

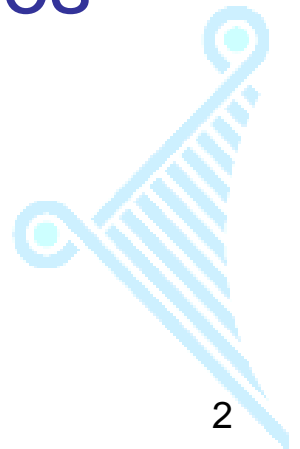
# Fiscal Policy in Ireland: Achievements and Prospects

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Reform

12<sup>th</sup> November 2015

# Overview

- Recent Economic Performance
  - Catch up and imbalances
  - Banking collapse and fiscal deficits
- Policy responses and fiscal challenges
- Future Fiscal Policy



# Strong Convergence Story in Second Half of 1990s

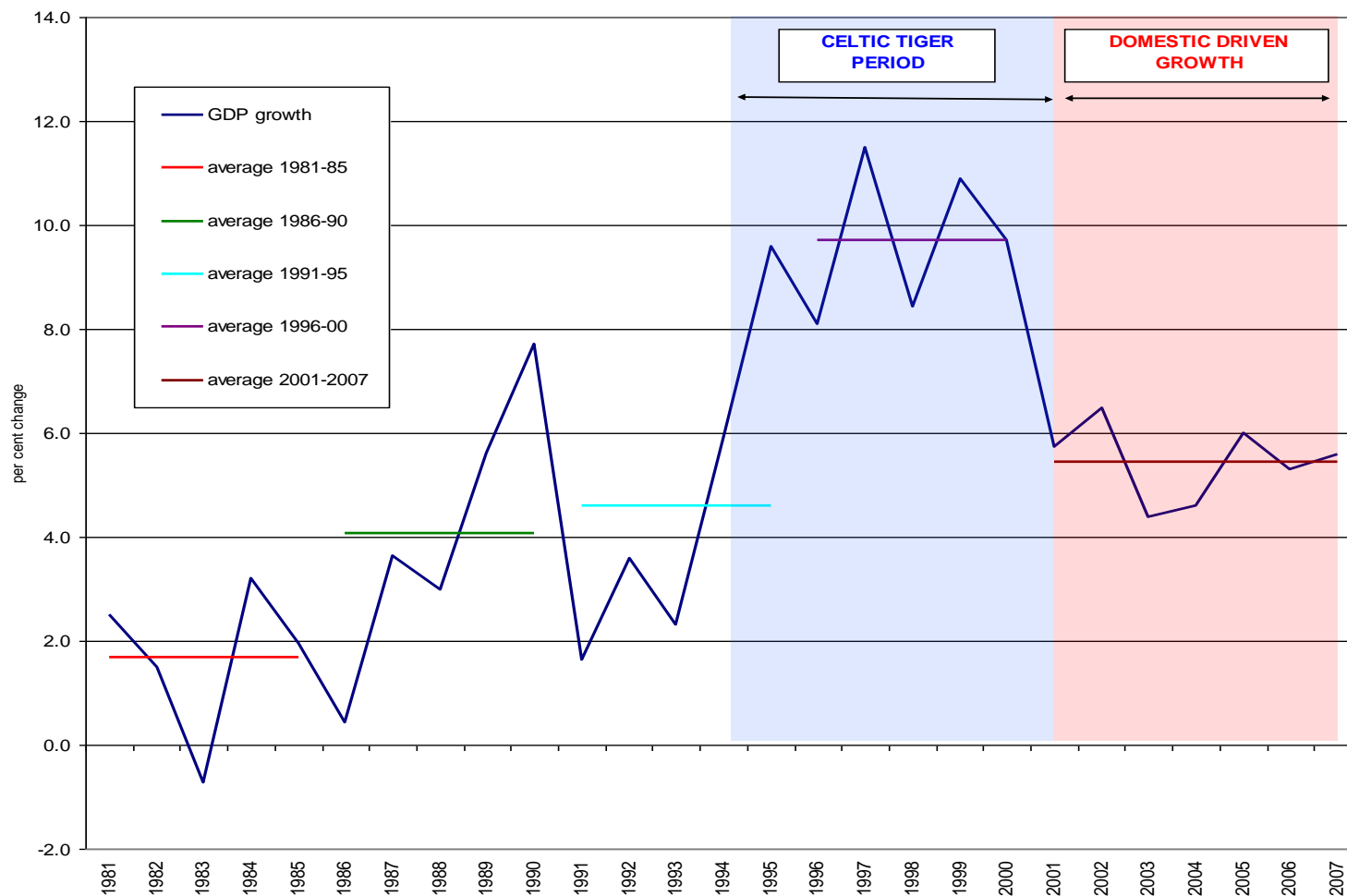
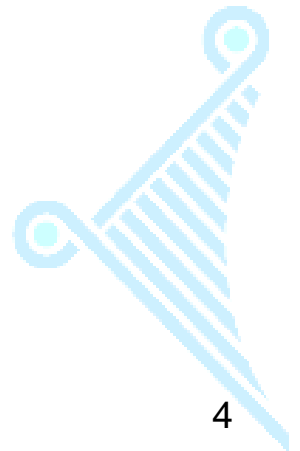


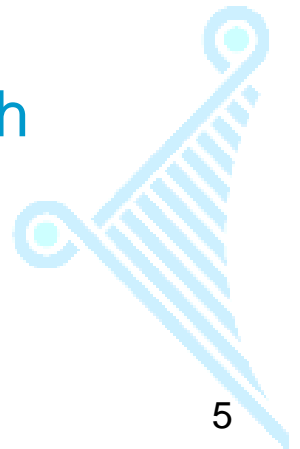
Chart shows: annual GDP growth over 1981-2007 period (source – CSO)

# Imbalances and the Property Bubble Post 2000 Story



# Post-2000 Developments

- Lost competitiveness → slower export growth
- Shift in drivers of growth:
  - away from exports
  - towards domestic demand
- Domestic demand driven by a housing boom
  - house building reached unsustainable levels
  - employment in construction unsustainably high
  - living standards were artificially inflated



