



# Irish Fiscal Advisory Council

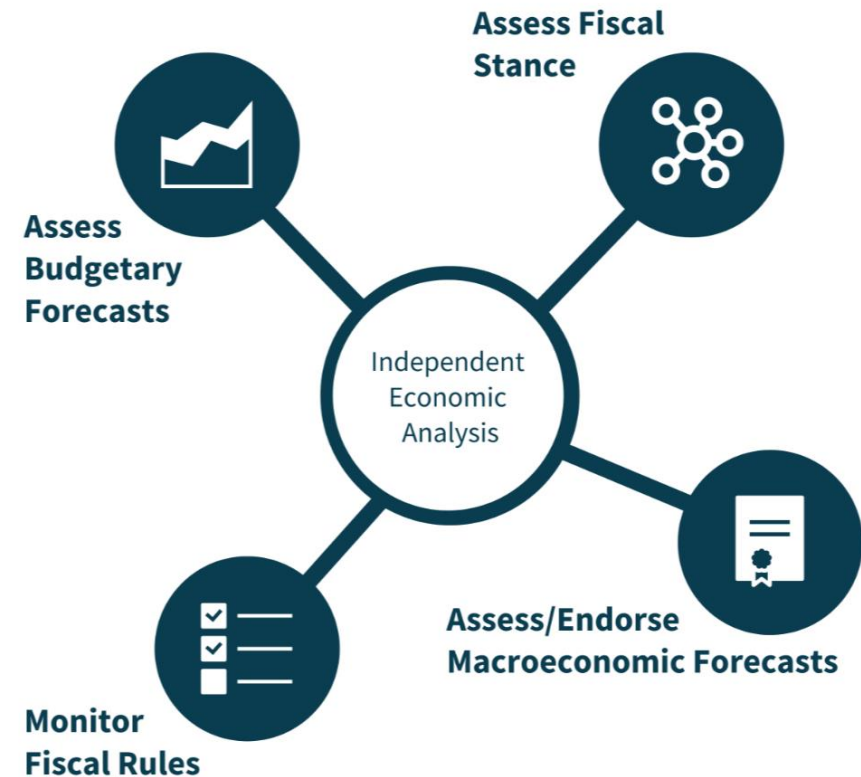
## **Fiscal Assessment Report**

*Managing the recovery*

December 2021

# Background

- The Fiscal Council is an official independent body with a mandate to assess the public finances
- The December 2021 *Fiscal Assessment Report* provides an assessment of Budget 2022 published in October.





# **Key messages**

# Key messages

## The economy is continuing to recover

- Pre-crisis levels of underlying activity were reached in the second quarter of 2021, but the recovery is uneven
- The economy is expected to grow at around 3% in the medium-term
- There are risks around the Government's investment plans due to capacity constraints
- Risks around the *Budget 2022* growth projections are broadly balanced

## *Budget 2022* forecasts a sharp narrowing of the deficit to 5.9% of GNI\* in 2021

- The deficit could ultimately be narrower due to higher revenue and underspends

## The Government's medium-term framework is welcome

- A spending rule sets current spending to grow at potential, assumed to be 5%, which would lower the debt ratio
- The medium-term forecasts based on the "Existing Level of Service" are more credible
- The new National Development Plan updates capital spending plans to 2030

## The new framework could be strengthened

- Departmental Expenditure ceilings should be set out as legally required
- The spending rule could be: 1) linked more closely to the domestic fiscal rules, 2) expanded to cover non-Exchequer spending and tax changes, and 3) given legislative backing

# Key messages

## For 2022, the Government stuck to its planned €4.7 billion budgetary package

- This provides around €1.6 billion to maintain existing services, €1.5 billion in new current spending and an increase of €1.1 billion in government investment
- The Budget forecasts a deficit of 3.4 per cent of GNI\* for 2022, but it could be lower
- Keeping to the planned package strikes an appropriate balance between supporting the economy and keeping the public finances on a sustainable path

## For the medium term, the Government needs to follow through on its strategy

- The plans would allow public investment to increase to record levels and maintain existing levels of services
- The budget would reach close to balance by 2023 and the debt ratio would fall to below 90% of GNI\* by 2025
- This would comply with the domestic fiscal rules

## However, it is unclear how major commitments on health and climate change fit into the Government's medium-term strategy

- The costing of *Slaintécare* has not been updated since 2017
- There is no estimate of the budgetary cost of implementing the Climate Action Plan
- The medium-term plans only allow for an average of €0.5 to €1.5bn per year of additional current spending without raising taxes or cutting spending in other areas
- The impact of ageing and overreliance on highly-concentrated Corporation Tax receipts needs to be addressed

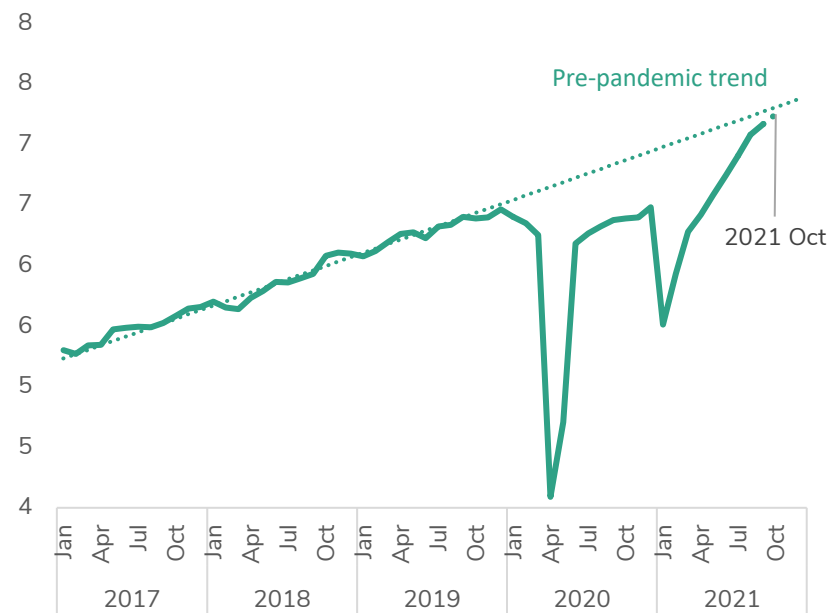
# **Economic and budgetary outlook**



# The economy is continuing to recover

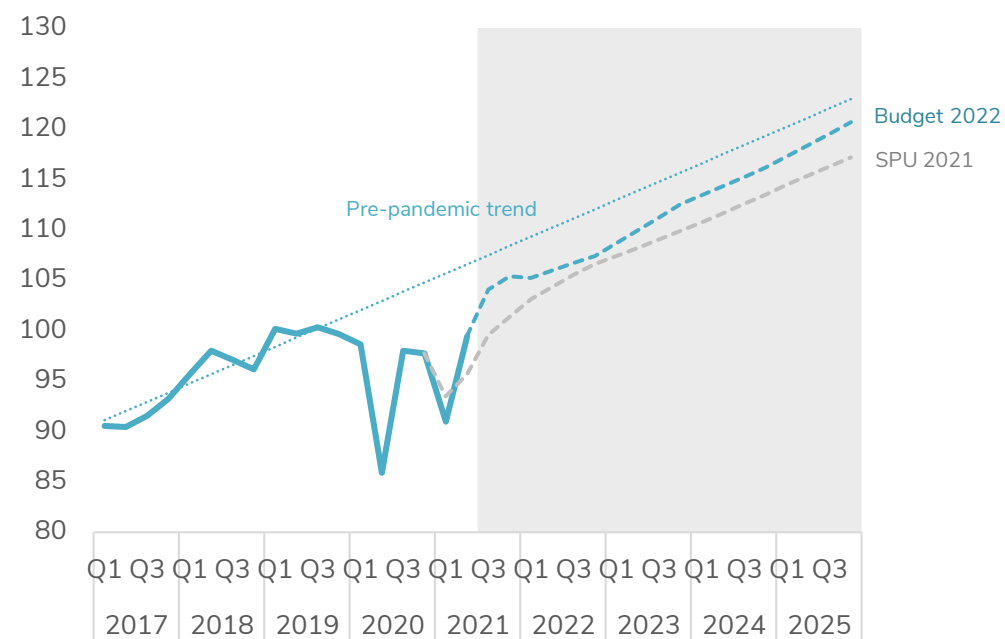
## Real cards spending and ATM withdrawals

