effectively and that the economy and public finances are managed in a prudent manner, with expenditure levels growing in line with sustainable revenues. In particular, the Expenditure

[20] Note that, in the context of discretionary revenue measures under the fiscal rules, non-indexation of the tax system is treated as a revenue-raising measure when individuals on average enter into higher tax bands as incomes rise.

Benchmark is a measure that is less prone to some distortions in the manner that the structural balance rule can be.[21]

The Expenditure Benchmark is not without its drawbacks and both rules should be complied with on an ongoing basis. There is still a risk that the pace of permitted spending growth under the Expenditure Benchmark rule might exhibit procyclical tendencies in future (i.e., rising as real GDP growth rises during a boom). This is an undesirable feature, yet one that can be monitored and adjusted for over time through policy choices.

Building on Debt-to-GDP Targets

A firmer commitment to adhering to all elements of the fiscal framework would obviate much of the need for debt targets as it would ensure that debt is still reduced to safer levels in a gradual manner. However, a well-specified debt target/limit can still serve as a useful device for governments to publicly commit themselves to as an anchor for sound public finances (e.g., Portes and Wren Lewis, 2015).

Recognising this, the Government recently announced debt-to-GDP targets of either 45 per cent or 55 per cent to be achieved by some time in the next decade (*SES 2017*). Debt targets are most useful when these are well-specified, and the proposed targets could benefit from further development.

Specifying debt targets as a share of nominal GDP makes little sense for Ireland, where nominal GDP is highly volatile and can tend to be a poor indicator of the tax base. In particular, it is subject to large distortions from the activities of foreign-owned multinational enterprises, which can have little significant revenue impact.

The suggested targets also lack a robust set of commitments and potentially would only be met over a very long period. *SPU 2017* notes that the period for meeting the targets is set for some year in the "mid-to late 2020s". In addition, by stating the debt-to-GDP ratios as targets rather than ceilings (like the SGP ceiling

[21] While the new rules are consistent with the principles of sound fiscal policy, any complex set of rules can sometimes give rise to anomalies. As with the structural balance pillar of the rules, the calculation of the expenditure benchmark is based on potential output growth, estimates of which can be subject to large revisions. Under the Expenditure Benchmark, however, the maximum allowable real expenditure growth is set as a 10-year average of estimated potential GDP growth rates. This averaging calculation can serve to smooth through some of the volatility in the estimates of potential output in a way that the structural balance pillar can fail to achieve.

of 60 per cent of GDP), it is not clear whether the Government intends to only ever reduce debt levels to those consistent with the target regardless of significant cyclical developments or windfall revenues.

Furthermore, the level of the proposed target cannot be considered low or particularly prudent. IFAC (2017a) showed that even a 45 per cent debt ratio target would, in historical terms, and using a hybrid measure that more appropriately captures fiscal capacity, be broadly equivalent to a 65 per cent debt ratio. This is still high, compared with pre-crisis levels and international norms. The recent development of a more meaningful level indicator for the national income is GNI*. When expressed against GNI*, even the lowest debt-to-GDP ratios identified by the Government would appear higher than the SGP's 60 per cent ceiling (Table 5).

Table 5: Illustrative Debt-to-GDP Targets/Ceilings using GNI*
Based on 2016 nominal GDP and nominal GNI* data

Debt Target/Ceiling as % GDP	Equivalent Debt Level as % GNI*
60	87.4
55	80.1
45	65.6

The use of specified debt ratios as a tool for budgetary management can be a useful innovation in the Irish context, but a more constructive approach is needed to defining prudent debt ratios. Several steps could be taken to help achieve this:

i. The target should be set relative to GNI* to achieve a prudent level of debt. Government, with good reason, views that GNI* "is a superior metric for assessing fiscal variables". Recognising this, it would be far more meaningful if the Government's specified debt ratios were denoted as share of GNI*.
ii. A clearer timeline and milestones for the proposed debt path (i.e., years by which certain debt levels are to be attained) should be identified to enable an assessment of performance over time.[22]

[22] The Department published its first *Annual Report on Public Debt in Ireland* in June 2017, which it intends to update annually. In reference to monitoring debt reduction, it notes that it is "it is important to set out key staging posts along the way in order to anchor progress and further enhance credibility". It also notes that "the first step is to comply with the legal requirements as set out in the Treaty on the Functioning of the European Union…to bring the debt ratio below 60 per cent of GDP." The *SES 2017* notes that "the *SGP* 60 per cent debt-to-GDP threshold will still be achieved in 2022". It is not clear whether this is the only target for which an exact year has been set or whether it is simply a forecast.

iii. The specified debt ratios should be stated clearly as either targets (e.g., a steady state position to be met on average) or as ceilings/limits.
iv. A broader assessment of long-term expenditure pressures should be considered as part of the determination of debt targets.

