induced travel restrictions ease, the timing of this has important implications for economic growth over the medium-to-long term.

Box A: Excess household savings could substantially boost economic activity

Irish households saved €29.6 billion in 2020. This was close to a quarter of total disposable income, double the gross savings in 2019, and quadruple the corresponding 2016 amount. Last year included a record-high €11.8 billion (37 per cent) in the second quarter alone, much of this down to restrictions and the sudden changes to everyday life caused by the pandemic.

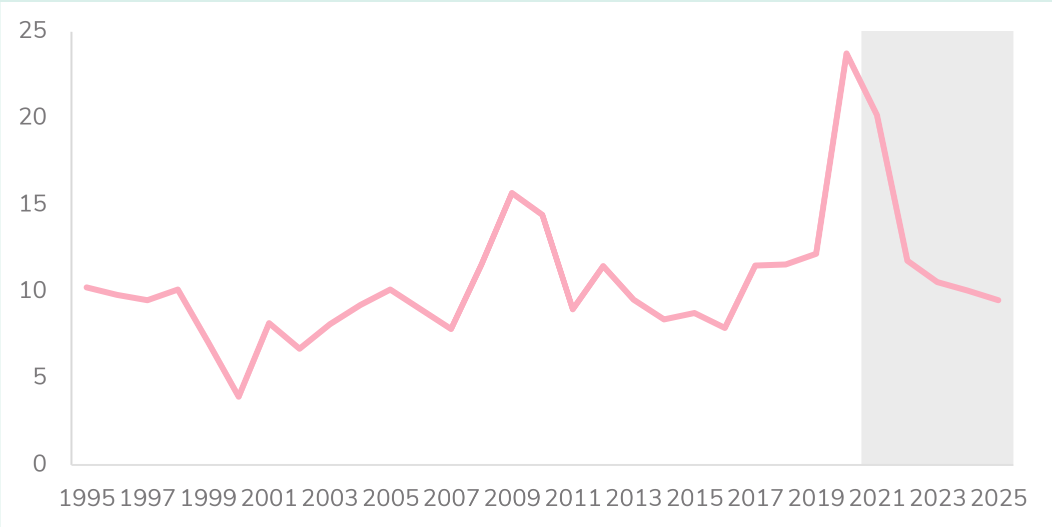
This box first assesses how much of the savings in 2020 were "excess" due to the pandemic, before analysing what an unwinding of these excess savings would imply for consumer spending and imports. If half of the excess savings were spent in the short term, this could add up to 2 per cent to household consumption. Based on the expected usage of excess savings, it is likely that the vast majority of what is consumed will contribute directly to the Irish economy (i.e., to GNI*). This reflects the relatively low import share of the activities most affected by the pandemic.

Assessing excess savings in 2020

Figure A1 presents Ireland's household savings ratio since 1995, supplemented with *SPU 2021* forecasts. The increase in savings in 2020 far exceeds any previous increase over recent decades. Although large increases in savings were observed in other countries across the developed world in 2020, Ireland's increase stands out as the highest among OECD countries.[8]

Figure A1: Household savings rose to 24 per cent of disposable income in 2020

Household savings as a percentage of gross disposable income



Source: CSO; and Department of Finance, SPU 2021.

One challenge for assessing excess savings is that the savings rate rose sharply to a higher level in 2017 before remaining well above its long-term average. The reasons for this shift are unclear. It could be related to some precautionary saving following the Brexit referendum, the impact of higher deposit requirements for mortgages, or the impact of an ageing population. This uncertainty makes it harder to assess what a "normal" post-Brexit savings rate would be.

A benchmark estimate of excess savings in 2020 can be found by applying the same savings ratio in 2019 to 2020 household gross disposable income. In this scenario, households would have

[8] Many factors could contribute to this relatively high saving in an international context including the support by Government to household incomes and the extent of restrictions during lockdowns.

saved €15 billion less in 2020. Lydon and McIndoe-Calder (2021), applying a more sophisticated methodology, recently estimated that €11 billion of excess savings were accumulated by Irish households in 2020 as a result of the pandemic.

Using CSO *Household Budget Survey* data across the distribution of income to identify typical spending in restricted parts of the economy, Lydon and McIndoe-Calder estimate that half of excess pandemic savings could have been accumulated by the top three deciles by household income. Although households with higher income generally have lower marginal propensities to consume, the authors note that this is not necessarily the case for transitory or unexpected income. They also cite evidence from the CSO's *Household Finance and Consumption Survey 2018* and suggest that at least half of excess pandemic savings could be spent on consumption over the coming years. This is based on responses to the survey about expectations for spending versus saving in the event of winning one month of household income in a lottery.