€ billion, seasonally adjusted



## Underlying domestic demand

2019 = 100, seasonally adjusted



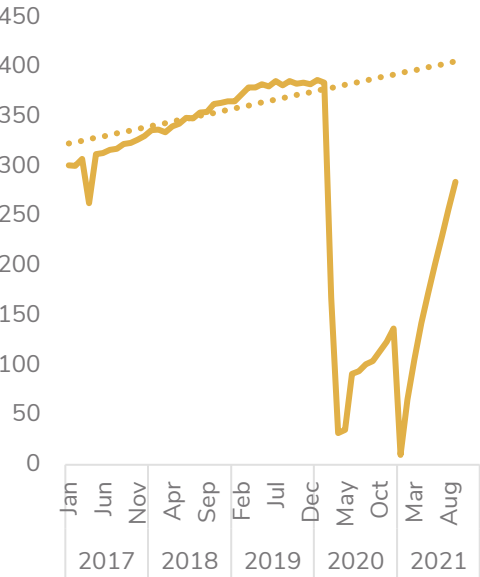
- Less scarring is projected in *Budget 2022*
- Growth of ~3% forecast for medium term

# But, the recovery is uneven

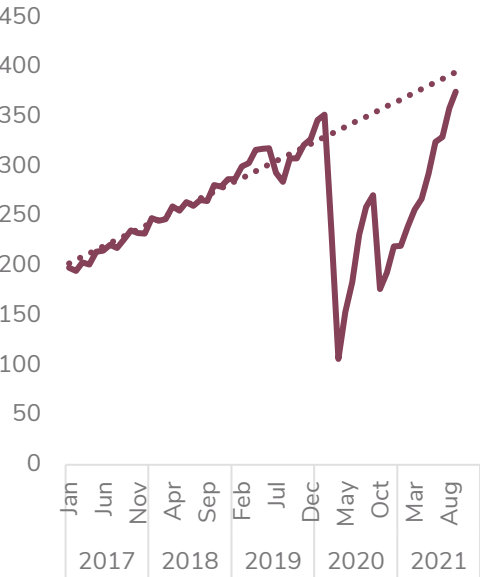
## Credit + debit card spending

€ million, monthly credit and debit card spending (seasonally adjusted)

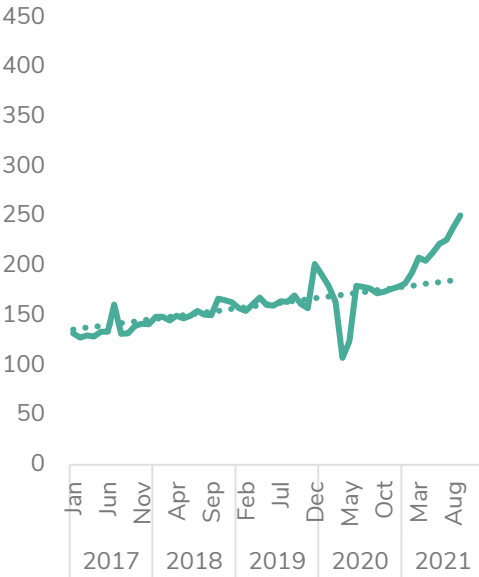
### Transport



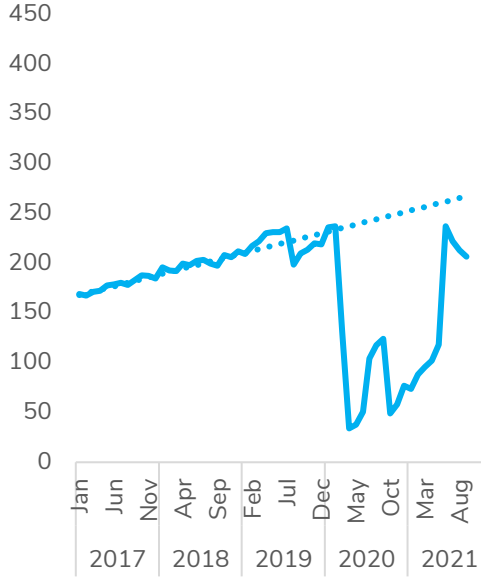
### Restaurants/dining



### Entertainment



### Accommodation





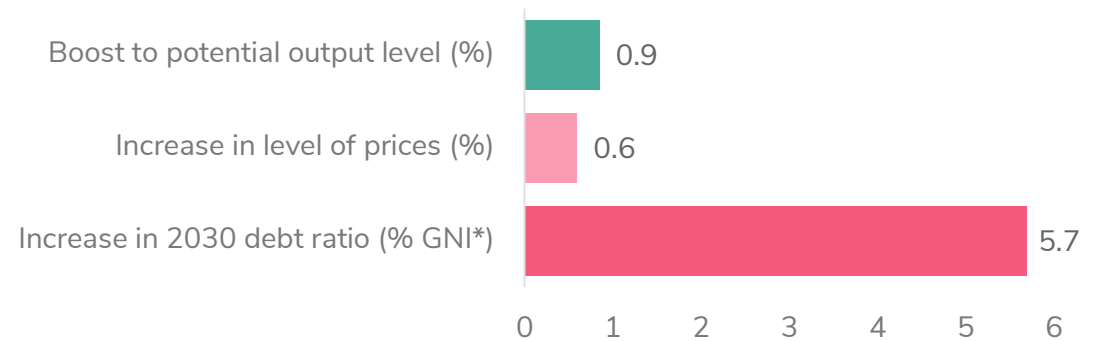
# Public investment will add to demand, but may hit construction capacity constraints

- The NDP plans to raise public investment to 5½ % of GNI\*
- This would require an estimated ~30K additional construction workers
- This could lead to higher prices

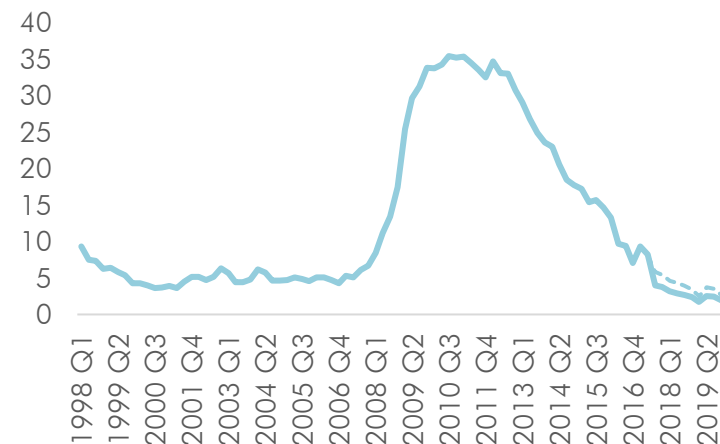
See new analytical note:  
[Ireland's next ramp-up in public investment](#)



