



**Irish Fiscal
Advisory Council**

Pre-Budget 2021 Statement

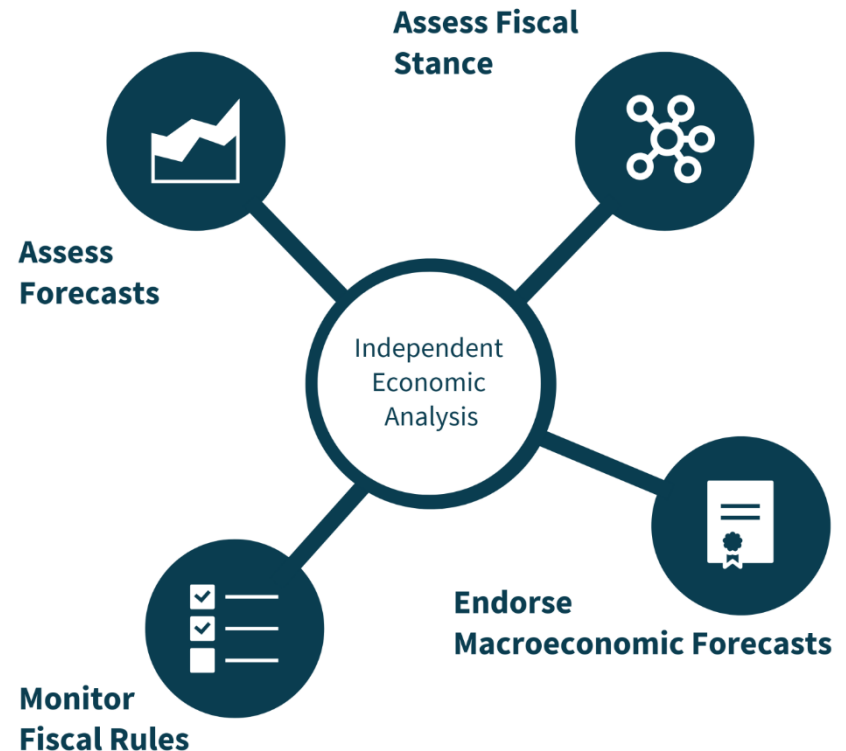
September 2020

Looking ahead to Budget 2021

17 September 2020

Pre-Budget 2021 Statement

- The Fiscal Council is an official independent body with a mandate to assess the public finances
- The *Pre-Budget 2021 Statement* updates the analysis of the May 2020 Fiscal Assessment Report (FAR)
- It looks ahead to Budget 2021
- The next FAR will be published in November



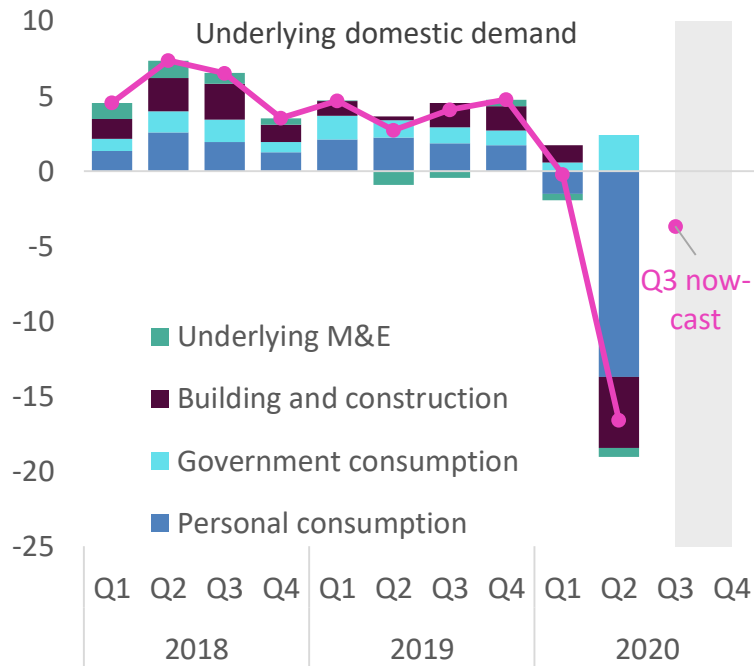
Key messages

- Covid-19 has had a severe impact, but activity is picking up
- Uncertainty is exceptionally high: Covid-19 and Brexit
- Spending has increased sharply and tax receipts are lower
- The debt/GNI* ratio is very high, but low interest rates help
- Support to business and household incomes should continue
- Large-scale multi-year stimulus is needed
- A contingency should be made for Brexit and Covid-19 worsening
- A “roadmap” is needed to set how tax and spending priorities will be balanced over the next 5 years
- Strengthening the fiscal framework would help

Covid-19 has had a very severe impact, but activity is picking up

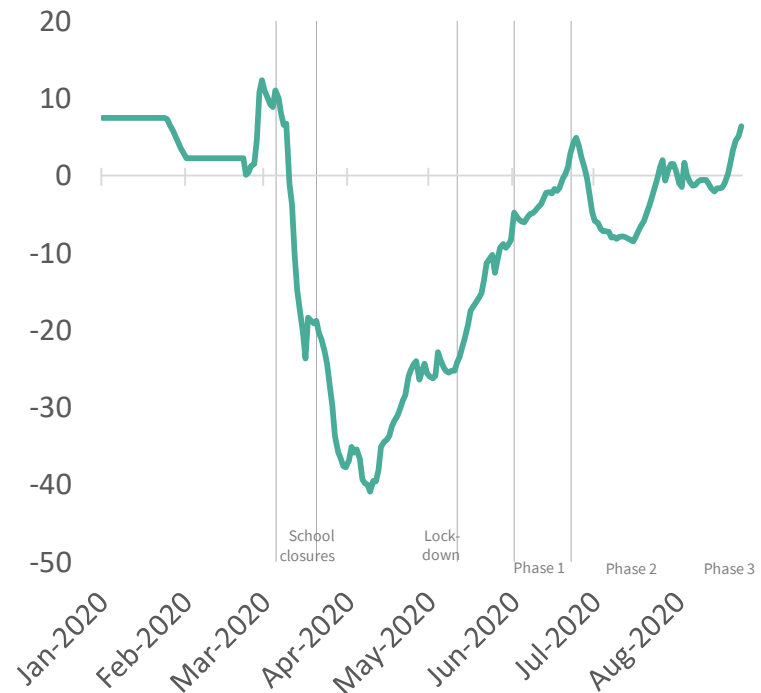
A. A sharp fall in activity took place in Q2

% change year-on-year in volume



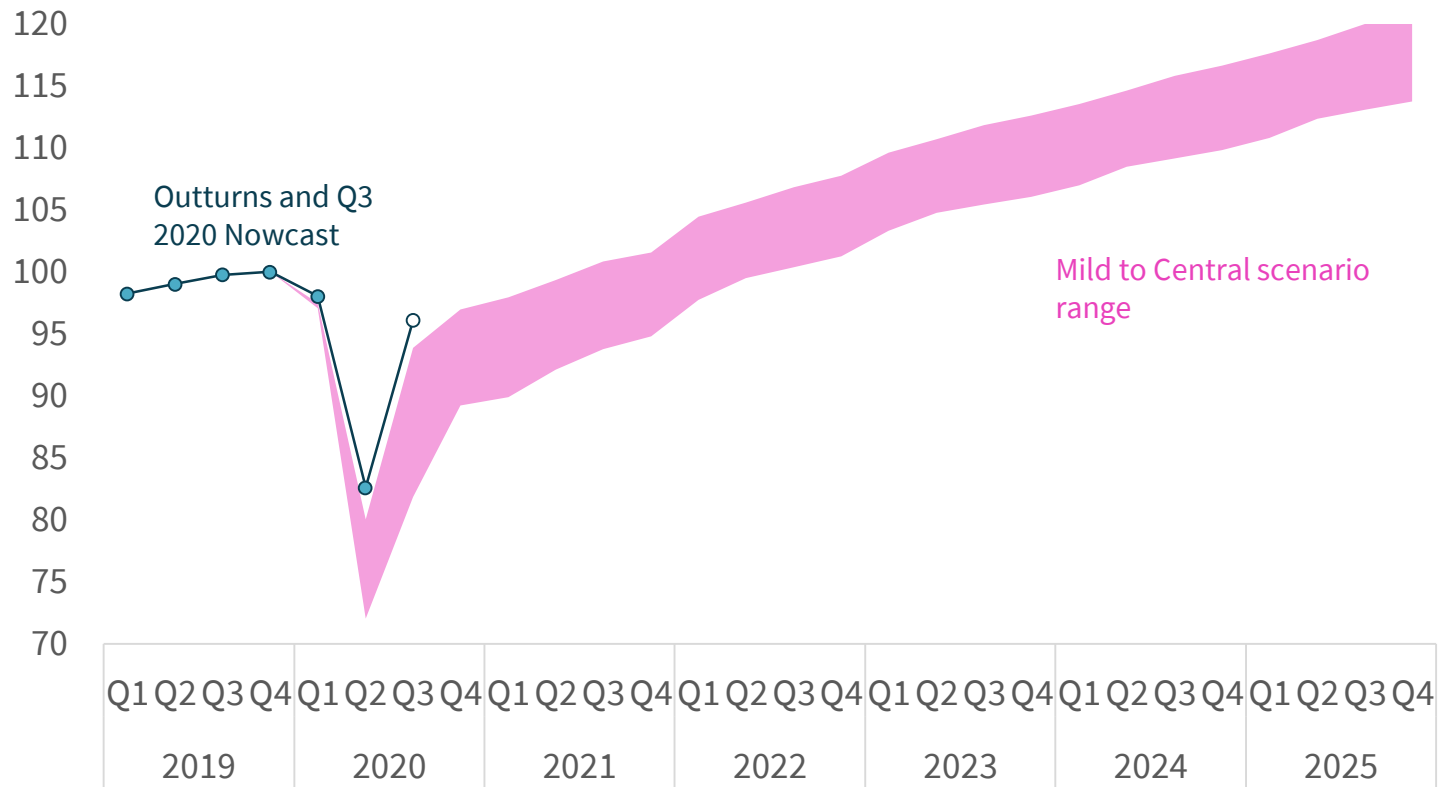
B. Consumer spending has picked up

% change year-on-year, 7-day average



Sources: CSO; Central Bank of Ireland (Card + ATM data); and Fiscal Council workings.

