

**BUDGET 2014**

**ECONOMIC AND FISCAL  
OUTLOOK**

**(Incorporating Economic and Fiscal Statistics and Tables)**



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Economic and Fiscal Outlook  
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## Economic Developments and Outlook 2013-2016

**Table 1: Key Macroeconomic Forecasts 2012-2016**

	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>
	<i>% change, unless otherwise stated</i>				
Real GDP	0.2	0.2	2.0	2.3	2.8
Inflation (HICP)	2.0	0.7	1.2	2.0	2.0
Employment	-0.7	1.6	1.5	1.3	1.3
Unemployment (% of labour force)	14.7	13.5	12.4	11.8	11.4
Nominal GDP (rounded to nearest €25m)	163,950	165,875	170,600	176,950	184,675

Source: CSO: 2012; Department of Finance 2013-16

### Summary

Following weakness in the second half of last year, which continued into the opening months of this year, there is now mounting evidence that a modest recovery is taking hold in the Irish economy. Quarterly national accounts data show an increase in activity in the second quarter, while subsequent high-frequency data – both hard and soft – are suggestive of an economy gaining additional momentum in the period since then.

Importantly, there are increasing signs of a stabilisation in domestic demand, with data pointing to a gradual recovery in both consumer and investment spending. The strength of employment growth in recent quarters is also indicative of a modest recovery in domestic demand. On the external front, the recent data-flow has been reasonably encouraging and this improvement in external demand should support the exporting sector in the second half of the year. However, product-specific developments in the pharma-chem sector are clearly having an adverse impact on the overall export performance.

For 2013 as a whole, GDP is now expected to expand by 0.2 per cent, with a small negative contribution from net exports offset by a positive contribution from domestic demand (including stock-building); this forecast takes account of the relatively weak outturn in the early part of the year and the assumption of a recovery in the period since then.

Current prospects are for an acceleration in the pace of economic growth in Ireland next year, with GDP forecast to increase by 2.0 per cent. The contribution from domestic demand is expected to strengthen, which is encouraging. On the assumption of a pick-up in trading partner growth, exports are set to increase once again, although the potential for further reductions in pharma-chem output presents a notable risk to this projection.

### Recent macroeconomic developments

#### External demand

Exports of goods and services declined in the first half of this year as relatively weak external demand and product-specific developments impacted negatively. In terms of the latter, merchandise exports were down by 5.5 per cent on an annual basis in the first half of the year largely because of reduced pharmaceutical and chemical exports, owing to the 'patent cliff' effect. On the other hand, services exports have performed reasonably well growing by 2.4 per cent, with exports of IT services performing particularly strongly.

The overall picture in our main export markets appears to be one in which activity bottomed-out in the first quarter, and where a gradual recovery is underway. Second quarter data in key regions surprised on the upside, while subsequent high-frequency data have for the most part been reasonably encouraging. Against this backdrop, Irish exports

are expected to record modest annual growth in the second half of this year. This, however, is unlikely to be sufficient to make up the lost ground stemming from the first quarter outturn, with the result that exports are expected to contribute negatively to aggregate demand this year, decreasing by 0.6 per cent.

### **Domestic demand**

Turning to domestic demand, there is growing evidence that a modest recovery is now under way. The quarterly profile for personal consumption expenditure has been somewhat erratic over the course of this year, in part due to a structural change in the vehicle registration system which has had the effect of smoothing the purchase of vehicles over the course of the year. Initial estimates for consumer spending for the first quarter were subsequently revised upwards, and the possibility of further revisions cannot be excluded, particularly in an environment in which high-frequency data (core retail sales) point to a relatively strong pace of expansion in the third quarter. The latest data show a year-on-year increase in core retail sales (excluding car purchases) of 1.1 per cent in August and a year-on-year increase in headline sales of 2.6 per cent. For the year as a whole, a modest reduction of the order 0.2 per cent in consumer spending is now in prospect.

Investment in the first half of the year fell by about 10 per cent, although this was in large part due to negative base effects associated with purchases of new aircraft, which have a large weight in overall investment. On an adjusted basis, investment both in construction and non-aircraft machinery and equipment has seen a return to growth (albeit from very low levels). The recovery in investment spending is likely to have continued in the period since then, so that investment spending is projected to increase by 4.9 per cent this year.

