Chapter 3

Assessment of Budgetary Forecasts

3. Assessment of Budgetary Forecasts

Key messages

- *Budget 2021* shows a sharp deterioration in the general government balance in 2020 due to the impact of Covid-19. A deficit of €21.6 billion is forecast (10.7 per cent of GNI*) for 2020. This reflects an increase of €18.6 billion in spending and a €4.9 billion fall in general government revenue.

- The 2020 deficit compares to a surplus of €1.9 billion (0.9 per cent of GNI*) in 2019. The deficit projection for 2020 has been revised down since *SPU 2020* (€23.1 billion). Stronger revenue (mainly corporation tax and income tax) more than offset upward revisions to spending for 2020.

- For 2021, the Government set out a large-scale support and stimulus package. The budget balance is forecast to improve only slightly, with a deficit of €20.5 billion (9.8 per cent of GNI*). This includes contingencies of €2.1 billion for Covid-19-related expenditure and €3.4 billion for unspecified measures to support the economy in response to the pandemic and Brexit.

- There is a very high level of uncertainty surrounding economic and fiscal forecasts in *Budget 2021*. The fiscal outlook will largely be determined by how quickly or slowly the economy bounces back. If restrictions on economic activity are tighter and/or last longer than assumed, then the deficit may be larger than forecast. In addition, new policy measures or extension of current schemes would contribute to a larger deficit in 2021.

- A significant amount (over €5.4 billion) of spending increases in 2021 is permanent in nature. As a result, significant deficits may be expected beyond 2021.

- The *Budget 2021* and accompanying documentation lacks clarity, making spending plans difficult to assess. Information on the costing of Covid-19 supports is limited. As the forecast horizon only extends to 2021, it is hard to assess how much of the spending increases in 2020 and 2021 are likely to persist beyond this horizon.

- With no projections beyond 2021 in *Budget 2021*, three scenarios are presented for paths for the public finances to 2025. Assuming no policy changes and taking into account demographic and price pressures, the general government balance is projected to improve. By 2025 the balance ranges from a small surplus to a deficit of over 6 per cent of GNI*.

- General government debt will rise significantly. Debt as a share of GNI* is projected to peak in 2021 (114.7 per cent of GNI*) and fall gradually without policy action from 2022. However, debt would remain above 100 per cent of GNI* out to 2025. There are risks around this forecast. In a milder scenario, the debt ratio could fall more quickly. However, a scenario in which there are repeated waves of economic restrictions throughout 2021 and 2022 would leave debt levels elevated and stagnant at around 135 per cent of GNI*.

3.1 Introduction

The fiscal forecasts for *Budget 2021* were made amidst the extreme shock due to Covid-19. Along with the economic outlook, the fiscal outlook is exceptionally uncertain. The economic downturn, combined with new policy measures such as income supports, means that *Budget 2021* projects a substantial deficit for this year and next. In line with the macroeconomic forecasts, *Budget 2021* only forecasts fiscal variables for 2020 and 2021.

This chapter assesses a wide range of recent data and focusses on official fiscal outturns from the Central Statistics Office (CSO), Department of Finance and the Revenue Commissioner, along with official Government forecasts consistent with *Budget 2021,* and other materials.

In 2019, the general government balance (excluding one-off items) reached a surplus of €1.9 billion, an improvement of €1.6 billion relative to 2018 (Table 3.1). For 2020, a large deficit has emerged due to the impact of Covid-19 and policy response.

Economic conditions are forecast to improve in 2021 supporting higher revenues. However, new/extended policy measures are deficit-increasing and hence the budget balance is forecast to only marginally improve in 2021. If heavier-than-assumed restrictions on economic activity were to be in place for 2021, that would lead to a larger deficit.

The large increase in spending in 2020 is mostly temporary and related to Covid-19. For 2021, it appears that temporary spending related to Covid-19 will be lower. Despite this, general government spending is increasing. This reflects an increase in general government spending of up to €8.4 billion in 2021 not related to Covid-19 or Brexit, of which €5.4 billion is a large permanent increase in Exchequer spending not matched by an increase in sustainable funding.

There is exceptional uncertainty surrounding the current macroeconomic and fiscal projections. Given the uncertainty, three scenarios for the public finances out to 2025 are presented (Box D and Box G).

Table 3.1: Summary of fiscal outturns (2019) and *Budget 2021* forecasts (2020–2021)
€ billion

	2019	2020	2021
General government balance	1.9	-21.6	-20.5
Total revenue	89.1	84.2	88.7
… % change	5.9	-5.5	5.3
Total expenditure	87.3	105.9	109.2
… % change	4.2	21.3	3.1
Interest expenditure	4.5	3.9	3.6
Primary expenditure	82.8	102.0	105.6
… % change	5.6	23.2	3.5
Primary balance	6.3	-17.8	-16.9
Nominal GNI* growth (% change)	7.6	-5.1	2.7

Sources: CSO; Department of Finance, and Fiscal Council workings.
Note: Rounding can affect totals.

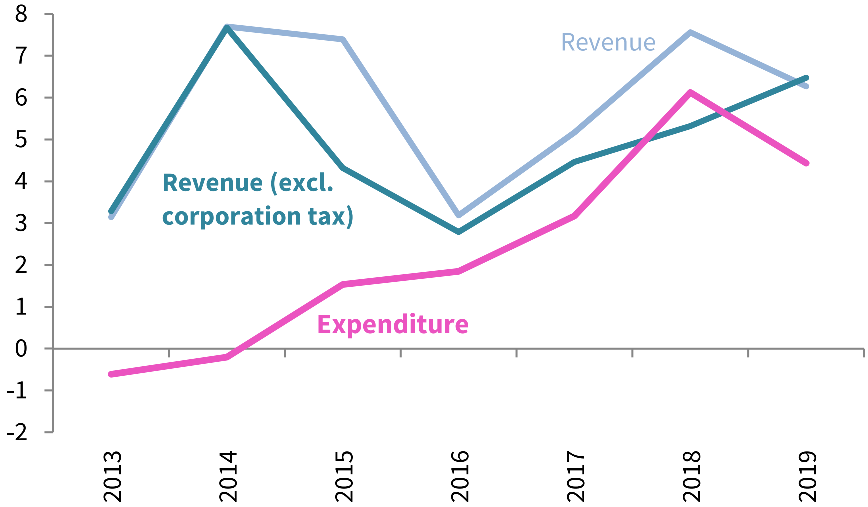
3.2 Assessment of 2019 Outturns

Balance, 2019

The **general government surplus** for 2019 was €1.9 billion, an improvement on 2018 (when a surplus of €0.4 billion was recorded). This improvement was aided by strong cyclical revenue growth, declining unemployment and falling interest payments (€0.9 billion lower than in 2018). Figure 3.1 shows underlying revenue and expenditure trends. General government expenditure growth accelerated over the past five years, with growth above 4 per cent in both 2018 and 2019. Despite this accelerating trend, spending growth has been generally surpassed by revenue growth, although by a smaller margin if corporation tax revenue is excluded.

Figure 3.1: Expenditure growth has accelerated since 2013

% growth, year on year



Sources: CSO; Department of Finance, and Fiscal Council workings. Get the data.
Note: Revenue and expenditure are in general government terms. They exclude one-offs as assessed by the Council, as per Table 1.1, Chapter 1.

The **primary surplus** (excluding one-off items) was €6.3 billion in 2019, €0.7 billion higher than 2018.[28] Given that interest payment fell, non-interest spending grew by more than 5.5 per cent in 2019 (excluding one-off items), slightly slower than revenue.

Expenditure, 2019

General government **primary expenditure** (excluding one-off items) grew by €4.6 billion in 2019. The largest increases for the year came from gross fixed capital formation (GFCF, €1.7 billion), intermediate consumption (€1.2 billion) and compensation of employees (€1.1 billion).[29] Spending in the Department of Health was €0.4 billion higher than planned. This is consistent with outturns in recent years, with the average annual overrun since 2015 being €0.5 billion.

Revenue, 2019

The outturn for **general government revenue** in 2019 was €89.1 billion, €2.8 billion higher than anticipated in *Budget 2020*. This overperformance relative to *Budget 2020* forecasts was mostly driven by corporation tax, PRSI and non-Exchequer

[28] One-offs are as assessed by the Council, given in Table 1.1, Chapter 1.
[29] Much of the increase in compensation of employees and intermediate consumption is related to increased health expenditure.

revenue (this includes revenue collected by non-market public corporations, the HSE and institutes of technology).

3.3 Forecasts for 2020 and 2021 in *Budget 2021*

Budget 2021 shows large deficits for both 2020 and 2021. This is due to the Covid-19 crisis, the impact of temporary policy measures introduced to mitigate the economic downturn, the large fall in tax revenues, and discretionary permanent increases in health, education and other spending. Exceptionally high uncertainty surrounds economic and fiscal forecasts at present.

Medium-term economic and fiscal projections should have been published in *Budget 2021*. In line with the macroeconomic forecasts, fiscal projections in *Budget 2021* were published for this year and next year, rather than the usual five-year horizon. While the heightened uncertainty makes producing medium-term projections difficult, such projections would help support a medium-term orientation for fiscal policy and enable monitoring of potential economic imbalances. It is essential that the Stability Programme in April 2021 presents a five-year forecast horizon.

More generally, the documentation accompanying *Budget 2021* lacks clarity, particularly on the expenditure forecasts. The main detail on expenditure is contained in the Expenditure report. While this report is detailed, it only covers voted Exchequer spending. As a result, there is limited publicly available information on non-voted expenditure or non-Exchequer general government expenditure. These two items combined account for a fifth of spending. This lack of clarity, combined with the short forecast horizon, makes it difficult to assess how much of the spending increases in 2020 and 2021 would be expected to be maintained into 2022 and how much is temporary.

Both macroeconomic and fiscal projections are largely dependent on the progression of Covid-19, both in Ireland and abroad. *Budget 2021* forecasts are formed on the assumption that there is no widely distributed vaccine in 2021. Since the publication of *Budget 2021*, a six-week period of nationwide Level 5 restrictions was announced.

Expenditure

For 2020, the *Budget 2021* anticipates an increase in general government expenditure of €18.6 billion (21.3 per cent). With interest costs set to fall by €0.6 billion, general government primary spending is projected to have increased by

€19.2 billion in 2020 (23.2 per cent). Approximately €16.7 billion of this has come from Covid-19 measures, with the remaining general government spending increases (€2.5 billion) likely to be permanent (Table 3.2).

Table 3.2: General government expenditure

€ million

	2019	2020	2021
Primary general government spending	82,828	102,015	105,625
Change in primary general government spending		19,187	3,610
Temporary spending		16,699	11,887
Permanent primary general government spending	82,828	85,316	93,738
Change in permanent primary general government spending		2,488	8,422

Sources: *Budget 2021*. Get the data.

Note: For 2020, temporary spending is made up of Covid-19 spending. For 2021, temporary spending incorporates Covid-19 spending, the Covid-19 Contingency Reserve and the Recovery Fund. Funding for preparing for Brexit and the Shared Island Fund are considered permanent. See Table 3.3 for a breakdown of amounts.

The *Budget 2021* projections imply that around 55 per cent of Covid-19 spending in 2020 will have been on income and wage subsidies. Both the Temporary Wage Subsidy Scheme (TWSS) and Pandemic Unemployment Payment (PUP) schemes having already been extended twice to officially run until 31st March 2021, with the TWSS now replaced with the Employment Wage Subsidy Scheme (EWSS). The remaining amount is split between a combination of measures. Increased health capacity was budgeted as costing over €2 billion, with other departments receiving additional funding of €4.7 billion (Table 3.3). Lastly, business supports in the form of direct transfers through the Restart Grant and others have been budgeted at around €0.9 billion for 2020.

Table 3.3: Covid-19 direct spending and tax measures

€ billion

	2020	2021
Tax Measures	1.8	0.75
Spending measures:	16.7	11.9
of which:		
PUP / TWSS / LR (March to September)	7.8	
PUP / EWSS (September to March 2021)	1.3	3.2
Additional Departmental Funding	4.7	1.4
Business supports	0.9	
Health (in addition to *Budget 2020*)	2.0	1.9
Recovery Fund		3.4
Covid-19 Contingency Reserve		2.1
Total	18.5	12.65

Sources: *Budget 2021*.
Notes: PUP stands for Pandemic Unemployment Payment, TWSS stands for Temporary Wage Subsidy Scheme, EWSS stands for Employment Wage Subsidy Scheme. Tax measures include rates waivers, VAT cuts, homebuying schemes, loss relief schemes. Departmental funding includes labour activation measures. Rounding can affect totals.

Budget 2021 added to spending in 2020, including the Christmas bonus, which again had not been included in budgetary planning. For 2021, this payment has again not been budgeted for, despite previous experience indicating it is highly likely to be paid.

After *Budget 2021*, Level 5 restrictions were effective as of 22nd October for a period of six weeks. This is expected to increase the 2020 general government deficit. Recently released revised estimates suggest that spending in 2020 is likely to be €1.6 billion higher than was forecast in *Budget 2021*, primarily due to additional welfare costs associated with the increased restrictions.[30] Some €1.3 billion of this additional spending is in the Department of Employment Affairs and Social Protection and the Social Insurance Fund.

For 2021, spending in gross voted terms is forecast to increase somewhat from the already high 2020 base (Table 3.4). Temporary spending related to Covid-19 is forecast to fall in 2021.[31] As a result, core gross voted spending (that which is likely

[30] https://ptfs-oireachtas.s3.amazonaws.com/DriveH/AWData/Library3/Documents%20Laid/pdf/PERdoclaid040320_041120_195458.pdf

[31] Even when including the Recovery Fund (€3.4 billion) and Covid-19 Contingency Reserve (€2.1 billion).

to be permanent) is forecast to increase by €5.4 billion (7.7 per cent). This is an acceleration compared to 2020 (€3.2 billion or 4.7 per cent).

Table 3.4: Gross voted expenditure
€ million

	2019	2020	2021
Core Gross Voted Spending	67,221	70,377	75,777
Covid-19 Spending	0	16,669	6,387
Brexit + Shared Island Fund	0	0	150
Covid-19 Contingency Reserve	0	0	2,100
Recovery Fund	0	0	3,400
Total Gross Voted Spending	67,221	87,076	87,814
Change in core Gross Voted Spending		3,155	5,400
Change in total Gross Voted Spending		19,855	738

Sources: *Budget 2021*.
Note: While not classified as "core" spending in the expenditure report, spending on Brexit and the Shared Island Fund are likely to be permanent. Funding for the Shared Island initiative is estimated to be €500 million over five years.

Looking at general government primary spending, the increase in spending is bigger for 2021 than in the previous year (€3.6 billion, Table 3.2). Temporary Covid-19-related spending is set to remain high, but is projected to be €4.8 billion lower than in 2020 (if one includes the Covid-19 Contingency Reserve and Recovery Fund as part of temporary spending in 2021). This implies there is an increase in permanent spending, not related to Covid-19 of up to €8.4 billion in 2021. This is consistent with the "Dual Strategy" set out in the Expenditure Report regarding Covid-19-related spending but also to increase spending on public services.

