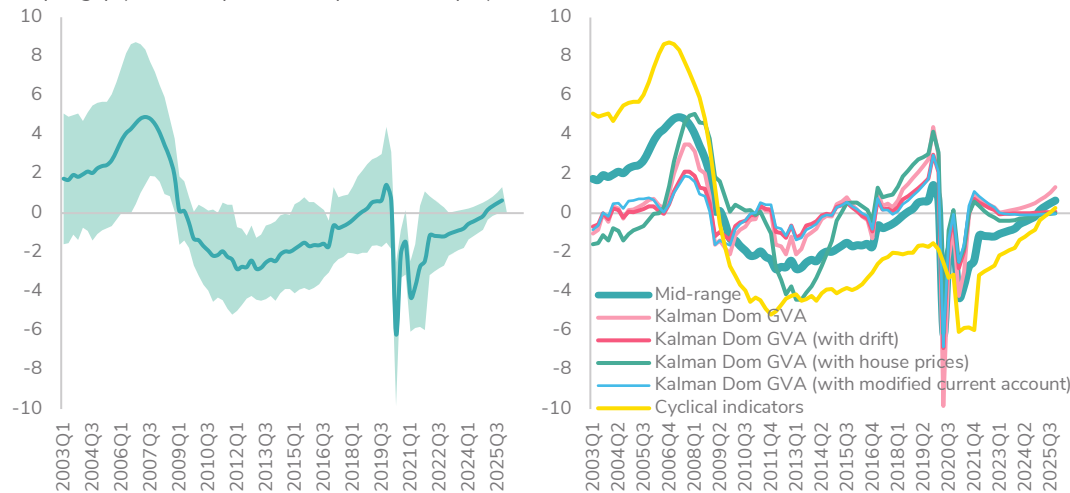


S3. The cycle and imbalances

This section looks at estimates of the Irish cycle and potential imbalances in the Irish economy. Estimates of the cycle are based on the Council’s models, which primarily focus on Domestic Gross Value Added — a measure of domestic economic activity that strips out sectors dominated by foreign-owned multinationals (see Casey, 2019). Potential output is the maximum level of economic output sustainable where output is not unduly influenced by external, domestic or financial economic imbalances. The output gap is the gap between actual output and its potential.

Council’s output gap models

Output gap (actual output as % of potential output)

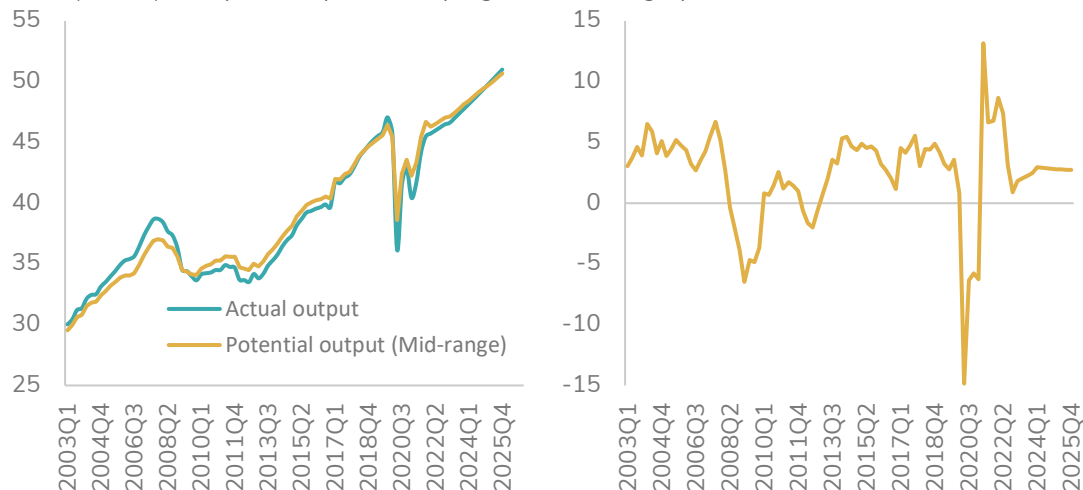


Sources: Fiscal Council workings.

Notes: Fiscal Council models of the output gap are applied to the Department’s SPU 2021 forecasts.

Council’s estimates of potential output

Levels (€ billion) in left panel and potential output growth rates in right panel



Sources: Fiscal Council workings.