# Economy too Dependent on House Building

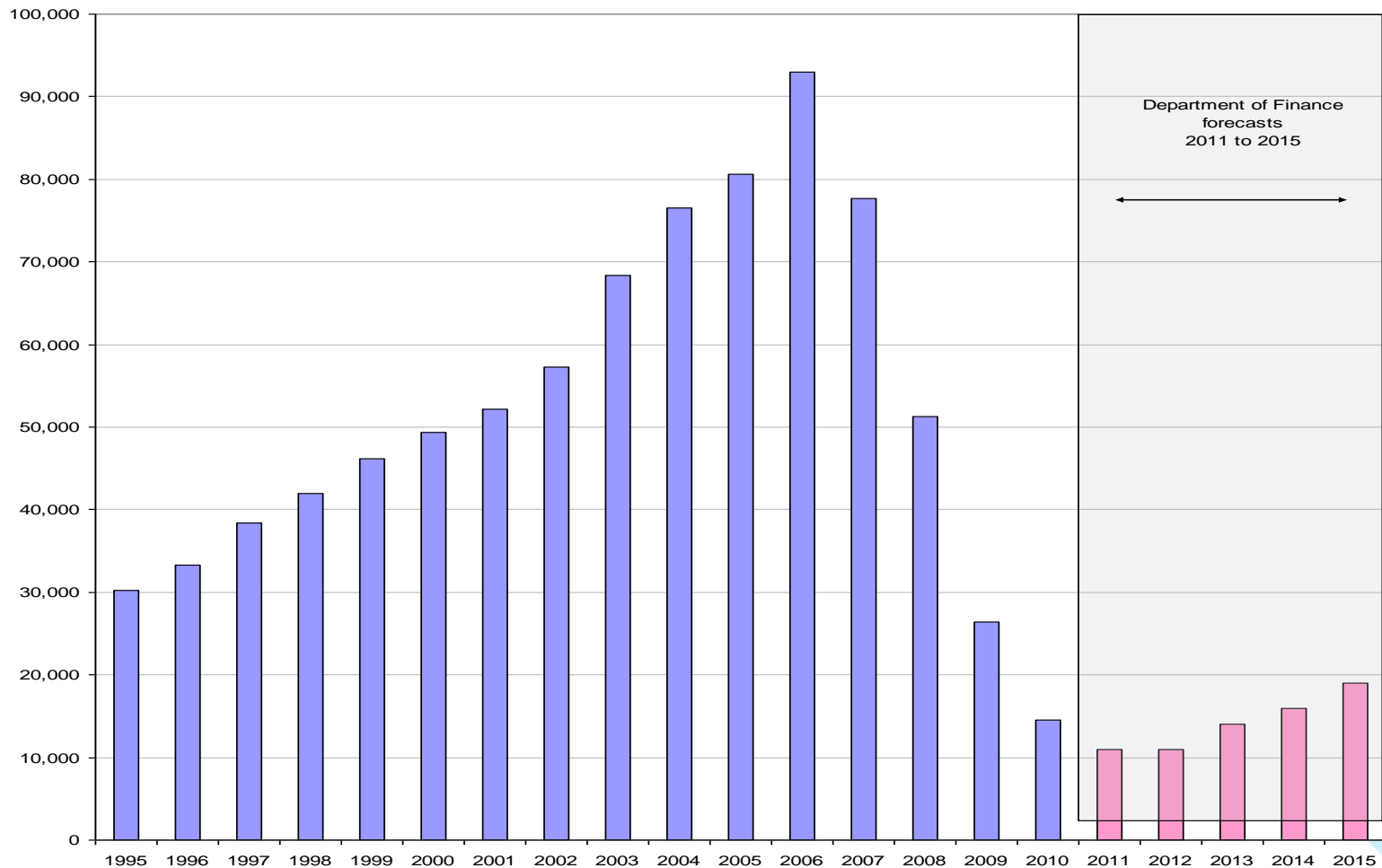


Chart shows: annual house completions (sources – CSO and DoF)

# Rapid Increase in House Prices

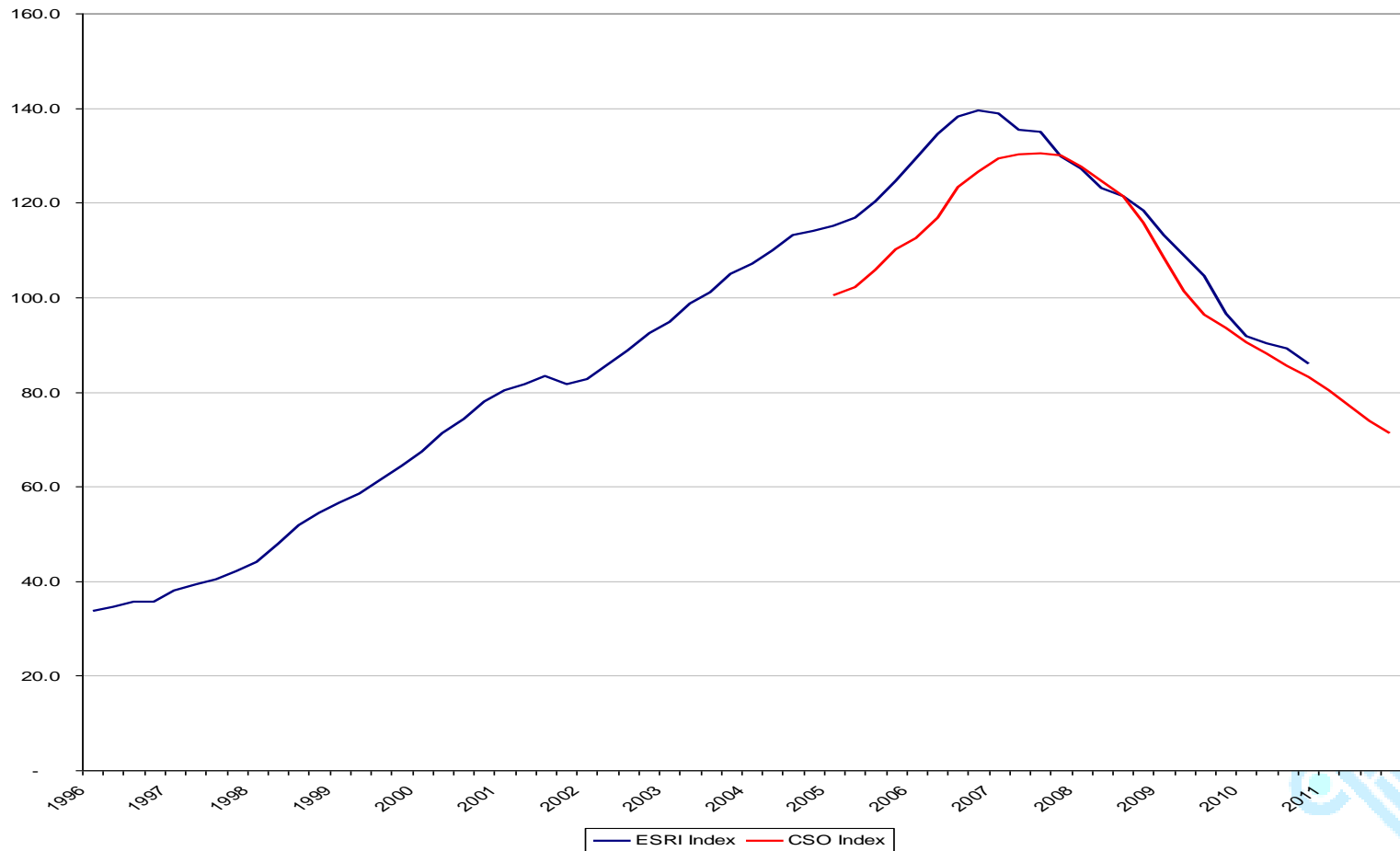


Chart shows: Permanent TSB / ESRI House Price Index & CSO Residential Property Price Index