Temporary Expenditure

The bulk of the temporary Covid-19 spending in 2021 relates to the labour market impacts of Covid-19, with €3.2 billion of social protection spending projected to be needed for elevated levels of unemployment and the extension of the Pandemic Unemployment Payment and the wage subsidy scheme. In addition, temporary health spending of €1.9 billion is included for the supply of protective equipment, testing capacity and other measures. A further €1.4 billion is spread across other departments for costs arising from Covid-19.

A €2.1 billion "Covid-19 Contingency Reserve" is also outlined in *Budget 2021* to meet any further costs arising due to the impact of the pandemic over the course of 2021. Given the likelihood of some upside expenditure risks materialising, specifically those related to the income support schemes, it is possible that the unallocated contingency funding would be used even in a relatively benign environment. Allocating funding for adverse scenarios is prudent, but there is limited information on the likely uses of these contingencies. It is important to note the distinction between "rainy day" funding and money that has yet to be allocated to a specific area, but will likely be spent. At €2.1 billion, the contingency allocation for Covid-19 is substantial and warranted but should still be accompanied with clear costings as to which scenarios would likely see the amount used, and why.

The €3.4 billion "Recovery Fund" is to be disbursed in 2021, with no scheduled rollover beyond the end of the year. This has not been allocated to any specific Department, with the intention being to retain flexibility so that it can be used for tailored policy measures to support the economy in 2021 amid both Covid-19 and Brexit. Few details have been provided on this allocation. The budget documentation notes that it is intended to be used to support the economy and will be allocated to "specific revenue or expenditure measures that can be most effective at that particular time". *Budget 2021* notes that the Recovery Fund will distribute reimbursements as part of the Covid Restrictions Support Scheme (CRSS) and can be used for other spending or revenue-reducing measures.[32]

In addition to planned increases in spending, a contingency allocation of €2.1 billion has been reserved for additional costs that arise as a result of health cost pressures or greater levels of unemployment. Given the likelihood of some upside expenditure risks materialising, specifically those related to the income support schemes, it is possible that the unallocated contingency funding would be used even in a relatively benign environment.

The macroeconomic forecasts underlying *Budget 2021* assumed that no vaccine would be widely available until 2022 at the earliest. As a result, no procurement costs of a vaccine were factored into fiscal projections.[33]

In addition to the increase in core spending, a further €1.9 billion is allocated to health in *Budget 2021* for Covid-19-related spending (€1.8 billion current, €0.1 billion

[32] Further indications are that it will focus on funding infrastructure development, labour market activation and other measures to support investment and jobs.
[33] As a rough calculation, applying a costing of €30 per person to a population of five million would imply a costing of €150 million. Additional costs (administration, distribution etc) may be substantial (relative to the cost of acquiring doses).

capital). Health expenditure may pose a risk to fiscal forecasts in *Budget 2021*. Expenditure in this area has proven difficult to manage in recent years.[34] A failure to contain Covid-19 effectively would lead to additional expenditure. However, in this event, it would seem likely that some of the unallocated resources for 2021 could be diverted toward health expenditure.

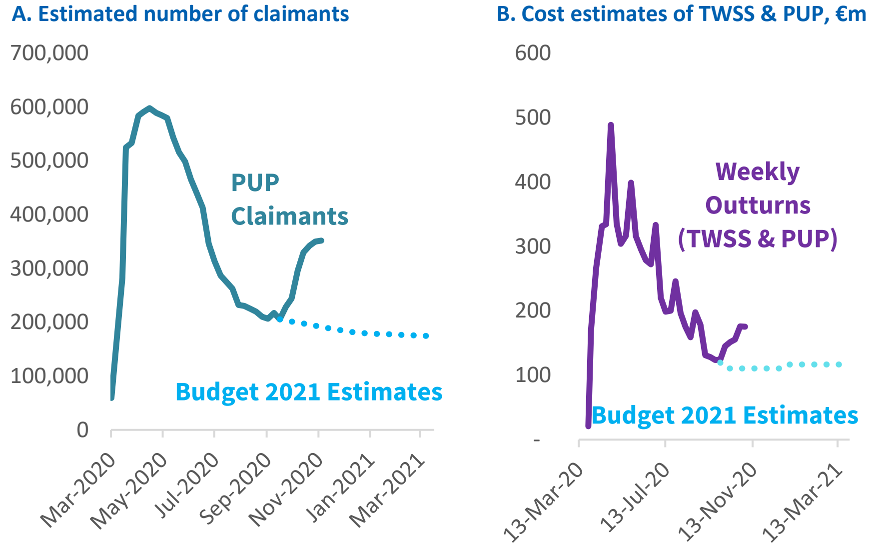
Covid-19 wage and income supports set up in 2020 will continue into 2021. The total allocation for Covid-19-related expenditure by the Department of Employment Affairs and Social Protection (DEASP) in *Budget 2021* is €3.2 billion.[35] This will cover payments for the PUP and EWSS, which have been costed at €1.4 billion for the first quarter of 2021, along with additional Covid-19-related Live Register costs.

The rates at which the PUP is paid are scheduled to reduce as employment recovers, with the scheme scheduled to end on 31st March 2021. Recent indications suggest however that both the PUP and EWSS will be extended in some format beyond the official end Q1 2021 deadline should demand remain high. A continuation of the schemes, for example on a stand-still basis for a further six months could cost approximately €2.8 billion in spending. While higher-than-expected numbers transitioning to the Live Register from the PUP and EWSS could also increase costs beyond the budgeted €3.2 billion.

It is unclear whether the Recovery Fund would contribute to these schemes, or whether any expenditure overrun would have to be funded by the Covid-19 Contingency Reserve and/or increased total expenditure.

[34] Recent years have seen overruns averaging of €0.5 billion per year.
[35] See Department of Finance (2020c).

Figure 3.2: Claimants of PUP to date and illustrative scenarios



Sources: *Budget 2021*, DEASP, Revenue Commission. Get the data.

The number of PUP claimants assumed under *Budget 2021* projections was forecast at 199,000 by the end of 2020, and to be at 174,000 when the scheme is due to end in March 2021 (Figure 3.2).[36] Monthly profiles have not been provided by the Department of Public Expenditure and Reform or DEASP, but the estimated number of claimants on the Live Register (drawing standard unemployment benefits rather than those introduced for Covid-19) by end 2021 in *Budget 2021* is around 380,000. To put this estimate in context, the most recent outturn for Live Register claimants was 203,172. Despite the large numbers on the EWSS, this suggests that the level of unemployment will remain high well into 2021, with modest levels of job recovery for those claiming the PUP.

It is important to note that fiscal forecasts in *Budget 2021* were based on the policy measures known or announced at that time. Some changes to income and employment supports have been announced since *Budget 2021*, as these forecasts did not anticipate the additional nationwide restrictions applied for six weeks effective from 22nd October. Repeat lockdowns or additional restrictions in 2021 could similarly result in both more claimants and a higher rate of payment under the PUP and EWSS. As for the CRSS, it is likely that payments will continue even under less strict restrictions. For example, the CRSS is expected to pay out an

[36] The remaining claimants are assumed to transition to regular jobseekers once the scheme expires in April 2020.

estimated €0.16 billion per month to businesses affected even under Level 3 restrictions.

In addition, the Pandemic Unemployment Payment has been restored to its higher level of €350 per week for those were earning more than €400 per week before the pandemic. These higher levels of payments are to continue until end-January 2021.[37] Given that the additional restrictions will result in increased numbers of those in the reinstated higher-income bracket of the PUP structure, the average cost per claimant would rise to around €337 for the period of increased payments from around €307. This would result in an estimated additional cost of around €10.6 million per week over previous rates.[38]

Table 3.5: Employment Wage Subsidy Scheme payment levels

€ per week

Weekly Wage	*Budget 2021* assumed payment	New payment (until 31st January 2021
€151 - 203	151.5	203
€203 - 300	203	250
€300 - 400	203	300
€400 - 1,462	203	350

Sources: Department of Finance. Get the data.

Note: Weekly wage refers to gross pay. Employees earning less than €151 or more than €1,462 per week are deemed ineligible for this scheme.

The forced closure of many firms will further result in more claimants. The October/November lockdown may have a slightly lower impact on employment as more sectors are deemed "essential" than was the case in April.[39] In addition, firms may be better placed to deal with severe health restrictions than was the case earlier in the year. Despite this, DEASP estimates put the potential employment losses of a Level 5 lockdown at around 167,000 extra claimants. This would put the total claiming at approximately 367,000 for the period of the restrictions (around 16 per cent of the workforce) and would likely lead to further permanent job losses as businesses become insolvent.

Changes have also been announced to the Employment Wage Subsidy Scheme since *Budget 2021*. These changes, due to be in place until the end of January 2021

[37] The other three rates of payment (€203, €250 and €300 per week) remain unchanged.

[38] This estimate assumes an average cost of around €120 million per week with an average of 356,000 claimants.

[39] For example, construction and some manufacturing activities are permitted to continue.

are shown in Table 3.5. As well as the payment levels increasing, the number of claimants is expected to increase over the six-week lockdown period. These additional costs will add to those budgeted as part of the extension to the EWSS scheme until April 2021. This assumes 350,000 workers, representing approximately 15 per cent of the total labour force, would be supported under the EWSS. The expected cost of this is €0.9 billion, or €0.3 billion per month. Taking these costings, the average spend for a worker being supported under the scheme is €214 per week over the first quarter of 2021. A full breakdown of these costs can be seen in Table 3.6.

Overall, the deficit is likely to be adversely affected by Level 5 restrictions introduced nationwide in late October. These will add to spending on income supports and subsidies, while the restrictions are likely to dampen wider economic activity and tax revenues. As mentioned earlier, spending is likely to be €1.6 billion higher relative to Budget Day forecasts.[40]

Table 3.6: Income support schemes

	Peak Claimants 2020	Peak Claimants (Month)	Latest Claimants	Est Avg Claimants Q1 2021	Est Avg Cost PP (Week €)	Est Avg Cost PP (Month €)
PUP	598,000	May	352,000	186,000	224	896
TWSS	415,000	July	-	-	-	-
EWSS	347,400	-	347,200	350,000	214	857
C-19 Illness Benefit	-	-	2,296	-	350	1,400
Live Register	244,562	July	203,172	227,000	168	672

Sources: Department of Finance, Revenue Commission, DEASP.
Note: Data accurate as of 26/11/2020. Cost estimates do not account for higher rates paid under the most recent Level 5 restrictions. Estimated costs of the EWSS do not include foregone PRSI.

Adding to this, further business supports may be required. For example, extending commercial rates waivers would come at a cost of around €0.1 billion per month. As contained in *Budget 2021*, €0.05 billion, around 1 per cent of total funding, has been made available for Covid-19-related costs in 2021 for the Department of Housing, Local Government, and Heritage. *Budget 2021* forecasts of €1.6 billion of local government revenue from rates, in line with normal revenue assumptions and

[40] Revised estimates show a €1.6 billion increase in expenditure relative to *Budget 2021*. €1.3 billion of this arises from the Department of Employment Affairs and Social Protection and SIF expenditure.

implying no further waivers. There is a risk that rate revenue may fall short, or further waivers would be granted, which would require greater spending.

Budget 2021 details that business supports with a direct fiscal impulse of €0.9 billion, liquidity supports worth €2 billion each in guarantees, tax warehousing, Irish Strategic Investment Fund (ISIF) investments, and €1.3 billion in loans were provided in 2020. Of these liquidity supports, no direct costs are assumed but will rather add to the Government’s liabilities and not to annual spending unless losses materialise. While business supports have a set cost, potential costs from liquidity supports or loan guarantees are more uncertain.

Box E: Covid-19 Support Measures

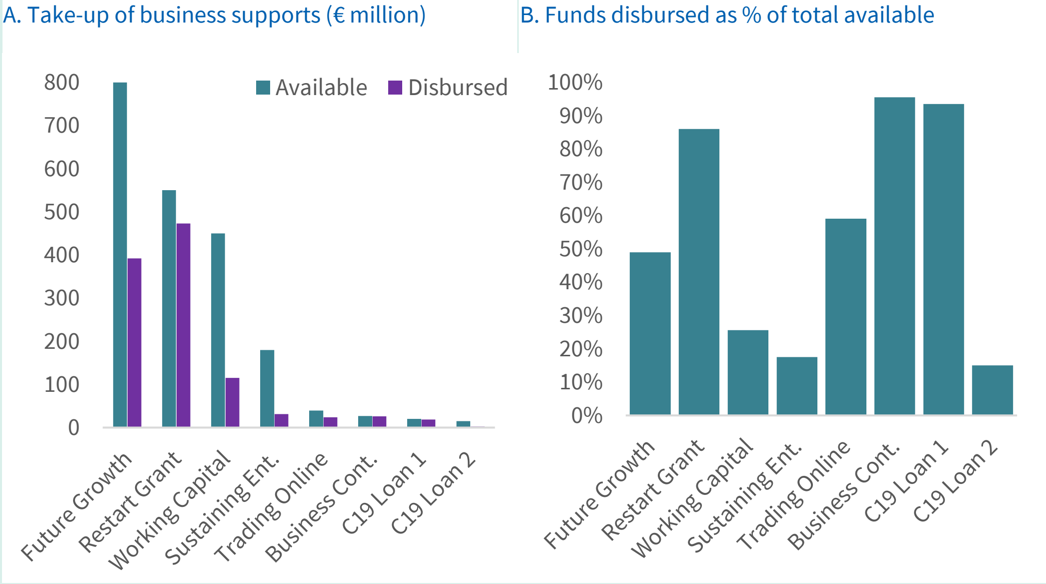
The level of governmental support for businesses, households, and the wider economy has reached around €26 billion in 2020. As part of the Government's effort to provide stimulus and support, a range of measures have been used, including tax cuts, employment subsidies, capital investment, loans, grants, guarantees and cash transfers.

This box provides an overview of some of the supports and policies introduced since March. We note three main findings. First, that the amount of overall support has been large and warranted. Second, more specific targeting and appropriate timing could boost take-up of certain measures. Third, areas such as capital investment and labour market activation remain open for further use.

Business support measures

Excluding tax cuts, rates waivers, and job retention schemes and other similar measures, the Government has allocated around €1.5 billion in liquidity loan supports to businesses affected by the crisis, with a further €0.6 billion in direct cash grants. Figure E.1 shows available data on the take-up of the most substantive of these schemes to date. Many of the business support measures have had lower-than-budgeted drawdowns. In general, measures such as direct cash grants and the smaller schemes have disbursed funds into the economy more quickly than the larger allocations of loans, guarantees and investments. Various factors may help to explain this: a reluctance to increase leverage, conditionality arrangements which are restrictive or insufficiently targeted to firms that have suffered the greatest falls in turnover, or a preference from firms for other supports may all play a role in determining demand.