Estimated impacts of additional public investment by 2030



% unemployment rate for construction sector\*



**Medium-term  
budgetary  
plans to 2025**

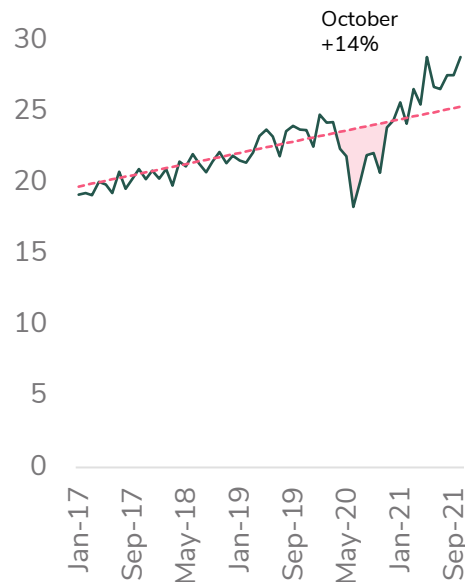


# Budget 2022 forecasts a sharp narrowing of the deficit to 5.9% of GNI\* in 2021

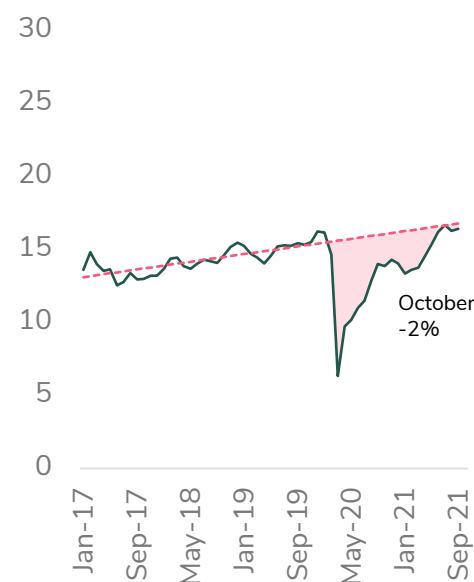
## Major taxes have recovered or outperformed

Annualised seasonally adjusted levels, € billion

### Income tax



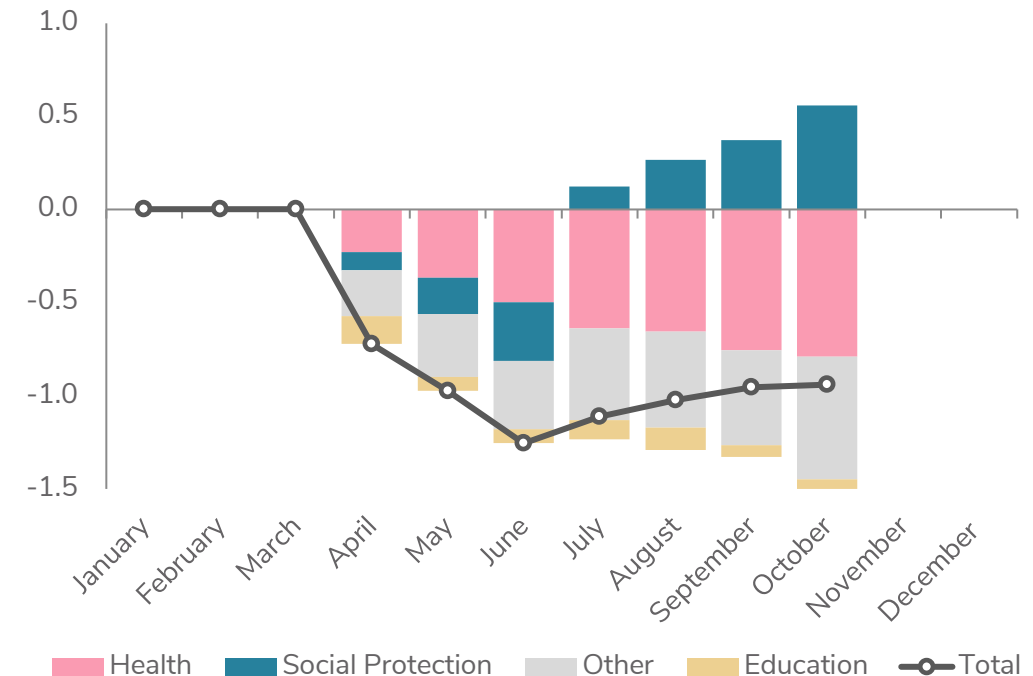
### VAT



Notes: Monthly tax data are seasonally adjusted and annualised (× 12). The pre-pandemic trend is calculated as a linear trend from Jan 2015 to Dec 2019.

## Most departments have underspent in 2021

€ billion (cumulative performance compared to SES profile)



- The deficit could ultimately be narrower due to higher revenue and underspends

# The Government's medium-term framework is welcome

A spending rule sets current spending to grow at potential assumed to be 5%

The medium-term forecasts based on the “Existing Level of Service” are more realistic

The new National Development Plan updates capital spending plans to 2030

# For 2022, the Government stuck to its planned €4.7 billion budgetary package

## Budgetary Package in 2022

€ billions

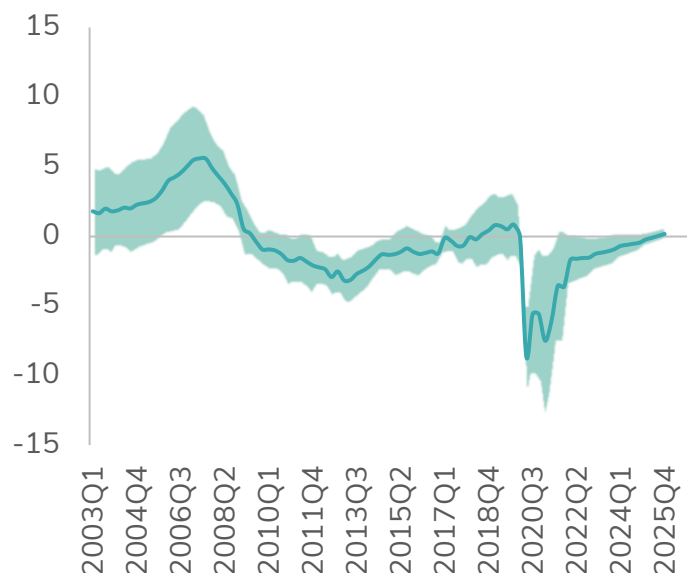
	2022
Demographics	0.7
Pay provisions	0.75
Existing Levels of Services (ELS)	0.2
Capital investment	1.1
New current spending resources	1.45
Tax measures	(0.45)
Total	4.7

- The Budget forecasts a deficit of 3.4 per cent of GNI\* for 2022, but it could be lower
- There are significant contingencies for Covid