In Ireland, the import content of both exports and domestic demand is relatively high, and early-year weakness in both of these components was reflected in declining imports. While imports of goods and services have subsequently picked-up, a modest decline is assumed for the year as a whole given the sharp fall in the first quarter.

Putting all of this together, GDP is projected to increase by around 0.2 per cent this year. GNP growth, which is largely unaffected by the patent cliff issue in the pharma-chem sector, is likely to be stronger at around 1 per cent this year.

## **Macroeconomic projections for 2014**

### **External demand**

Turning to the outlook for next year where, on the basis of the latest IMF World Economic Output projections, the external environment should be broadly supportive of an improvement in our export performance. For instance, weighted by their share in Irish exports, GDP growth in our main export markets is expected to increase by around 1.7 per cent next year (compared with around 0.6 per cent this year). The competitiveness improvements that have materialised over the past few years are also expected to impact positively, as evident from *inter alia* announcements on inward investment during this year. While the impact of the patent cliff may continue to weigh on goods exports, the pace of decline should be less severe than in 2013. An increase in exports of 1.9 per cent in 2014 is now projected, with net exports expected to contribute positively to GDP growth again.

**Table 2: External Assumptions**

<i>% Change</i>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>
<b>External GDP Growth</b>					
World	3.2	2.9	3.6	4.0	4.1
United States	2.8	1.6	2.6	3.4	3.5
Euro Area	-0.6	-0.4	1.0	1.4	1.5
United Kingdom	0.2	1.4	1.9	2.0	2.0
<b>Technical Assumptions</b>					
Euro-Sterling Exchange Rate	0.81	0.85	0.84	0.84	0.84
Euro-Dollar Exchange Rate	1.29	1.32	1.34	1.34	1.34
Brent Crude (US \$ per barrel)	112	109	104	98	94

*Source: IMF World Economic Outlook, October 2013 except for oil prices (futures prices) and exchange rates which are presented as ten-day moving averages as of late-September unchanged thereafter.*

### **Domestic demand**

Domestic demand is also expected to contribute positively to GDP growth in 2014. Personal consumer spending is expected to strengthen in response to the improvement in the labour market situation – rising employment should support household disposable incomes while falling unemployment should boost confidence and lead to a modest decline in the savings rate. The stabilisation of domestic activity should also support a continuing improvement in investment spending, both in construction and machinery and equipment.

Imports are projected to increase by 1.5 per cent next year, in line with the increase in final demand. In overall terms, therefore, GDP is projected to increase by 2.0 per cent next year; GNP growth is anticipated to be slightly lower at 1.7 per cent.

### **Medium-term growth prospects 2015 and 2016**

Beyond next year, the baseline scenario is one of a gradual strengthening of domestic demand over the medium term. A continuation of employment growth is expected to support further modest increases in personal spending, although high levels of household indebtedness and the need to repair household balance sheets mean that the savings rate will remain relatively high (although declining) over the medium term. Government consumption is set to contract in line with policy objectives of a reduction in public service numbers. Investment is set to increase at a modest rate as house-building picks up from current low levels (supported by demographic factors) and machinery and equipment investment gradually reverts to more normal levels.

Over the medium term, Ireland's export performance is expected to improve in line with the assumption of more favourable external conditions and further improvements in our price and cost competitiveness. The drag from the patent cliff on pharma-chem exports is also expected to diminish over the forecast horizon, as the global patent expiry process nears an end and new products come on stream.