Figure E.1: Take-up of Covid-19 business support measures



Source: Department of Enterprise, Trade and Employment, and Fiscal Council Workings.
Notes: Latest data accurate as of 28/10/2020

Tax measures

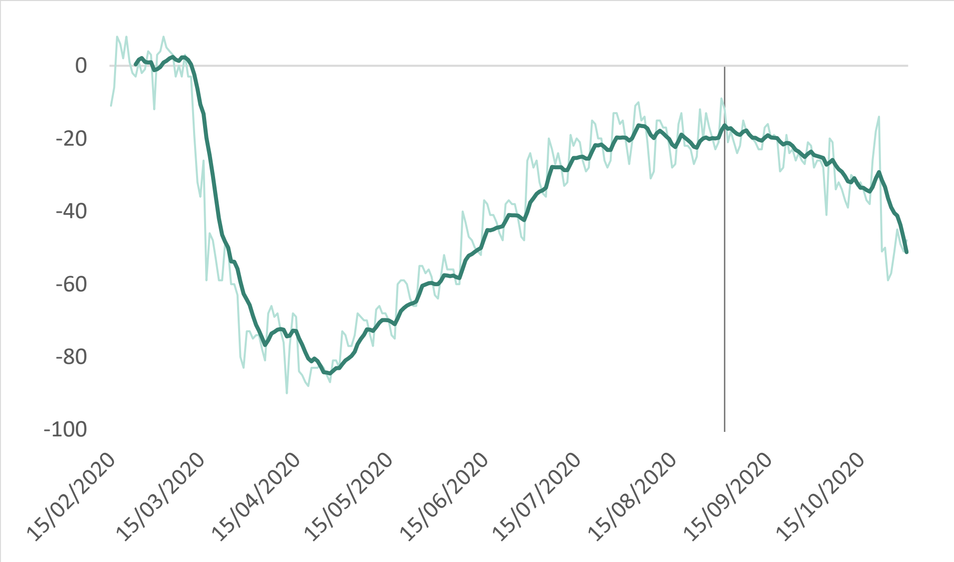
Tax cuts, rebates and waivers with a direct budgetary impact have been outlined to the value of around €1.8 billion in 2020, with measures in 2021 estimated at €0.7 billion. Over a third of this total relates to commercial rates waivers for businesses, allowing for immediate liquidity to flow to firms. The drawdown of most of the residual amount budgeted as part of the tax measures depends heavily on how consumer demand, particularly in key sectors like tourism and hospitality, progresses over the coming months.

As Figure E.2 shows, activity in retail and recreational sectors was faring relatively well in August and September, after recovering strongly from its April low. At such levels, well targeted tax measures could be expected to stimulate demand. The VAT cuts enacted by the Government could allow for consumers to save on purchases, or for struggling businesses to receive a direct liquidity boost by restricting the passthrough of the rate reduction. Such a policy might also be expected to normalise pre-Covid-19 consumer habits in an uncertain health environment.

The introduction of Level 5 restrictions in October however, as the tax measures were enacted, has meant that consumers have had little opportunity to avail of the schemes, assuming their expiration dates remain unchanged. Activity is now weaker again relative to pre-Covid-19 periods and is likely to remain so for the duration of the Level 5 restrictions

Figure E.2: Mobility data for retail and recreation

Deviation from Baseline



Source: Google; and Fiscal Council workings.
Note: The marker line denotes the introduction of the VAT rate cut from 23% to 21% on September 1. The bolder line represents the 7-day moving average of the underlying data series.

In addition to these restrictions on spending, other factors which might limit the effectiveness of the measures are that the VAT cuts merely subsidise purchases which would have taken place anyway, particularly with respect to consumer durables. Limited passthrough of the rate cut, as businesses increasing need liquidity, and ongoing consumer uncertainty could also dampen its effect.

Labour-market activation

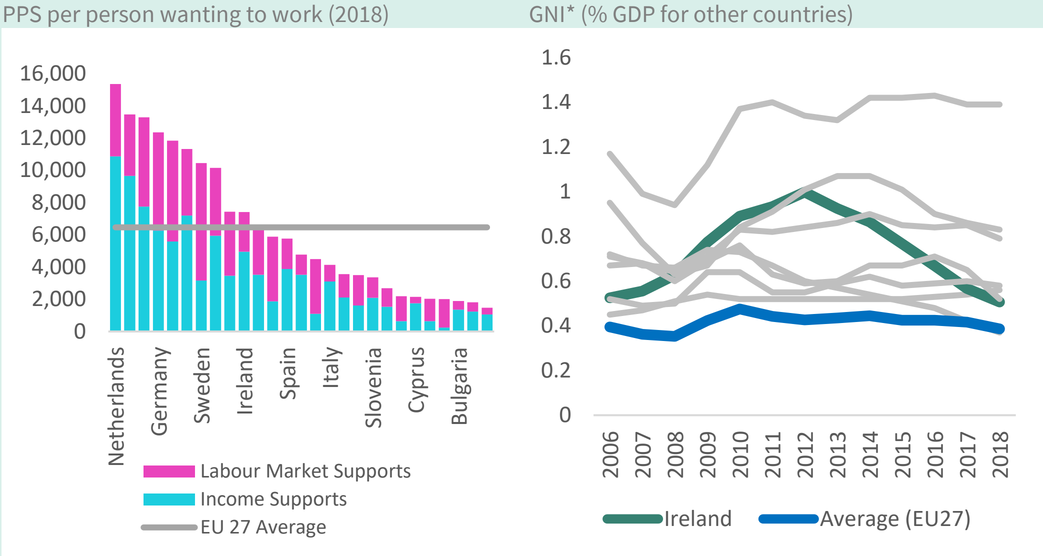
As part of the July stimulus measures, the Government allocated additional funding for labour market activation of around €200 million, with €130 million to be used in 2020 and the remainder in 2021. This was supplemented by an allocation of €10 million in *Budget 2021.* As a percentage of *Budget 2020* figures, this total is around a 20 per cent increase.

Figure E.3 shows that by various measures, Ireland spends around the EU average on such policies in normal times, but is far below the highest spenders.

In 2021, the employment outlook implies that significant spending increases would be needed to close the gap between current funding (including the recent additional allocations) and demand for social welfare services in the form of labour market activation schemes. This stretch on services can manifest in areas such as the caseworker-client ratio in social welfare centres. With Ireland's ratio already considerably above the best-practice figure of around 150:1, the greatly increased caseload as a result of the pandemic will see this ratio deteriorate further.[41]

Figure E.3: Expenditure on Income and Labour Market Activation Supports

PPS per person wanting to work (2018) GNI* (% GDP for other countries)



Source: Eurostat, and Fiscal Council workings.

With health restrictions likely to continue, many of those in unemployment will likely become long-term unemployed, defined as a period of six months or over. Among other benefits, labour-market activation policies are one of the ways in which the Government can both reduce unemployment in the short run, and increase human capital in the long run.

Investment measures

Public investment tends to have a larger impact on economic activity compared to other forms of public spending (Ivory, Casey and Conroy, 2020; Varthalitis, 2019; Hall, 2010; Bénétrix and Lane, 2009; Giordano et al., 2007). As well as having higher multipliers, public investment can also contribute to productivity in the future. With social distancing limiting the effectiveness of demand stimulus in sectors where demand is low due to health risks, public investment can also be a key tool to divert resources and stimulate demand to areas that are less constrained. In particular, it can be useful to make up for shortfalls in construction demand and jobs that might not return quickly.

In terms of responding to the current crisis and providing stimulus for the recovery, public investment has not been expanded much, relative to pre-existing plans. General government gross fixed capital formation—a broad measure of how much the Government spends on capital projects in a given year—was set to rise from €8.8 billion to €9.1 billion between 2020 and 2021 according to *Budget 2020* plans. The *Budget 2021* projections put the respective levels of investment at €9.3 billion and €9.8 billion for the same years — a combined increase of €1.2 billion. For context, this amounts to about 3.8 per cent of the increase in total general government spending over the two years relative to the *Budget 2020* plans.

However, public investment is set to rise to high levels. Ireland's level of public investment as a share of GNI* is set to rise to 4.7 per cent in 2021. This would be the highest level since 2009, just prior to the sharp cuts to investment introduced after the financial crisis. This would also

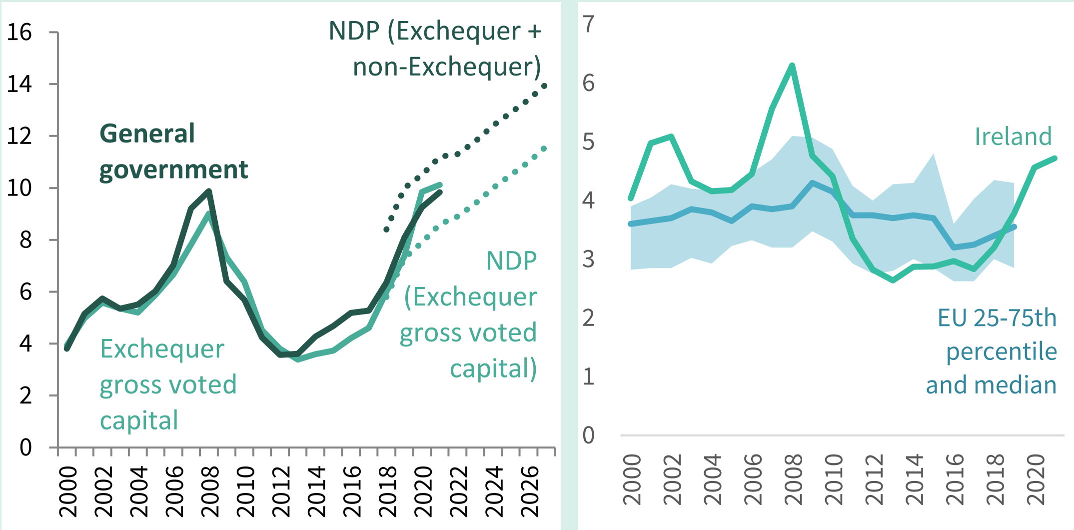
[41] IMF (2017a) noted that this figure had declined from 800:1 in 2013 but remained high at 500:1 in 2015.

see Ireland having relatively high levels of investment in the context of the EU where normal ranges over the past two decades were between 3 and 4.5 per cent of GDP.

Figure E.4: Public investment is set to rise to high levels

A. Investment spending broadly as planned
€ billions

B. High in the context of the EU
% GNI* (% GDP for other countries)



Sources: National Development Plan (NDP), 2018–2027; CSO; Department of Public Expenditure and Reform; Eurostat; and Fiscal Council workings.
Notes: The NDP notes that commercial semi-state bodies, state-owned enterprises and other non-Exchequer bodies make their investment decisions in line with business plans that, for the vast majority, did not extend past 2021 at the time of the publication of the NDP.

Permanent Expenditure

Alongside Covid-19 related temporary measures, *Budget 2021* included €5.4 billion of permanent increases to core gross voted spending, with up to €8.4 billion in terms of general government spending (as shown in Table 3.2 and Table 3.4). These increases are unrelated to Covid-19 under the Government's "Dual Strategy" to continue to increase spending in core areas. These increases in spending are likely to be permanent. These include €1.9 billion in health, €0.7 billion in education and children areas, €0.7 billion in social protection, €0.7 billion in housing and €0.7 billion in transport.

A further €1 billion increase is evident in non-voted current spending areas (not including cash interest payments on national debt). There is little transparency on what is driving this increase in terms of budget documentation.[42] However, from the White Paper that is published prior to the Budget (Department of Finance, 2020b), the Council understands that it predominantly relates to an increase in Ireland's EU budget contribution for 2021, which is likely to be a persistent increase. About half of this would appear to be driven by estimated increases in customs revenue under the disorderly Brexit scenario, which are transferred to the EU budget. The other half appears to be driven by an increase in the non-customs element of the EU budget contribution.

Despite the volume of information provided with Budget Day documentation, it is not possible to ascertain where a substantial portion of increases in non-Exchequer spending comes from. There is very little information provided in budgetary documents for areas outside of the Exchequer — these areas typically account for about one-fifth of government spending. It is possible that the increases in spending outside of the Exchequer are temporary also, but it is not possible to be definitive on this without more information and with such a short forecast horizon being adopted in *Budget 2021*. The increases appear to reflect capital spending more than current spending, though capital spending increases would also attract long-lasting increases in current spending too.

[42] While the white paper gives information on non-voted spending, this is done on a pre-budget basis.

Budget 2021 also included significant permanent increases in core (non-Covid-19-related) spending. Core current health spending is set to increase by €1.9 billion in 2021. No estimates were made available as to how much of this increase is split between pay and non-pay items.

Table 3.7: General government expenditure forecasts in *Budget 2021*
€ billion

	2019	2020	2021
General gov. expenditure	87.3	105.9	109.2
Compensation of employees	23.0	24.6	25.8
Intermediate consumption	12.5	16.8	14.8
Social payments	31.7	39.3	38.4
Interest	4.5	3.9	3.6
Subsidies	1.7	6.1	4.8
Gross fixed capital formation	8.1	9.3	9.8
Capital transfers	1.9	1.9	2.2
Other	3.9	4.0	4.4
Unallocated resources	0.0	0.0	5.5
Primary expenditure	82.8	102.0	105.6
Primary expenditure (% GNI*)	38.8	50.3	50.7

Sources: *Budget 2021*.
Note: Primary expenditure is calculated as total expenditure minus interest payments.

Core social protection spending is to increase by €741 million in 2021. This reflects the assumption that the state pension age will remain at 66 in 2021. Increasing the state pension age—as had been legislated for but was subsequently deferred by Government pending a review—would have led to expenditure being reduced by up to €0.6 billion (Fiscal Council, 2020b).

Welfare payments, other than those related to Covid-19, were held fixed in nominal terms. The full-year cost of the October 2020 increase in public pay will add €0.3 billion to public spending in 2021 compared with 2020, reflecting the cost of increments and the full-year effect of the final pay increase paid in autumn under the current pay deal. No further pay deal is currently in place.

Risks for transport revenues remain in 2021. An allocation was made to the value of €0.45 billion this year to fund shortfalls from March, representing around 45 per cent of total 2018 revenues for CIÉ.[43] Given that levels of activity are forecast to remain

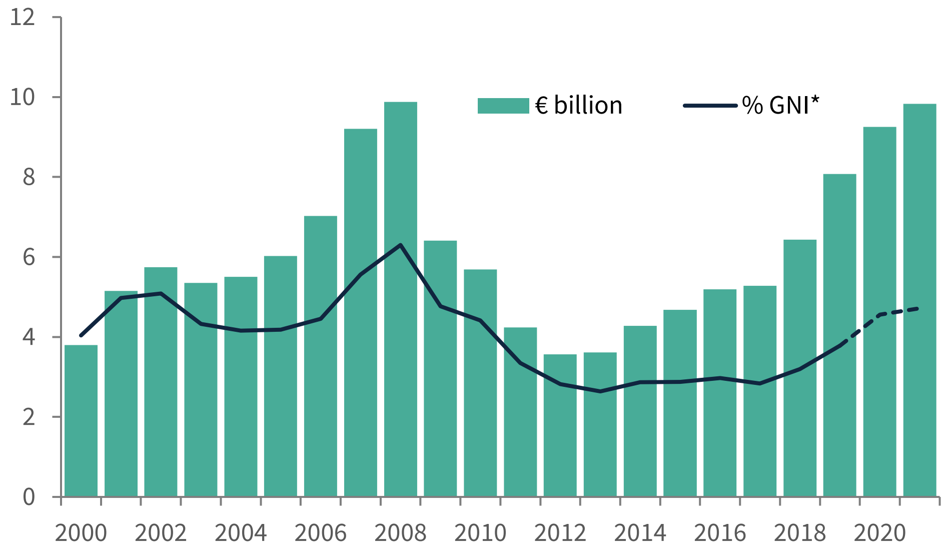
[43] See CIÉ (2019).

low throughout all of 2021, the allocation of €0.395 billion for the year in *Budget 2021* may prove insufficient. Further risks remain from structural changes in the commuting and travel habits of both domestic and international travellers.