# Sharp Decline in Economic Activity

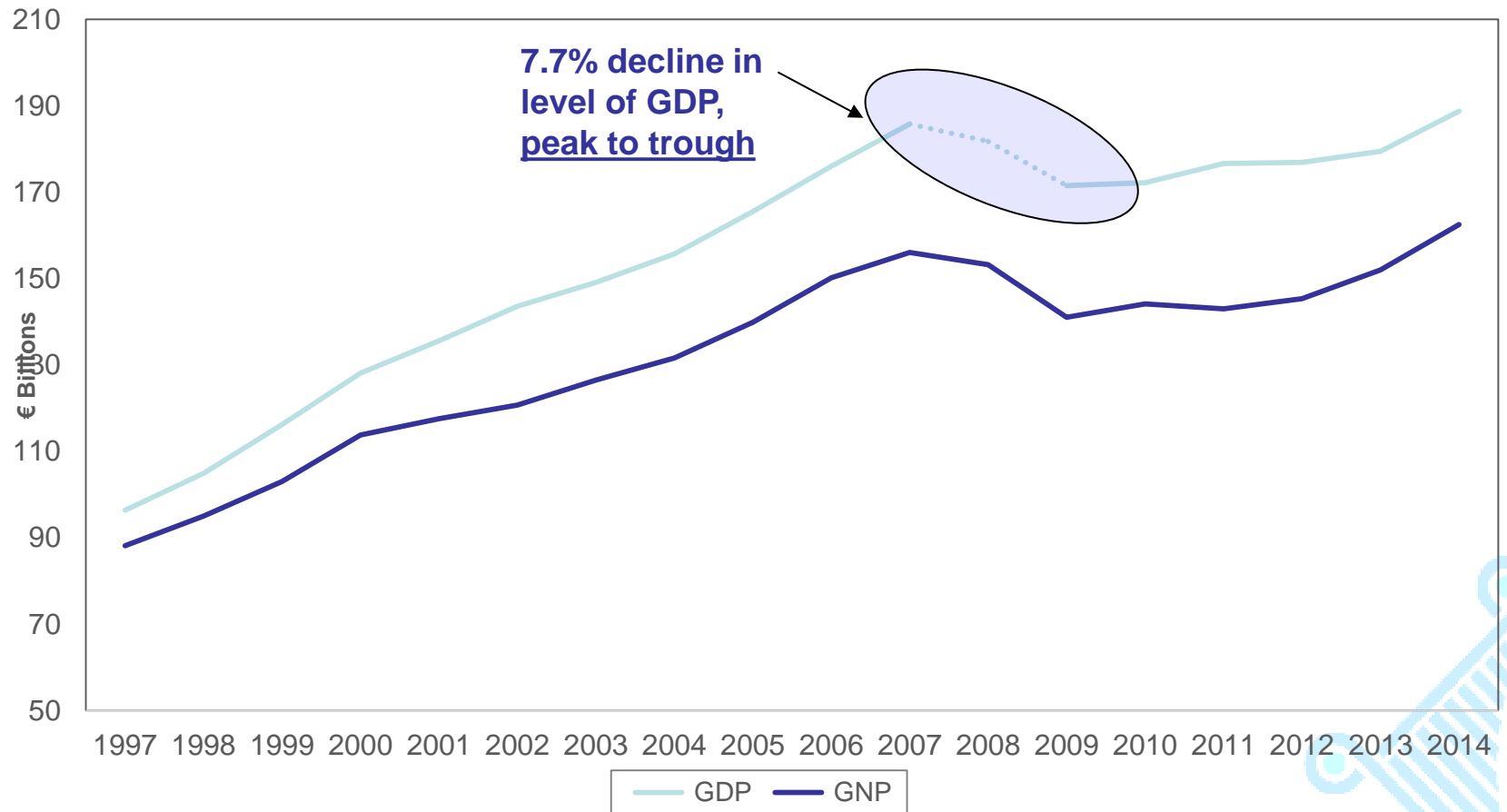


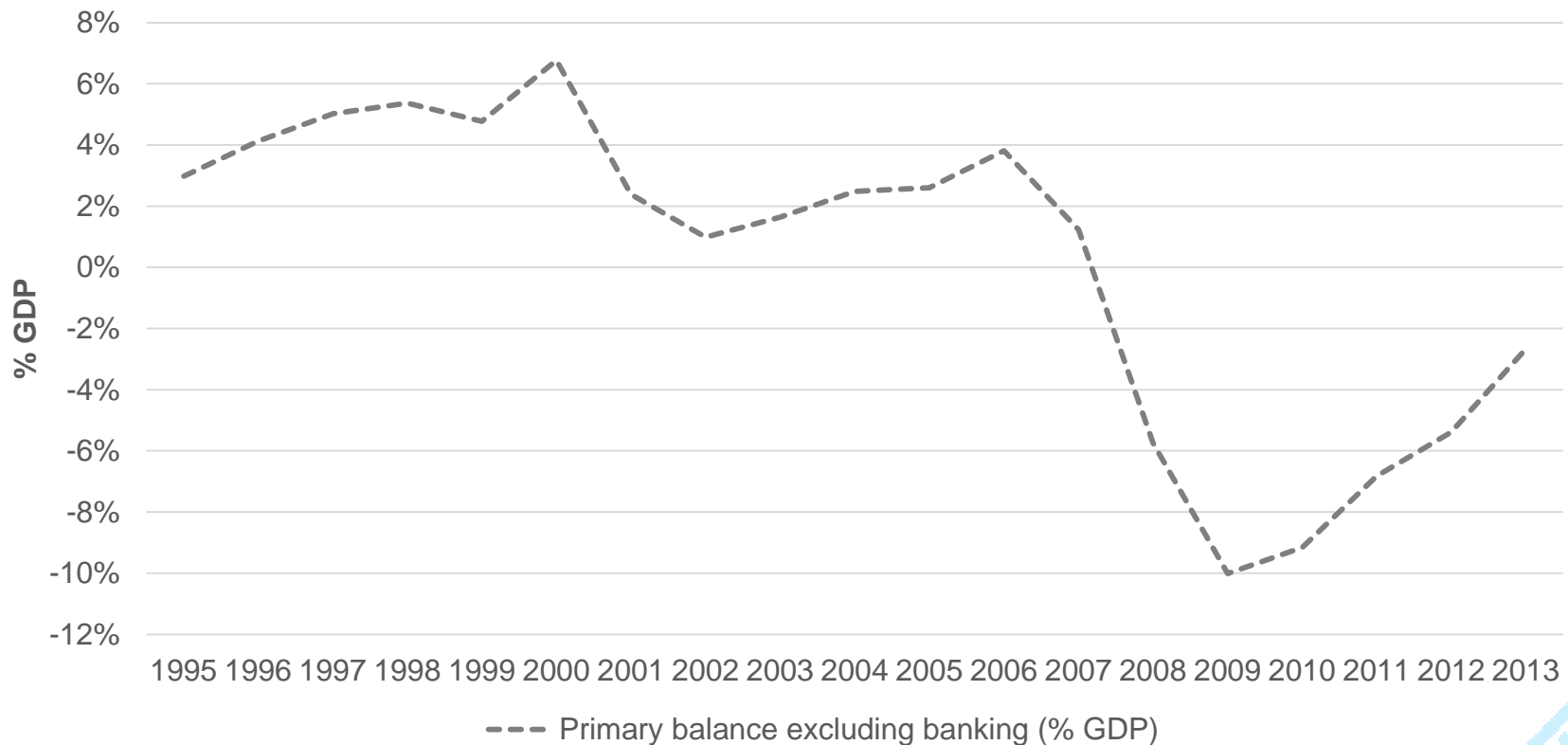
Chart shows: level of real GDP and GNP (source – CSO)



# Effect of Downturn on Public Finances

- Divergence between spending and revenue during the downturn:
  - Expenditure by Departments reached a peak of €62.3bn in 2009
  - Tax Revenues reached a trough of €31.8bn in 2010
- Expenditure pressures during the downturn not just related to the banking system:
  - Spending on unemployment supports increased by almost 200% between 2007-2010.
  - Medical Card recipients have increased by 665,000 (37.7%) between 2007 and 2014
  - Student and pupil numbers at all levels of education have increased significantly