# Keeping to the planned package for 2022 is appropriate

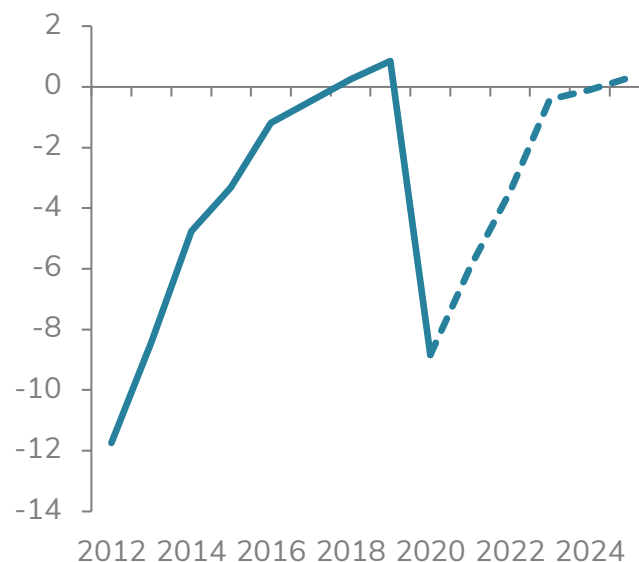
## Output gap

% gap between actual and potential economic output



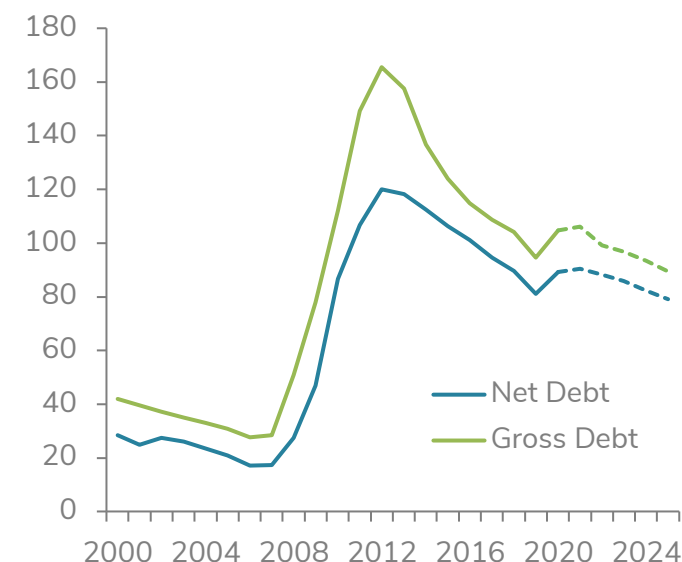
## General government balance

% GNI\*



## Gross and Net Government debt

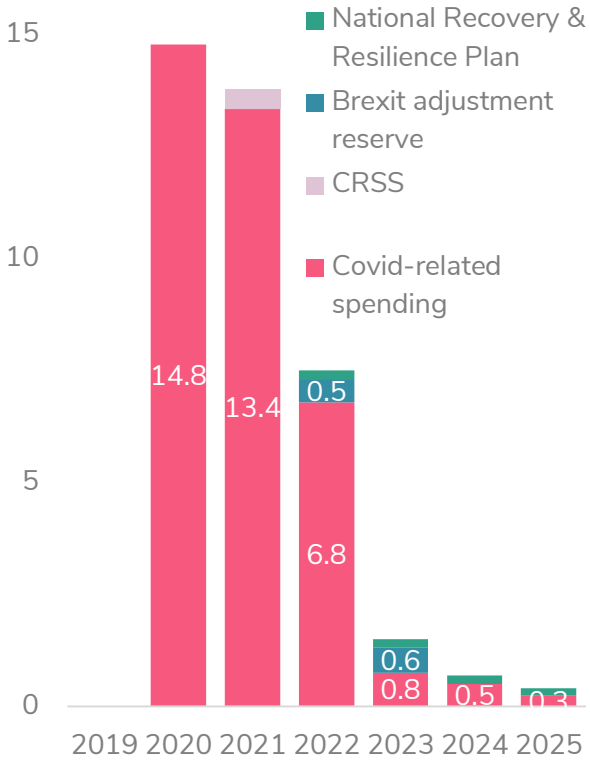
% GNI\*



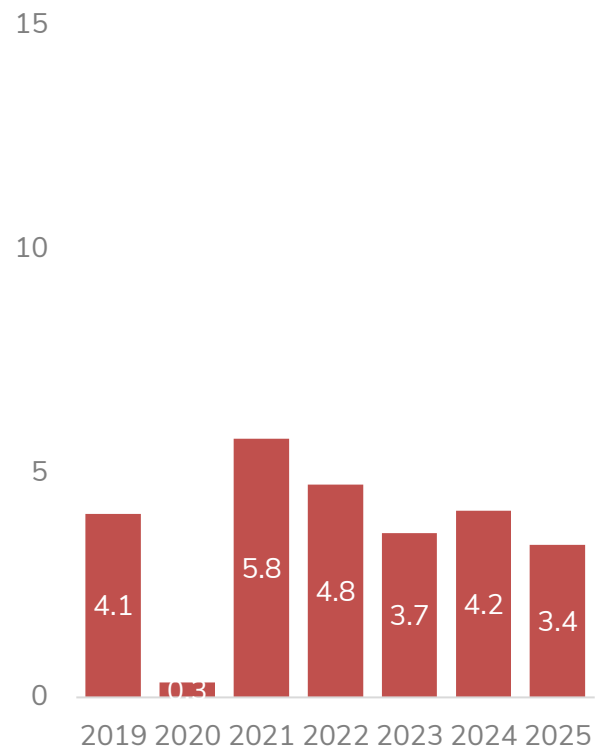
- This strikes an appropriate balance between supporting the economy and keeping the public finances on a sustainable path