So far, the economy appears close to the Mild/Central range in the May FAR

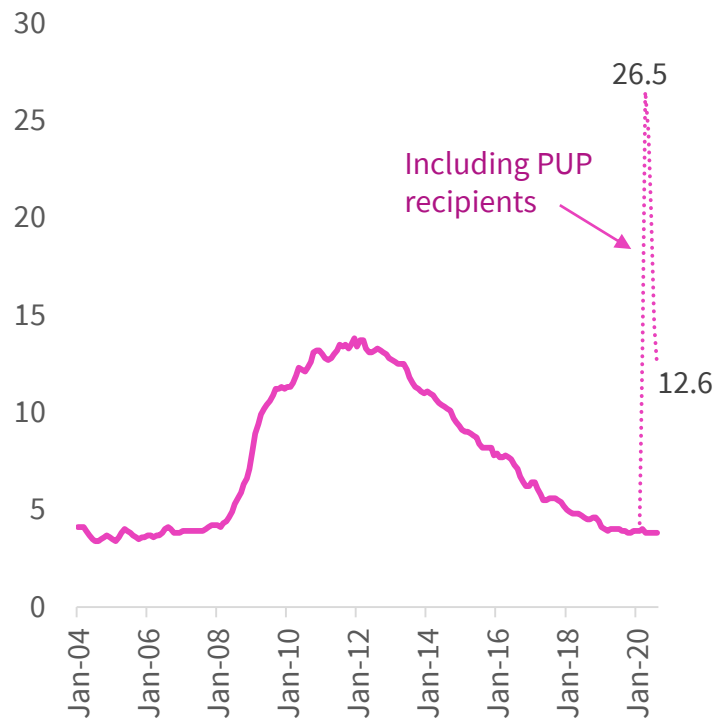


Sources: CSO; and Fiscal Council workings.

But, unemployment remains high and some sectors are still disrupted

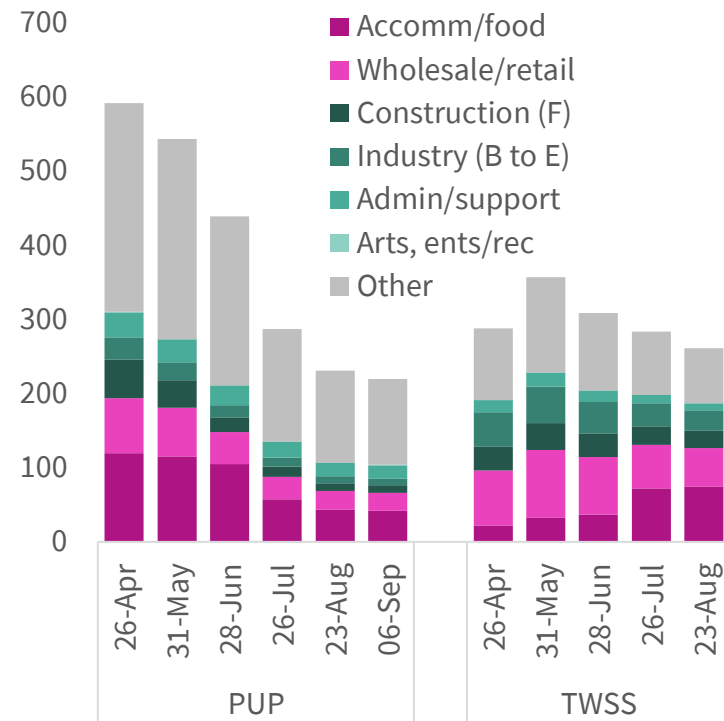
A. Unemployment rates remain high

% labour force (ages 25-74)



B. Some sectors rely heavily on supports

Thousands of people availing of supports



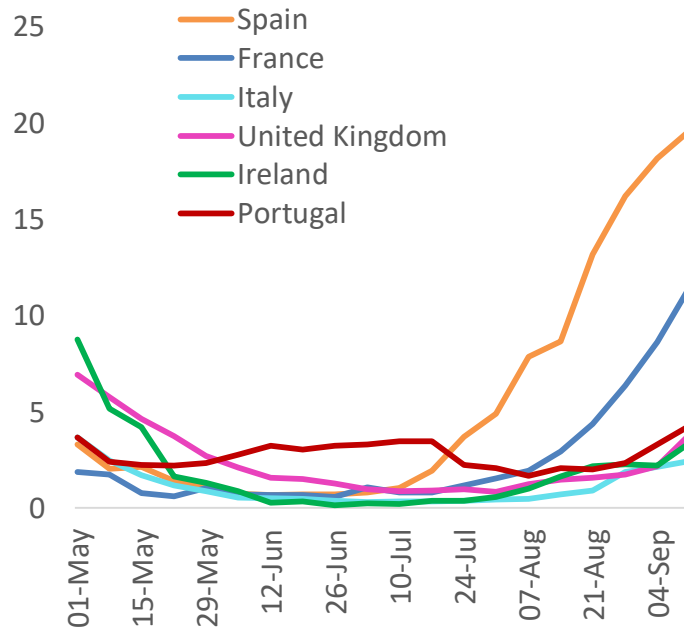
Sources: CSO; Central Bank of Ireland; and Fiscal Council workings.

Note: PUP = Pandemic Unemployment Payment; TWSS = Temporary Wage Subsidy Scheme.

Uncertainty remains high around Covid-19

A. Weekly confirmed cases

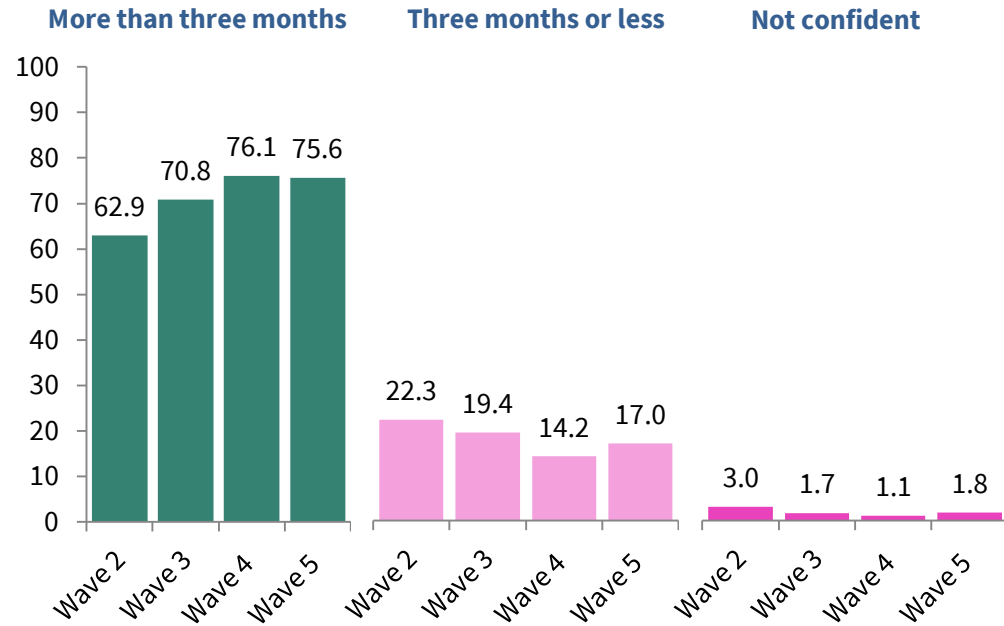
Weekly cases per 100,000 population



Source: CSO; European Centre for Disease Control; and Fiscal Council workings.

B. Businesses slightly more confident of operating through crisis

% enterprises indicating confidence in financial resources to operate throughout Covid-19 crisis



Sources: CSO (Business Impact of Covid-19 Surveys).

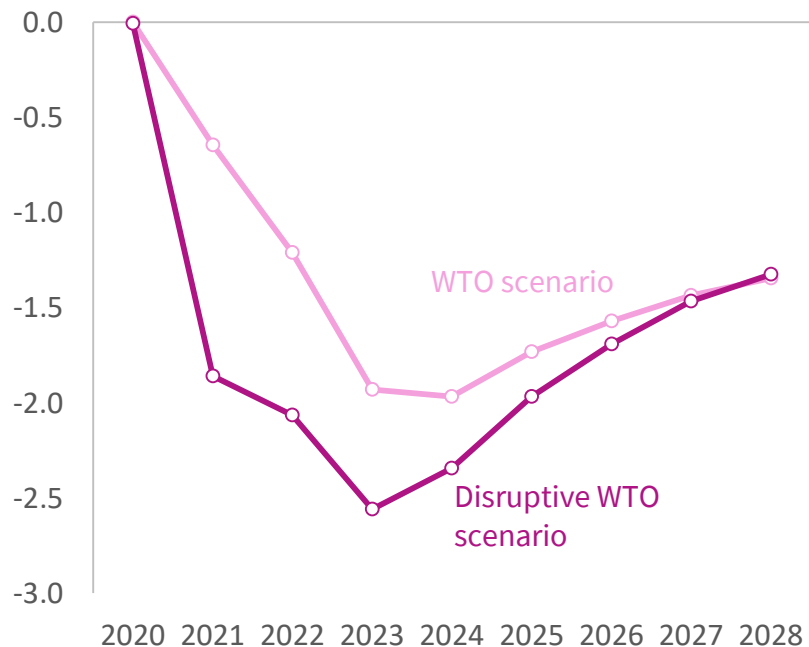
Notes: Different response periods covered by each survey wave:

Wave 2 (20 April - 3 May); Wave 3 (4 May - 31 May); Wave 4 (1 June - 28 June); and Wave 5 (29 June - 26 July).

A no-deal Brexit would harm growth

A: Impact on economic output of a WTO Brexit scenario (relative to FTA)

Percentage point impact on level of output

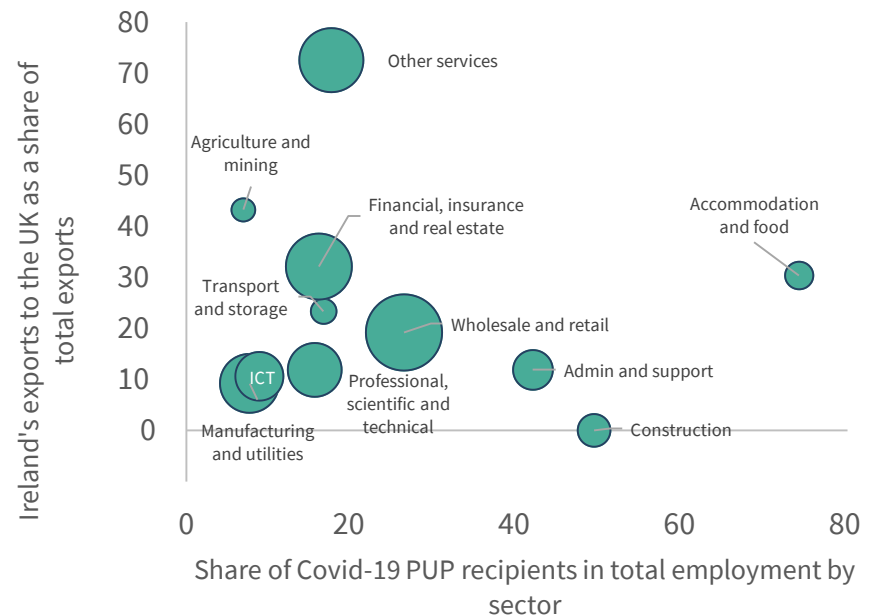


Sources: Central Bank of Ireland (2020); and Fiscal Council workings.