Public investment is set to rise to high levels. Gross fixed capital formation is forecast in *Budget 2021* to grow by €1.2 billion in 2020 (Figure 3.3).[44] Central and local government are both expected to contribute approximately €0.6 billion each.[45] This is an upward revision of €0.3 billion since *Budget 2020*. Forecasts suggest that government investment as a share of GNI* will increase in both 2020 and 2021, which will take it to high levels in an historical and international context (Box E). Gross voted capital expenditure is forecast to grow more strongly in 2020 (€2.5 billion). This increase is larger than the General Government increase as some of the gross voted capital expenditure is classified as intermediate consumption.

Figure 3.3: Government investment is set to increase to high levels

General government gross fixed capital formation



Sources: CSO and *Budget 2021*. Get the data.

Note: Dashed line indicates forecast values.

Overall general government expenditure is forecast to increase further in 2021 (€3.3 billion or 3.1 per cent), leaving it €21.9 billion above its 2019 level. Overall, there have been large revisions to forecasts of general government expenditure over recent forecast rounds (Figure 3.4). Fiscal forecasts in *SPU 2020* incorporated some temporary additional spending measures introduced for 2020. Since then, various

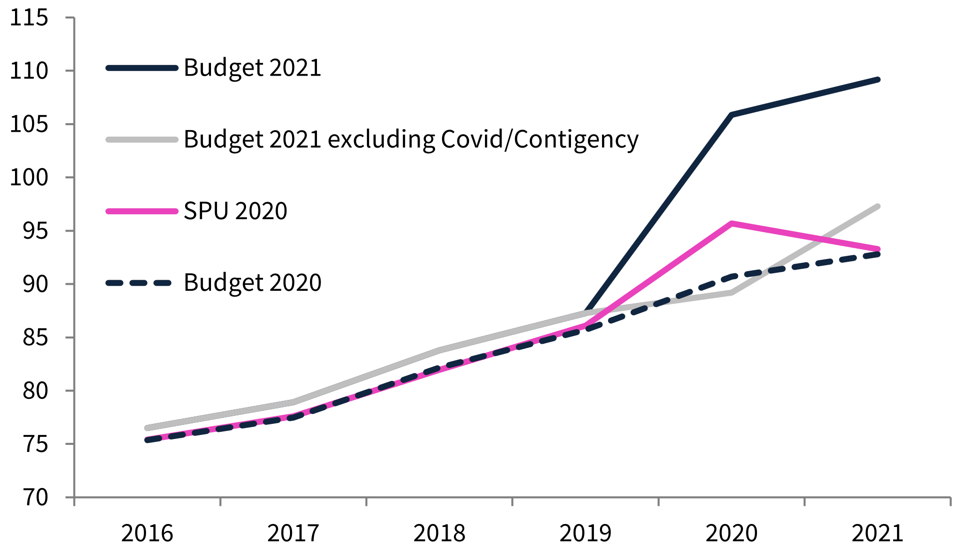
44 An increase of €0.9 billion was projected in *Budget 2020*.

45 Spending by Approved Housing Bodies (AHBs) is expected to increase by €0.4 billion.

policy announcements have been made that affect expenditure in 2020 and 2021. *Budget 2021* incorporates a broader range of measures affecting spending in 2020 and 2021. Figure 3.4 shows that the large revisions seen in *Budget 2021* largely reflect temporary Covid-19 spending and contingencies.

Figure 3.4: General government expenditure has seen large revisions in recent rounds

€ billion

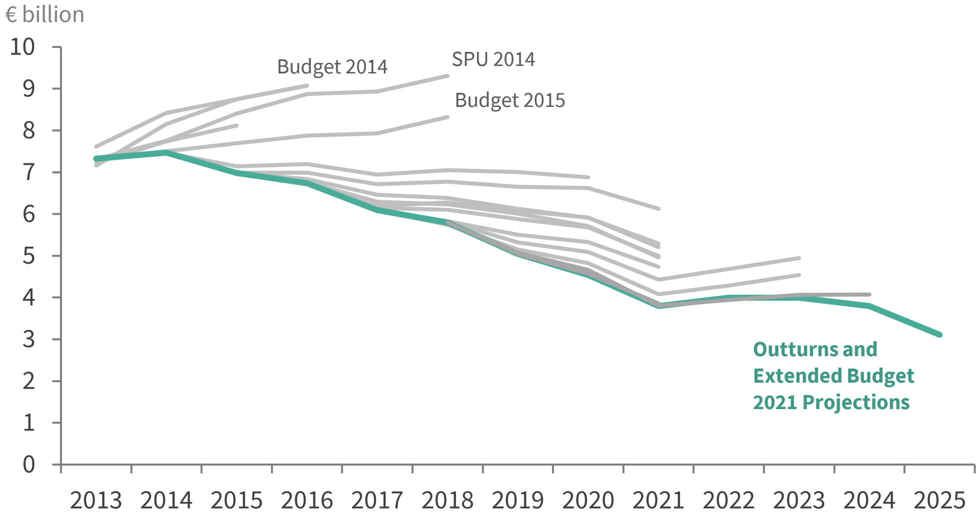


Sources: *Budget 2020*, *SPU 2020* and *Budget 2021*. Get the data.
Note: Covid-19 spending here also includes the Covid-19 contingency reserve and the Recovery Fund.

Interest expenditure

Figure 3.5 shows the reduction in forecast and actual interest costs. It also shows that interest costs have been consistently lower than forecast for a number of years. Given the short forecast horizon in *Budget 2021*, the impact of large deficits and increasing funding requirements is not evident in the forecasts.

Figure 3.5: National debt cash interest payments have been less than expected



Sources: Department of Finance. Get the data.

Despite the absolute amount of Irish government debt increasing in 2020 and 2021, the cost of servicing this debt is forecast (in *Budget 2021*) to fall in 2021. Improvements in government creditworthiness, policy actions by the ECB and other central banks, and the secular decline in interest rates have contributed to the reduction of the interest rate at which the government can borrow. Retiring higher coupon bonds and refinancing at lower rates has in turn brought down the effective interest rate on Irish government debt. The falls in interest rates more than outweigh the increase in the stock of debt, hence debt service costs fall. In the coming years, the marginal rate will be important due to high funding requirements both for new borrowing and rolling over existing liabilities.

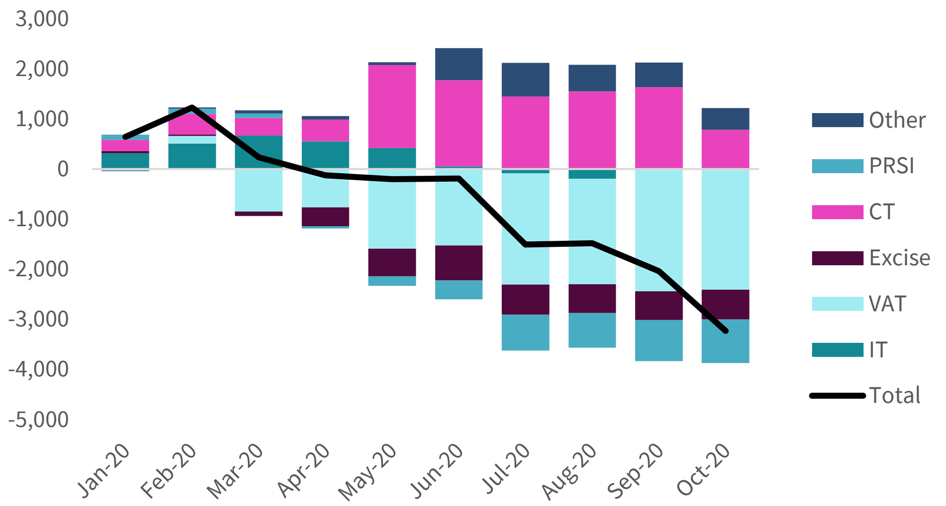
Revenue

The sharp fall in economic activity in 2020 has lowered government revenue substantially. A reduction in income and employment has meant lower direct taxes and social contributions. Income tax and PRSI combined are anticipated to have fallen by €3.3 billion. Falling consumption and VAT policy changes have meant lower indirect tax receipts (*Budget 2021* forecasts a fall of €2.7 billion in VAT and excise receipts). At the same time, corporation tax receipts are expected to grow by €1.4 billion.

Policy measures to support the economy have also contributed to the reductions in revenue. Measures such as VAT reductions, rates waivers, loss relief, and others such as the Help-to-Buy scheme have been costed at around €1.8 billion for 2020.

Figure 3.6: Cumulative revenue change

€ million (y/y)



Source: Department of Finance. [Get the data](#).

A key development has been the robustness of some tax revenues compared with the fall in activity: while up to 40 per cent of the workforce was unemployed or on support schemes at the peak of the crisis, income tax revenue for 2020 is anticipated to be only marginally below its 2019 level. Part of this can be explained by the strong performance of income tax receipts in early 2020, before the pandemic struck (Figure 3.6). In seasonally adjusted terms, income tax receipts rose by more than 9 per cent in January relative to December.

Table 3.8: *Budget 2021 Revenue Measures*

€ million

Measure	2021 Impact	2022 Impact
VAT reduction for Tourism / Hospitality	-336	-
Non-Indexation of Tax Bands/Credits	192	-
Carbon Tax Rate Increase of €7.50	108	147
Excise Increases on Tobacco	57	57
Help to Buy Scheme Extension	-43	-43
Income Tax Credit Increases	-29.7	-30.4
Farmers Flat Rate Increase of 0.8%	-10	-12
USC Qualifying Threshold Increase	-6	-7
Other Measures	-6.1	-6.8
Total	-73.8	104.9

Source: Department of Finance.
Note: Reduced VAT rate for hospitality sector has a 2020 impact of €65 million, while changes to income tax credits have a cost of €13 million in 2020.

Focusing on **Exchequer tax revenue**, *Budget 2021* forecasts a fall of €2.6 billion (4.4 per cent) in 2020. A much sharper fall was forecast in *SPU 2020* (a fall of €9.7 billion or 16.4 per cent). The upward revision to tax revenue is mainly driven by income tax (€3.3 billion) and corporation tax (€2.1 billion). These upward revisions are due to stronger-than-anticipated outturns for the year to date.

The usual methodology to compile official forecasts would project the change of revenue using the change in the associated macroeconomic driver, multiplied by an elasticity.[46] The elasticity reflects how closely receipts move with its macroeconomic driver. Where applicable, any assumed impacts of policy changes are also included. In addition to these factors, judgement is often applied. This can be helpful to take account of specific factors such as changes in behaviour or where the elasticities may be misleading.

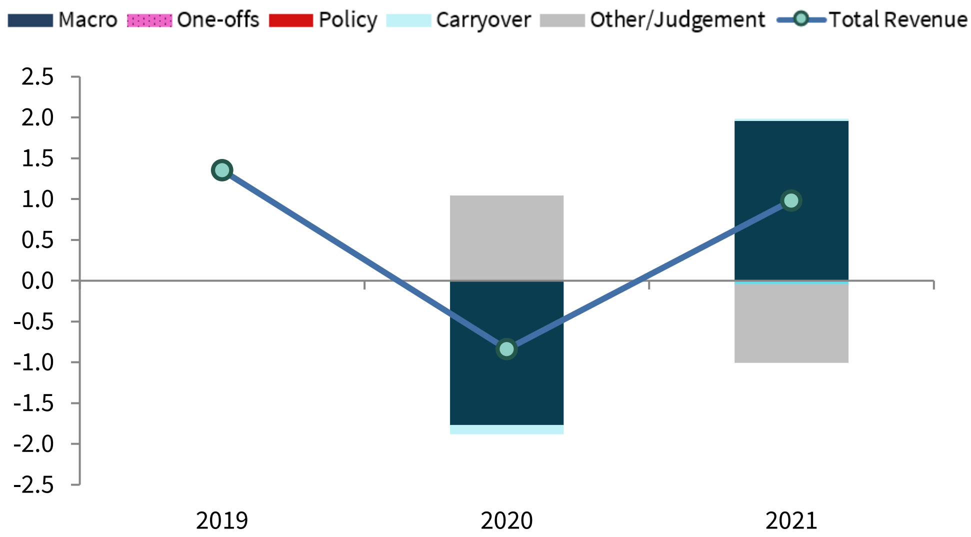
As nine of the 12 months of returns were available, *Budget 2021* forecasts for this year involves forecasting three months of receipts. These forecasts were arrived at in consultation with the Revenue Commissioners and account for any Budget Day tax policy changes that affect receipts for the remainder of 2020. For 2021, a typical forecasting approach was applied, using macroeconomic drivers and elasticities.

[46] When forecasting at budget time, in-year forecasts typically do not follow this methodology. Forecasts from the SPU are updated manually to account for recent outturns and any policy changes in the budget. Forecasts beyond the current year typically use an elasticity combined with a macroeconomic driver.

There may be reasons to anticipate factors other than those typically considered as affecting on receipts. For example, income tax receipts in 2020 have not fallen as severely as simply applying an elasticity and macroeconomic driver would imply. This appears to be due to employment and income losses being concentrated at the lower end of the income distribution. Due to the highly progressive income tax schedule, these employment and income losses result in smaller income tax losses, as those on lower incomes are subject to a lower-than-average tax rate. Conversely, when this employment returns, one should not anticipate as big an increase in income tax receipts as a standard approach would imply. Year-on-year comparisons of income tax receipts in 2020 also benefit from a strong performance in the first quarter of the year.

Figure 3.7: Judgement has been used to smooth changes implied by macro drivers for income tax (PAYE and USC)

€ billion change year-on-year



Sources: Department of Finance, and Fiscal Council workings. Get the data.
Note: “Other” reflects other factors/judgement applied by the Department of Finance and carryover impacts from previous policy measures. The elasticities used by the Department of Finance are used for this exercise (2.1 for PAYE income tax, 1.2 for USC). See Appendix C for more details.

While tax forecasts for 2020 in *Budget 2021* were not compiled by applying a macroeconomic driver with an elasticity, correcting for policy changes/one-offs and applying judgement, we can simulate what such a forecasting methodology would have implied for 2020. As a result, we can infer what level of judgement is implied from the forecasts for 2020 given in *Budget 2021*.

For income tax, the usual tax elasticity would imply a much larger fall in income tax in 2020 than is likely to have occurred. Positive judgement in the forecast for 2020 reflects the stronger than predicted return for the year to date (Figure 3.8).[47] As a result, in 2021, there is an offsetting negative judgement to unwind these effects. This means that the recovery in employment and income is assumed to be less tax-rich than would be typically the case. Other factors play relatively minor roles in both 2020 and 2021.