Compliance with the Fiscal Rules

In the *Fiscal Assessment Report June 2017*, the Council assessed compliance with the letter and spirit of the domestic and EU fiscal rules for 2016 and 2017 to be insufficient. For 2016, within-year spending increases contributed to a breach in the first pillar of the fiscal rules, the required improvement in the structural balance. Were it not for the inclusion of a one-off AIB transaction in the spending base for 2015, the second pillar (the Expenditure Benchmark) would also have been breached, albeit not by a significant deviation.

As shown in Table 6, official projections suggest that there is a risk of further non-compliance with both the Structural Balance pillar and Expenditure Benchmark pillar for 2017. *Budget 2017* plans showed an expected breach of the Expenditure Benchmark by €0.2 billion. Data revisions and other factors mean that the estimated breach is now closer to €0.6 billion, albeit still not a significant deviation.

This underlines the need to avoid within-year spending increases and suggests that expenditure should be managed carefully as the room for manoeuvre under current plans is very limited. A two-year assessment of the structural balance is projected to result in a significant deviation in 2017, based on the plans contained in *SPU 2017*. Note that, as in Table 1, historical data have been updated since the publication of the *SES 2017* to reflect revised national accounts and public finances data. This should lead to revisions to *SES 2017* forecasts for *Budget 2018,* which would likely alter the outlook shown in Table 6.

An important issue for assessment of compliance is the treatment of one-offs under the Expenditure Benchmark. The European Commission has recently revised its approach so that one-offs are now removed from spending levels assessed under the Expenditure Benchmark, including for 2015 and 2016 which is also relevant to the two-year assessment for 2017. The Minister has stated his disagreement with the Commission's expected approach due to its retrospective nature.[23]

The Council shares the view that a retrospective application of new changes to how the fiscal rules are assessed is not an appropriate approach to take when assessing compliance. The Council's current outlook for compliance (Table 6) does not incorporate this for periods before this decision came into effect. However, the Council also previously noted that the additional spending made possible by the one-off technical boost to the spending base for 2015 due to the reclassification of AIB shares as expenditure should not have been used to facilitate a looser budgetary stance in 2016 (IFAC 2016a). Availing of this once-off transaction to allow further spending increases went against the spirit of the rules and represented an unnecessary stimulus considering the fast growth in the economy and on-going risks to the public finances.

Table 6: Current Outlook for Compliance for 2017

% GDP unless stated

A. Budget Condition	Required	Expected	At MTO?			
Structural Balance	-0.5	-1.2	**Not at MTO**			
B. Adjustment Path Condition						
I. Change in Structural Balance	**Required**	**Expected**	**Compliant**	**Deviation (% GDP)**	**Deviation (€bn)**	**Significant Deviation[1]**
One-year change (p.p.)	0.6	0.2	**No**	-0.4	-1.0	No
Two-year avg. change (p.p.)	0.6	0.23	**No**	-0.37	-1.0	**Yes**
II. Expenditure Benchmark[2]	**Permitted % Growth**	**Expected % Growth**	**Compliant**	**Deviation (% GDP)**	**Deviation (€bn)**	**Significant Deviation[1]**
One-year growth rate (%)	1.3	2.2	**No**	-0.2	-0.6	No
Two-year avg. growth rate (%)	0.7	0.3	Yes	-	-	-

Sources: CSO; Department of Finance; and internal IFAC calculations.
Note: Fiscal outturns from latest CSO Annual Government Finance Statistics. One-offs and discretionary revenue measures are as reported by the Department of Finance unless the Council assesses these classifications to be invalid (see Appendices 2 and 3 of '*Ex-Post* Assessment of Compliance with the Domestic Budgetary Rule in 2016', IFAC 2017). Expenditure, revenue and output gap estimates as reported by the Department of Finance in *SPU 2017*. Requirements under the rules may be unfrozen under certain conditions.
[1] "Significant deviations" refer to thresholds that determine potential triggering of sanctions and equate to ≥0.5 per cent of GDP for one-year or an average of ≥0.25 per cent of GDP for two years.
[2] Expenditure Benchmark requirements are set as growth limits in real terms (i.e., before allowing for economy-wide price inflation). Recent changes mean that the impact of expenditure one-offs are systematically removed from spending levels assessed, with one-off revenue measures removed from discretionary revenue measures (Section 1.1.2, Vade Mecum Update (European Commission, 2017)). This is assumed not to apply for the 2017 *ex-ante* assessment, as *Budget 2017* policies were outlined in October 2016, shortly before the new methodology was introduced.