Notes: Impacts shown are calculated as World Trade Agreement (WTO) impacts minus the Free Trade Agreement (FTA) impact, when compared to a no Brexit counterfactual.

B: Exposures for Ireland's exports due to a hard Brexit are not positively correlated with exposures to Ireland's domestic economy due to Covid-19

Measure of exposure to respective shocks (larger numbers indicate more vulnerability)



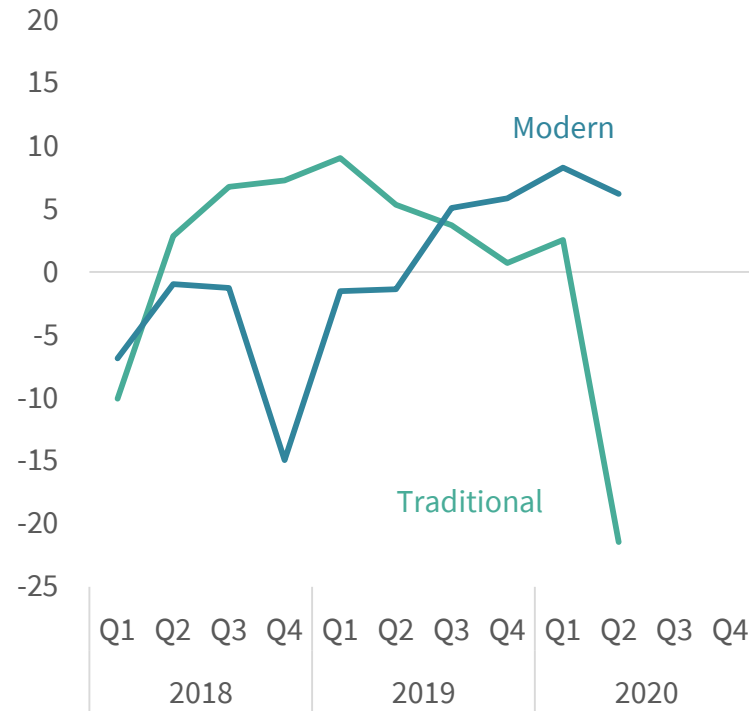
Sources: Department of Employment Affairs and Social Protection; Revenue; and Fiscal Council workings.

Note: Weights shown correspond to the sector's share in taxes (VAT, income tax, corporation tax, and capital gains tax), based on data from the Revenue.

Overreliance on corporation tax remains a medium-term risk

A. Industrial production shows divergences

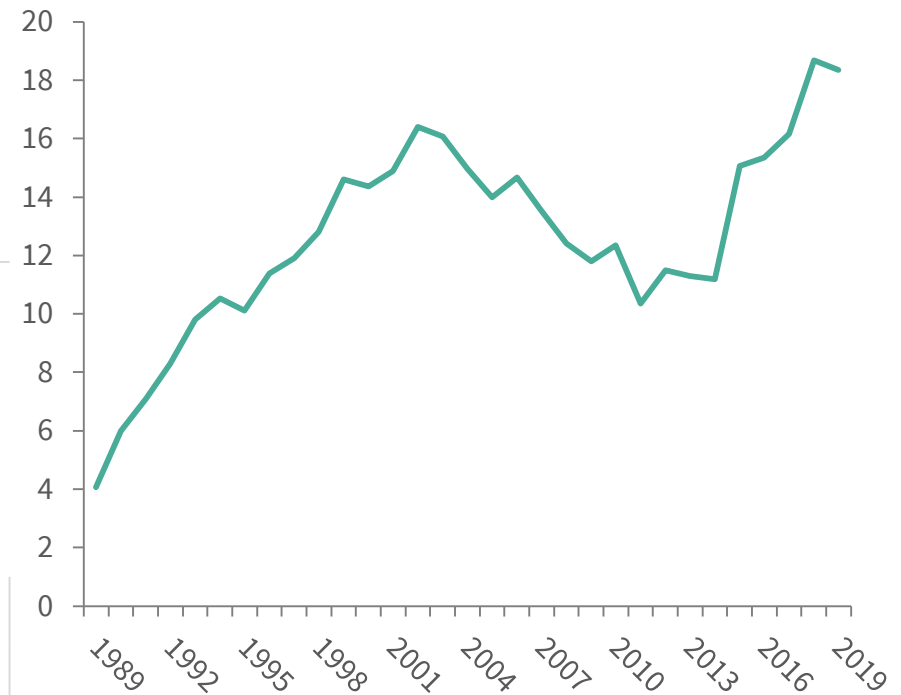
% change year-on-year in volume



Sources: CSO; and Fiscal Council workings.

B. Reliance on Corporation tax has increased

% Exchequer tax revenue

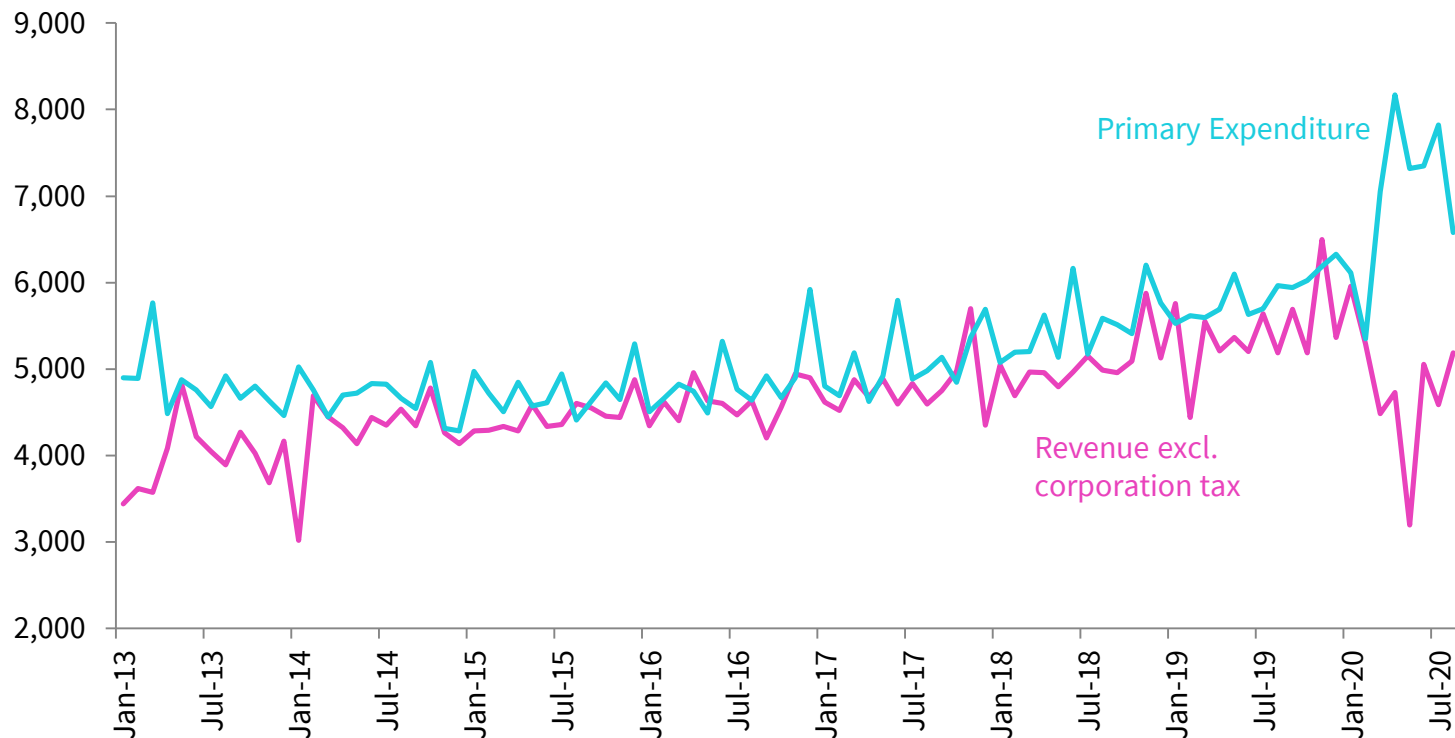


Sources: Department of Finance; and Fiscal Council workings.

Covid-19 has led to a sharp rise in government spending and a falloff in taxes

Central Government Revenue & Primary Expenditure

€ million (seasonally adjusted)



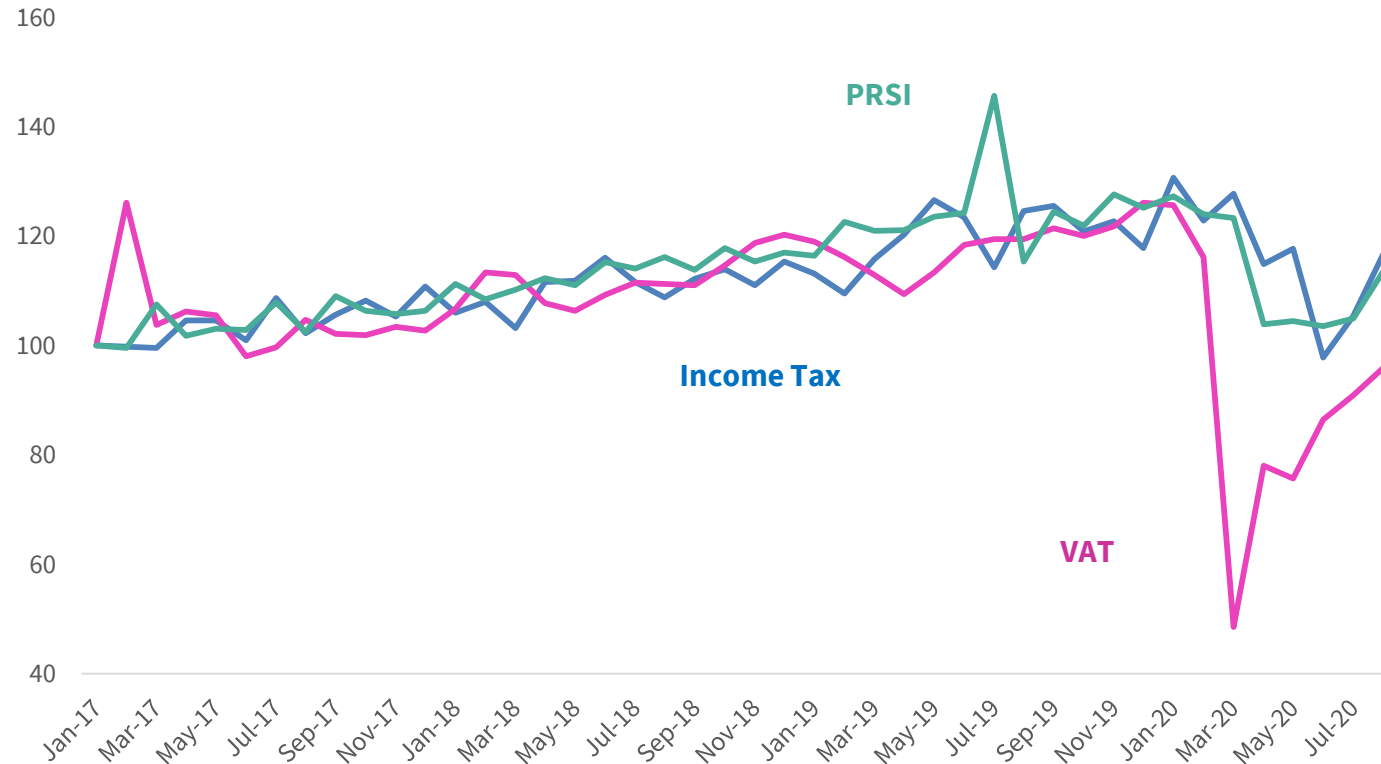
Sources: Department of Finance and Fiscal Council workings.