In a typical downturn, savings rise largely due to precautionary motives, and this is undoubtedly a factor for many Irish households over the past year. However, given the concentration of job losses due to the pandemic among younger workers and those employed in sectors with lower earnings, it is likely that the rise in savings has instead been driven by households whose incomes were not directly affected thus far.[9] This is more likely to reflect pent-up demand related to Covid-19 restrictions on activities and mobility.

What could an unwinding of excess savings imply for consumption?

The pace at which excess savings are unwound in a re-opening is an important factor in the economic recovery from the shock of Covid-19. Much uncertainty remains over the strength and timing of a savings-driven boost to personal consumption expenditure, and indeed the ability of businesses to accommodate higher demand after a long year of disruptions caused by the pandemic.

Nonetheless, assuming that half of €11-15 billion in excess savings will be spent by consumers in 2021 and 2022, this would represent an upside risk to *SPU 2021* forecasts, which only factor in about €2½ billion of consumption out of excess savings.[10] If a higher figure such as €6.5 billion (the mid-point of €5.5–7.5 billion) is assumed to be spent, this could add up to 1.5 per cent to the level of consumption across 2021 and 2022. In terms of the savings ratio, this would imply a temporary reduction of 2 percentage points on average across 2021 and 2022 — albeit this would still mean a high household savings ratio this year.

While some households have paid down debts or replaced durable goods, it is likely that most households will increase their spending on higher-priced services in a re-opening of the economy. These services include restaurant dining, hotel accommodation, and entertainment (such as theatre, music, or sporting events). However, goods consumption could also rise, given non-essential retail has now re-opened. While some forms of missed spending due to the pandemic will not be recovered due to inability to substitute over time, Lydon and McIndoe-Calder note that additional spending by households on a broader basket of goods and services, or more expensive alternatives within an unchanged basket, cannot be ruled out.

What is the likely import share of higher consumption?

One aspect of the overall gains arising due to any increase in personal consumption in Ireland concerns the import content of the goods and services. For decades, globalisation and technological change have seen an increasing number and volume of imported goods and services available to consumers in Ireland. As a small open economy reliant on trading partners abroad for many everyday products — for example, cars are not manufactured in Ireland and therefore must be imported — it appears reasonable to assume that the import content of households' final

[9] Lydon and McIndoe-Calder (2021) observe the correlation between tightening and loosening of Covid-19 restrictions with daily cards and ATM spending, concluding that excess savings are more likely to resemble "additional income" rather than precautionary savings.

[10] This lower expected amount by the Department reflects recent KBC survey evidence.

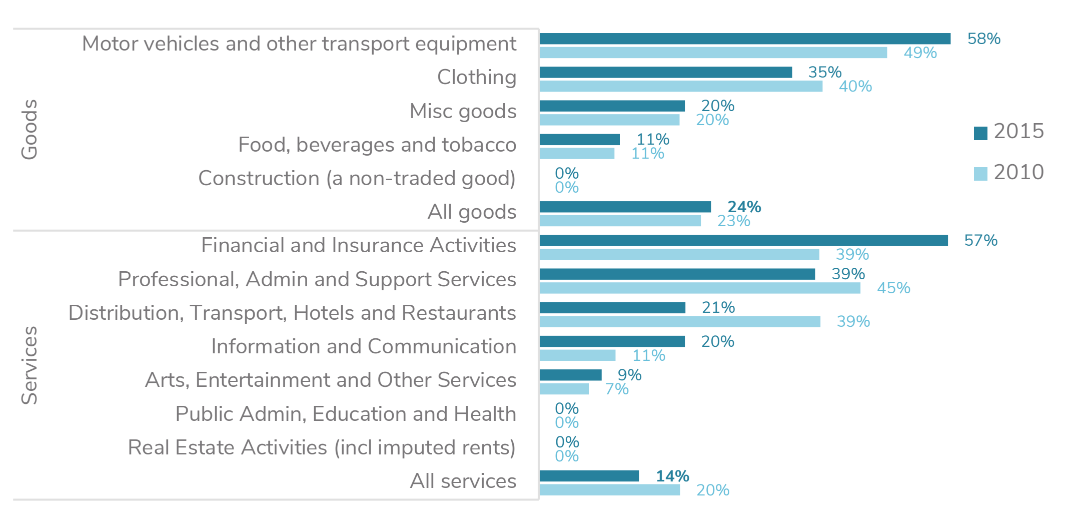
consumption expenditure is high. However, the import content of final consumption expenditure appears to be less than 20 per cent.

