Irish Fiscal Advisory Council

Press Release: Fiscal Assessment Report, June 2018

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The Irish Fiscal Advisory Council publishes its 14th Fiscal Assessment Report today (Wednesday 6th June 2018). In the report, the Council assesses the Government's budgetary stance; its forecasts; and its compliance with the fiscal rules. It finds:

> **The Government should at least stick to its plans for 2019 and anything more expansionary is not likely to be appropriate. There is no case for additional fiscal stimulus in 2019 beyond existing plans as set out in *SPU 2018*.** An appropriate policy for next year would be to increase spending in line with the sustainable long-term growth rate of the economy. This would imply an approximate limit for spending increases or tax cuts of up to €3½ billion (i.e., the "gross fiscal space") as the starting point for any budgetary plans for 2019. Unexpected increases in tax revenues or lower interest costs should not be used to fund further budgetary measures. The cost of previously announced measures – including sharp increases in public investment – means that the Government's scope for new initiatives in Budget 2019 will be limited.
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> **Improving the budget balance by more than planned would be desirable.** It would be desirable for the Government to improve the budget balance by more than planned, especially given the risks of overheating and the opportunity provided by favourable times.
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> **The Government needs a credible plan for the medium term.** Focusing on the right budgetary stance and being prepared to be more cautious than the fiscal rules allow is the correct approach for the Government to follow. Yet there is a danger that the current policy framework is insufficiently equipped to prevent a return to procyclical fiscal policy. Sensible tools such as the Rainy

Day Fund and a medium-term debt target need more development if they are to be effective. A working paper accompanying this report shows how a truly countercyclical Rainy Day Fund could work with modest changes to the fiscal rules.

A rapid cyclical recovery has taken place since at least 2014 and this is continuing at a strong pace. Most coherent estimates suggest that the domestic economy has been growing faster than its potential growth rate since 2014. The economy is estimated to be producing close to its medium-term potential in 2018 and will move beyond it next year and after. There are also burgeoning pressures in the housing sector, where persistent undersupply has been evident. Faster-than-assumed growth in housing output – although needed – could prompt overheating pressures unless offsetting measures are taken elsewhere. The Council welcomes the Department's publication of alternative estimates of the cycle to help to provide a sound basis for setting the economy and the public finances on a sustainable path.

It is inevitable that negative shocks will occur in future years. There are clear downside risks over the medium term, mainly those associated with Brexit, US trade policy and the international tax environment. As the IFAC report shows, corporation tax receipts would be particularly vulnerable to an exit of a large, foreign-owned multinational firm, given the high concentration of payments among the top ten contributing firms.

Against this backdrop, Ireland's debt burden is still among the highest in the OECD and improvements on the budgetary front have stalled since 2015. Improvements to the underlying budget balance have stalled despite the strong cyclical recovery – one that is reinforced by a number of favourable tailwinds. The IFAC report highlights that government spending has drifted upwards in recent years when compared to earlier plans. This has happened as the economy and revenues have performed better than expected.