Note: Transactions without general government impacts are excluded. Total Revenue is Exchequer tax and non-tax revenue plus appropriations in aid and excess capital resources. Primary Expenditure is Gross Exchequer Expenditure minus national debt interest. Data are adjusted using the STL decomposition method over monthly observations for the duration of the sample period 2013-2020.

Key tax heads have fallen, but appear to be stabilising or starting to recover

Seasonally adjusted monthly revenues

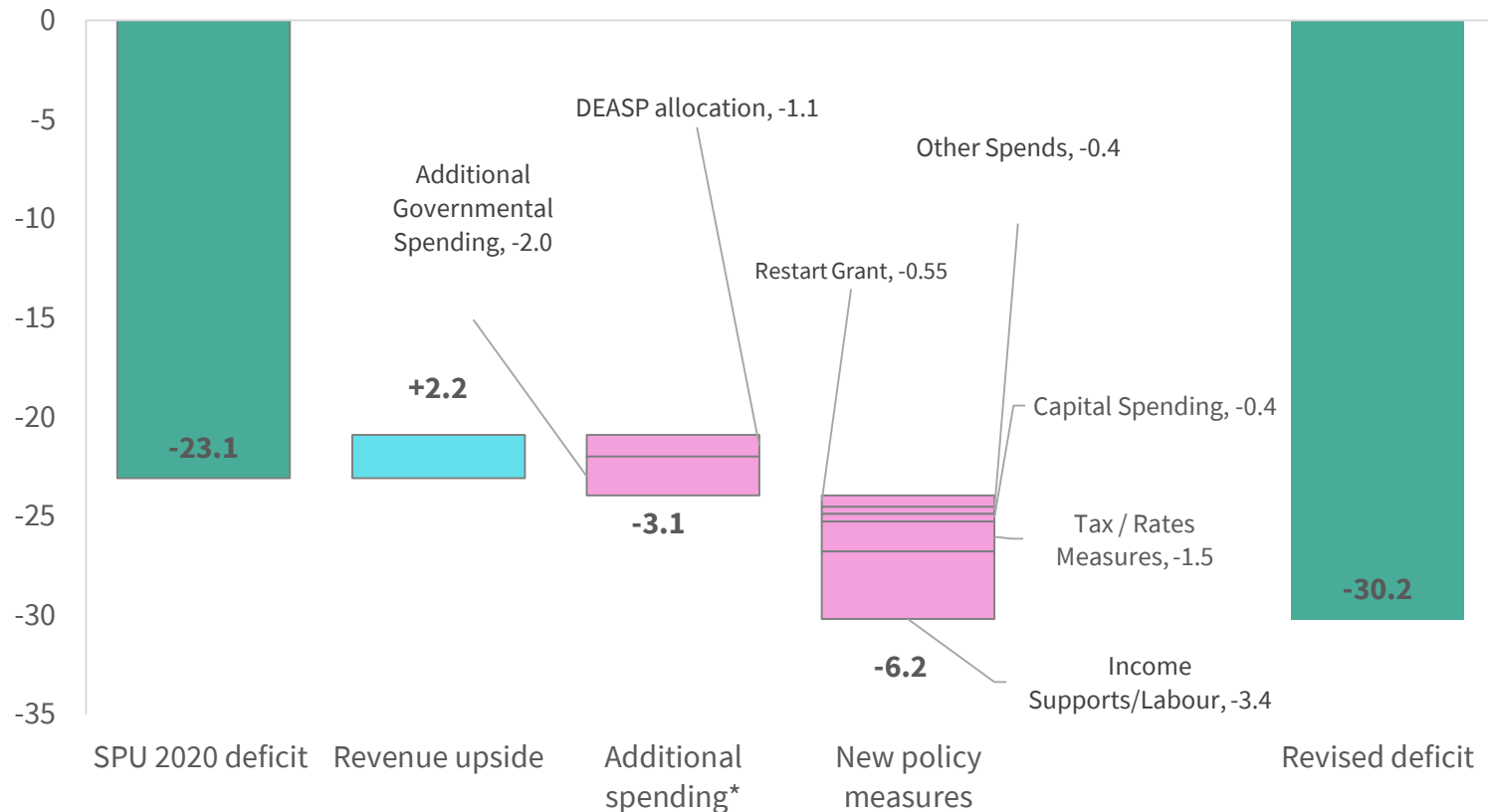
Jan 2017 = 100



Sources: Department of Finance and Fiscal Council Workings

Notes: Data are seasonally adjusted monthly outturns using the Census X-13 method. Panel B uses unadjusted monthly outturns. IT = Income Tax; CT = Corporation Tax; and PRSI = Pay-Related Social Insurance.

New Covid spending measures have increased the deficit for 2020



Sources: Department of Finance.

Notes: Blue bars show items which reduce the projected deficit. Pink bars show items which contribute to a widening of the projected deficit. * Additional spending outside of new policy measures relates to certain general government adjustments. The “DEASP allocation” refers to the budget allocated to the Department of Employment Affairs and Social Protection. See Box B for further details on the full range of supports launched since the onset of the crisis.

The budget deficit for 2020 is now likely to be in the range of €24-30 billion

Updated estimates of the impacts of Covid-19 on the budget balance

% GNI* and € billions, 2020

Scenario	Budget Balance (€ billions)	Budget Balance (% GNI*)
<i>SPU 2019</i> forecasts (April 2019)	1.2	0.6
Mild Scenario	-23.7	-13.0
Central Scenario	-30.1	-17.4
Severe Scenario	-40.2	-23.8

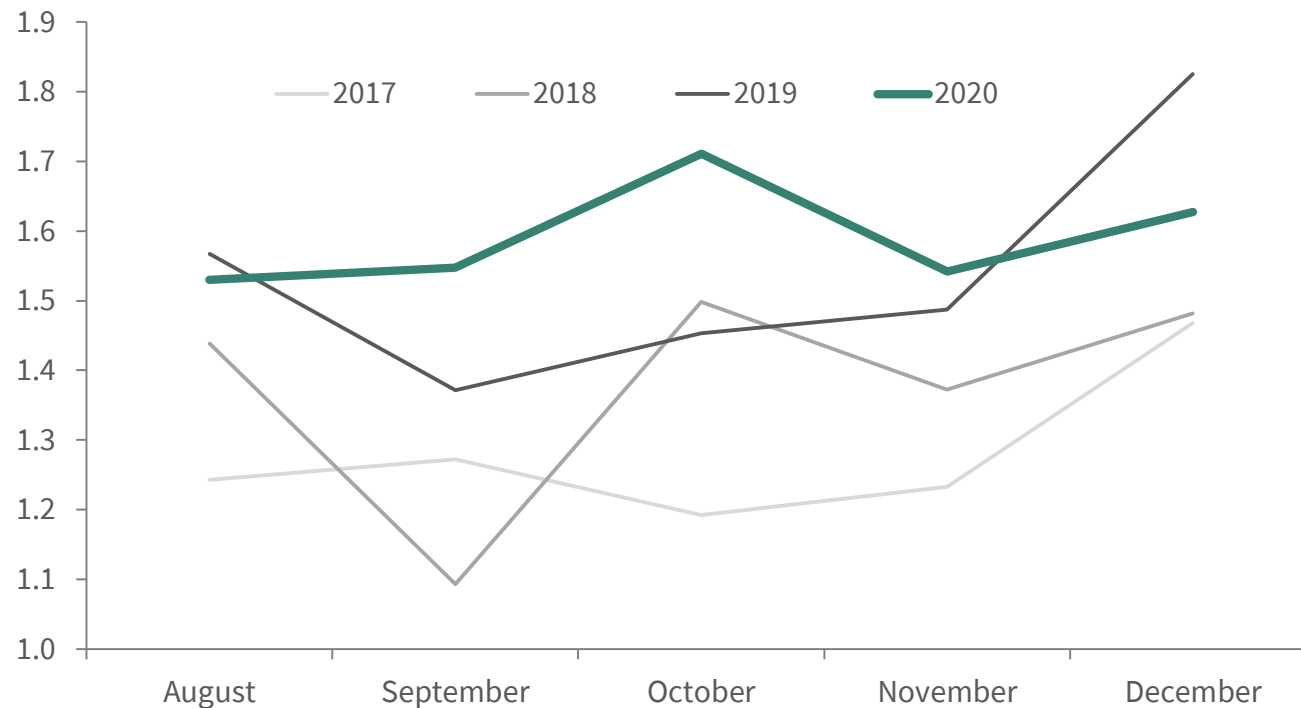
Sources: *SPU 2020*, Department of Finance, and Fiscal Council workings.

Notes: Calculations include the effects of government supports outlined in both May and July. Note that the *SPU 2019* forecasts are used for comparison as, unlike the *Budget 2020* forecasts, these exclude the projected impact of a disorderly Brexit in 2020. The scenarios are based on the Council's *May 2020 Fiscal Assessment Report*.