**Table 3: Macroeconomic prospects and external balance, 2012 – 2016**

	2012	2012	2013	2014	2015	2016
	€m	<i>year-on-year percentage change</i>				
Real GNP	132,984	1.8	1.0	1.7	1.7	2.1
Real GDP	162,855	0.2	0.2	2.0	2.3	2.8
Nominal GDP	163,938	0.8	1.2	2.9	3.7	4.4
	<i>current</i>					
<b>Components of GDP</b>	2012 €m	<i>year-on-year percentage change</i>				
Personal consumption	82,634	-0.3	-0.2	1.8	1.2	1.1
Government consumption	25,096	-3.7	-0.9	-1.9	-1.5	0.2
Investment	17,434	-1.0	4.9	6.8	5.9	5.1
Stock changes (% of GDP)	376	0.2	0.4	0.2	0.2	0.2
Exports	176,735	1.6	-0.6	1.9	2.7	4.2
Imports	136,990	0.0	-0.4	1.5	2.1	3.5
<b>Contributions to real GDP growth</b>		<i>annual percentage point contribution</i>				
Domestic demand		-0.8	0.3	1.4	1.1	1.2
Stock changes		-0.4	0.2	-0.2	0.0	0.0
Net exports		1.6	-0.2	0.8	1.2	1.6
		<i>€ millions</i>				
Nominal GDP (rounded to nearest €25m)		163,950	165,875	170,600	176,950	184,675
<b>External balance</b>		<i>per cent of GDP</i>				
Current account (% of GDP)		4.4	4.4	4.0	3.8	3.7

Source: 2012 - CSO; 2013 to 2016 - Department of Finance

Rounding may affect totals

### The labour market 2013-2016

After a number of very difficult years, a recovery in the labour market is now clearly taking hold. For instance, data from the quarterly national household survey (QNHS) show that annual employment growth averaged 1.5 per cent in the first half of the year. Encouragingly, this reflected an increase in both full-time and part-time employment and was broad-based across the majority of sectors in the economy.

Available indicators point to continued employment growth in the period since the second quarter, so that employment growth of 1.6 per cent is now projected for this year as a whole. Given the assumed path for domestic demand – which is more jobs-rich than externally-driven growth – employment growth of 1.5 per cent is now projected for next year, with further increases in employment projected over the forecast horizon.



## The fall in productivity this year

Labour productivity, defined as output per worker<sup>1</sup>, is one of the most important variables in economic analysis, as it is a key driver of living standards over the longer term. While volatile on an annual basis, productivity growth in Ireland has averaged around 2½ per cent per annum since the early 1990s.

This year, however, labour productivity is projected to decline by 1¼ per cent. One of the reasons behind this unusual phenomenon would appear to be the changing composition of economic activity. Output is currently falling in the pharmaceutical sector due to the patent cliff issue. The pharma-chem sector accounts for about a quarter of exports and about 12 per cent of gross value added (GVA), but the labour share of this sector is small relative to its profit share. No adverse impacts from the fall in output on employment in the sector have been recorded to date. When sectoral output decreases without a corresponding impact on employment, productivity is depressed. As this sector is very large relative to Ireland's overall GDP, aggregate economy-wide productivity is thereby being reduced.

While other factors may be at work, this compositional shift in activity would appear to be one of the factors underlying this apparent productivity puzzle. It should also be highlighted that this is a temporary phenomenon and a more normal productivity pattern is expected next year and over the medium-term as output growth accelerates.

Unemployment has continued to fall over the course of this year, with a survey-based rate of 13.7 per cent in the second quarter. Live Register data point to a further decline subsequently – in September, the standardised unemployment rate was 13.3 per cent, its lowest in three and a half years. For the year as a whole, the unemployment rate is forecast to average 13.5 per cent. With continued employment growth in prospect, a further decline in the unemployment rate to an average of around 12.4 per cent is envisaged for next year. However, historical experience demonstrates that an increase in labour supply – through the migration and participation rate channels – tends to accompany employment improvements in Ireland. As a result, even with employment growth over the forecast horizon, the unemployment rate is unlikely to fall very rapidly. The baseline scenario therefore is one in which the unemployment rate reaches around 11½ per cent by the mid-part of this decade; however, there is some upside potential to the labour market outlook stemming from the measures introduced as part of the *Action Plan for Jobs 2013* and the *Pathways to Work* initiatives, which may have a larger-than-assumed impact on employment levels (and consequently on unemployment) over the short- and medium-term.