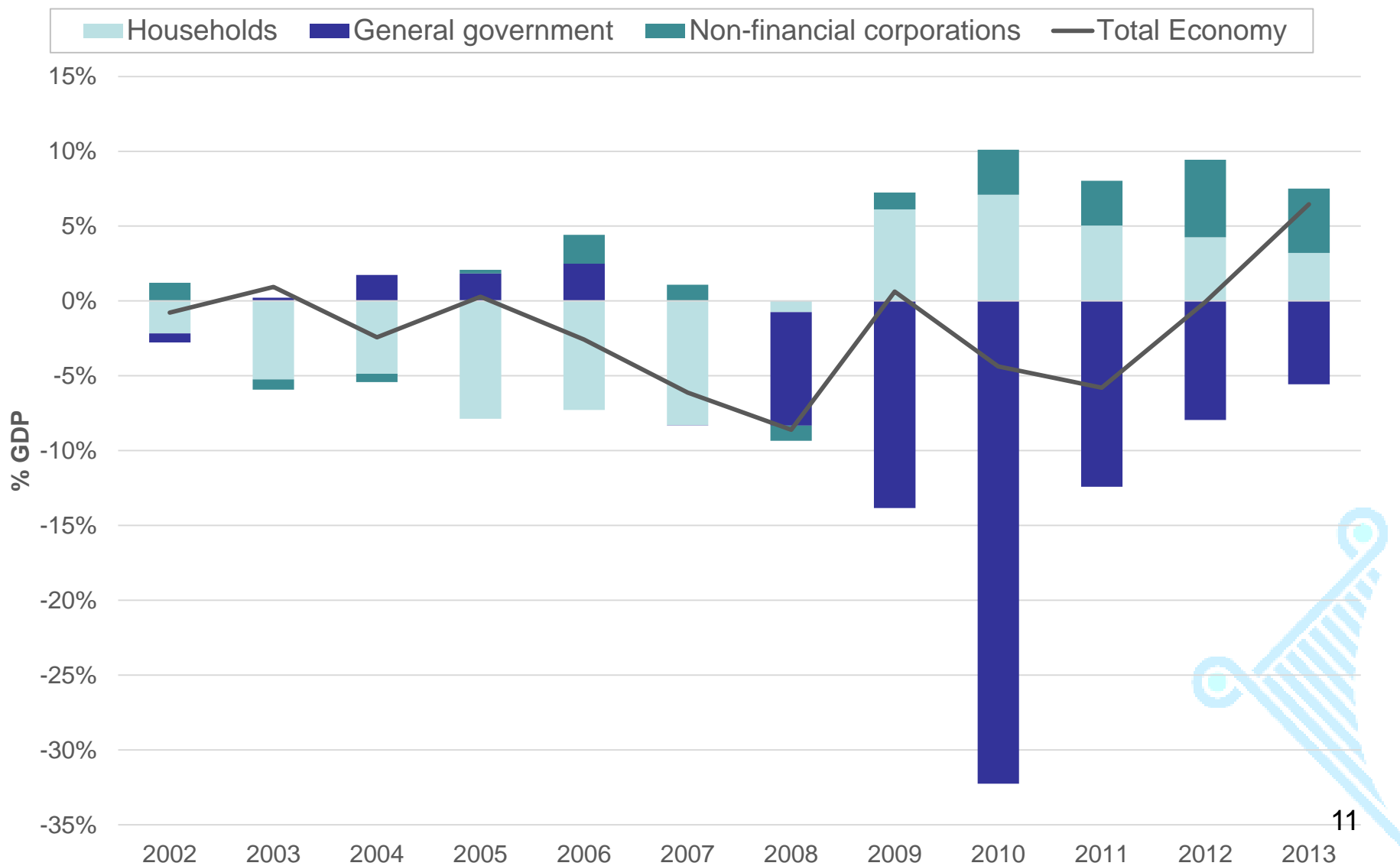
# Primary Fiscal Balance – 1995 to 2013



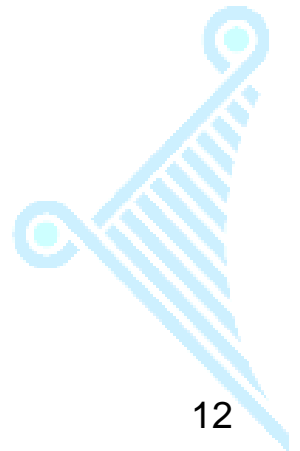
Source: Department of Finance. Figures for 2015-21 based on Budget 2016

# Change in “Flow of Funds” of Different Sectors

## Ireland 2002-2013

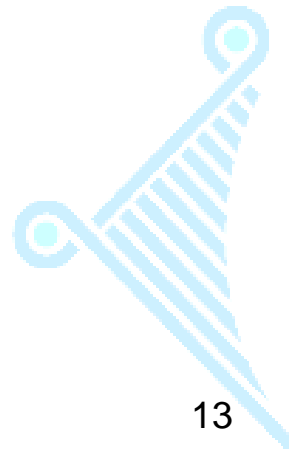


# Fiscal Policy Response

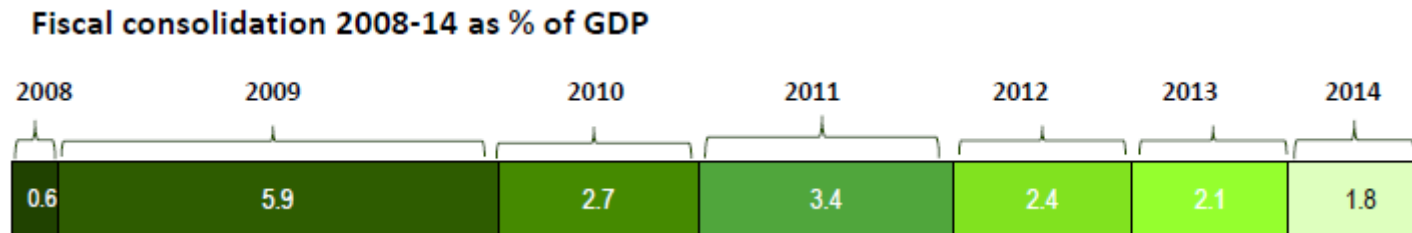


# Guiding Principles

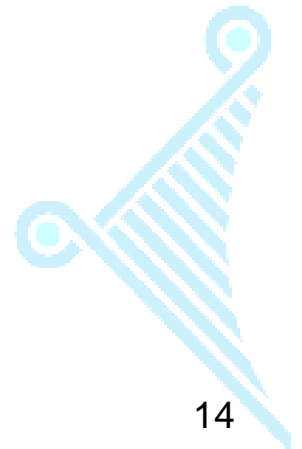
- Restoring sustainability to public finances
  - Medium-term consolidation framework
  - Measures to correct the unsustainable fiscal deficit
- Repairing the banking system
- Improving competitiveness