Health costs remain a risk for 2020

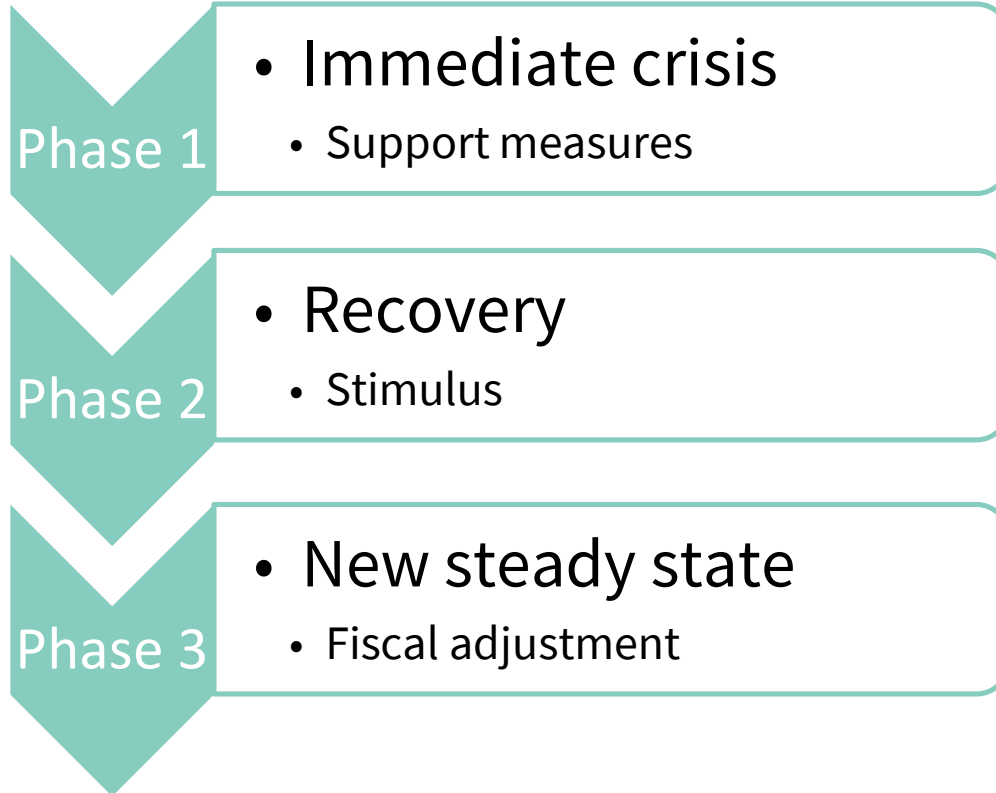
The pre-Covid budget allowed less for spending in late 2020 than previous patterns suggested would be necessary

€ billion, total gross voted health expenditure by month



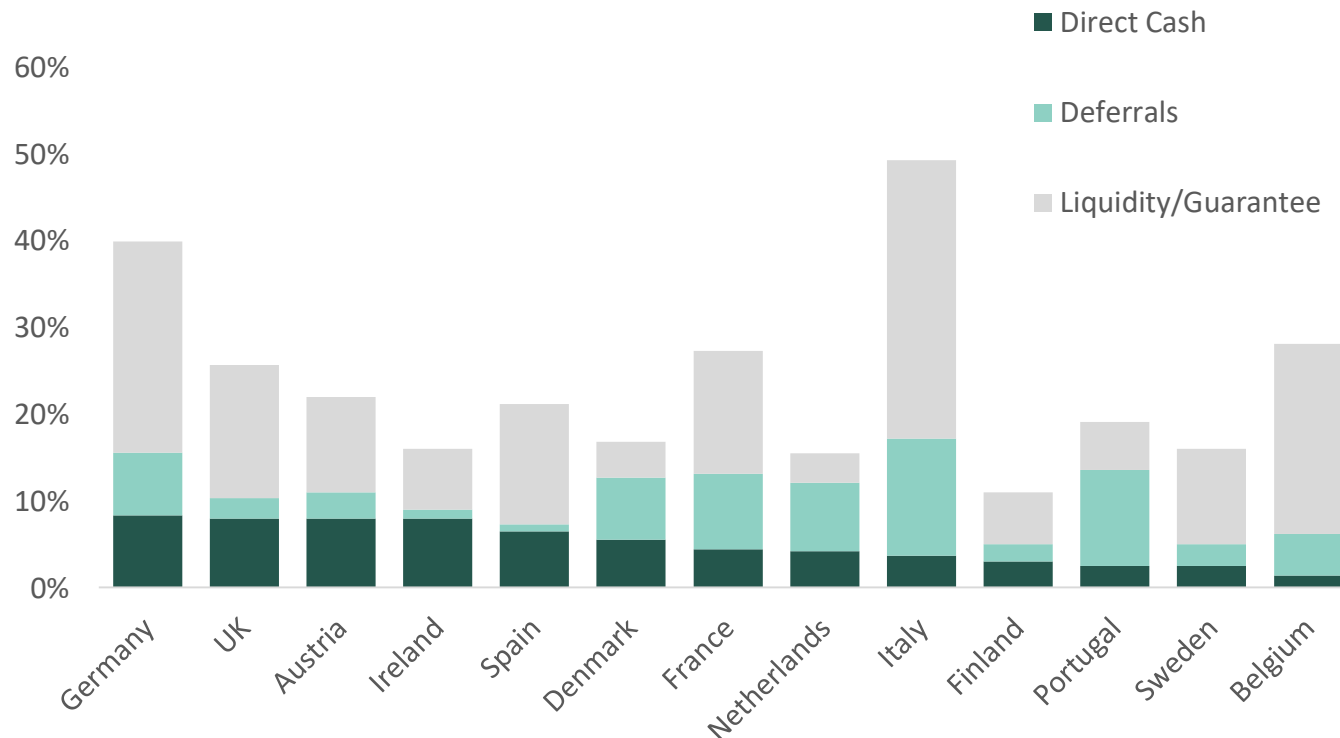
Sources: Department of Finance; and Fiscal Council workings.

Note: 2020 refers to the monthly profile as per the *Budget 2020* forecasts. Figures for earlier years are outturns.



The policy response has been broadly in line with other countries

% GDP (% GNI* for Ireland)



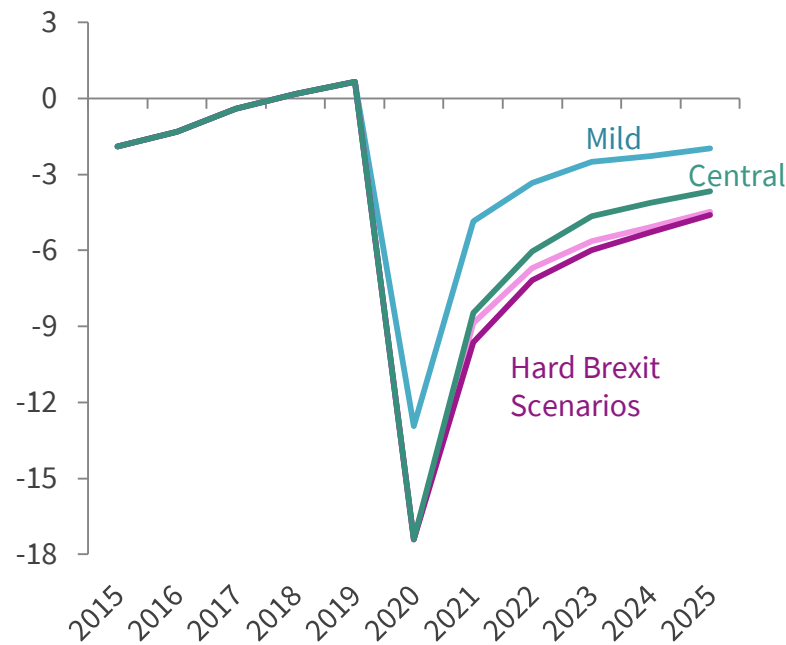
Sources: IMF, OECD, Bruegel, and Fiscal Council Workings.

Notes: Credit guarantees are reported as the estimated coverage of private sector activity as a proportion of GDP, GNI* for Ireland.

The deficit should narrow, but the debt ratio will remain very high

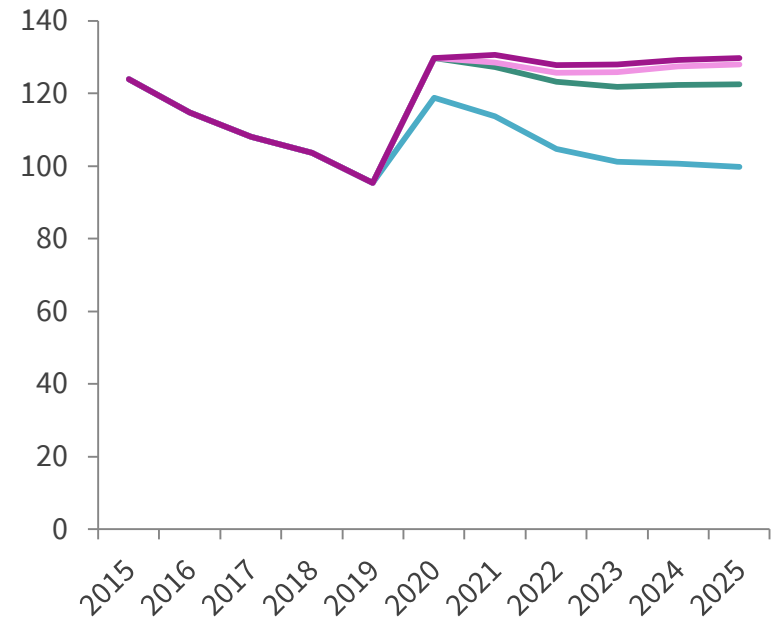
A. Large deficits are likely

% GNI*



B. With debt ratios to climb to high levels

% GNI*

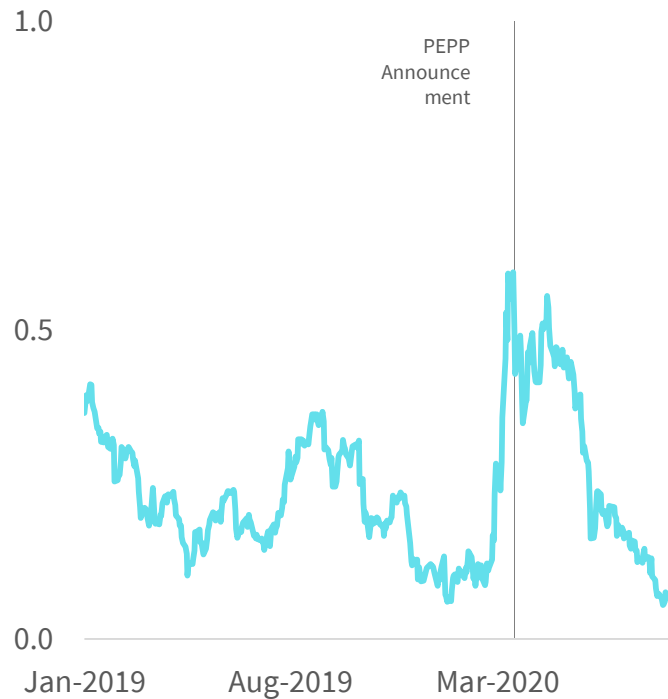


Sources: CSO; Department of Finance; Central Bank of Ireland; Fiscal Assessment Report, May 2020: “The Fiscal Impact of Covid-19”; and updated Fiscal Council workings.