**Table 4: Labour market developments**

	2012 ('000s)	2012 % change (unless otherwise stated)	2013	2014	2015	2016
Employment	1,837	-0.7	1.6	1.5	1.3	1.3
Unemployment rate (QNHS basis)	317	14.7	13.5	12.4	11.8	11.4
Labour productivity (GDP per person employed)		0.9	-1.3	0.5	0.9	1.5
Compensation of employees*		0.1	1.5	3.5	3.1	3.6
Compensation per employee		-1.8	0.6	1.9	1.7	2.4

Source: 2012 - CSO and Department of Finance calculations; 2013-16 - Department of Finance projections.

\* This refers to whole economy non-agricultural wages.

<sup>1</sup> Or more accurately GDP per hour worked.

## Price developments

Inflationary pressures remain contained, given spare capacity in the economy and associated weak pricing power. In the first three quarters of this year, the harmonised index of consumer prices (HICP) increased by just 0.6 per cent relative to the same period of last year. Goods prices fell by 0.6 per cent, in part due to declining energy prices; exchange rate developments also played a role in depressing goods price inflation. On the other hand, the price of consumer services increased by 1.9 per cent in the year-to-date. For the year as a whole, HICP inflation is now projected to average 0.7 per cent this year.

Looking ahead to next year, a modest acceleration in the pace of consumer price inflation is in prospect. Taking into account the budgetary measures as well as other drivers of inflation, the HICP is projected to increase by 1.2 per cent next year.

**Table 5: Price developments**

	<i>Annual % Change*</i>				
	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>
GDP deflator	0.6	0.9	0.8	1.4	1.5
Private consumption deflator	0.6	1.0	1.3	1.8	1.8
Harmonised index of consumer prices (HICP)	2.0	0.7	1.2	2.0	2.0
Export price deflator (goods and services)	4.2	0.5	0.6	1.2	1.4
Import price deflator (goods and services)	3.9	0.4	1.1	1.3	1.4

*Source: 2012 - CSO and Department of Finance calculations; 2013-16 - Department of Finance projections.*

## Fiscal Outlook 2013-2016

**Table 6: Key Fiscal Forecasts 2013-2016**

<i>% of GDP</i>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>
Underlying General Government Balance	-7.3	-4.8	-2.9	-2.4
General Government Debt	124.1	120.0	118.4	114.6
Exchequer Borrowing Requirement (€billion)	11.3	9.6	6.0	2.9