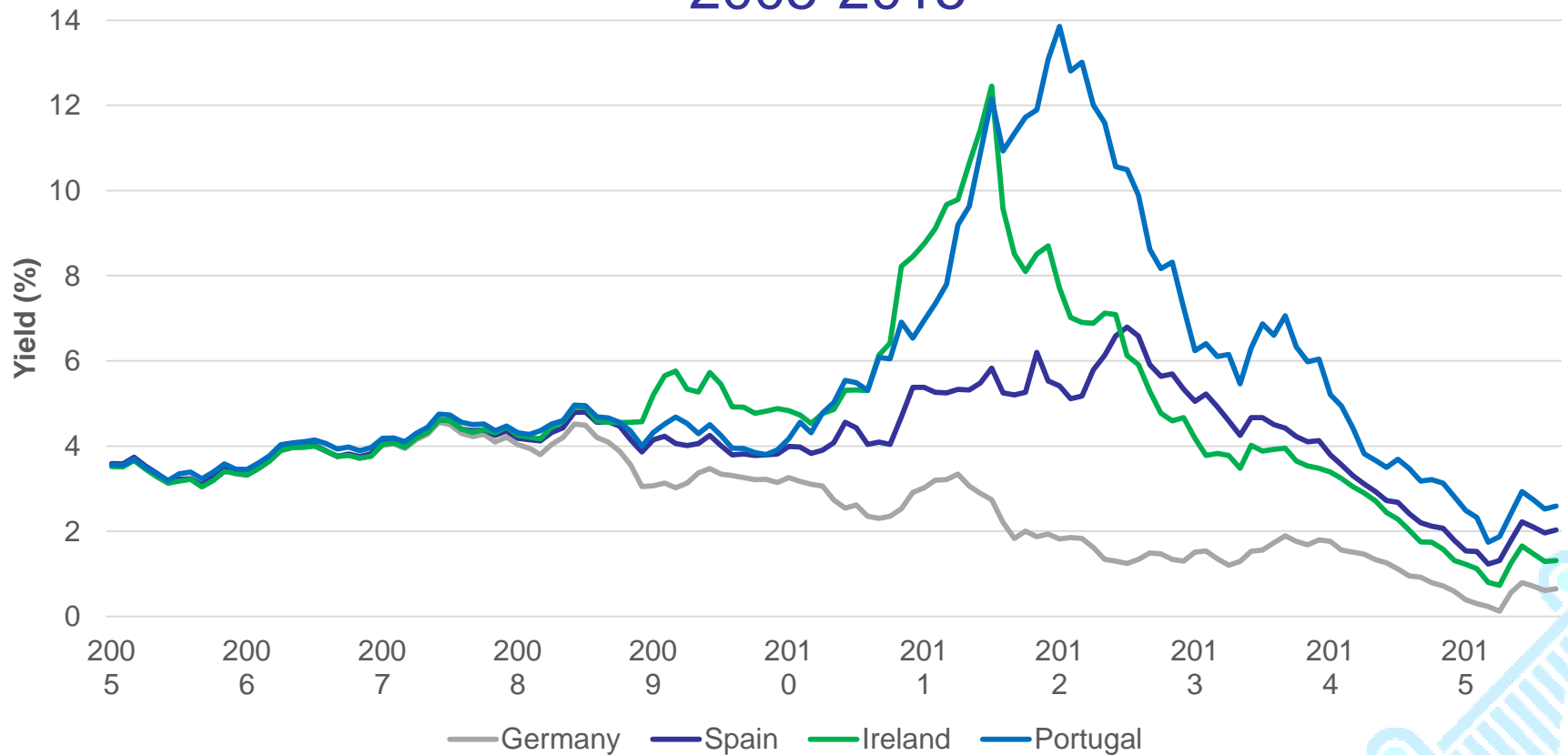
# Fiscal Consolidation 2008-2014



- Total fiscal consolidation of almost €30bn (19% GDP) in 2008-2014
  - Revenue measures accounted for €11bn
  - Expenditure measures accounted for approx. €19bn



## Selected Eurozone 10-Year Bond Yields: 2005-2015



Source: European Central Bank

# Fiscal Consolidation Principles

- Upfront Consolidation Effort
- More Spending Cuts than Revenue Raising
- Better targeted, focused capital spend
- Cut costs of delivering public services
- Protect vulnerable groups where possible and essential services
- All other spending areas scaled back
- Ministers / managers given cash ceilings – prioritisation and structural planning needed





# Key Consolidation Measures

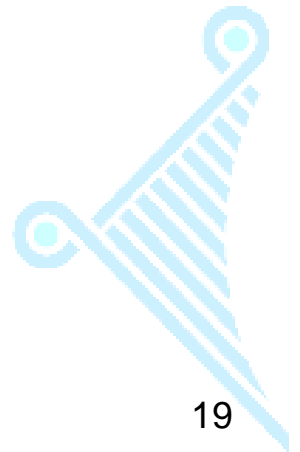
- Mid-2008: efficiency review; admin savings; capital
- 2009 (three budgetary events)
  - Income levy; expenditure growth arrested; pay increases stopped
  - Public service pension levy (pay cut)
  - Increased revenues (levy, PRSI); broad-based expenditure reductions
- 2010: €4bn adjustment (2.5% of GDP) – all expenditure based
  - Social welfare and public pay rates reduced
- 2011: €6bn adjustment (3.5% of GDP)
  - Taxation, social welfare, capital and other expenditure measures
- 2012: €3.8bn adjustment
  - 60% expenditure based with additional focus on indirect taxation (VAT)
- 2013: €3.5bn adjustment
  - Focus on current expenditure reduction and introduction of the Local Property Tax
- 2014: €2.5bn adjustment (€3.1bn when including one-off measures)
  - Haddington Road Agreement

# Linked with Public Service Reform

- Detailed Action-based reform plan
- Lean, policy focused public service
- Greater use of external service providers
- No areas of public service administration 'protected' from contribution to national savings effort
- Greater public (part-)contribution for receipt of public services



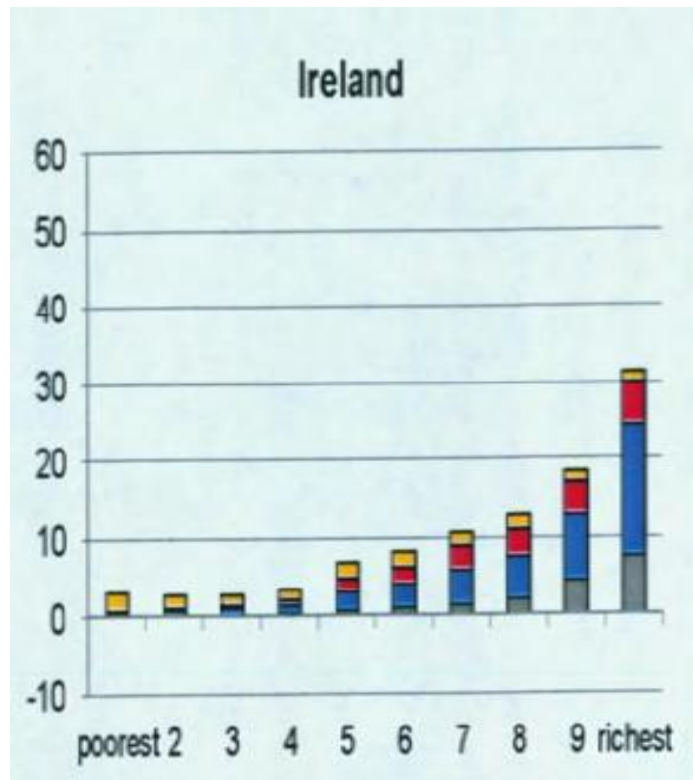
# Selected Impacts



# Illustrative Impacts on Different Groups

	2008	2012	% Change
20 year old jobseeker	€198pw	€100pw	-49%
Child benefit	€534pm	€428pm	-20%
Senior Public manager	€103,000pa	€74,000pa	-28%
Avg PS Employee	€48,000	€39,000	-19%
Old age pensioner	€212pw	€219pw	+3%

# Relative Impact of Austerity Measures

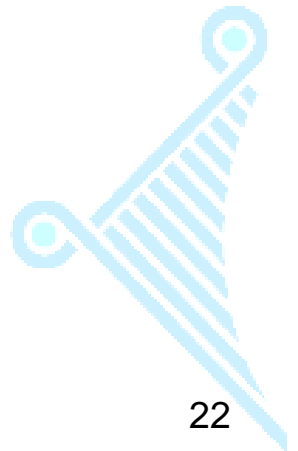


- Pensions and Benefits at lower deciles
- All other measures generally have higher impact at higher income

■ Employer SIC   ■ Worker SIC   ■ Income taxes   ■ Benefits and pensions   ■ Public sector pay (net)