# The plans are supported by lower temporary spending and modest growth in current spending

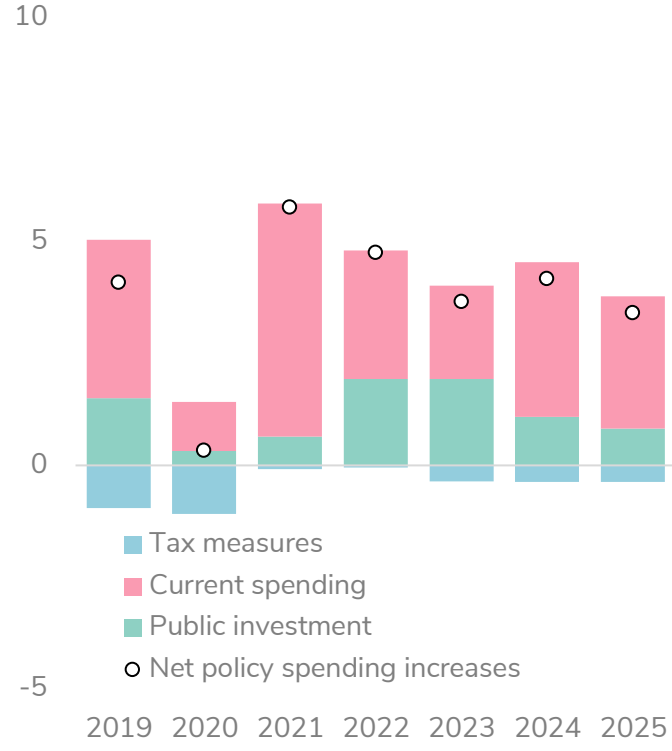
**Temporary Spending**  
€ billions



**Permanent Spending increases**  
€ billions, net policy spending

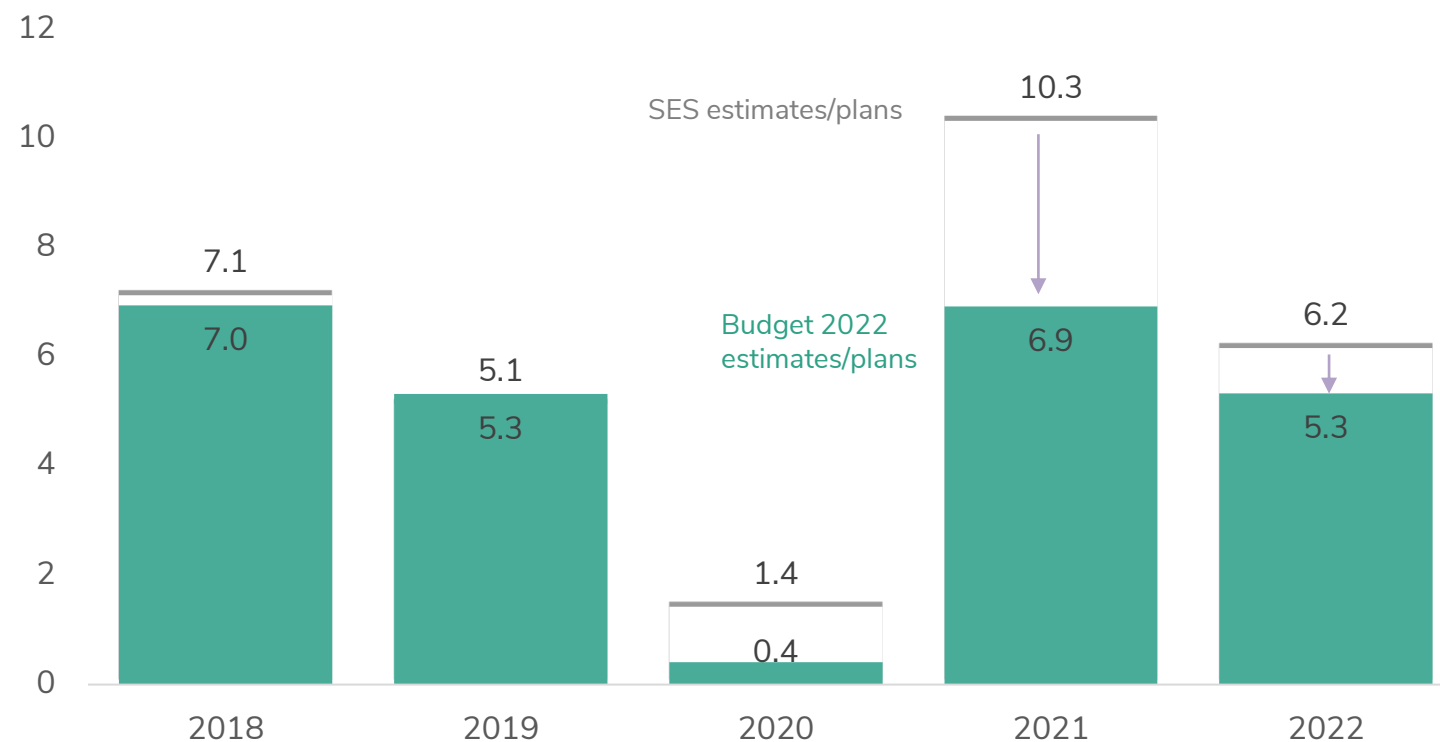


**Investment adds to spending increases**  
€ billions



# Spending plans have been scaled back somewhat

Net policy spending  
% change year-on-year

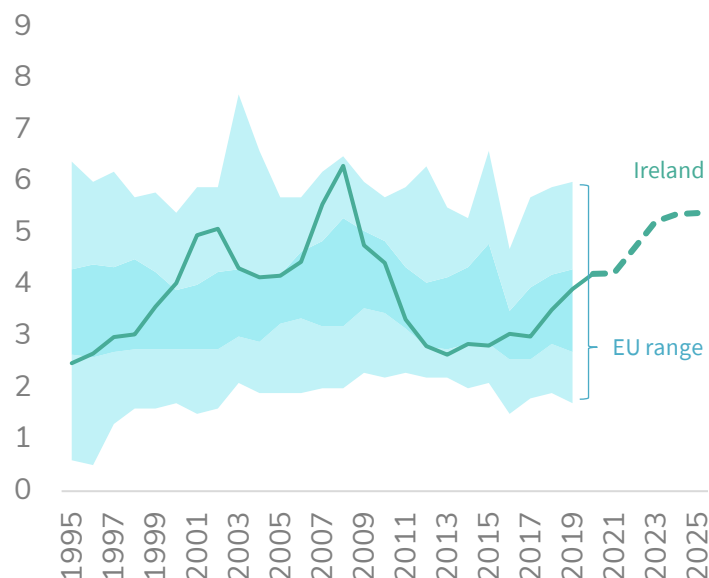


- SES plans were at the limit of what was prudent

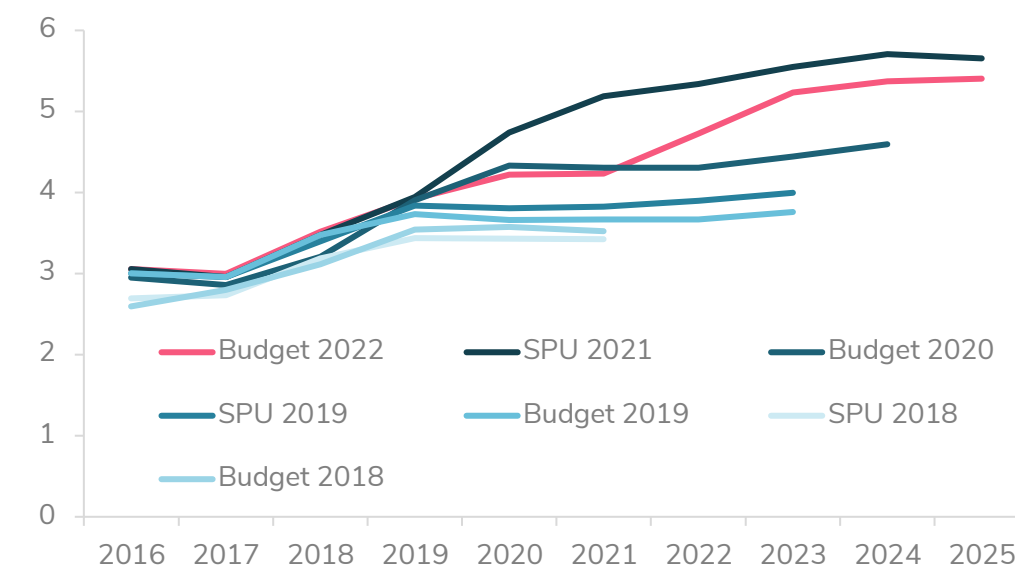


# Public investment is set to rise to very high-levels

Capital spending to rise above EU norms  
% GNI\*



Capital spending above previous plans, but lower than SPU 2021  
% GNI\*



- Investment set to remain high to 2030
- This should help to address climate and housing issues
- More details are needed on the plans and their expected economic impact

# Over a longer period, the ramp-up in public investment is being achieved without increasing borrowing

## Comparing 2025 and 2019

2025 figures compared to 2019, general government basis

	p.p change in GNI*	€ Billion change	% Change	Annualised growth rate
Revenue	-1.5	22.8	25.8	3.9
Tax Revenue	1.7	23.0	38.8	5.6
Non tax revenue	-3.2	-0.2	-0.7	-0.1
Income tax	1.0	9.9	43.0	6.1
Corporation tax	0.3	4.3	39.3	5.7
VAT	0.3	5.6	36.7	5.4
Other tax revenue	0.0	3.3	31.7	4.7
Spending	-1.0	23.7	27.5	4.1
Public investment	1.5	6.8	80.0	10.3
Interest	-1.0	-1.4	-31.3	-6.1
Current primary spending	-1.5	18.4	25.1	3.8
Budget Balance	-0.5	-0.9		
Level of GNI*		66.3	30.8	4.6

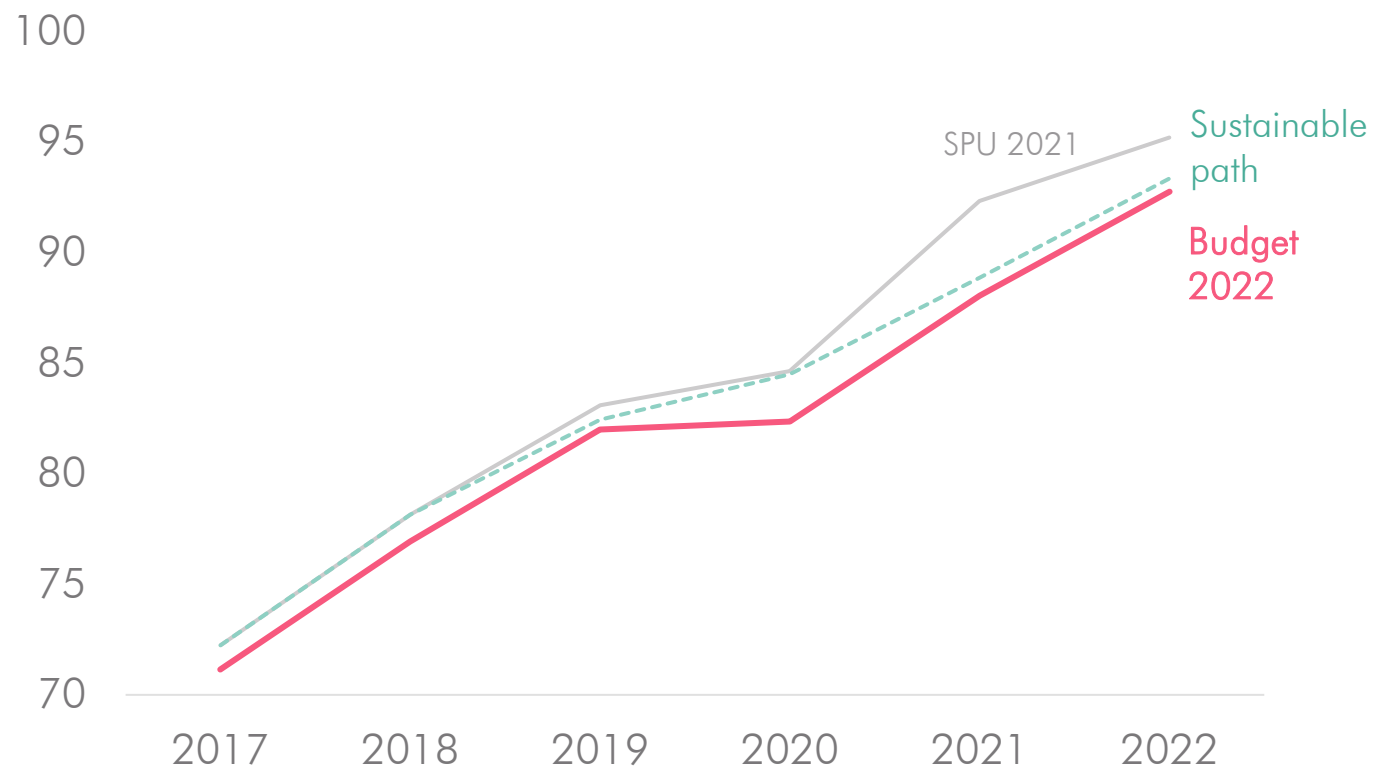
Sources: CSO; and Budget 2022.