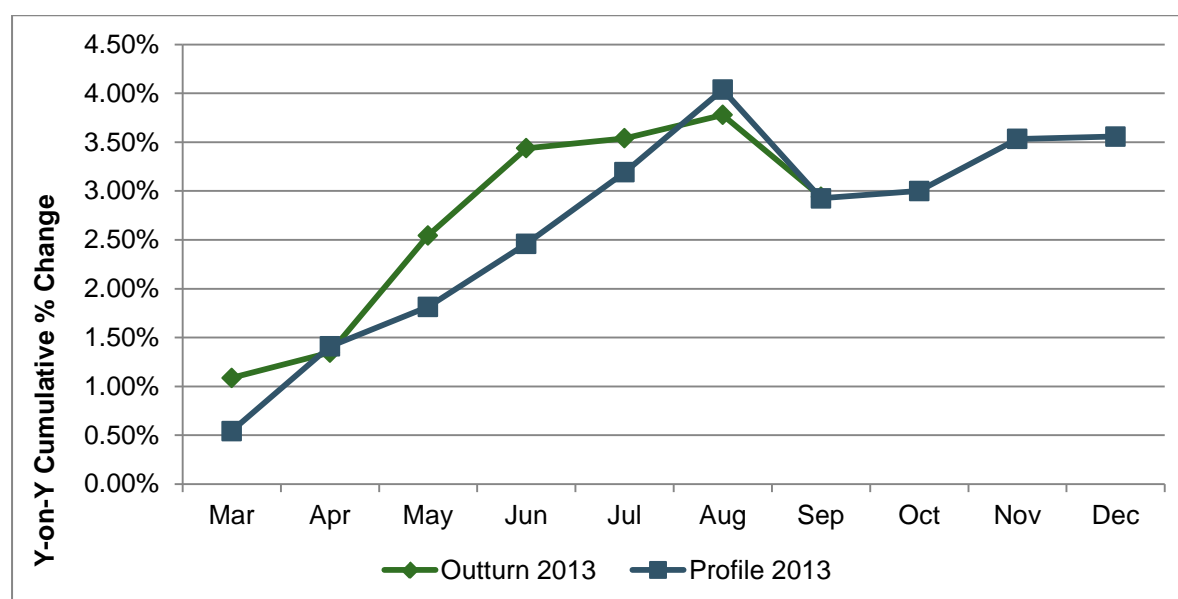
*Source: Department of Finance*

### **Fiscal Outlook 2013**

Ireland remains on track to meet its obligations under the Excessive Deficit Procedure with a forecast underlying general government deficit of 7.3% of GDP which represents a slight improvement to the underlying deficit of 7.4% of GDP which was estimated in April's Stability Programme Update. Tax revenues remain broadly in line with projections and are expected to finish the year in the region of €38bn. Expenditure is also expected to perform in line with expectations as set out in the April 2013 Revised Estimates Volume. In addition to the solid performance of taxes and expenditures, there have also been a number of one-off developments impacting both positively and negatively which will be discussed in more detail below.

Looking at the performance of tax revenues in the period to end-September, taxes remain in line with the 2013 profiles despite some variations at individual tax head level.

**Figure 1: End-September Cumulative Tax Revenue Outturn vs Profile**



*Source: Department of Finance*

As has been evident all year, excise duties continue to be below profile and a shortfall of €200m is expected for the year, with declines in receipts from alcohol and tobacco the main contributors. The shortfall in value-added tax (VAT) can be largely explained by a sector-specific issue unrelated to personal consumption expenditure. Encouragingly, VAT in September, reflective of trading during July and August, was up €80m on expectations. This is consistent with the uptick in retail sales over the summer and the impact of the change in the car registration system. Nevertheless, this positive momentum in the

domestic economy will be more than offset by the sector-specific VAT issue and a shortfall on the 2013 Budget day target of €200m is expected.

Turning to income tax, the largest tax head, performance in the year to date has been healthy. The position at end-September is a small shortfall of €80m. This is substantially attributable to lower-than-expected DIRT receipts as a result of the low interest rate environment. Encouragingly, PAYE and other income tax receipts are actually ahead of target to end-September, reflective of the better-than-expected performance of the labour market. However, with one more DIRT payment scheduled for October, it is likely that there will be some further moderate slippage in the income tax heading.

Against these downsides, there has also been an over-performance relative to expectation in some key tax heads, with corporation tax performing particularly well, up €240m against profile at end-September. On the basis of information to hand, it is likely that this over-performance will be maintained for the full year. Stamp duties represent the other big contributor to the surplus, with volumes increasing across the board, from property transactions to share disposals. In particular, the over-performance of the pension levy in 2013 relative to expectations is welcome and comes as a result of an appreciation of the capital value of pension funds. Taking stamp duties as a whole, the estimated end-year outturn relative to Budget is now a surplus of €130m.

Taking account of the end-September position, the Department of Finance is now of the view that tax revenues will finish the year as a whole some €125m or 0.3% below the 2013 Budget day targets.

Aside from tax revenues and expenditure, a number of one-off developments are shaping the end-year outlook. In terms of non-voted expenditure, probably the most significant figure is the €1,100m payment under the eligible liabilities guarantee (ELG) scheme and IBRC Derivative guarantee required as a consequence of the liquidation of IBRC. Also related to the promissory note transaction, there was a technical general government accrued interest adjustment of c. €200m. Furthermore, the EU Budget contribution will be c.€300m higher than the amount included in Budget 2013 due to a combination of higher EU spending and upwards revisions to Ireland's estimated gross national income (GNI) for previous years on which our EU Budget contribution is calculated.

Benefitting the Exchequer position in 2013 were some significant financial sector transactions. The sale of the Bank of Ireland contingent capital instruments in January saw the Exchequer receive €1,057 million, while all told the sale of Irish Life to Great Canadian Western brought in €1,340 million. However, it should be noted that the vast majority of the receipts generated from the sales are classified as a 'financial transaction', and as such they do not improve the general government balance, the basis on which our deficit targets are set.