Looking specifically at PAYE, 2020 receipts are forecast to be higher than would be implied by simply applying a standard elasticity and macroeconomic driver.[48] This is equivalent to applying a much lower elasticity (60 per cent lower) and not applying judgement. If this same low elasticity were applied in 2021 (without applying judgement), this would also yield forecast receipts close to that in *Budget 2021*.

While unwinding the 2020 judgement in 2021 income tax forecasts may be reasonable, there is a risk to income tax forecasts from the macroeconomic drivers. As described in chapter 2, substantial income growth is forecast for 2021. This would imply either that the employment recovered in 2021 is not exclusively focused in low paying sectors, or that wage growth in high-earning sectors for existing workers will be substantial. Either case would pose an upside risk to income tax forecasts in 2021.

PRSI receipts are anticipated to fall in 2020 by 16.6 per cent. For the first three quarters of 2020, the fall has been 9.8 per cent. This fall is more severe than is the case for income tax and reflects the fact that income tax is more progressive and has a broader base.[49] As a result, the distributional nature of the job losses has not insulated PRSI receipts to the same extent. For 2021, PRSI is forecast to grow by 17.8 per cent, almost recovering to its 2019 level.

[47] As mentioned earlier, income and employment losses in 2020 have been focused on the bottom of the income distribution. As the Irish income tax system is highly progressive, this fall in income and employment has less of an impact on income tax receipts than would otherwise be the case.

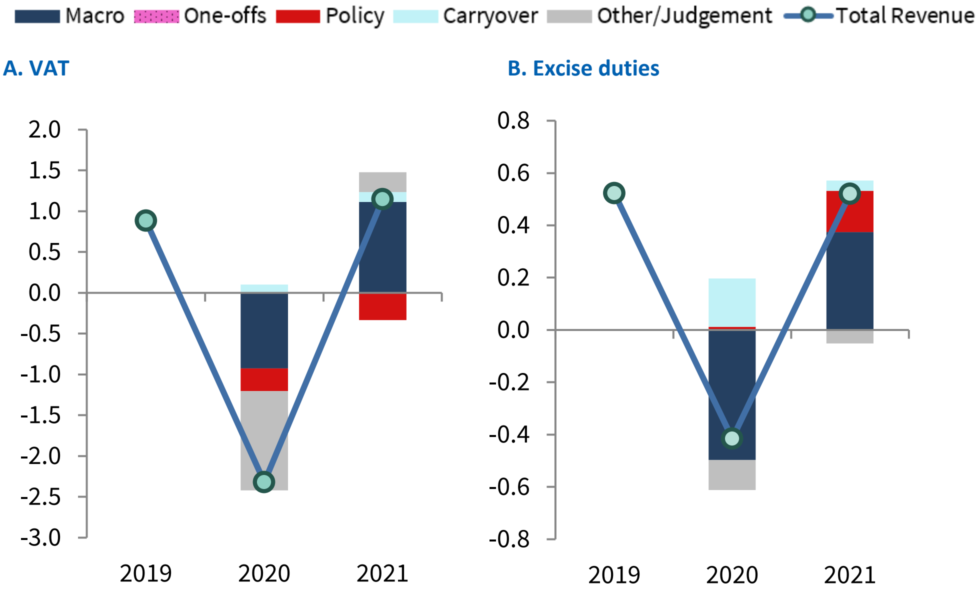
[48] PAYE makes up about 70 per cent of total income tax receipts. USC makes up approximately 14 per cent.

[49] In addition, full PRSI was not charged to employers or employees in instances where the TWSS or EWSS were in operation, unlike income tax.

VAT receipts are anticipated to decline in 2020 by €2.3 billion (15.3 per cent). This reflects the projected fall in consumption. Policy also plays a role (the reduction in the higher rate of VAT). In addition, there is some negative judgement implied (€1.2 billion or 9.5 per cent of receipts). This reflects forbearance measures in place from the Revenue Commissioners in 2020 (approximately €1 billion).

Figure 3.8: VAT and excise see substantial falls in 2020, rebounding in 2021

€ billion change year-on-year



Sources: Department of Finance, and Fiscal Council workings.
Note: "Other" reflects other factors/judgement applied by the Department of Finance and carryover impacts from previous policy measures. See Appendix E for more detail.

For 2021, VAT receipts are forecast to recover somewhat, reflecting the recovery in personal consumption (Figure 3.8). Positive judgement is applied in 2021 (€0.2 billion) overall, driven by two contrasting factors. Firstly, it is assumed that forbearance measures from the Revenue Commissioners will not continue into 2021, leading to positive judgement.[50] Secondly, *Budget 2021* forecasts take account of a change in the accounting of VAT paid on imports. This is expected to delay some receipts in the later part of the year until 2022 (this is expected to have an impact of around €160 million and is expected to be a permanent change). *Budget 2021* forecasts an increase in receipts of €1.1 billion (8.9 per cent) in 2021. This reflects policy measures that will reduce revenues being offset by assumed repayments of

[50] This is applied as positive judgement, as the negative judgement in 2020 leads to a lower base for 2021 forecasts. As a result, model forecasts for 2021 are affected by the judgement applied in 2020.

warehoused taxes in 2020 to the value of €0.375 billion.[51] Repayment failures or extending VAT reductions beyond their legislated expiration dates risks adding to the €0.8 billion in estimated foregone revenues for 2020 and 2021 and would weigh heavily on intake for the year.[52]

Excise duties are forecast to fall in 2020 (€0.4 billion or 7.0 per cent). This decrease is driven mainly by reduced personal consumption.[53] Downward judgement of €0.1 billion is implied for 2020. Excise receipts are forecast to grow in 2021 (€0.5 billion or 9.6 per cent). This is driven by both improved macroeconomic conditions and also policy changes (increase in the carbon tax and tobacco tax).

Customs receipts are expected to increase in 2021 due to Brexit (€0.7 billion). However, only €0.2 billion of this increase will be retained by the Exchequer, with a €0.5 billion increase in EU contributions. Were a trade deal to be successfully negotiated, then these impacts could be expected to be much lower.

Receipts from the local property tax (LPT, €0.5 billion) are assumed in *Budget 2021* to be unchanged in 2020 and 2021. Originally, valuations were to be updated on 1st November 2019. This was subsequently deferred by a year to November 2020. The Minister has announced a further deferral of the LPT valuation date from 1st November 2020 to 1st November 2021. If a revaluation had gone ahead on 1st November 2019 with no change in the rate of the tax, 2020 receipts would be approximately €729 million. This suggests that the revenue lost because of not proceeding with revaluations on 1st November 2019 on a no-policy-change basis was in the region of €247 million annually.

Corporation tax (CT) receipts have grown for the first three quarters of this year (up €1.6 billion or 27.9 per cent). Again, this illustrates how this revenue source can contrast with the performance of the domestic economy. When *Budget 2021* forecasts were compiled, returns for nine of the 12 months were available. Previously it has been shown that November corporation tax receipts are well

[51] In general government terms, these receipts would still be accrued to 2020. A further €0.375 billion is expected to be collected in 2022. As a result, €0.75 billion out of the €1 billion of 2020 warehoused liabilities is expected to be collected.

[52] A VAT cut for the hospitality sector enacted in 2011 ran to 2019, well beyond its scheduled initial expiration date of 2013.

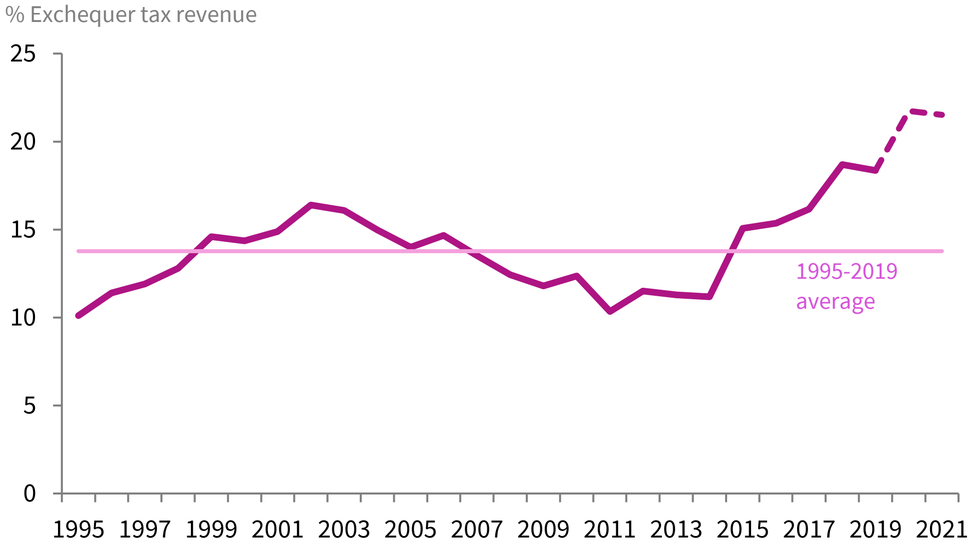
[53] Revenue (2018a) report that 43 per cent of 2017 excise duties were derived from alcohol and tobacco. A further 34 per cent of excise duties came from petrol and diesel.

correlated with June receipts (Department of Finance, 2017e). If one assumes that this relationship holds, then corporation tax receipts in 2020 would likely be €12.6 billion (€0.3 billion higher than *Budget 2021* forecasts).

Economic shocks such as Covid-19 and Brexit are likely to strongly affect many domestic firms. These firms could suffer substantial losses, which could then be used to offset CT liabilities in future years. By contrast, sectors that are dominated by foreign-owned multinationals (particularly pharmaceuticals and the digital sector) could perform quite well in this environment.

While the Department assesses that the OECD's Base Erosion and Profit Shifting (BEPS) process may reduce CT receipts in the future, this impact is expected to arise from 2022 and is therefore beyond the forecast horizon in *Budget 2021* (see Box A). These impacts are reflected in the scenario analysis (Section 3.4). *Budget 2021* forecasts a moderation in growth of CT receipts in 2021. The strength of CT receipts relative to other tax headings means that the CT share of tax revenue is forecast to increase to its highest ever levels (Figure 3.9). Policy measures are not set to play a role in determining the outturns for either 2020 or 2021, as the €0.45 billion in accelerated loss relief introduced in the July stimulus should be neutral in general government terms. It is subject to the risk, however, that affected firms do not recover significantly to see net CT revenue balance next year.

Figure 3.9: Corporation tax is forecast to reach a record high share of tax revenue



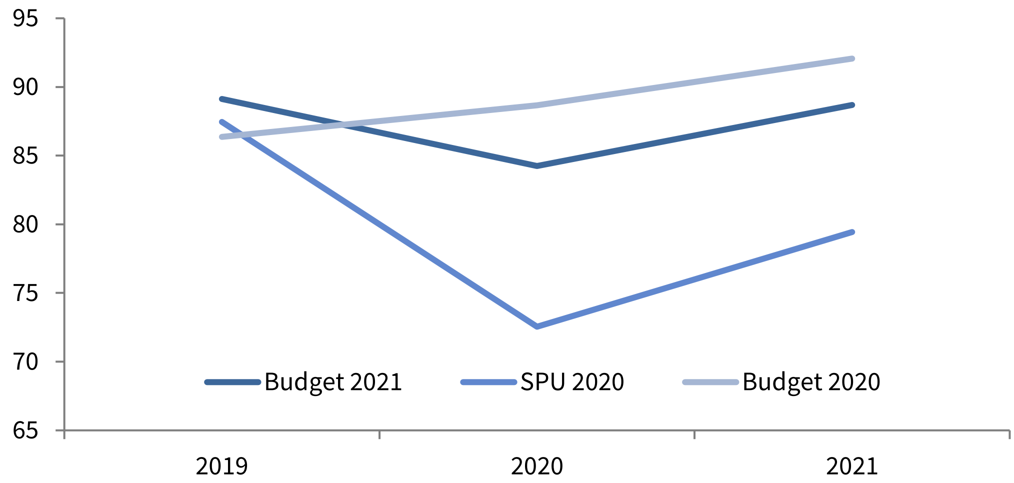
Sources: Department of Finance, and Fiscal Council workings. Get the data.
Note: Dashed line indicates *Budget 2021* forecasts.

Budget 2021 forecasts of non-tax revenue for 2020 are €0.3 billion higher than forecast in *Budget 2020*. The upward revision mainly reflects higher-than-projected payments to the Exchequer from the Central Bank, arising from its disposals of Floating Rate Notes. However, most of this income does not affect general government revenue. Payments from the Central Bank are expected to continue into 2021, albeit at a much lower level (down from €2 billion to €0.4 billion).

The large impact of Covid-19 on Exchequer revenue in 2020 is reflected in general government revenue. It is forecast to decline by €4.9 billion (5.5 per cent) in 2020 to €84.2 billion (Table 3.9). This is a €11.7 billion upward revision compared to *SPU 2020*. This upward revision also affects 2021 receipts, which have also been revised up significantly (€9.3 billion).

Figure 3.10: Forecasts of general government revenue have seen large revisions in recent rounds

€ billion



Sources: *Budget 2021, SPU 2020, and Budget 2020*. Get the data.

Budget 2021 projects that general government revenue will recover somewhat in 2021, in line with the economy (Figure 3.10). Growth of €4.4 billion (5.3 per cent) is forecast. With this growth, revenue almost returns to 2019 levels. However, excluding corporation tax receipts this leaves general government revenue 6.7 per cent lower than what was forecast a year ago in *Budget 2020* (3.7 per cent lower if corporation tax receipts are included). Revisions imply a shallower fall in revenue in 2020, but also a more gradual recovery in revenues in 2021.

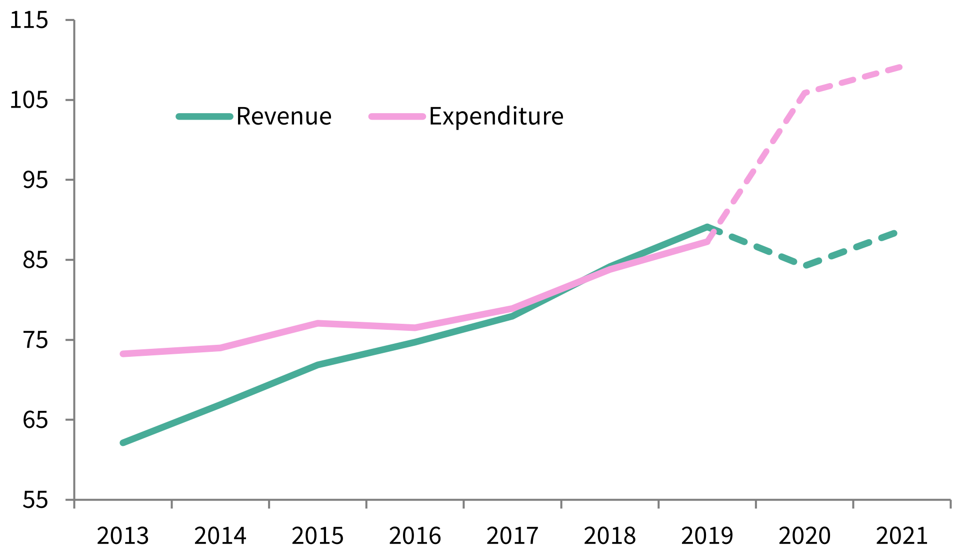
Table 3.9: *Budget 2021* general government revenue forecasts
€ billion

	2019	2020	2021
General gov. revenue	89.1	84.2	88.7
Taxes on production and imports	27.5	24.9	25.7
Current taxes on income, wealth	36.6	37.5	38.3
Capital taxes	0.5	0.5	0.4
Social contributions	15.8	14.0	15.4
Property income	1.6	1.1	0.4
Other	7.1	6.3	8.5

Source: Department of Finance.