Notes: Changes are in the format 2025 level minus 2019 level. As a result, positive values indicate a variable increasing over the period or taking up a larger share of GNI\* than was the case in 2019. The annualised growth rate shows what rate of growth applied for every year from 2019 would yield the 2025 level forecast in *Budget 2022*.

# For the medium term, the Government needs to follow through on its strategy

## Net policy spending

€ billion



- The budget would reach close to balance by 2023
- The gross debt ratio would fall to below 90% of GNI\* by 2025
- This would comply with the domestic fiscal rules

Sources: CSO; Department of Finance forecasts; and Fiscal Council workings.

Notes: Policy spending is general government expenditure less interest costs, one-offs, and the estimated costs associated with cyclical unemployment. The “sustainable” increases assume that spending grows in line with potential output and actual price inflation.

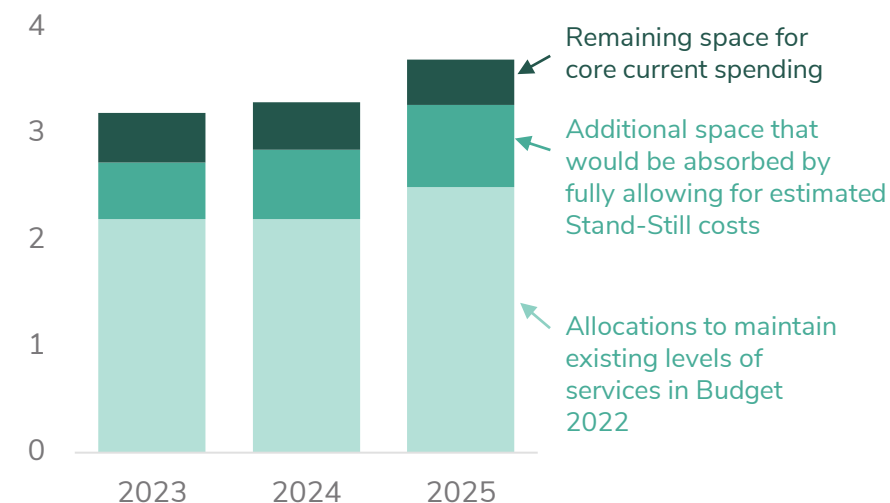
# However, it is unclear how major commitments fit into the Government's medium-term strategy

Climate Change Action Plan

Slaintecare

The medium-term plans only allow for an average of € 0.5 to €1.5bn euro per year of new core current spending *without* raising taxes or cutting spending in other areas

Stand-Still costs for the medium-term are considerable  
€ billion, year-on-year increase in current spending



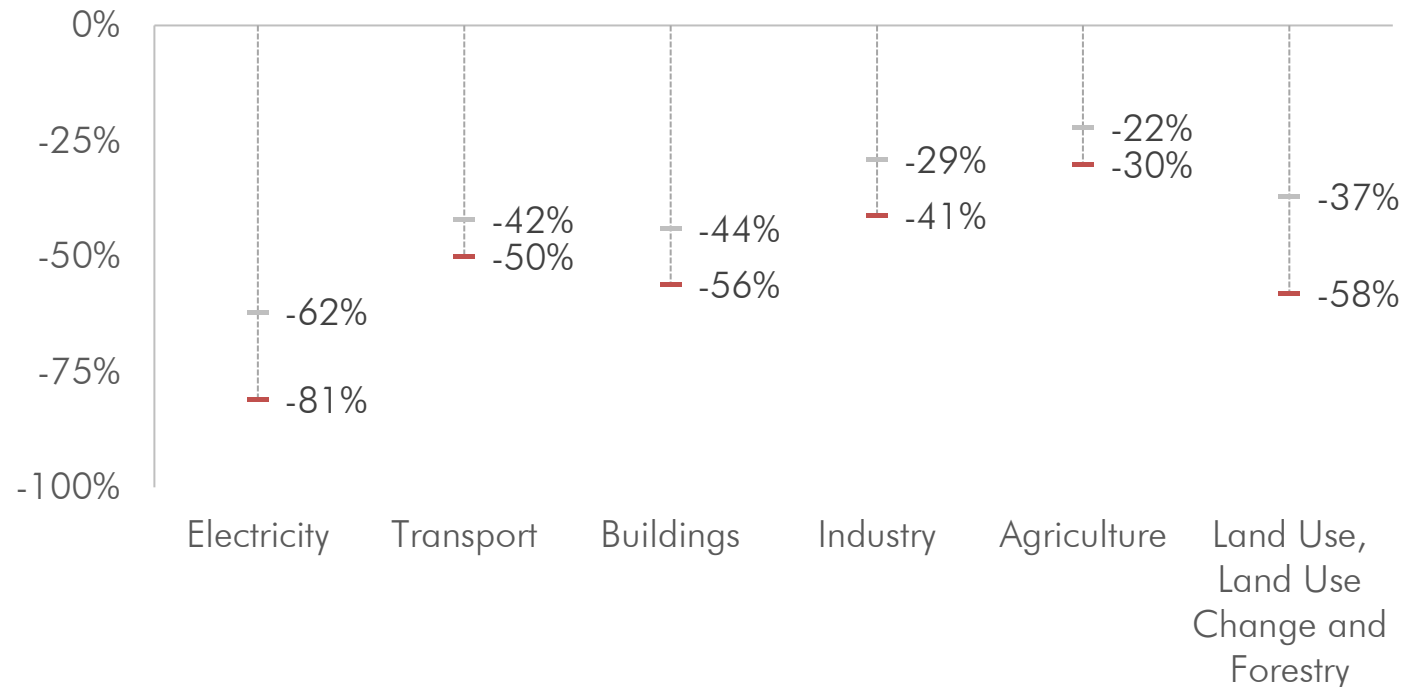
Source: Department of Finance, and Fiscal Council workings.

Notes: The Stand-Still approach estimates the costs of maintaining existing public service levels and value of welfare payments, taking into account inflation, wage increases, and demographic pressures. Core current figures relate to annual changes in the level of core current spending as per *Budget 2022*, Existing Level of Services (ELS) allocations are to maintain existing policies, given demographic and price pressures and represent 3% of gross voted core current spending levels as per *Budget 2022*.