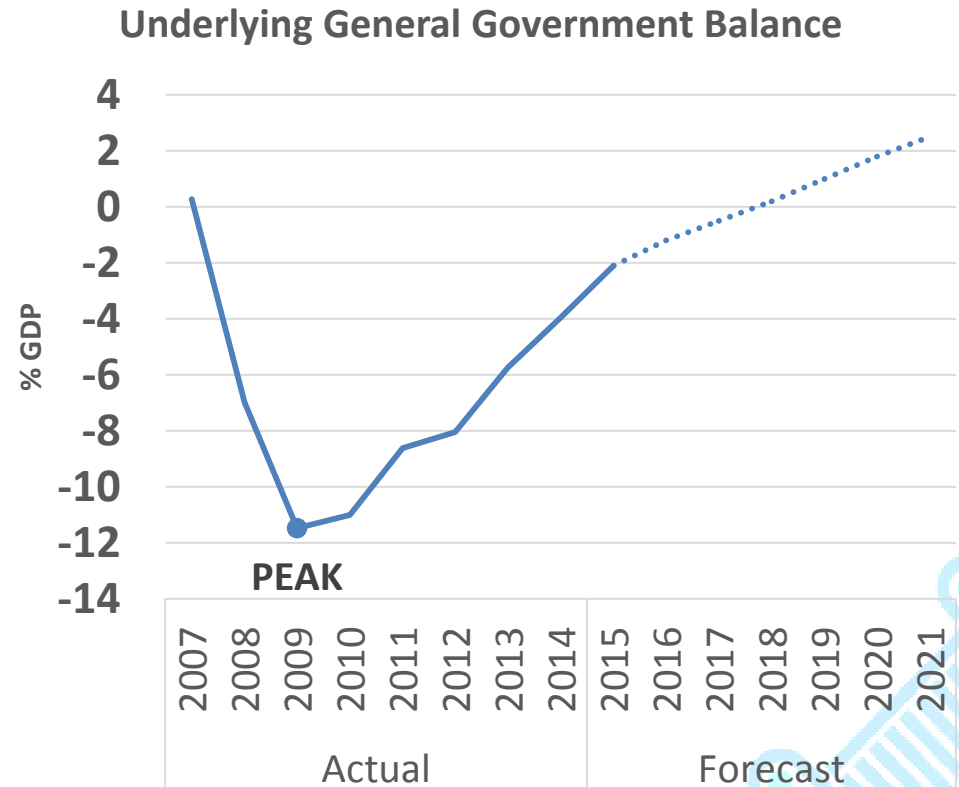
Source European Commission

# Future Fiscal Policy



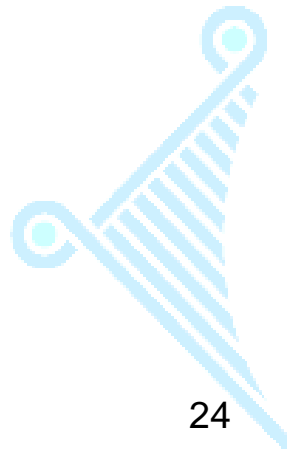
# Public Finances now on Stable Footing

- **Deficit Peaked in 2009**
  - Progress made towards <3% GDP target in years since
- **Successful Exit from EU/IMF programme in December 2013**
- **Ireland will exit the European Commission's EDP in 2016:**
  - Primary balance forecast in 2015
  - On-going primary surpluses



# Fiscal Policy Context and Considerations

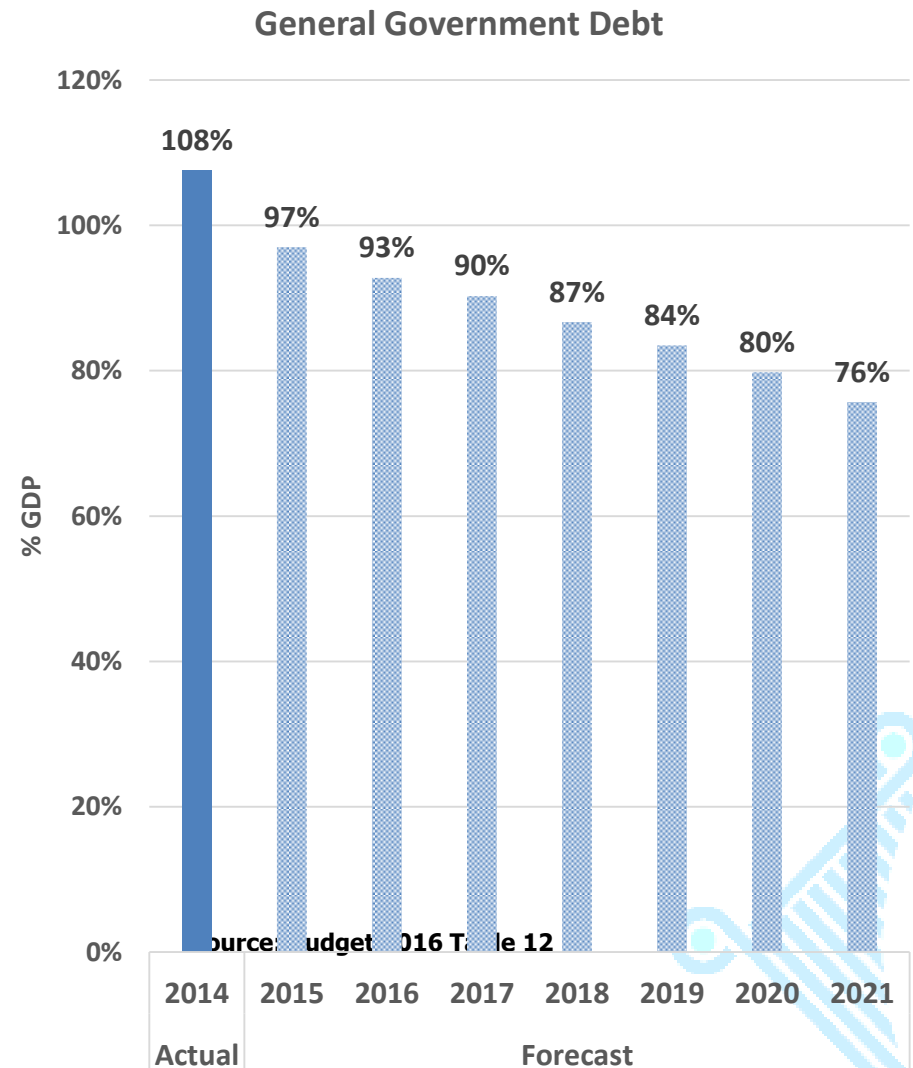
- High Public Debt
- Future Demographic Pressures - Slower future growth
- EU fiscal rules
- Need to run counter-cyclical policies