[23] See the Response of the Minister for Finance and Public Expenditure & Reform to the Fiscal Assessment Report, June 2017. Note that *Budget 2017* policies were outlined in October 2016, shortly before the new methodology was published.

A recent pattern of within-year increases in expenditure has been one aggravating factor that contributed to limited compliance with the fiscal rules in recent years and should not be continued. Though individually small, in-year increases like those for 2015 and 2016 raise the base level of spending for future years. If repeated, these would leave the public finances more exposed to risks relative to earlier plans, and would further jeopardise compliance with the fiscal rules in later years.

Looking ahead, and beyond 2018, there is more scope for government expenditure to expand in line with the economy's sustainable pace of growth, while gradually reducing debt levels. The current estimates for the fiscal rules indicate that primary spending, in the absence of discretionary tax changes, can grow by over 5 per cent on average per annum over the period 2019-2021 once the medium-term objective has been attained.

Rainy Day Fund

A Rainy Day Fund could be a useful countercyclical buffer and a tool for shock absorption. By establishing such a buffer, it is intended that some savings could be set aside in good times to provide liquidity, which could be made available when – in bad times – stimulus may be desirable. This would provide a counter-cyclical element to fiscal policy. *SES 2017* projections show that the intended annual contributions have halved from the €1 billion that was originally planned, with the remaining €500 million now intended to be used to "finance investment in physical and social infrastructure".

The Council welcomes the idea of a Rainy Day Fund, but it has yet to be substantiated in a meaningful way and appears to have relatively limited value in its stated form. There are three main areas to expand on:

First, the countercyclical nature of the fund should be robust. Annual contributions to the fund currently are to be fixed at €500 million each year applying over 2019-2021 according to *SES 2017*. However, for a fund to be truly countercyclical, it would have to – in some meaningful way – respond to changing cyclical conditions. If, for example, cyclical or transient revenues were to accelerate rapidly, there would need to be some mechanism by which the fund would smooth over such unsustainable peaks in revenue.

Second, how the fund is intended to operate in tandem with the fiscal rules should be clarified. As noted in the *Summer Economic Statement 2017*, "allocations to the Rainy Day Fund would have no impact on the general government balance as they are classified as a financial transaction." However, it is unclear how these allocations would impact spending that would be allowed under the rules. For instance, the rules do not recognise funds that are saved in a government fund as discretionary changes in fiscal policy or "spending". Under the rules, such allocations could represent unspent fiscal space. Moreover, there needs to be a clear understanding of how drawdowns from the fund to facilitate additional stimulus would be possible without leading to a breach of the rules and potential sanctions (assuming a policy of minimum compliance).

It is also unclear as to why contributions to the fund are not treated as becoming successively larger each year. The SES shows annual allocations of fiscal space to the proposed Rainy Day Fund as €0.5 billion for each of 2019, 2020, and 2021. On the face of it, annual contributions of €0.5 billion over three years appears to imply a fund totalling €1.5 billion by 2021 (0.8 per cent of 2016 GNI*). However, fiscal space refers to available changes in spending levels. If €0.5 billion of fiscal space is used in 2019, this amount is assumed to be used for all subsequent years also (i.e., an increase in the annual level of spending by €0.5 billion). If another €0.5 billion of fiscal space is used up in year two, then this would mean €1 billion as the level of annual spending in year two. It follows that using €0.5 billion of fiscal space each year for three years would lead to a level of spending totalling €3 billion (€0.5 billion + €1.0 billion + €1.5 billion).

Third, there is a need to clearly define the procedures underpinning the fund. Rules of governance should be outlined, which would include safeguards to ensure appropriate use; criteria for access to the fund's resources; whether amounts to be allocated each year are to be fixed or variable; and whether other structural issues (such as for addressing the accrued liability of public service occupational pensions) will also be addressed by this or other funds.

Recognising these issues and the limited information that is currently available in relation to how the Rainy Day Fund is intended to operate, the Council would urge the Government to publish a document on the Rainy Day Fund.

Public Investment

There are valid concerns that levels of public investment have been relatively low in recent years (Kennedy, 2016). One suggestion has been that this is a result of the fiscal rules inhibiting investment spending. While the rules do impose a requirement for budgetary choices to be made so that the overall thrust of policy should be put on a sustainable path, it is worth exploring the view that the rules restrict investment spending. Several points, in particular, are notable in this respect:

First, most of the flexibilities in the fiscal rules – limited though they are – are designed to help facilitate investment spending by governments. Second, while limits for new budgetary measures (i.e., gross fiscal space) are set by long-term growth rates and the distance from a structural deficit target, scope for additional spending on investment can still be funded by higher taxes or reductions in other spending. Third, there are numerous examples of EU Member States that are meeting the same fiscal rules and where investment levels are comparatively high.