# Climate change costs may significantly impact the public finances

## Proposed Emissions Reductions by Sector

% reductions by 2030 relative to 2018



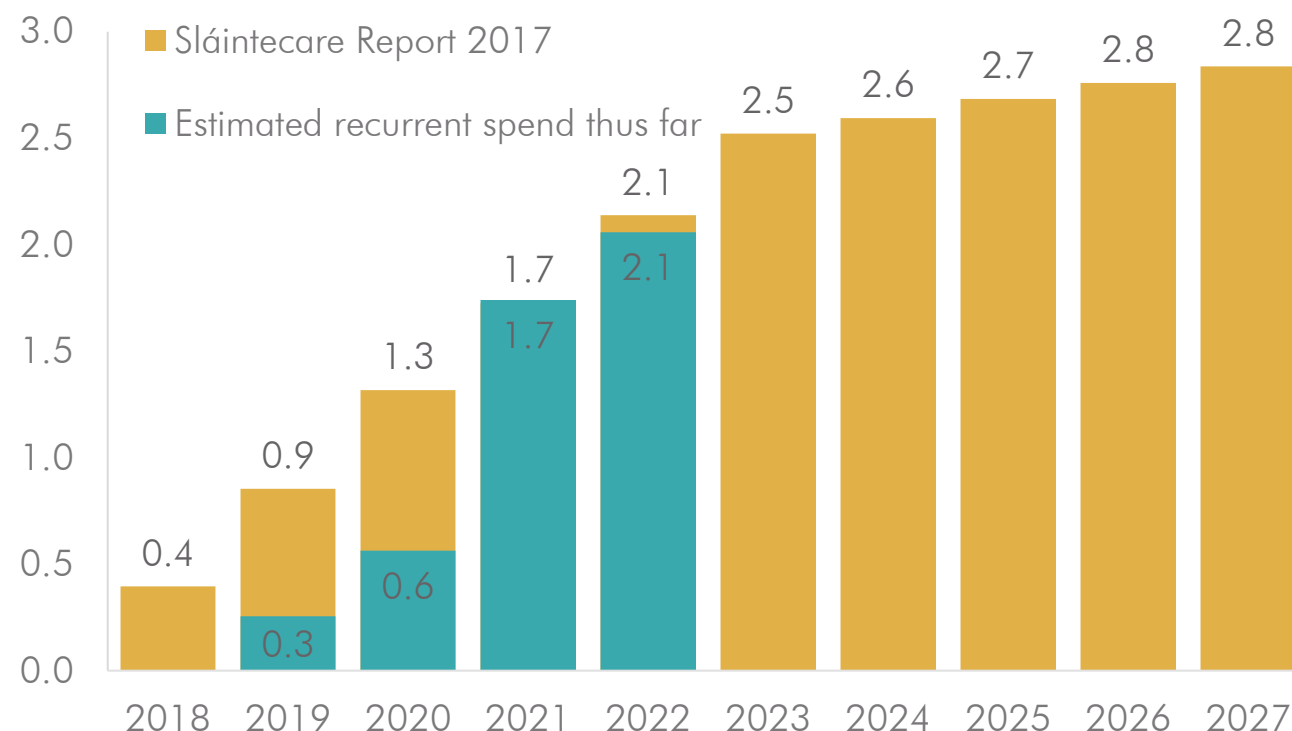
Sources: Climate Action Plan 2021

Note: Ranges are to be finalised in the Climate Action Plan 2022 following the legal adoption of carbon budgets and sectoral emissions ceilings

- There is no estimate of the budgetary cost of implementing the Climate Action Plan

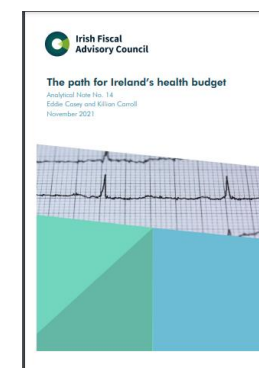
# More clarity is urgently needed on health costs

Estimated expenditure on Sláintecare  
€ billion



- The cost of healthcare has been rising
- Budgeting has been poor
- The cost of *Sláintecare* reforms has not been updated since 2017 and no estimates are available after 2022











See new analytical note:  
[The path for Ireland's health budget](#)



Source: Sláintecare Report 2017; Department of Health; and own workings.

Notes: The “estimated spend thus far” represents the increase in recurrent annual health spending that is associated with Sláintecare as derived from budget day plans. The actual increases may vary, however, as these are plans rather than outturns, and the figures are not precise, in that costs tend to be mixed in with the costs of other more general expansions in publicly provided health services.

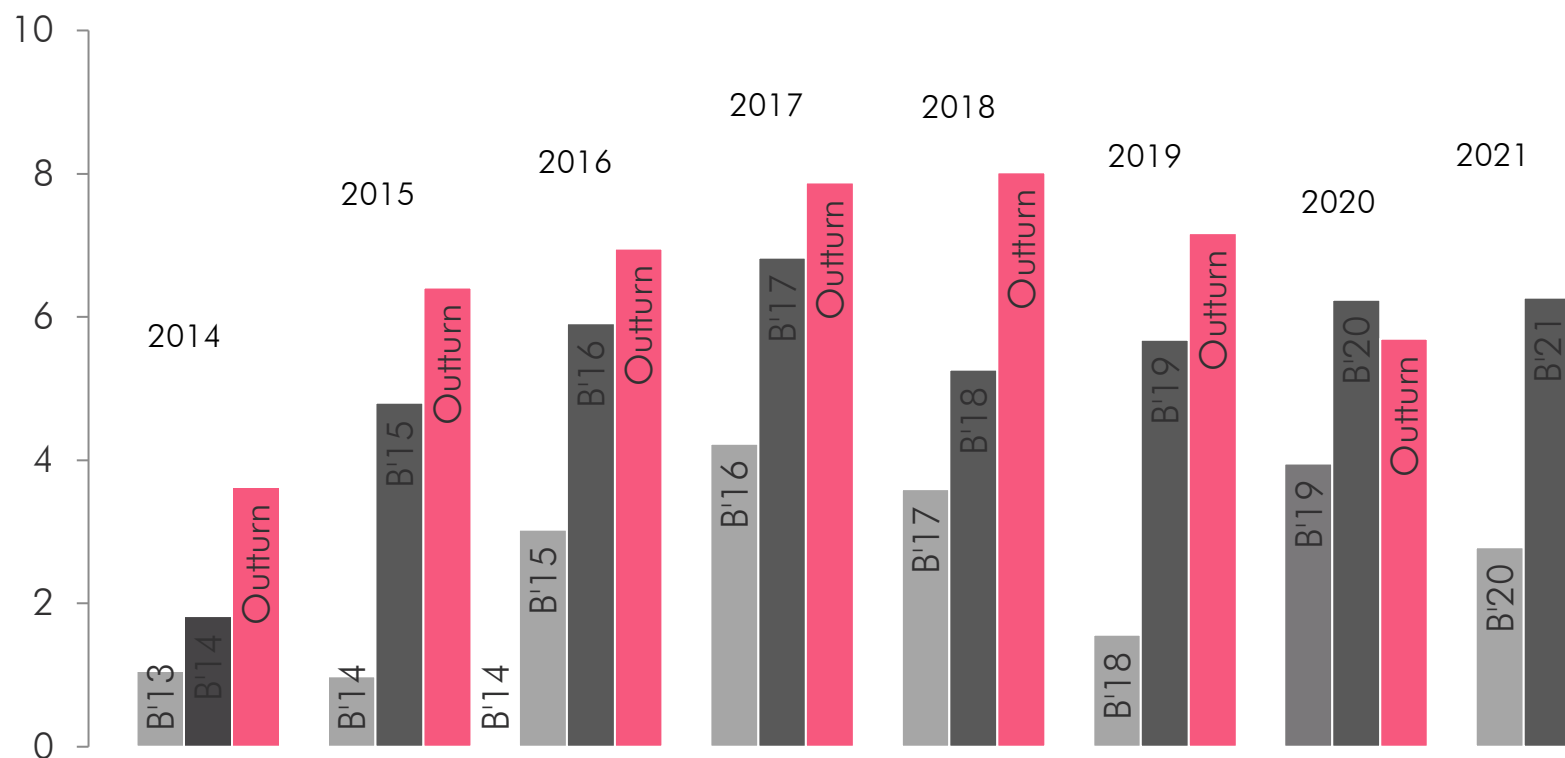
# The new budgetary framework is welcome, but could be strengthened