Most consumer goods in Ireland are imported. However, only a small share of the value of consumer spending on goods is spent on imports overall. This reflects the inclusion of the cost of government product taxes on consumer goods (such as Value Added Tax) and the costs charged for wholesale and retail services. In 2015, 58 per cent of consumer spending on goods was on imports before product taxes and markups of wholesalers and retailers were taken into account. However, once these were included, only 24 per cent of consumer spending on goods was spent on imports (little changed from 2010), with 34 per cent of consumer spending on goods going to the Exchequer and domestic wholesalers and retailers.

Figure A2 compares the import contents of selected final household consumption categories based on data from the CSO's Input-Output Tables for 2010 and 2015.[11] The chart shows that the highest import content has remained motor vehicles including other transport equipment (58 per cent in 2015, from 49 per cent in 2010), while other largely imported items include financial and insurance services (57 per cent), professional, administrative and support services (39 per cent), and clothing (35 per cent).

Figure A2: How much final consumption expenditure is imported

% of final household consumption expenditure



Source: CSO, Supply and Use and Input-Output Tables 2010 and 2015; and Fiscal Council workings.

Overall, services consumption is shown to have an average import content of 14 per cent, down from 20 per cent in 2010. (As noted above, goods consumption is somewhat higher at 24 per cent, little changed from 2010). For the sectors within services consumption worst affected by Covid-19 — distribution, transport, hotels, and restaurants; and arts, entertainment, and other services — the combined import content is 18 per cent, meaning most of the increase in consumption on these activities contributes directly to national income.

It is also likely that some households will use savings for investment purposes, such as home renovations, or as a deposit for a house purchase. Although related products for such usage of savings have relatively high import shares — for example, financial and insurance services — the direct import share of a new house purchase as it affects consumption is zero given construction

[11] This uses the imports at basic prices attributed to households by two-digit CPA product code, as a share of final household consumption expenditure at purchasers' prices (reflecting margins earned by wholesalers/retailers, and product taxes such as value-added tax — we thank Eóin Flaherty in the CSO for assistance with interpreting these data).

and real estate services (including imputed rents) are not traded. However, investment spending on such products requires significant imports of indirect inputs such as steel.[12]

If excess savings are instead utilised to go on holidays abroad, this would effectively extinguish the benefit to the Irish economy of these savings. Although holidays overseas count directly towards personal consumption expenditure, the import content of this spending is very high, and the income and activity is gained by the destination abroad.

However, the return of overseas trips to Ireland can partly offset this effect, aided by high-spending visitors (especially those from the US), and visiting emigrants. Virus fears and the current impracticality of international travel due to quarantine and other restrictions mean that pent-up demand for travel to and from Ireland is likely to be significant over coming years. As noted by FitzGerald (2021), a relevant precedent for this dynamic is the exceptional number of visitors to Ireland following World War II.

Construction has been disrupted by the pandemic, with the outlook for non-residential construction uncertain

Investment in building and construction has been significantly disrupted by the pandemic. Lockdowns have prevented the completion of ongoing construction projects, while commencements of new units have slowed significantly. Nonetheless, demand for residential construction in Ireland remains strong, and the sector has been quite agile in responding rapidly once restrictions have eased. The Department forecasts a fall in new dwelling completions to 18,000 units in 2021 and 20,000 in 2022, compared to the 21,000 units completed in 2020. However, as discussed in Section 1.1, completions were reasonably strong in the first quarter despite Level 5 restrictions being in place for the quarter. This could imply a faster delivery of new dwellings than is forecast, especially if excess savings are channelled into housing investment.

However, the outlook is far more uncertain for non-residential construction. This is due to its high share in total output (10 per cent of GNI*) prior to the pandemic, and the possibility that construction of office units may scale back considerably as a result of the pandemic and its lasting impact on remote working. In contrast, the Government's fiscal projections indicate a large ramp-up in public investment (see Figure 2.6). Depending on the extent of delivery, this could make up for some of the likely reductions in office building over the coming years.

[12] The expenditure-side components of modified gross national income (GNI*) reflect final goods and services, and the allocation of imports between the components of final demand determines the import content of each of consumption, investment, and exports. However, a higher import content for investment and intermediate consumption is relevant for multiplier effects of increased domestic demand; all else equal, a country with greater domestic industrial capacity will benefit more from higher demand if this results in larger spillover effects for the domestic value chain.