Crucially, under existing plans, investment levels are set to ramp up quite rapidly over the medium term while remaining consistent with future compliance with the fiscal rules. Gross voted Exchequer capital spending is due to rise from an annual outlay of €4.2 billion in 2016 to €7.8 billion in 2021. This would return public investment to levels that are comparatively high in the international context (Figures 9a and 9b). These plans to ramp up investment spending are also consistent with all elements of the fiscal rules being complied with over the later years of the forecast horizon (to 2021).

There is also remaining scope for as yet unallocated, but planned levels of capital spending to be directed to any areas that are deemed as a priority. *Budget 2017* committed €2.2 billion of the €5.14 billion to be allocated under the ongoing review of the Capital Plan to the area of housing. In addition, the Mid-Year Expenditure Report allocated a further €0.5 billion per annum to capital spending over the period 2019-2021.

Public investment levels were cut disproportionately during the period of consolidation since 2008 (following a period of considerable investment spending that addressed previous infrastructural deficits (*June 2017 Fiscal Assessment Report*). While non-investment spending levels (excluding interest) were reduced by 7.6 per cent between 2008 and 2014, the level of annual public investment spending was more than halved (a reduction of 57.1 per cent). Reductions in investment were concentrated in Transport and Housing & Community Amenities, with reductions of €2.2 billion and €1.6 billion respectively.

Figure 9a: Public Investment as a Share of Total Revenue

% total general government revenue

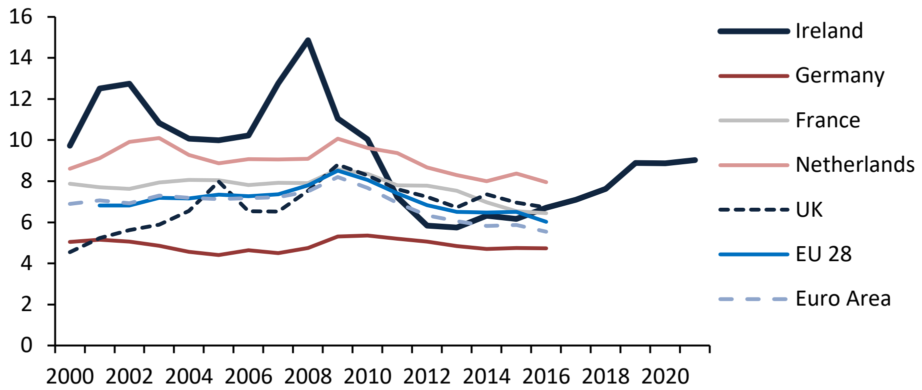
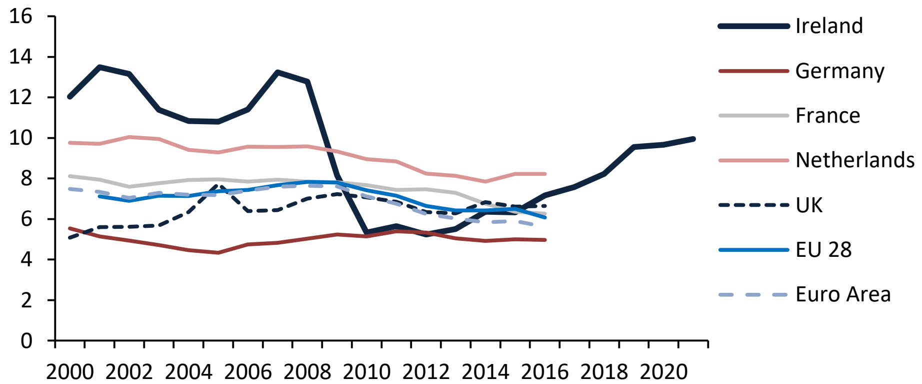


Figure 9b: Public Investment as a Share of Primary Expenditure

% total general government non-interest expenditure



Sources: Department of Finance; Eurostat and internal IFAC calculations.
Note: Gross fixed capital formation as a share of general government primary expenditure and as a share of total general government revenue. Forecast years as per *SES 2017*.

Recent decades have seen a procyclical pattern in the public finances, which has been even more markedly visible in public investment spending. High levels of investment spending pre-crisis gave way to sharp consolidation in the post-crisis period. Notwithstanding the sharp reductions in public investment in recent years, current plans suggest that investment levels will rise to relatively high levels again over the medium-term. Adhering to all elements of the new fiscal framework would mean that government expenditure can expand in line with the economy's sustainable pace of growth. This would help to prevent forced cuts to investment spending in future downturns, and would help to smooth out spending on investment projects over future cycles.

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