Notes: The “Hard Brexit scenarios” are based on the macroeconomic impacts associated with the WTO and disorderly WTO scenarios in Central Bank (2020), with these impacts applied to the Central scenario.

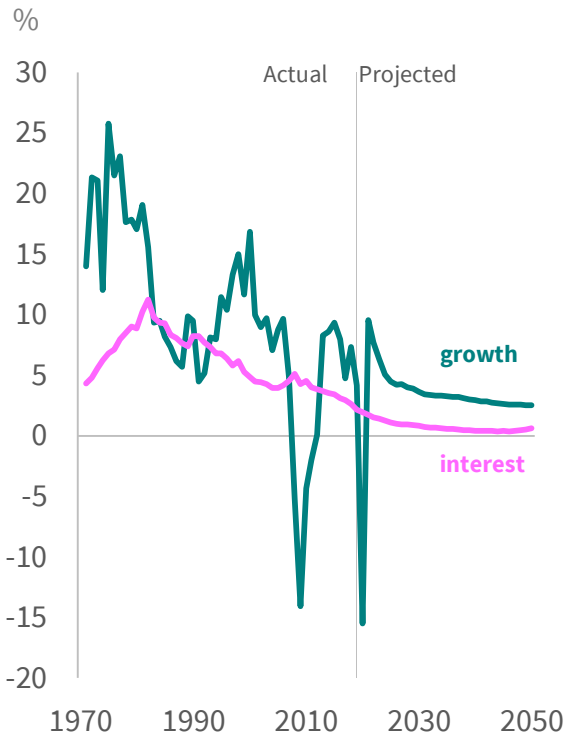
Very low interest rates support debt dynamics, but longer term risks

A: Spreads contained following ECB programme
Spread between Irish and German 10-year yields



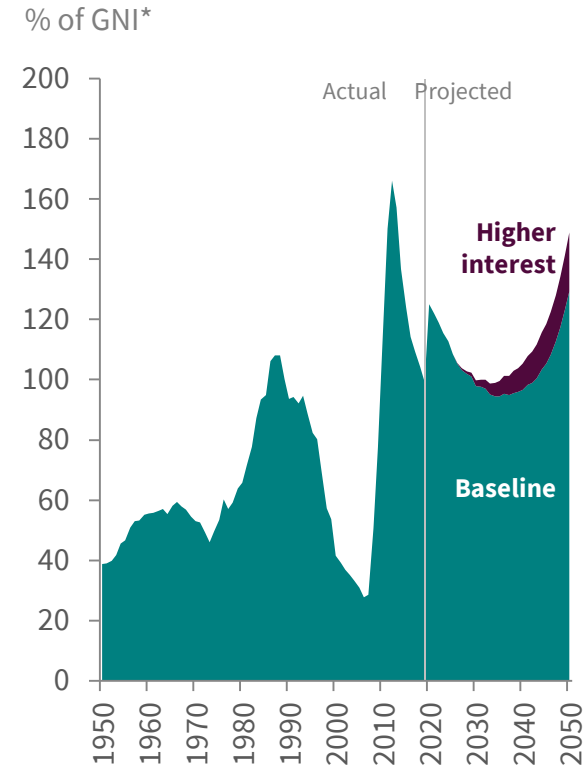
Source: Datastream; and Fiscal Council workings.
Note: Spreads are the difference between Irish and German ten-year yields. “PEPP” is the European Central Bank’s pandemic emergency purchase programme (PEPP) — a non-standard monetary policy measure initiated in March 2020.

B. Growth is projected to exceed interest over the next 30 years



Sources: CSO; and Fiscal Council projections.
Notes: “Growth” refers to annual nominal GNI* growth rates. “Interest” is the average effective interest rate on government debt (calculated as general government interest costs over the previous period’s general government debt). See Fiscal Council’s July 2020 Long-term Sustainability Report.

C. A percentage-point upward shift in the risk-free yield curve



Sources: CSO; and Fiscal Council projections.
Notes: See Fiscal Council’s July 2020 Long-term Sustainability Report.

A sizeable multi-year fiscal stimulus package is required

Supports should continue as needed

Package should be phased over several years

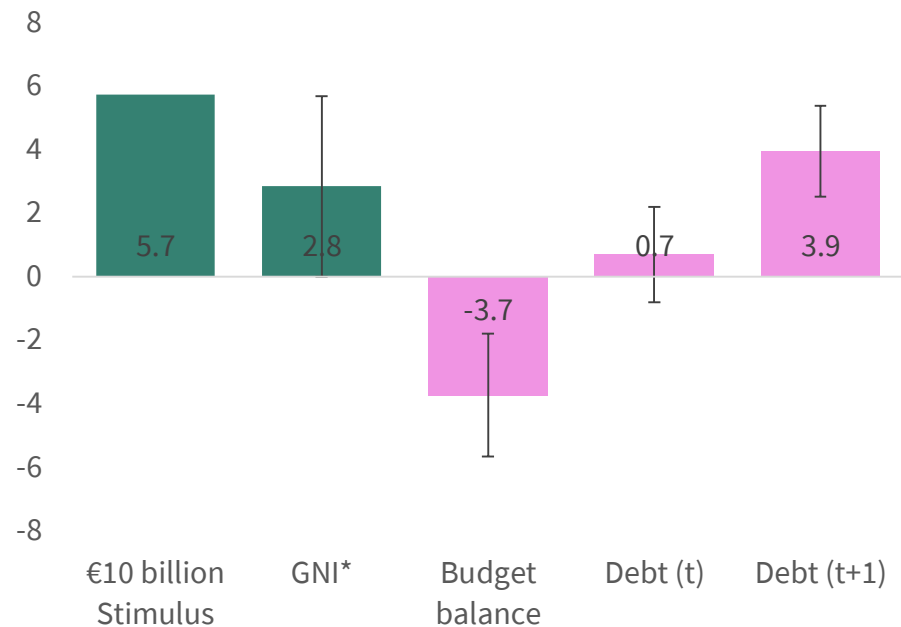
Size of stimulus should be assessed based on updated forecasts

Stronger focus on investment and activation measures would help

Measures should be targeted and temporary

Illustrative Scenario of €10 billion stimulus

% GNI*, 2020 impact



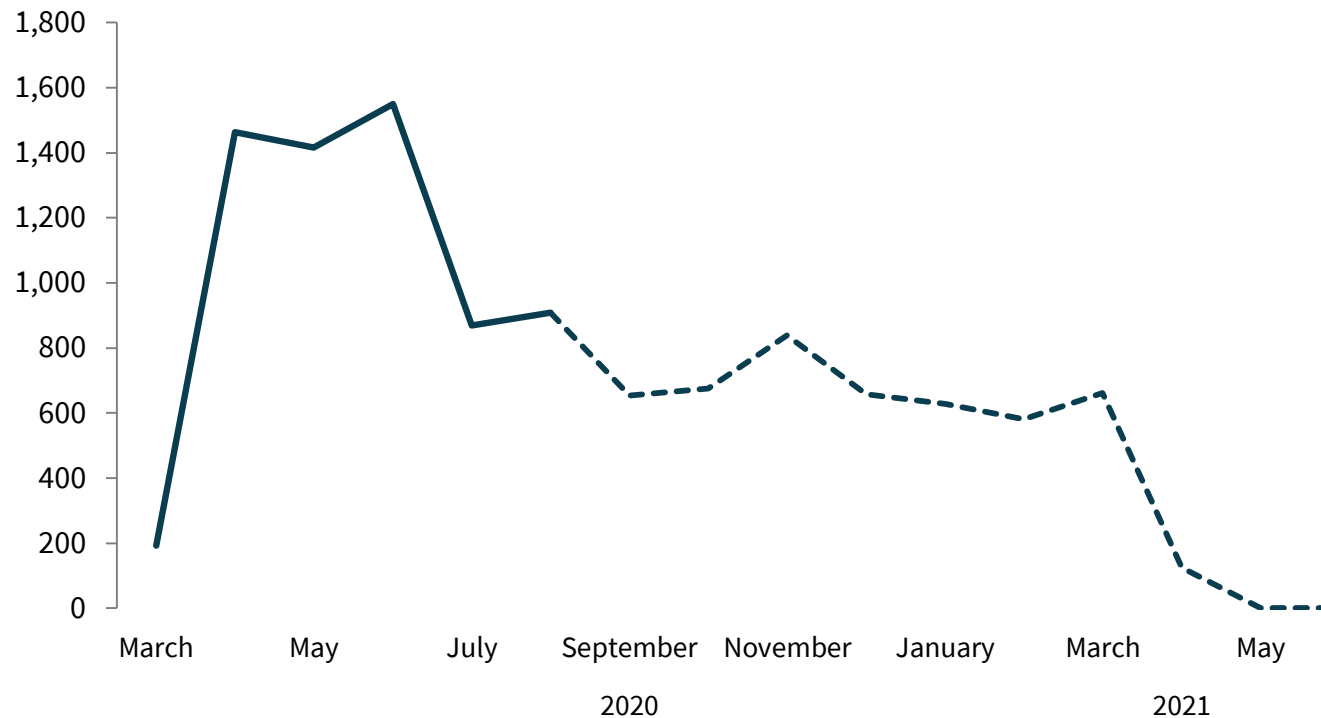
Source: Fiscal Council workings.

Notes: The stimulus of €10 billion is assumed to unwind in one year. The ratios are based on nominal GNI* for 2020. An overall deficit multiplier of 0.5 is the central estimate, while error bars examine multipliers ranging from zero to one.