Objective	Budget 2022	Council calling for this since	Progress	
Present five-year-ahead forecasts	Four-years-ahead	Nov-17		Mostly there
Base projections on realistic spending plans	Much more realistic than previous rounds, and Budget 2022 accommodates Stand-Still costs	Jun-16		Mostly there
Commit to medium-term fiscal objectives	With the spending rule, more formal numerical targets introduced, but need development	Nov-17		Mostly there
Consider measures to strengthen fiscal framework	Spending Rule and Existing Level of Services are excellent initiatives but can be improved further	Nov-17		Some
Provide transparent costings of major policy changes	Still not clear if Major Programme for Government policies including Sláintecare are factored in	Dec-20		Some
Show how rules will be complied with	Document sets out structural balances that appear compliant, but some areas are overlooked	Dec-20		Some
Indicate how taxes would be adjusted if needed	No information on this, but Tax and Welfare Commission established	Dec-20		Limited
Make non-Exchequer forecasts more transparent	Marginal improvement in transparency shown	Nov-19		Marginal/none
Clarify how the Rainy Day Fund will be used in future	No mention of it	Jun-16		Marginal/none
<b>Overall progress</b>				<b>Some</b>

- Link the new “5% Spending Rule” more closely to the domestic fiscal rules
- Expand it to cover non-Exchequer spending and tax changes
- Give legislative backing

# Departmental Expenditure ceilings should be set out as legally required

Change in gross voted current expenditure ceiling relative to initial ceiling  
% deviation from original ceiling



Sources: CSO; Department of Finance; and Fiscal Council workings.

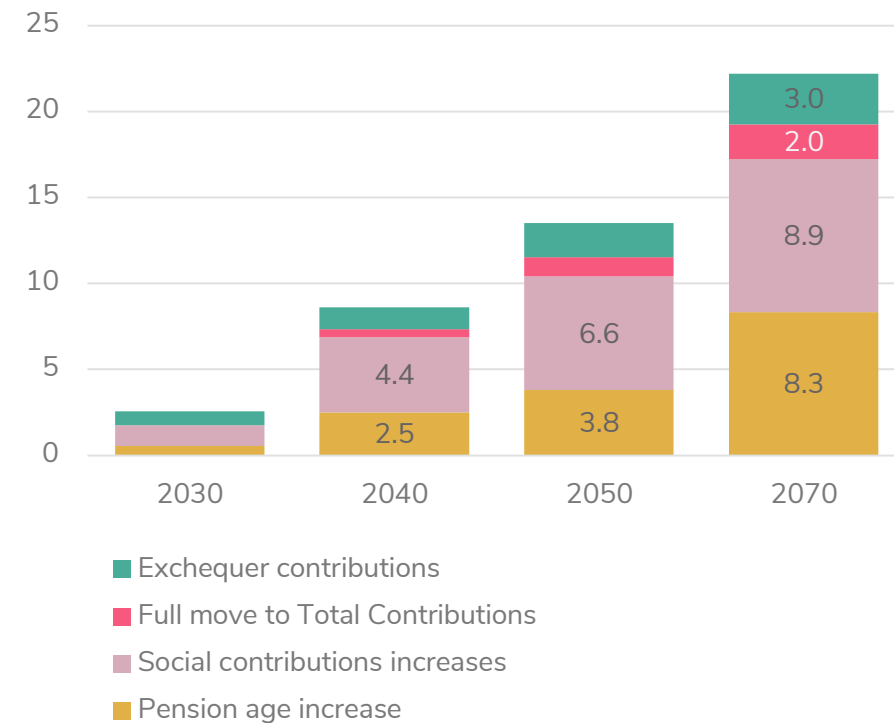
Note: Bars show the change in forecasts from various budgets followed by outturns, versus the earliest budget forecast for that year (e.g., B'15 = expenditure forecasts in Budget 2015 minus the earliest forecast for the specified year). Red bars relate to the change in outturn expenditure versus the earliest forecast for expenditure for the year specified above. Note that figures for Budget 2021, and the outturn for 2020 are Covid-19-adjusted (they incorporate only "core" expenditure).



# Pensions Commission recommendations need to be addressed

- The Pensions Commission recommendations address the long-term sustainability of the pension system
- The Government needs to commit to implementation of pension reform
- Delaying changes has costs and raises questions about the credibility of the measures
- Recommendations rely heavily on tax increases to address funding shortfalls

Reform package recommended by Pensions Commission  
€ billions, cumulative funding raised by source

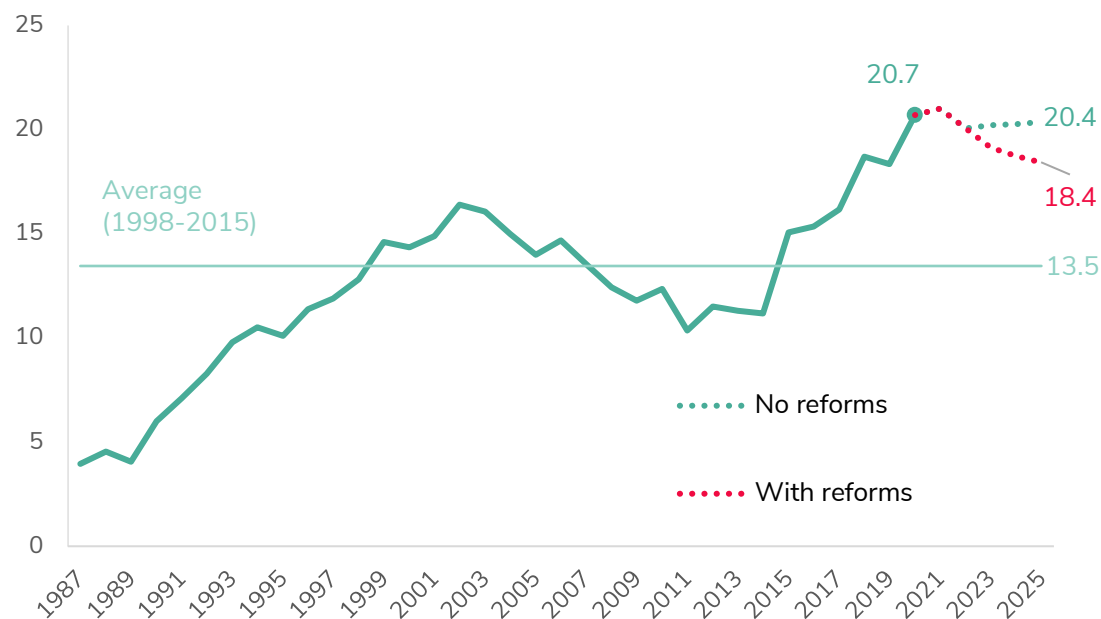


Source: [Commission on Pensions \(2021\)](#).

# Overreliance on corporation tax receipts needs to be reduced

## Corporation tax to fall as a share of tax revenue

Corporation tax (per cent share of Exchequer tax revenue)



- Overreliance on corporation tax receipts is a major risk
- The Department of Finance estimates €2bn in lost revenues from reforms to the tax base, while raising the rate to 15% could raise revenues
- However, revenues are increasingly concentrated in a small number of international firms
- Any additional increases in receipts should be saved in the “Rainy Day” Fund

# Key messages

- The economy is continuing to recover
- *Budget 2022* forecasts a sharp narrowing of the deficit to 5.9% of GNI\* in 2021
- The Government's medium-term framework is welcome
- The new framework could be strengthened
- For 2022, the Government stuck to its planned €4.7 billion budgetary package
- For the medium term, the Government needs to follow through on its strategy
- However, it is unclear how major commitments on health and climate change fit into the Government's medium-term strategy