Taxes on production and imports are forecast to fall most rapidly, by €2.5 billion (9.2 per cent). This mirrors the fall forecast for VAT and excise receipts in Exchequer terms. Taxes on income and wealth (mainly income and corporation tax) are forecast to increase by €0.8 billion (2.3 per cent). Social contributions (mainly made up of PRSI) are forecast to fall by €1.8 billion (11.4 per cent) in 2020.

Figure 3.11: General government revenue and expenditure
€ billion



Sources: Department of Finance, and CSO. [Get the data](#).

As with the expenditure forecasts, revenue forecasts in *Budget 2021* were made on the assumption of higher levels of confinement measures not being introduced in 2020. The introduction of six-week nationwide Level 5 restrictions in late October after the budget will result in lower employment, hence weaker income tax and

PRSI. Given that employment losses are likely to be concentrated in low-paying sectors, the impacts may be somewhat lower than would be the case if employment losses were spread evenly across the income distribution. Consumption is also likely to be affected, lower VAT and excise receipts are likely.

Box F: Seasonal Adjustment of Exchequer Tax Revenues

Monthly cash tax and spending data published each month in the Exchequer Returns display cyclical, seasonal, and trend patterns that make direct comparisons between time periods challenging.

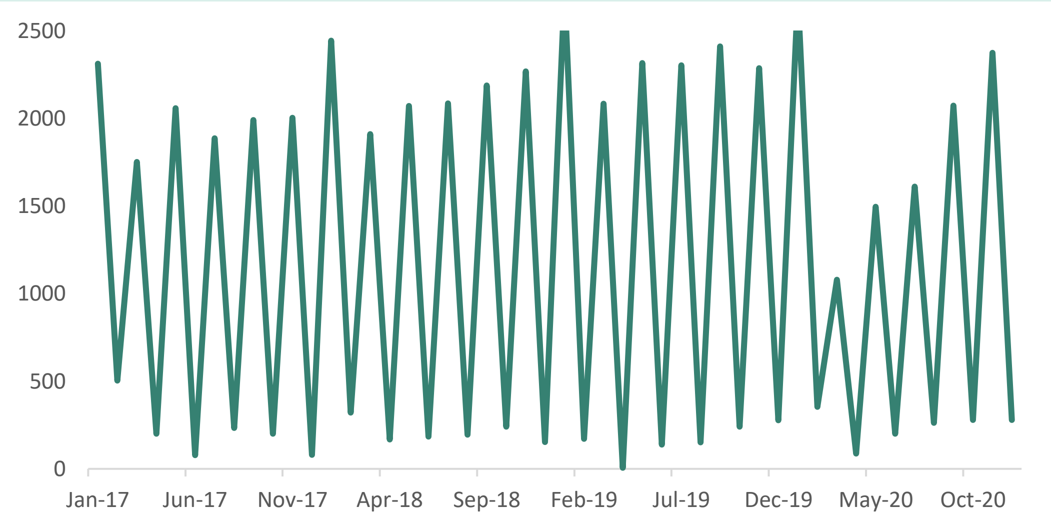
Revenue streams can vary significantly from month to month depending on the time of the year – and/or on expected variations in the timing of the year for economic transactions or tax payment dates. For example, high spending around Christmas boosts VAT receipts, as can be seen in Figure F.1 below, while November is the key month for Corporation tax receipts.

This can make it difficult to analyse underlying developments over time. The process of seasonal adjustment can be used to estimate and remove these various components of a time series dataset that often dominate the period-to-period changes, allowing for more reliable comparison of high-frequency datapoints. This has become critical during the Covid-19 crisis as the economic situation and policies have shifted rapidly.

The standard approach to assess these data has been to compare year-to-date figures between years to control for seasonal factors. Due to the sharp movements in activity this year, and multiple policy interventions, this approach is less reliable currently. This box sets out a method used by the Council in recent months to assist in analysing tax and spending by the Government when conditions have evolved quickly and when a clear interpretation of economic developments is vital.

Figure F.1: VAT outturns in Ireland

€ million



Source: Department of Finance.

Methodology

Two conditions should be met to consider seasonal adjustment. First, the time series dataset should ideally be at least five years long (Cholette, 1979), and, second, clear evidence of seasonality should be present.[54]

First, the data is preadjusted for missing observations, calendar effects, and other issues, before being disaggregated into estimated random and predictable components, such as seasonality, trend, and shocks. The relationship can be described as:

$$X_t = T_t + S_t + C_t + U_t$$

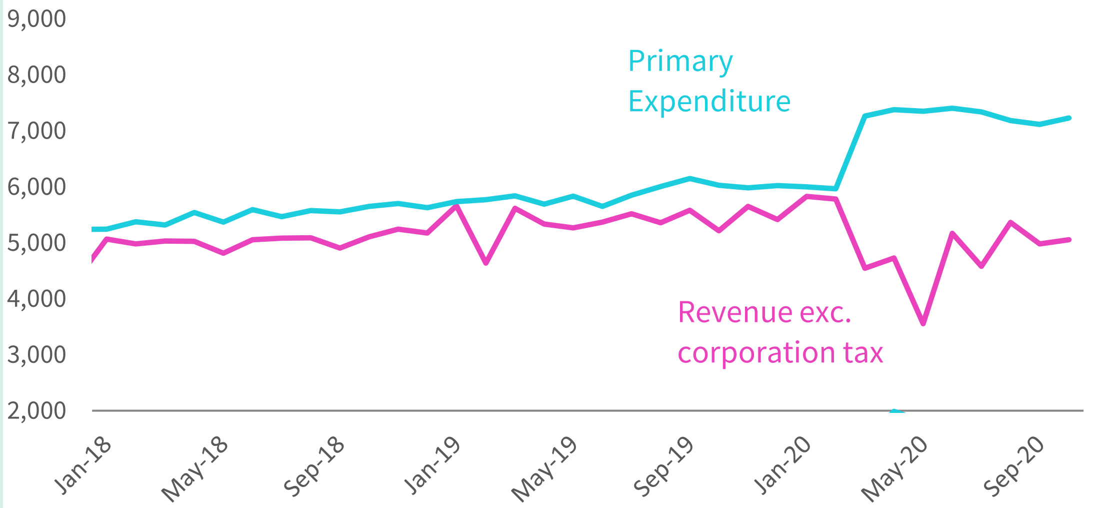
Where the original series is the sum of the trend (T), seasonal (S), calendar (C), and irregular components (U) respectively. The final seasonally adjusted series therefore is equal to the original series adjusted for both seasonal and calendar effects.

An Example: VAT returns in Ireland

Figure F.2 contains an illustrative example of isolating the components identified above, where Exchequer VAT returns from 2004 to the present day are decomposed using the TRAMO-SEATS method.[55] As can be seen above, the presence of trend, seasonal and irregular effects is clear. Much of the variation in this series can be attributed to the fact that VAT returns are due on a bi-monthly basis, leading to significant movements in the figures from month to month. However, consistently strong trend growth is observable alongside unexpected shocks.

Figure F.2: Seasonally adjusted revenue and primary expenditure

€ million



Source: Department of Finance and Fiscal Council workings.

Looking at 2020, the stop-start nature of economic activity since March, along with policy changes such as VAT forbearance and rate cuts has made standard comparisons such as between month-on-month or year-on-year outturns more difficult to interpret. For example, both Figures F.1 and F.3 show clearly the impact of the health restrictions on VAT intake, but with some significant differences. In the unadjusted case, VAT demonstrates predictable fluctuations as economic transactions become due. In normal times this would be less of an issue for interpreting the level of VAT returns but, with the economic policies taken in response to Covid-19, the usual correlations between months have broken down. Seasonally adjusted

[54] The IMF (2017b) recommends this for quarterly datasets, specifically Quarterly National Accounts.

[55] More information on this technique is available in Gómez and Maravall (1996).

returns, as seen below, allow us to have a more intuitive understanding of where the current level stands relative to previous outturns.

Insights for fiscal policy

By providing a more appropriate assessment of the underlying starting point, using seasonally adjusted data can help inform the path of future outturns.

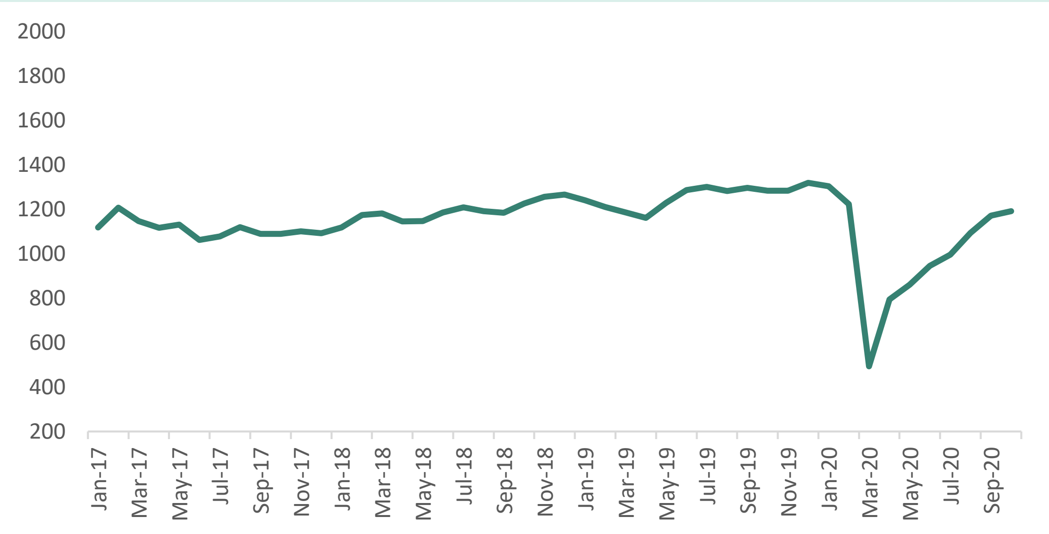
For example, on this basis, VAT in recent months is around 8.6% below the level in January. This provides a good starting point for making projections going forward. By contrast, the cumulative figure of 2020 is over 19% lower than the year before, but that does not provide a helpful guide to projecting forward as it is consistent with a wide range of levels.

For longer-term projections - even monthly profiles over a period of one year ahead for example - cumulative receipts and expenditures for a certain part of the year are often used to forecast. Clearly, such estimations can be contaminated by one off shocks, periods of above or-below trend growth, policy changes, or other factors. Applying the same process to both revenues and expenditures, as displayed in Figure F.2, can help inform an understanding of where the government's budget balance may settle in a given year.

Despite this, using seasonally adjusted data is not a panacea to understanding the underlying dynamics of the Government's finances. The process operates with a margin of error that can make precise estimations difficult. That said, it remains a valuable tool for analysts interested in evaluating rapidly changing economic situations.

Figure F.3: VAT outturns seasonally adjusted

€ million



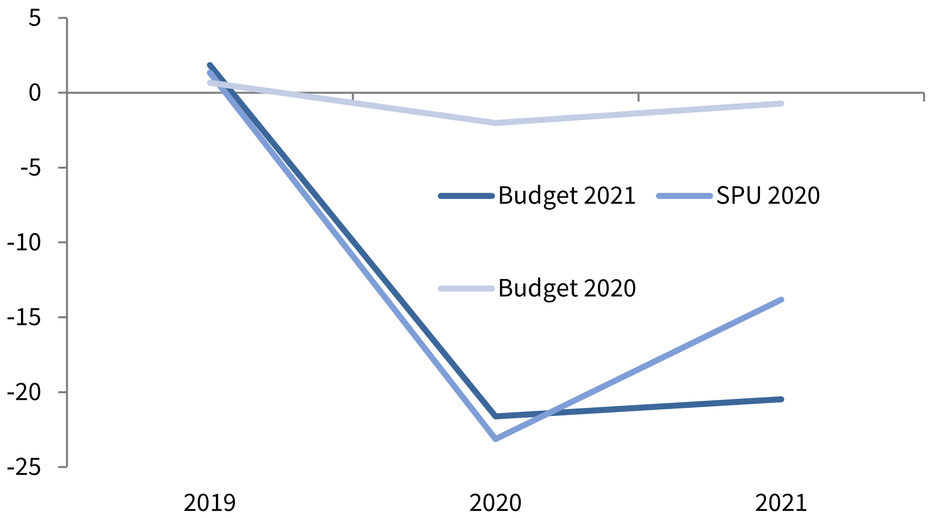
Sources: Department of Finance and Fiscal Council workings.

Budget balance, 2020 and 2021

Budget 2021 anticipates a **general government deficit** of €21.6 billion (10.7 per cent of GNI*) in 2020. To give a sense of the scale and speed of revisions, Figure 3.12 shows the last three forecasts of the general government balance.

Figure 3.12: Recent vintages of the general government balance

€ billion

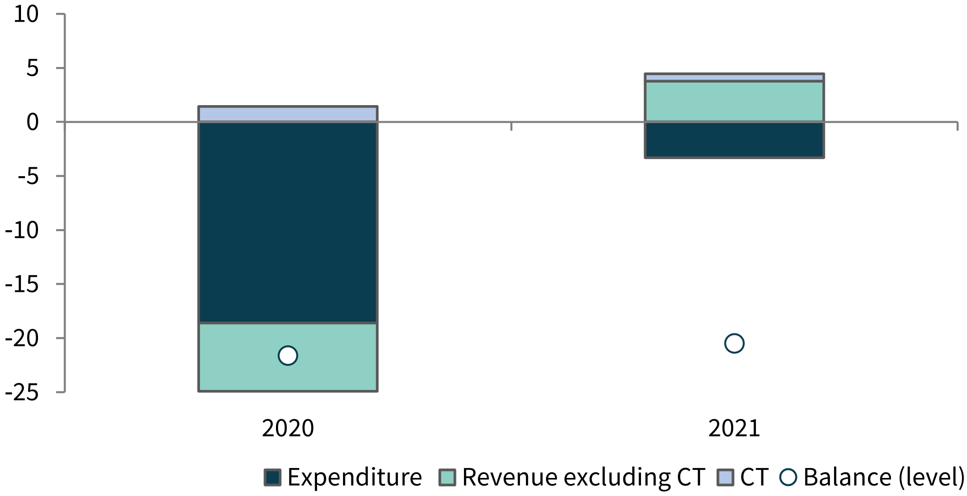


Sources: Department of Finance, and CSO. Get the data.
Note: One-offs are those assessed by the Council as applicable.