A contingency for Brexit and for a higher COVID-19 costs would help

Monthly costs of Covid-19 income support schemes

€ million



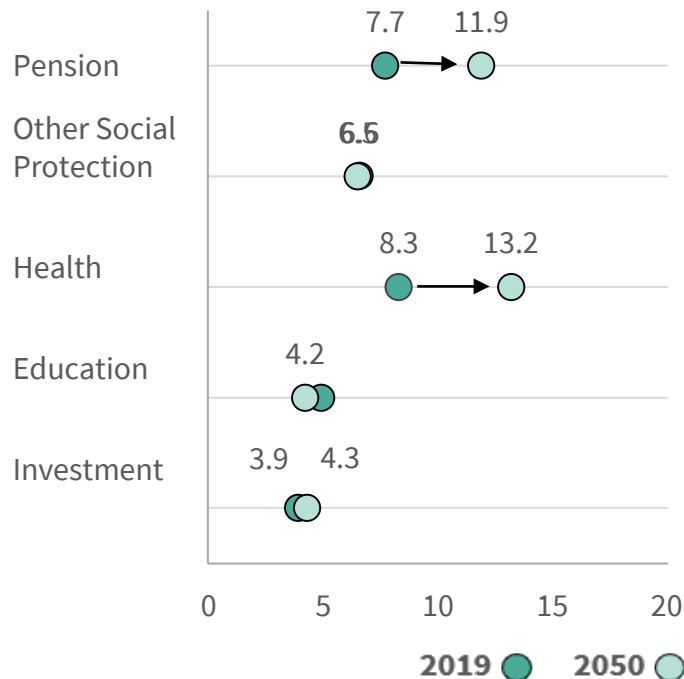
Sources: Government of Ireland, Revenue, and Fiscal Council workings.

Notes: Dashed line indicates a path of future weekly costs for both the PUP and TWSS which would result in an annual costing of €8.9 billion. Some months have 5 payment dates rather than 4 hence may appear more costly than surrounding months (June 2020, August 2020 November 2020 and March 2021).

In the medium term, there are pressures from high debt, ageing and climate change

A. Health and pension spending should rise

% of GNI* (general government basis)

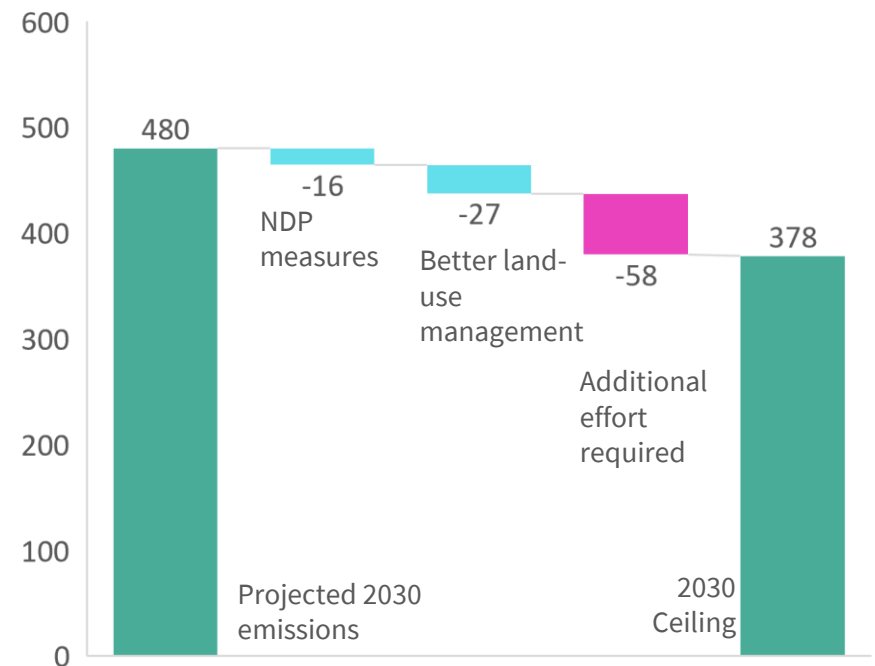


Sources: Eurostat; CSO; Department of Public Expenditure and Reform; Department of Finance; and Fiscal Council projections.

Note: The bars in Panel A are in terms of shares of 5-year age cohorts, except for the 85+ age category. The underlying total population is 4.9 million in 2020 and 6.0 million in 2050. For Panel B, Pension includes public sector pensions; Health includes long-term care.

Additional measures are needed to meet the 2030 ceiling

Levels of greenhouse gas emissions (Mt CO₂eq)



Sources: Source: Climate Action Plan 2019.

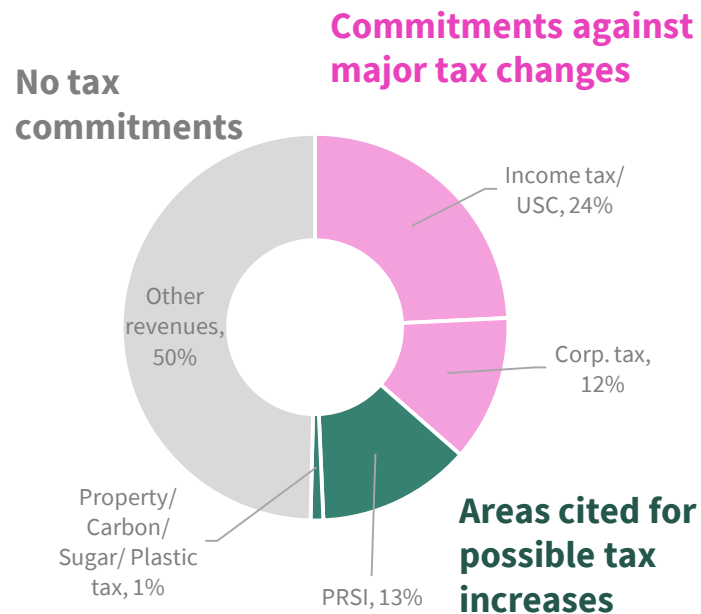
Note: NDP = National Development Plan.

A roadmap is needed for how the Government will balance competing priorities

1/3 of revenue, almost half of spending has been taken off the table

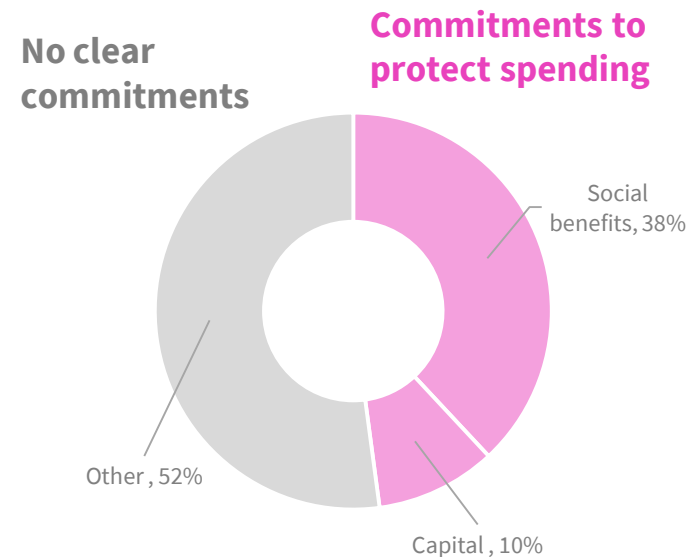
A. Revenue measures

% total general government revenue



B. Health and pension spending should rise

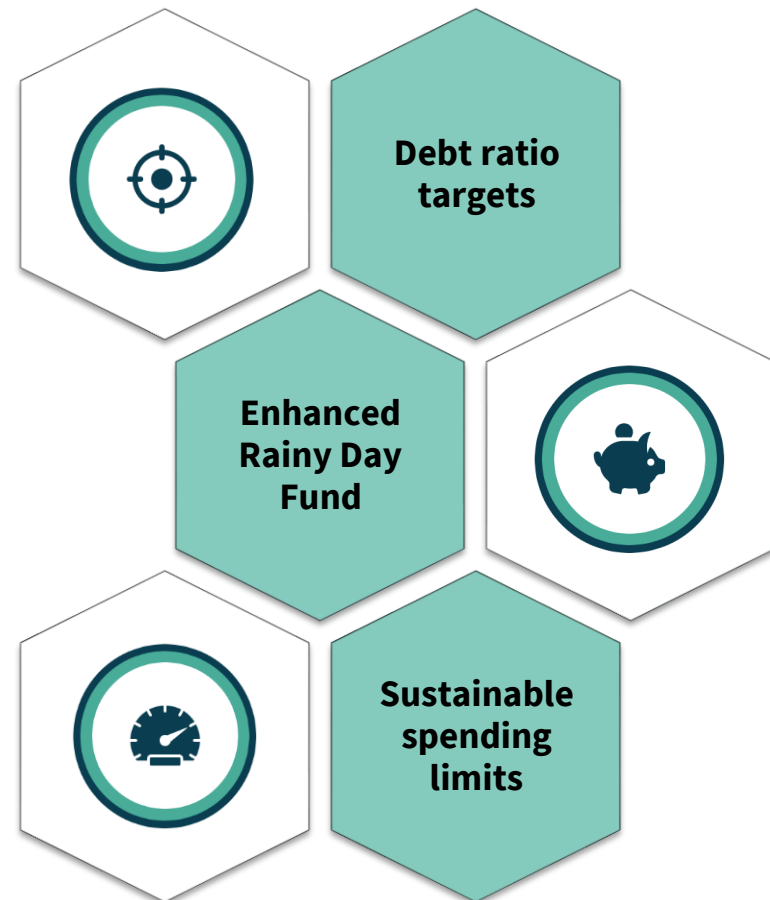
% total general government spending (excl. interest)



Medium-term stability should be supported by the fiscal framework

- Domestic and EU rules allow flexibility for exceptional circumstances in 2020
- This should continue in 2021
- But, Ireland will enter an EU Excessive Deficit Procedure (EDP)

Measures to strengthen the fiscal framework



Key messages

- Covid-19 has had a severe impact, but activity is picking up
- Uncertainty is exceptionally high: Covid-19 and Brexit
- Spending has increased sharply and tax receipts are lower
- The debt/GNI* ratio is very high, but low interest rates help
- Support to business and household incomes should continue
- Large-scale multi-year stimulus is needed
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- A “roadmap” is needed to set how tax and spending priorities will be balanced over the next 5 years
- Strengthening the fiscal framework would help

Supporting slides

Central Government Revenue to end-August 2020

€ million cumulative, unless stated

	2020	2019	Difference	Difference (%)
Exchequer Tax	34,248	35,050	-802	-2.3
Income Tax	13,886	14,080	-194	-1.4
Vat	7,794	9,901	-2,108	-21.3
Corporation Tax	6,478	4,928	1,550	31.4
Excise Duty	3,337	3,916	-579	-14.8
Other Taxes	2,754	2,224	529	23.8
PRSI Receipts	6,773	7,459	-686	-9.2
Other Revenue	3,206	3,251	-45	-1.4
Total	44,227	45,760	-1,533	-3.4

Sources: Department of Finance and Fiscal Council workings.

Note: Note: Other taxes include stamps, capital taxes, motor tax, customs and other unallocated tax receipts. Other revenue includes the National Training Fund, other A-in-As, non-tax revenue, and capital resources. PRSI and National Training Funds include their corresponding excess as indicated in the memo items.