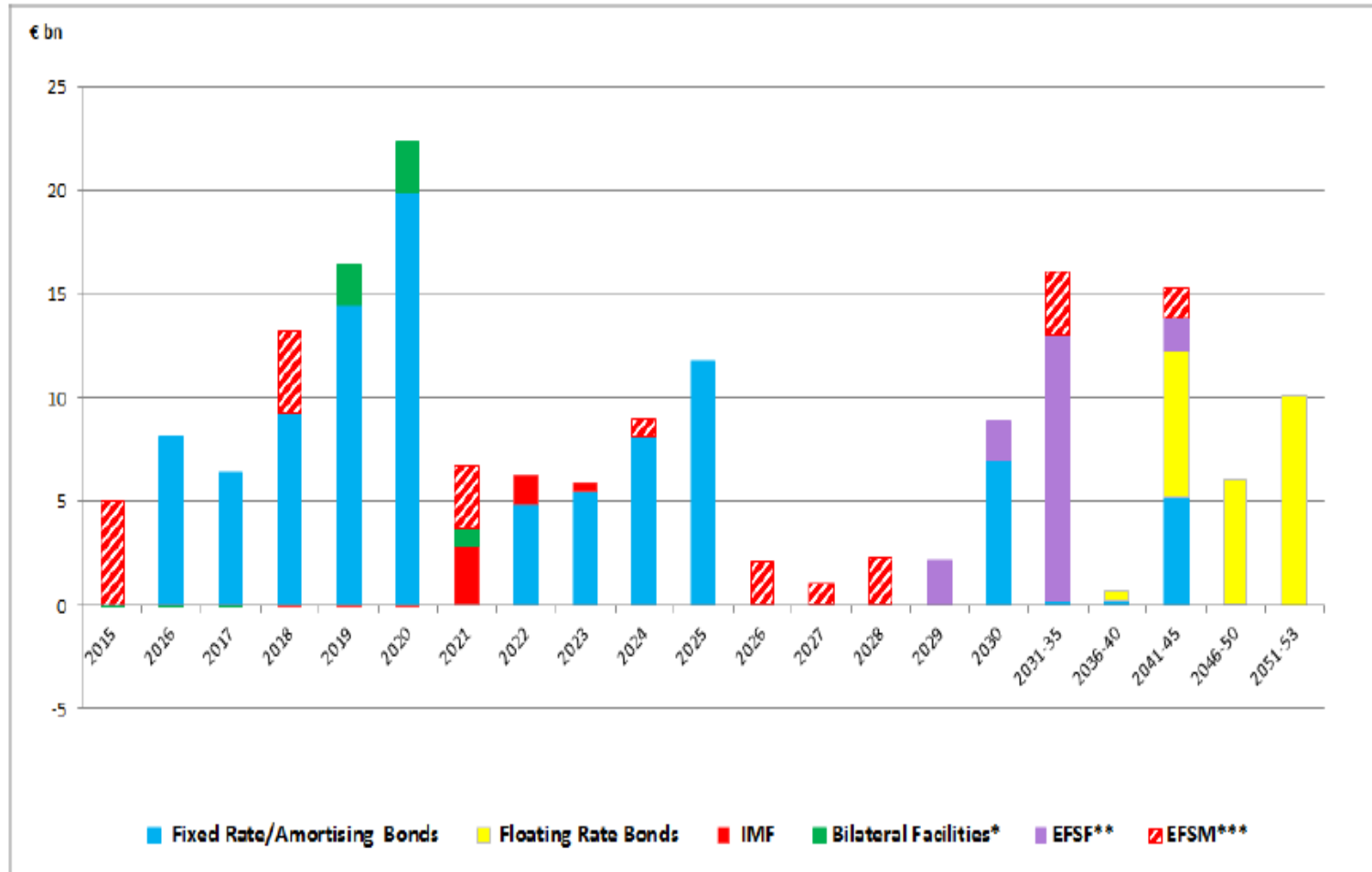


# High levels of Public Debt

- General Government Debt forecast at 97% at end-2015 (significantly higher than 2007 levels of 25%).
- Unlike in 2008, limited room for absorption of another fiscal or economic shock
- Progress must be made over coming years to reduce debt to more sustainable level (60% of GDP target)
- Net debt end of 2015 at 80% of GDP



# Maturity Profile of debt at end-September 2015



Source: NTMA

# Stabilising Debt Interest Costs

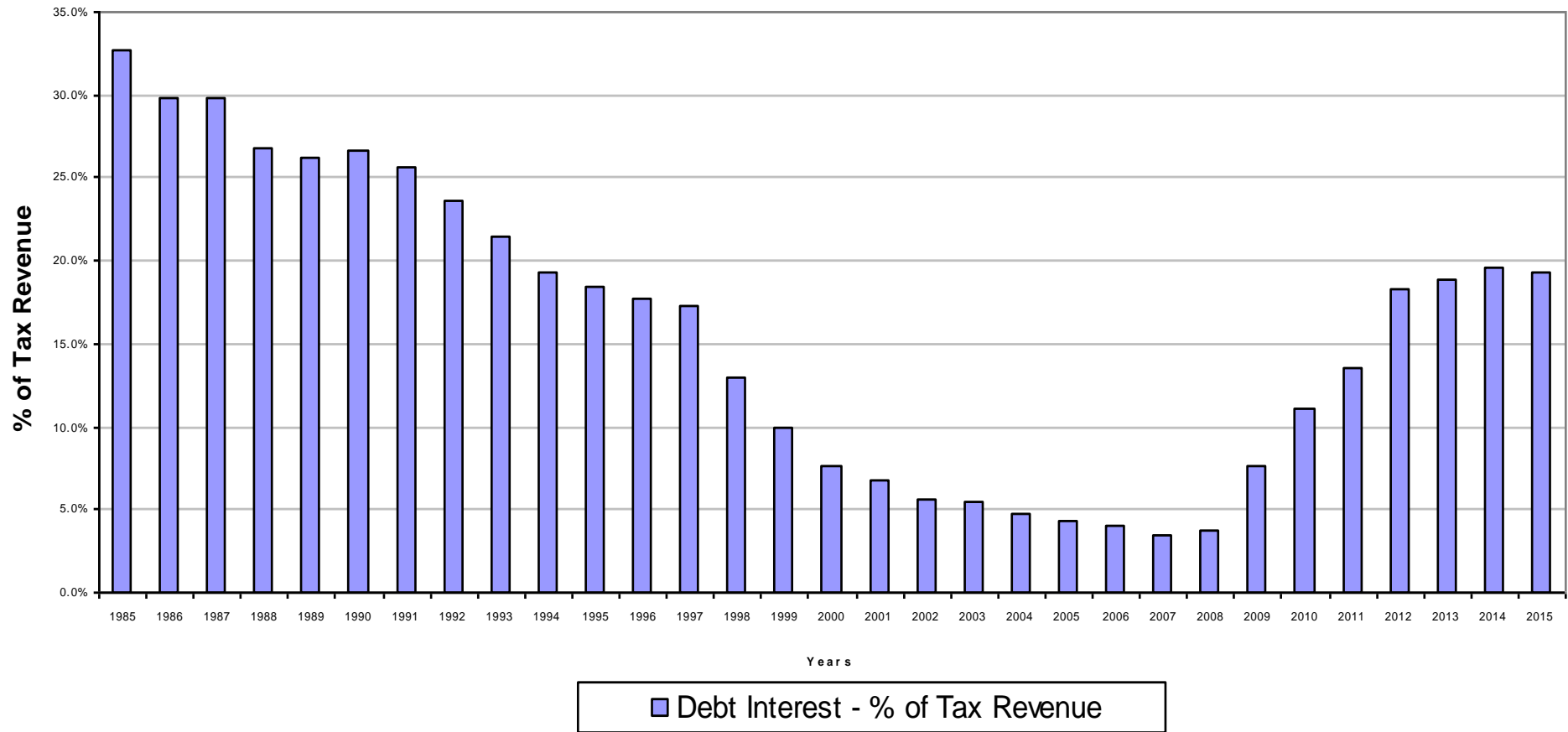


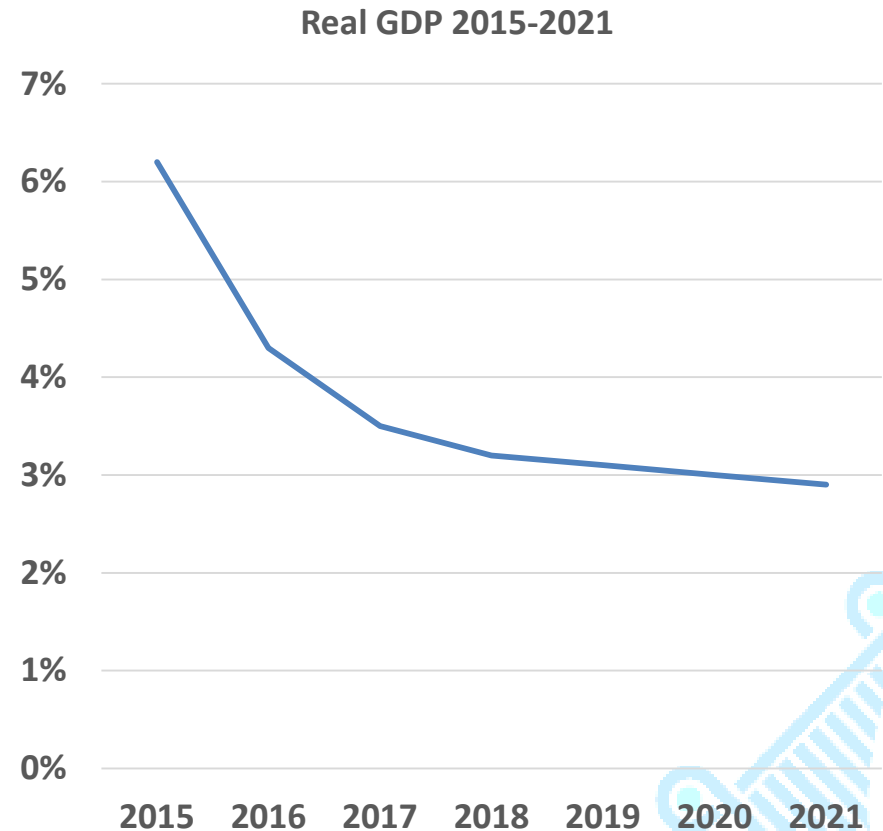
Chart shows debt interest payments as per cent of tax revenue (source – D/Finance & NTMA)

# New EU Fiscal Rules

- Revised EU fiscal structure has two arms: Corrective and Preventive
- Ireland will enter preventive arm post-2015 with deficit below 3% of GDP:
  - Medium-term Objective (MTO) defined in structural terms
  - Annual Structural Adjustment greater than 0.5% of GDP
  - Expenditure Benchmark sets limit on expenditure growth – grow in line with potential output.
- Once MTO is reached Expenditure Benchmark applies but uncertainty about application of rules and ability to deliver counter cyclical policies

# Growth to Moderate in Near Future

- Exceptionally high levels of growth in 2014 and 2015 set to moderate next year.
- However, average growth rate over the 2017-2021 period forecast at 3% annually.
- Expenditure will be anchored in the underlying growth rate of the economy going forward.