For 2021, a deficit of €20.5 billion (9.8 per cent of GNI*) is forecast in *Budget 2021*. This is only slightly lower than the 2020 forecast level. While spending is anticipated to increase further in 2021, Figure 3.13 shows that this will be largely offset by higher revenue. Whether the deficit does improve depends on many factors, including whether the outturn in 2020 is higher or lower than expected.

Figure 3.13: Expenditure and revenue contributing to changes in the general government balance

€ billion, annual change



Sources: Department of Finance, and CSO. Get the data.
Note: Changes in expenditure are recorded as their impact on the balance (i.e. expenditure increases are recorded as negative, as they worsen the balance). The level of the general government balance is also shown. CT refers to Corporation Tax.

3.4 Medium-term Fiscal Scenarios and Risk Analysis

Five-year-ahead fiscal projections, as usually provided in the Budget and SPU, are key to informing budgetary choices. With uncertainty exceptionally high, this section develops three fiscal scenarios out to 2025 that are consistent with the three scenarios set out in Chapter 2. The Extended *Budget 2021* scenario is designed so that it matches general government expenditure and revenue forecasts (for 2020 and 2021) published in *Budget 2021*. These scenarios reflect both different economic outcomes and the different policy measures required in each scenario, assuming that policy reactions are broadly in line with those to date.

The Extended *Budget 2021* and Milder scenarios do not take into account the six-week Level 5 restrictions which were announced after *Budget 2021* projections were made. As a result, projections for these two scenarios for 2020 may overstate revenue (unless tax receipts outperform) and understate expenditure. The Repeated Waves scenario does incorporate an assumed increase in restrictions in Q4 2020.

Box G: Policy Measures and Fiscal Scenarios

This box sets out three fiscal scenarios based on the macroeconomic scenarios set out in Chapter 2. These scenarios are based on the implementation of announced and existing policy measures. For periods of heightened confinement measures, it is assumed that the Government mobilises the same supports as have been used to date. For the Repeat Waves scenario, there are additional 8 week-long periods of heavy restrictions assumed for Q4 2020, Q2 2021, Q4 2021, Q2 2022 and Q4 2022. No vaccine is assumed to be widely available until Q1 2023. In the Milder scenario, a vaccine is assumed to be widely available and distributed by the middle of 2021.

We identify the Covid-19 related-expenditure budgeted for 2021 using data from the Expenditure report. For the Extended *Budget 2021* scenario, we assume that this expenditure is not carried forward into 2022 or beyond (when a vaccine is assumed to be widely available). As outlined earlier, this still implies a significant increase in permanent expenditure in 2021, which carries into 2022. In all three scenarios, this permanent increase in expenditure is reflected in forecasts of spending. However, in the short run, the amount of temporary Covid-19 spending varies between the three scenarios. For the Milder scenario, not all of the budgeted Covid-19-related expenditure is needed in 2021, as Covid-19 is controlled mid-way through the year. Conversely, in the Repeat Waves scenario, much of the Covid-19 spending continues into 2022, as described below.

Income supports/Unemployment payments.

In periods of heavy restrictions, we assume that the enhanced PUP and the EWSS are available. We base the costs of the EWSS on the published estimates of how much it is expected to cost for the recently announced 6-week period of heavy restrictions. This implied a cost of €340 million per month.

Four of the additional periods of heavy restrictions occur after Q1 2021, when the EWSS is assumed to have ended, hence the full cost is in addition to what is included in the Extended

Budget 2021 and Milder scenarios. In all other periods, those who are unemployed are assumed to receive the standard Jobseeker's Benefit/Jobseeker's Allowance payments. This is different from the policy employed since the beginning of the pandemic, but it is the basis on which *Budget 2021* forecasts were made. An obvious risk to spending levels is that these enhanced unemployment payment rates are extended beyond Q1 2021.

We assume that social welfare payments are indexed in line with private-sector wages after 2021. Pension expenditure (state pensions and public-sector pensions) is projected to increase by approximately €1 billion per year on average over 2022–2025. This is driven by both demographic change and increases in line with private sector wages. It is assumed that the statutory retirement age remains at 66 during the forecast horizon.

Health expenditure

We assume that the additional funding planned for health spending is sufficient in the Extended *Budget 2021* scenario. For the Milder scenario, we assume the same level of health expenditure in 2020 compared to the Extended *Budget 2021* scenario. For 2021, as a vaccine is assumed to be available in the middle of the year, we assume that Covid-19-related healthcare expenditure in 2021 is half of that in the Extended *Budget 2021* projections. This results in a saving of €1 billion, mainly assumed to be in intermediate consumption.

For the Repeat Waves scenario, we assume that each additional period of heavy restrictions implies additional healthcare costs of €0.5 billion per 8-week period in 2020 and 2021. We assume that in 2022 this cost halves, as some capacity and equipment has already been built up. As a result, for the Repeat Waves scenario, there is an additional €0.5 billion of health spending in Q4 2020, Q2 2021 and Q4 2021. For Q2 2022 and Q4 2022, there is additional health spending of €0.25 billion.

Beyond 2021, for all three scenarios, health spending is projected forward using Fiscal Council Stand-Still (Fiscal Council, 2019b) estimates (with the exception of the periods of heavy restrictions for the Repeated Waves scenario). These are estimates of the cost of maintaining 2021 service levels, after taking account of service demand (driven by demographics) and price pressures. In all scenarios, Covid-19 specific health spending is excluded from the base when projecting into the later years.

Business supports

For the Extended *Budget 2021* and Milder scenarios, it is assumed that loan guarantees do not lead to fiscal costs. As a result, the only costs incurred are the additional €0.13 billion in business supports which are included in *Budget 2021* projections.

The maximum amount of exposure to the State under the credit guarantee scheme is currently €2 billion. Under the Repeat waves scenario, we assume that business support schemes are expanded. Under these more adverse economic conditions, borrowers have a higher credit risk and subsequently large amounts of nonrepayment and default. As a result, €500 million of losses arise in 2023 and a further €1 billion in 2024.[56] There is risk outside the scenario that the State would have to intervene in other cases, potentially leading to higher costs.

Public pay bill

For the Extended *Budget 2021* scenario, *Budget 2021* forecasts of compensation of employees are used for 2020 and 2021. Thereafter, Fiscal Council Stand-Still Scenario estimates are used (Fiscal Council, 2019b). These take account of increases in public sector employment required to hold service levels constant in light of increasing demand due to demographic change.

[56] This does not include the non-repayment of warehoused tax liabilities. This is addressed below in the revenue section.

We account for some health staffing being considered temporary in 2021. This is quite small however, as most of the Covid-19-related health spending is understood to be on equipment (intermediate consumption in general government terms).

Pay rates are assumed to increase in line with private sector wages. There are slight differences between the three scenarios for the public sector pay bill, as inflation and private sector wage pressures differs in each of the three scenarios.

Capital spending

For the Extended *Budget 2021* and Repeat Waves scenarios, capital spending takes the values forecast in *Budget 2021* for 2020 and 2021. For the Milder scenario, capital spending is slightly lower in 2021 as some capital expenditure for 2021 is Covid-19 related.

After 2021, general government capital spending is assumed to be 4.4 per cent of GNI*. This reflects previous government plans to have Exchequer capital spending amounting to 4 per cent of GNI*. A further 0.4 percentage points of non-exchequer spending is assumed, with general government public investment assumed at 4.4 per cent.

As GNI* is different in each of three scenarios, this mechanically leads to different levels of capital expenditure in each of the three scenarios. In 2025, capital spending in the Milder scenario is projected to be €0.8 billion higher than in the Repeat Waves scenario.

Unallocated resources

Budget 2021 outlines that there are €5.5 billion of expenditure which is yet to be allocated to specific areas for 2021. This is in addition to the areas covered above. Specifically, €3.4 billion relates to the *Recovery Fund,* with the remaining €2.1 billion for other expenditure which may arise (Covid-19 Contingency Reserve). In the Extended *Budget 2021* and Repeat Waves scenario, it assumed that these resources are spent in full. For the Milder scenario, it is assumed that the Recovery fund is spent in full, with half of the Covid-19 contingency fund spent in 2021 (€1.05 billion). In the Repeat Waves scenario, it is assumed that the €2.1 billion of spending under the Covid-19 contingency fund is required in 2022 also.

Revenue

In terms of government revenue, we assume that there is no difference in policy between the three scenarios. In effect, this assumes that there are no major policy changes that yield or cost significant revenue, apart from those already announced in *Budget 2021*.[57]

We assume that the carbon tax is increased by €7.50 per tonne/CO2 every year out to 2025. We also assume this does not trigger major behavioural responses, hence the yield from each increase is the same as that given in *Budget 2021* documentation (€108 million in the initial year, €147 million in a full year).

Two temporary policy changes have been made to VAT. The temporary reduction to the higher rate of VAT (from 23 per cent to 21 per cent) is due to expire on 28th February 2021. For the three scenarios it is assumed that thereafter the rate reverts to its previous higher level. This leads to €160 million of extra receipts in 2023 and thereafter. The VAT rate applicable to tourism and hospitality sectors has been reduced from 13.5 per cent to 9 per cent. This is scheduled to revert at the end of 2021. For the three scenarios we assume that the lower rate is maintained out to 2025. Previous experience suggests that a temporary cut to this VAT rate can remain for much longer than anticipated. Were this VAT rate to revert to 13.5 per cent, it would yield approximately an additional €335 million of receipts annually from 2022 onwards.

Budget 2021 forecasts were made based on around €2 billion of warehousing of income tax and VAT in 2020. It is expected that about €1.5 billion of this will be recouped in 2021 and 2022,

[57] For income tax, beyond 2022, it is assumed that tax bands widened in line with wage rates. As a result, there is no yield from non-indexation beyond 2022.

with €0.5 billion proving to be non- recoverable. In the Repeat Waves scenario, we assume that an additional €0.5 billion is not recovered in 2021/2.

Changes in the macroeconomic driver multiplied by the elasticity are used for projections of revenue. Judgement applied to forecasts in 2020 and 2021 is assumed to unwind over the following two years. As a result, there is no judgement applied for 2024 or 2025 (apart from corporation tax).

For income tax, receipts in 2020 fell much less sharply than developments in income combined with a standard elasticity would have suggested. This reflects the distributional pattern of job losses to date which have been focused in lower paid sectors. In effect, this means the actual elasticity which is applying to income tax receipts is much lower than would typically be the case. When employment and income recovers, one might expect a similarly low elasticity to apply.

To incorporate this formally, we use three different elasticities to project income tax. We use a low elasticity (60 per cent lower than standard) when unemployment is high. We use a slightly higher elasticity when unemployment recovers somewhat. Finally, when unemployment gets close to pre pandemic levels, the standard elasticity applies.[58]

Corporation Tax

Judgement is applied to corporation tax receipts after 2021. This is to take account of the possible impact of the OECD's BEPS initiative. The amount of judgement applied is based on the estimates given in the *January 2020 Fiscal Strategy* published by the Department of Finance (2020b). Corporation tax receipts are reduced relative to the baseline level by €0.5 billion in 2022, €1 billion in 2023, €1.5 billion in 2024, and €2 billion in 2025.

In addition to the BEPS based judgement, further negative judgement of a similar quantity is also applied to corporation tax receipts. This is a prudent approach that aims to reflect the risk of a gradual loss of some of the corporation tax receipts that might be considered "excess" relative to domestic economic growth. Fiscal Council (2020a) showed that up to €5.4 billion of 2019 corporation tax receipts could be considered excess. Despite this negative judgement, corporation tax receipts are projected to stay relatively flat (from 2020) in the extended *Budget 2021* scenario.[59]

Budget dynamics and interest costs

An interest model nested in the Council's Fiscal Feedbacks Model was used to generate interest projections, with the assumption that marginal interest costs were about 1 per cent in each scenario. This is an increase relative to current levels (with Irish ten-year bond yields averaging -0.5 per cent over the past three months) and, hence, is a somewhat prudent assumption.

While there are upside risks to this assumption for more severe scenarios, more accommodative monetary policy would also be possible in those scenarios, which would be expected to drive down interest rates. The Extended *Budget 2021* and Repeat Waves scenarios mirror projected interest costs for 2020 and 2021, while the Milder scenario has lower costs for 2021.

[58] Income tax receipts in 2022 are forecast to surpass 2019 levels in the Extended *Budget 2021* scenario. This is consistent with the projection that nominal non-agricultural income will exceed its 2019 level in 2022.

[59] Despite the negative judgement applied, 2025 levels of corporation tax in the Extended *Budget 2021* scenario are €0.7 billion higher than was the case in the central scenario in the May 2020 Fiscal Assessment Report.

Expenditure

The three scenarios show that there is still some uncertainty surrounding the level of expenditure for 2020. For 2021, there is much greater uncertainty around expenditure, with projections from the three scenarios ranging from €105.0 billion to €114.8 billion.

In the Milder case, the economy recovers quite rapidly after Q2 2021. As a result, reduced unemployment results in falling social payments in 2021, and enhanced income supports such as the PUP and EWSS end as scheduled in Q1 2021. Only €4.5 billion of the €5.5 billion of unallocated resources (in *Budget 2021*) for 2021 is spent (in addition to all of other schemes mentioned). In addition, half of the 2021 Covid-19-specific health spending budgeted for in *Budget 2021* is assumed not to occur in the Milder scenario (resulting in spending being €1 billion lower). While the Milder scenario assumes a less severe Brexit, there is no assumed reduction in spending to prepare for Brexit. This is because such spending is assumed to be planned and committed to before the final outcome of negotiations is known.

From 2022 onward, spending in the Milder scenario is driven mainly by demographics and price pressures, given by the Fiscal Council's "Stand-Still" estimates (Fiscal Council, 2019b). An ageing population results in higher spending, particularly in areas such as pensions and health (increasing by almost €2.5 billion per annum over 2022–2025). Some savings on social payments are made as unemployment continues to gradually fall, from 6.3 per cent in 2022 to just under 5 per cent in 2025. Primary spending growth averages 4.3 per cent over 2023–2025.

In the Repeat Waves scenario, the unemployment rate averages almost 16 per cent in 2021. This leads to significantly higher spending on social payments and subsidies (€14.4 billion higher than 2019). There is also additional health spending of €500 million relative to the Extended *Budget 2021* scenario.

Expenditure in the Repeat Waves scenario falls in 2022, as the unemployment rate falls below 13 per cent. As unemployment continues to fall over 2023–2025, this partially offsets spending increases in other areas in line with demographics and price pressures. Due to the rising level of debt, interest costs rise in 2022 and 2023, before falling thereafter.

Expenditure in all three scenarios converges to a similar level by the end of the forecast horizon (Table 3.10). This reflects the assumption that additional spending is largely mobilised in the short term to tackle direct Covid-19 effects. The differing expenditure profiles incorporates differences in terms of Covid-19- related expenditure unwinding at different stages depending on the scenario. The Milder scenario gives a faster fall in expenditure in 2021 and 2022 as a result. Unemployment stays higher for longer in the Repeat Waves scenario. Savings from unemployment falling in the later years leads to more modest spending growth in 2023–2025 than is the case in the other scenarios.