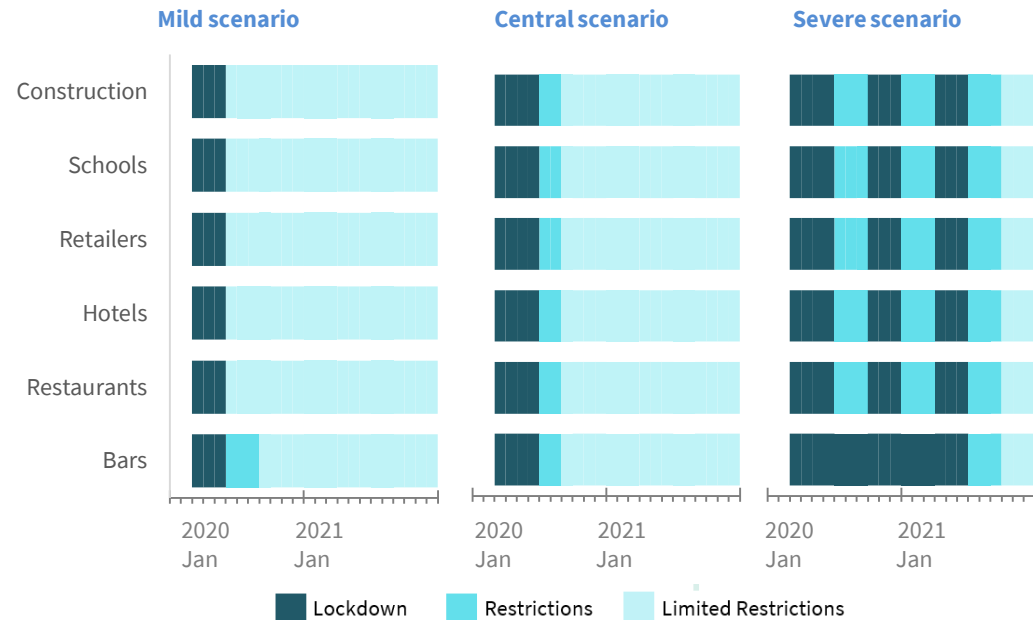
Three scenarios to 2025

Scenario	Description
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Mild Faster recovery. More successful containment measures, economic supports, and progress on treatments.

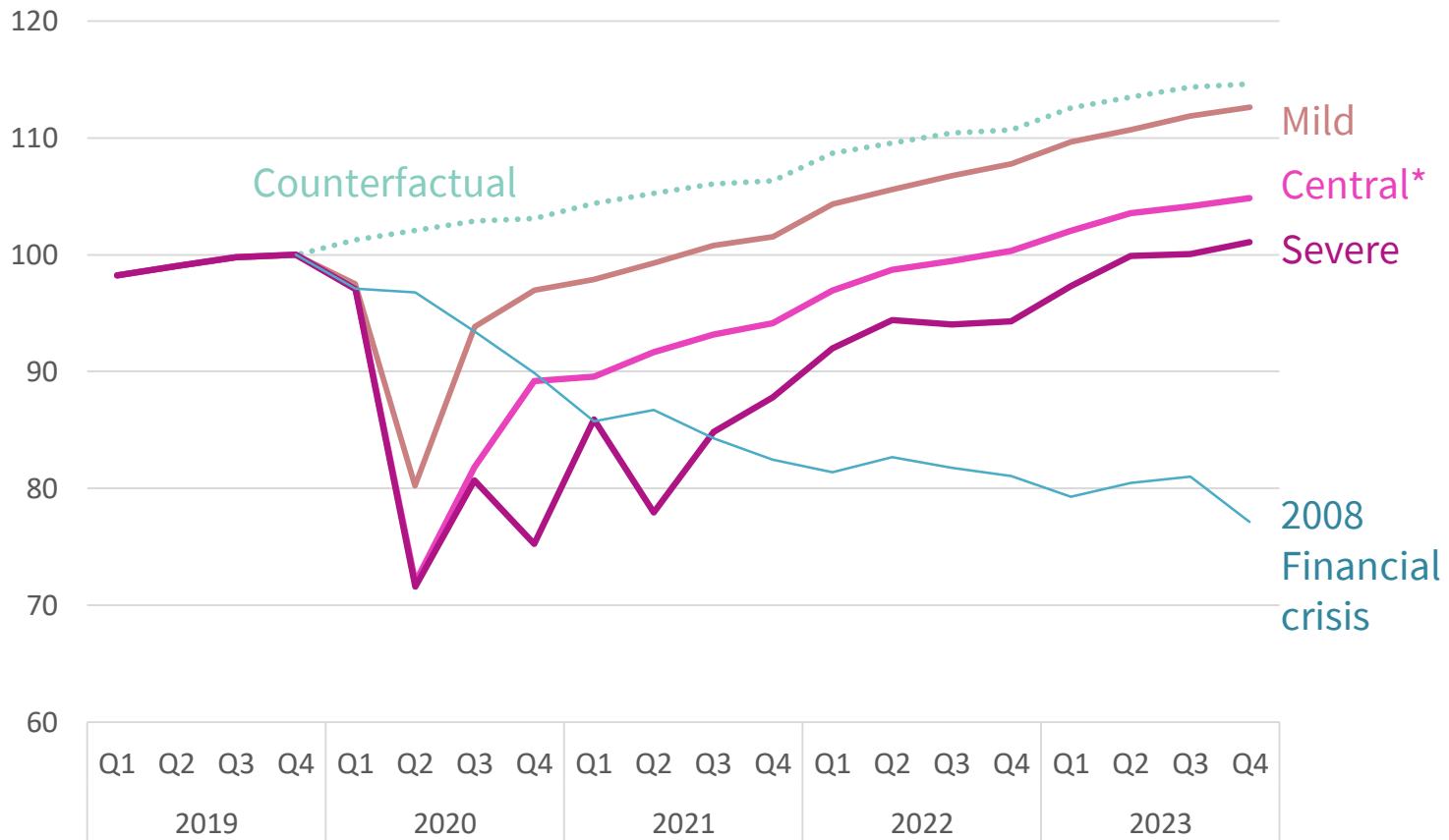
Central Extended *SPU 2020* forecasts. Assume a sharp contraction in Q2 2020, followed by a very protracted recovery.

Severe Protracted recovery marred by repeat lockdowns and wider financial distress.



The range of economic paths to 2025 is very wide

Underlying domestic demand (Index: Q4 2019 = 100)

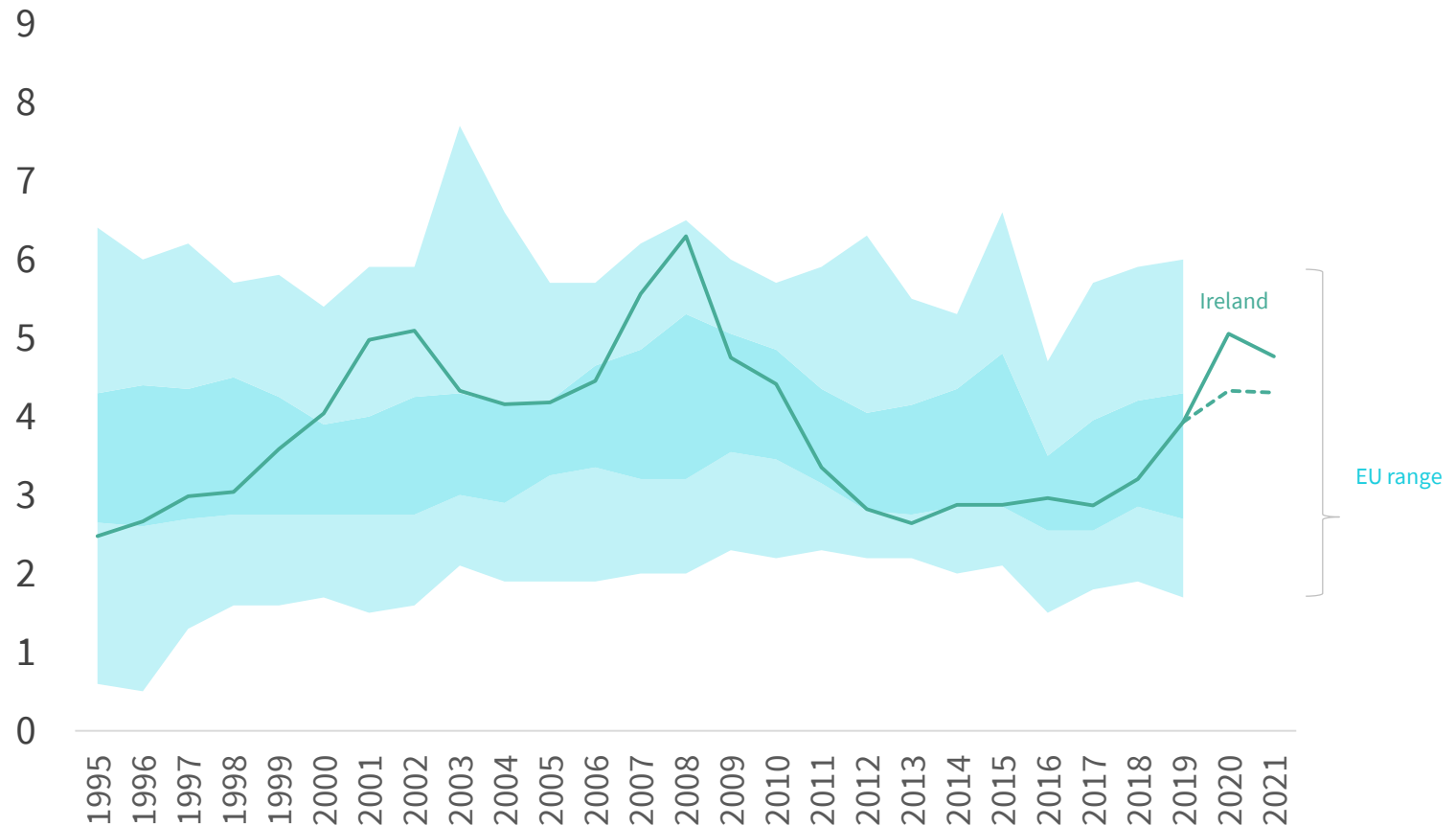


Sources: Department of Finance; and Fiscal Assessment Report, May 2020.

Note: * The Central forecasts are a replica of the official Department of Finance projections published in SPU 2020 (see Box D of the May 2020 FAR).

Public investment can be a key tool in stimulus

% GNI*



Sources: Fiscal Council workings.

Notes: The range is for all EU countries. Inner band is the middle 50 per cent of countries. Outer band is the full (max to min) range. The dashed green line for Ireland represents the ratio of public investment to modified GNI* based on the Budget 2020 forecasts for nominal GNI* (nominal investment amounts are unchanged).