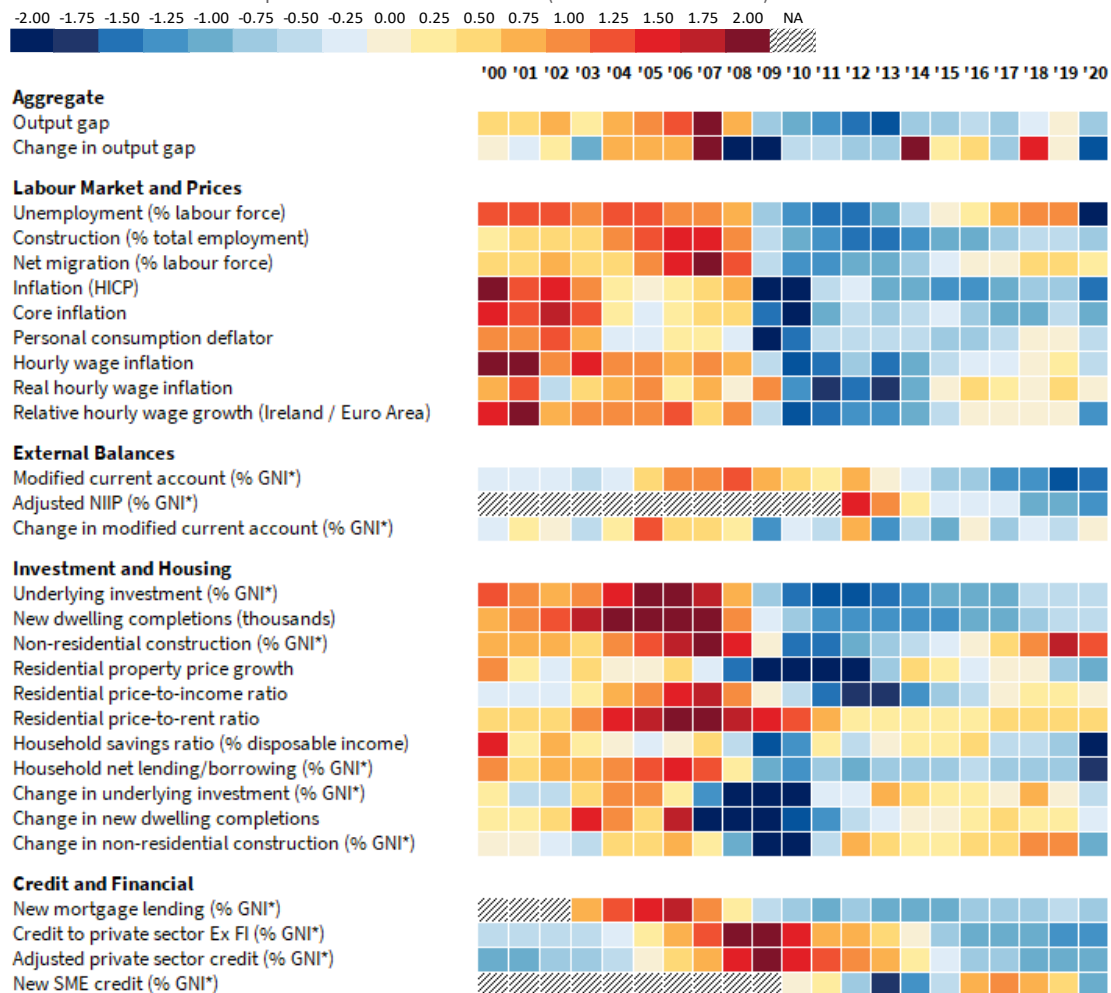
Notes: Fiscal Council models of the output gap are applied to the Department’s SPU 2021 forecasts.

As well as producing estimates of the cycle, the Council monitors potential economic imbalances that might be overlooked by single indicators like output gaps. It focuses on four areas in particular: (1) the labour market and prices; (2) Ireland’s external balances with the rest of the world; (3) investment and housing; and (4) financial conditions.

The following heat map assesses potential imbalances across four areas based on their departure from historical norms. Colder (bluer) indicators suggest spare capacity, while hotter (redder) suggest potential overheating or other imbalances.

Heat map of economic imbalances

Tiles show the extent of departure from historical norms (in standard deviations)



Sources: The main sources for the data underpinning the table are the CSO; Central Bank of Ireland; Department of Finance; and Fiscal Council workings. For more information on the data used and basis for deriving the heat map, see Timoney and Casey (2018).