Table 3.10: Expenditure, Revenue and Balance under the three Scenarios

€ billion

	2019	2020	2021	2022	2023	2024	2025
Expenditure							
Milder	87.3	105.9	105.0	98.9	102.6	106.5	109.8
Extended *Budget 2021*	87.3	105.9	109.2	99.4	102.6	106.3	109.6
Repeat Waves	87.3	107.1	114.8	107.7	104.4	108.0	110.2
Revenue							
Milder	89.1	84.2	91.0	96.4	101.3	105.7	110.5
Extended *Budget 2021*	89.1	84.2	88.7	92.4	96.2	100.0	104.2
Repeat Waves	89.1	83.1	81.6	85.1	88.6	91.3	94.1
Balance							
Milder	1.9	-21.6	-14.0	-2.5	-1.4	-0.8	0.7
Extended *Budget 2021*	1.9	-21.6	-20.5	-7.0	-6.4	-6.3	-5.4
Repeat Waves	1.9	-24.0	-33.2	-22.5	-15.8	-16.7	-16.1

Sources: CSO; *Budget 2021*, and Fiscal Council workings.
Notes: The three scenarios are as outlined in Box D in Ch2.

Revenue

General government revenue falls in all scenarios but recovers at different speeds. For 2020 and 2021, the *Budget 2021* forecasts of Exchequer tax and general government revenue are used for the Extended *Budget 2021* scenario.

In the Milder scenario, the recovery assumed in 2021 yields an increase in receipts of €6.7 billion, meaning revenue exceeds its 2019 level (Table 3.10). Increases in employment and wage rates yield increased income tax receipts. Revenue growth moderates thereafter, averaging 4.7 per cent over 2023–2025.

Table 3.11: Revenue by heading and scenario

€ billion

	2019	2020	2021
Income tax			
Milder	22.9	21.5	23.1
Extended *Budget 2021*	22.9	21.5	22.7
Repeat Waves	22.9	21.5	20.5
VAT			
Milder	15.1	12.8	14.3
Extended *Budget 2021*	15.1	12.8	13.9
Repeat Waves	15.1	12.3	12.5
Corporation tax			
Milder	10.9	12.3	13.5
Extended *Budget 2021*	10.9	12.3	13.0
Repeat Waves	10.9	12.2	12.4
All other gen govt. revenue			
Milder	40.2	37.6	40.1
Extended *Budget 2021*	40.2	37.6	39.0
Repeat Waves	40.2	37.1	36.2

Sources: CSO; *Budget 2021,* and Fiscal Council workings.

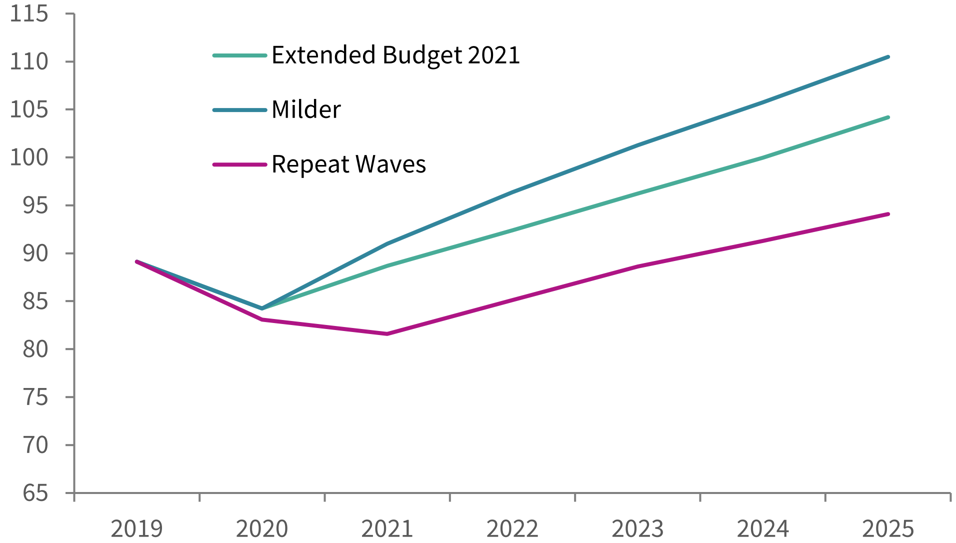
Notes: Three scenarios are considered in this exercise. They are as outlined in Box D in Ch2.

In the Extended *Budget 2021* scenario, the gradual recovery of employment income and consumption leads to strong revenue growth (averaging 4.7 per cent over 2021 and 2022). Despite this, general government revenue does not exceed 2019 levels until 2022. Thereafter, revenue growth slows to an average of 4.1 per cent (2023 to 2025).

Under the Repeat Waves scenario, general government revenue recovers far more slowly, not exceeding 2019 levels until 2024 (Figure 3.14). The lower potential growth rate in the Repeat Waves scenario (0.5 percentage points lower relative to the Extended *Budget 2021* or Milder cases) is reflected in slower revenue growth in 2024 and 2025 (3.0 per cent on average as opposed to 4.1 per cent in the Extended *Budget 2021* scenario).

Figure 3.14: General government revenue under three scenarios

€ billion



Sources: *Budget 2021*, and Fiscal Council workings. Get the data.

Budget Balance

Figure 3.15 shows the general government balance under the three scenarios. As outlined earlier, these scenarios assume no major tax policy changes (except for VAT and the carbon tax as detailed in Box G). Spending over the medium term reflects Covid-19-related expenditures along with the estimated costs of holding service levels constant, while accommodating price pressures. Were a further/increased fiscal stimulus package introduced in the coming years, this would likely result in higher spending and a deterioration of the balance, while fiscal adjustment in later years could improve the balance.[60]

All three scenarios are more favourable than those presented in the May Fiscal Assessment Report (Fiscal Council, 2020a). While there are a number of differences in the assumptions, the main difference is that the starting point for revenue in 2020 is likely to be significantly better than originally assumed. This largely reflects unexpected improvements in corporation tax receipts and the better than expected performance of the economy.[61]

[60] Increases in spending above those needed to maintain current service levels would also have negative implications for the general government balance (relative to those shown here).

[61] Other tax heads, notably income tax, have been more robust than expected but this will likely lead to a shallower recovery so there is less of an impact in the later years of the projections.

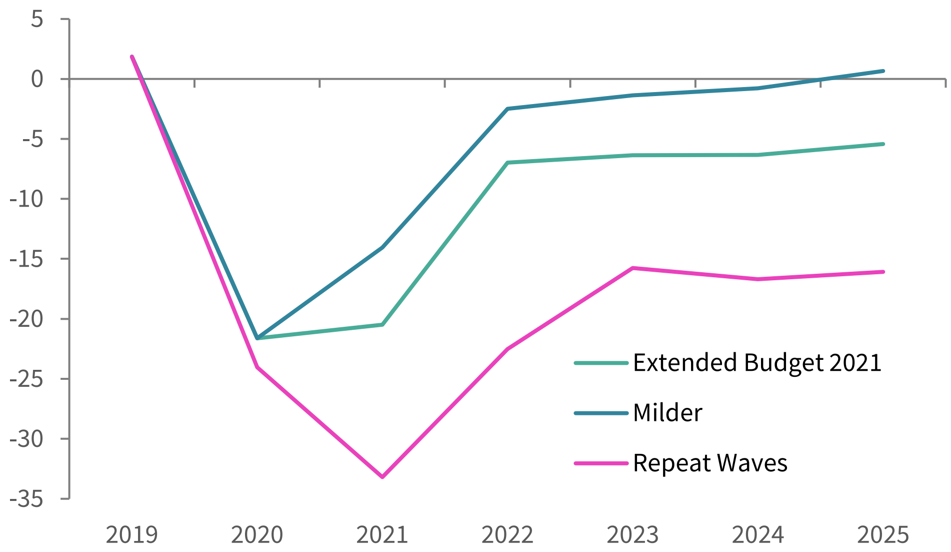
The Milder scenario shows a rapid improvement in the general government balance in 2021 and 2022. This leaves a small deficit in 2022 of 1.1 per cent, which improves to a position of surplus in 2025 (0.3 per cent of GNI*).

The Extended *Budget 2021* scenario shows a modest improvement in the budget balance in 2021. In 2022, there is a more significant fiscal improvement as unemployment and Covid-19-related expenditure falls. The balance improves at a more modest rate thereafter, with the deficit at 2.1 per cent of GNI* by 2025.

The Repeat Waves scenario shows a further deterioration of the general government balance in 2021, mainly driven by increased spending. A slow recovery thereafter leads to substantial deficits being run out to 2025 (where a deficit of more than 6.5 per cent of GNI* is projected).

Figure 3.15: General government balance under three scenarios

€ billion

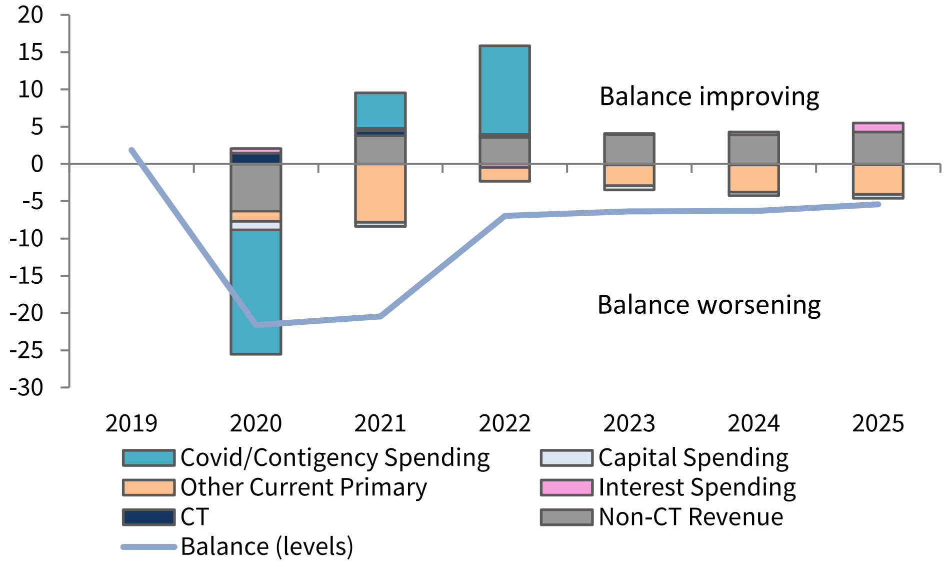


Sources: *Budget 2021,* and Fiscal Council workings. Get the data.

Figure 3.16 shows the contributions to the change in the general government balance in the Extended *Budget 2021* scenario. The deterioration in the balance in 2020 is caused by both Covid-19-related expenditure and falling revenue (excluding corporation tax). While Covid-19 spending falls and revenue increases in 2021, this is offset by increases in other current spending. 2022 sees a large improvement in the balance. This is driven by Covid-19-related expenditure falling along with increases in revenue. Changes in the balance thereafter are modest, with increases in revenue largely being offset by increases in current primary spending. This reflects the substantial costs in maintaining public service levels due to demographics and price pressures.

Figure 3.16: Contributions to the change in the General government balance

€ billion, Extended *Budget 2021* scenario, year-on-year change



Sources: *Budget 2021*; and Fiscal Council workings. Get the data.

Notes: Covid/Contingency Spending includes the Covid-19 Contingency Reserve (€2.1 billion) and the Recovery Fund (€3.4 billion) in 2021. Positive values correspond to balance improving items (increasing revenue or falling expenditure). Negative values represent balance worsening items (falling revenue or increasing expenditure).

General government debt

While the *Stability and Growth Pact* reference value of 60 per cent is set in terms of debt-to-GDP, it is worth remembering that for Ireland this 60 per cent of GDP reference value would be equivalent to 100 per cent of GNI* (using 2019 nominal outturns for both variables).[62]

Budget 2021 anticipates the debt ratio will rise to 107.8 percent of GNI* in 2020 due to the large deficit. In addition to the absolute level of debt increasing, national income is forecast to fall in 2020. Both numerator and denominator effects contribute to the debt to GNI* ratio increasing sharply.

The debt to GNI* ratio is forecast to increase further in 2021 to 114.7 per cent. While a recovery in GNI* tends to lower the ratio, the increase in the absolute level of debt in 2021 dominates.

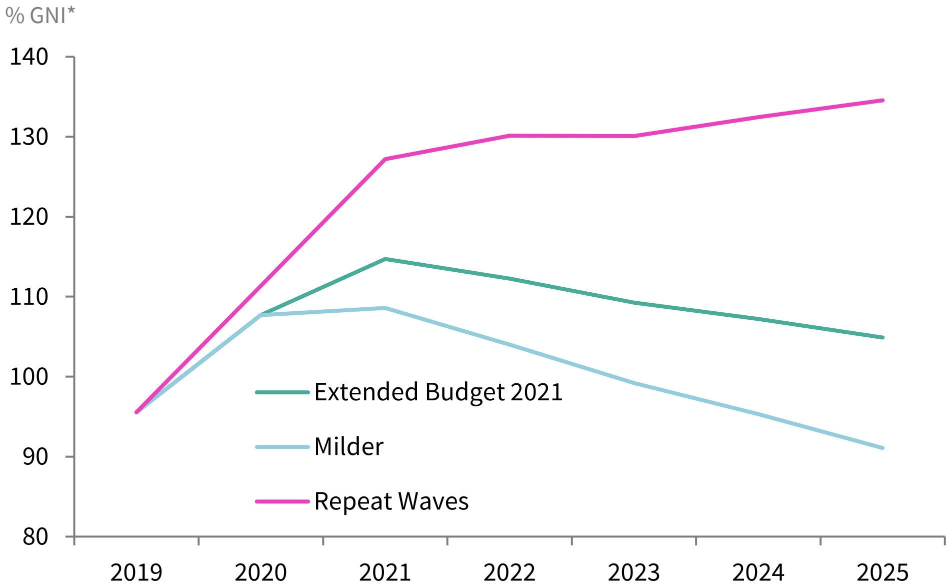
[62] Gross general government debt fell below 60 per cent of GDP in 2019.

Figure 3.17 shows general government debt to GNI* for the Milder, Extended *Budget 2021* and Repeat Waves Scenarios out to 2025. These are consistent with the different scenarios for the general government balance shown in Figure 3.15.

In the Milder scenario, after an initial increase in 2020, the ratio stabilises and then declines. As a result, the debt to GNI* ratio reaches a lower level in 2025 (91.1 per cent) than in 2019 (95.6 per cent). The Extended *Budget 2021* scenario mirrors *Budget 2021* forecasts for 2020 and 2021. Thereafter, the ratio is projected to fall gradually to about 105 per cent by 2025.[63]

In the Repeat Waves scenario, the debt to GNI* ratio increases sharply in 2020 and 2021. Thereafter, the ratio increases more gradually, almost reaching 135 per cent of GNI* by 2025. Without policy action, the debt ratio increases throughout the forecast period and is at a high level.

Figure 3.17: General government debt



Sources: *Budget 2021* and Fiscal Council workings. Get the data.
Notes: Scenarios are outlined in Boxes D and G.

[63] Unlike in the May Fiscal Assessment Report, the improvement in growth is sufficient to put the debt GNI* ratio on a downwards trajectory.