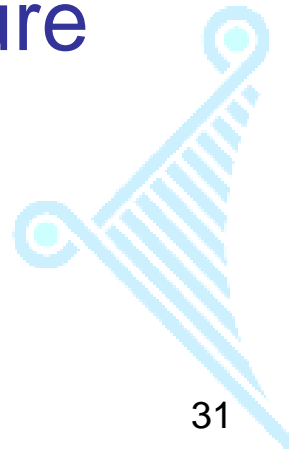
# Key Fiscal Forecasts: 2015-2021

% of GDP	2015	2016	2017	2018	2019	2020	2021
General Government Balance	-2.1	-1.2	-0.5	0.2	1.0	1.8	2.5
Structural Budget Balance	-3.2	-2.5	-1.4	-0.3	0.6	1.5	2.5
Change in structural balance		0.8	1.1	1.1	0.9	0.9	1.1
General Government Debt	97.0	92.8	90.3	86.7	83.5	79.8	75.7
Exchequer Balance (€ billion)	-2.8	-1.7	-4.0	-0.6	0.2	1.8	3.7

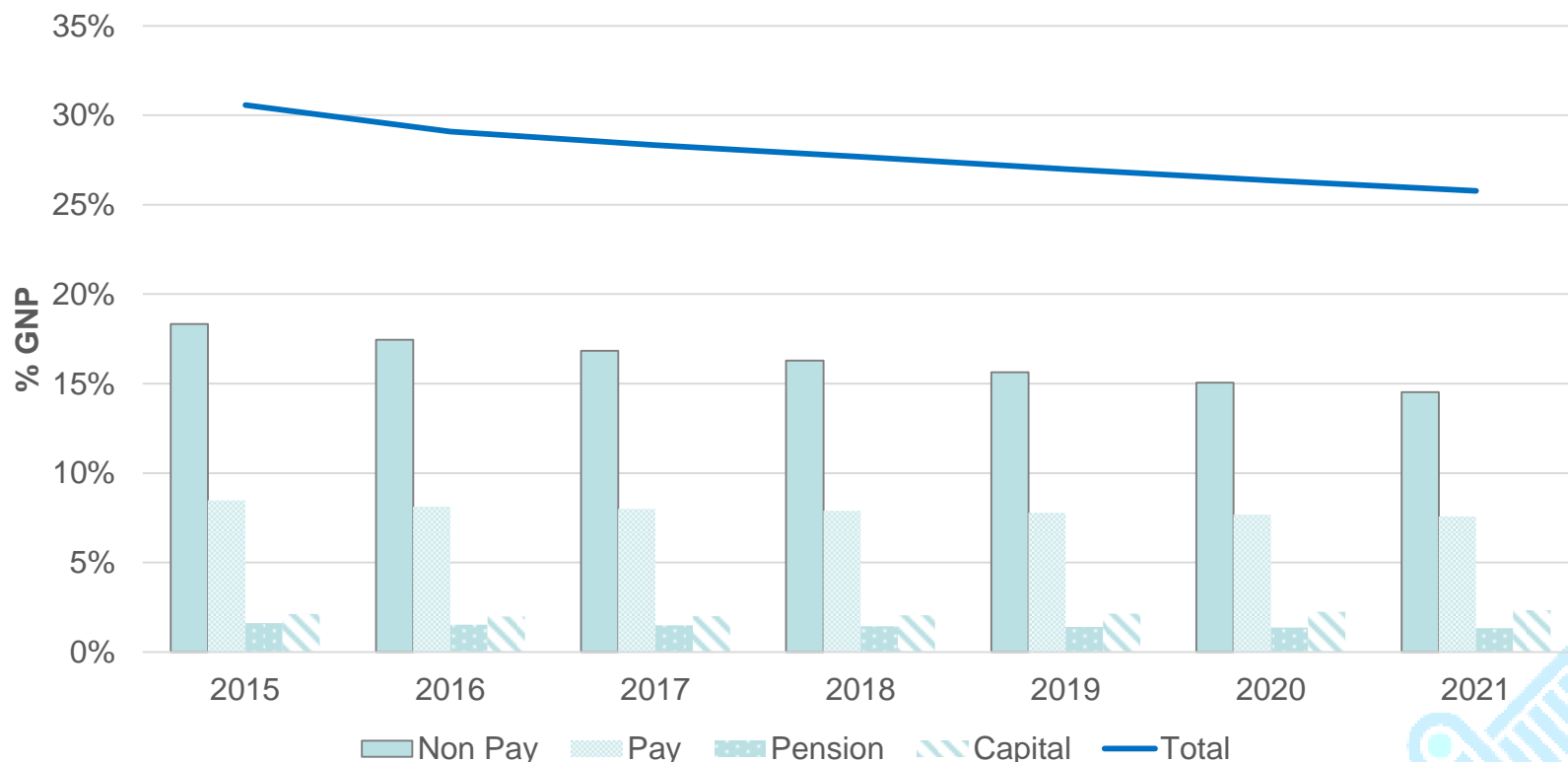
Source: Department of Finance. Rounding affects totals.

# Implications of Fiscal Targets

- Medium-term fiscal framework
- Medium-term Expenditure Framework
  - Challenge to operationalise given EU fiscal rules
  - Spending to fall as a % of GNP
- Comprehensive Review of Expenditure every 3 years
- 5 year capital plan
- 3 year pay deal



# Government Expenditure (excl. debt servicing costs) 2015-2021 (%GNP)

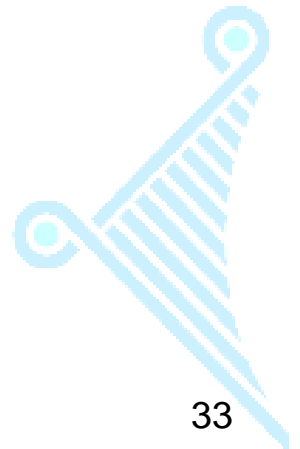


Source: Department of Public Expenditure and Reform, Department of Finance



# Some Selected Lessons on Fiscal Policy

- Manage better in good times
  - Reduce cyclicalities of government revenues
  - Cautious on estimates of potential output
  - Greater surveillance of imbalances
- Costs of Policy mistakes greater in Monetary Union
- Policy challenge in Ireland was to regain market confidence - pro- cyclical policy costly
- Medium-term policy framework essential



# Some Selected Lessons on Fiscal Policy

- Need top down fiscal targets
- Improved Fiscal Architecture
  - Fiscal Advisory Council has been established
  - Fiscal Responsibility Bill enshrining rules
  - Medium-term spending ceilings now operational
- Comprehensive Reviews of Expenditure
  - On-going Evaluation
    - Performance Information
- Link Spending Plans with Public Service Reforms