Turning to the spending side, the *Revised Estimates for Public Services 2013 (REV)* set out the allocations for Departmental expenditure in 2013. In gross spending terms<sup>2</sup>, this 2013 allocation, at €54.6 billion, is 2.2% down on the latest 2012 gross expenditure outturn figure of €55.8 billion. On the basis of the detailed monthly gross and net profiles that were published with the REV, the overall gross Departmental voted expenditure at end-September was €39.7 billion, or €730 million (-1.8%) below profile. Of this €730 million,

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<sup>2</sup> Overall expenditure by Departments, whether funded directly by the Exchequer or through Departmental receipts ("appropriations-in-aid")

€426 million is on the day-to-day, current expenditure side, with €304 on capital. While a large element of this reflects timing issues which will be resolved before the end-year there are likely to be some moderate end years savings in aggregate terms.

In relation to net voted expenditure, the end-September position was €879 million below profile. In addition to the gross expenditure position set out above, higher than anticipated receipts from PRSI contributions and National Training Fund were recorded. It is expected that this will persist for the remainder of the year and impact favourably on the end year position.

Overall, the end year position for Departmental expenditure is expected to be in line or below profile.

National debt servicing costs in 2013, on a cash basis, are now expected to be around €500 million lower than estimated at the time of the SPU in April. This reduction primarily reflects a more favourable interest rate environment generally and the fact that in light of its relatively healthy cash position, the NTMA does not intend to engage in any further market activity this year.

In terms of one off factors impacting on 2013, after a clarification by Eurostat on the timing of recording of the disposal of non-produced assets, the sale of the fourth generation mobile internet licences which took place in 2012, and the impact of granting the licence to run the national lottery to Premier Lotteries Ireland in October 2013, are now recorded in 2013 and 2014 respectively. This has a net impact of improving the general government deficit by c. €325m in 2013 and by €405m in 2014.

Finally, a lowering of the denominator from 2013 onwards also makes achievement of the future fiscal targets more difficult. In the SPU, a nominal GDP figure of €167.9bn was forecast for 2013. Taking onboard a weaker than expected first half of 2013, the revised estimate for the end-year outturn is €165.9bn. This increases the headline deficit by about 0.1 percentage points of GDP.

Taking all of these factors into account, the general government balance for 2013 is forecast at -7.3% of GDP, representing a modest improvement to the SPU forecast, and is crucially, again, within the EDP ceiling of 7.5%.

### **Impact of consolidation on the fiscal position in 2014**

Implementing any budgetary adjustment package imposes short-term costs on the economy as taking money out of the economy by reducing government expenditure and/or raising taxes has a dampening effect on overall activity and employment, all other things being equal. However, international experience, as well as the recent Irish experience, has offered some guidance as to how to minimise such negative impacts.

The adjustment package being implemented by Budget 2014 has been developed with the explicit goal of minimising, to the greatest extent possible, the impact of the necessary adjustments on the economy. Tax and expenditure consolidation measures of €2.5 billion are complemented with additional resources and savings of some €600 million, giving a total adjustment package of €3.1 billion. In addition a significant portion of the tax measures are focused in a way that their impact on employment, and thus demand should have limited, if any, negative impact on economic activity. Table 7 sets out that the estimated loss in tax revenue arising from the introduction of new budgetary measures of

€1.85 billion in 2014 is about €400 million. This is commonly referred to as “negative buoyancy”. The €400 million loss in tax revenue has been factored into the overall budgetary arithmetic set out in Table 9.

**Table 7: The Impact of *Budget 2014* on the Fiscal Position in 2014**

	<u>€m</u>	<u>€m</u>
<b><u>Total Budget Package (Net New Measures)<sup>3</sup>:</u></b>		<b>1,850</b>
<b><u>Net New Tax Measures:</u></b>		<b>350</b>
Stamps		285
Income Tax (including DIRT)		216
Excise Duty (including VRT)		103
Other		35
Capital Gains Tax		-1
Corporation Tax		-5
VAT (including from Excise Increases)		-283
<b><u>New Expenditure Measures:</u></b>		<b>1,500</b>
Current		1,400
Capital		100
<i>Impact of New Consolidation Measures on Budget 2014 Tax Forecast</i>		-400
	<b><u>WHITE</u></b>	<b><u>BUDGET</u></b>
	<b><u>PAPER</u></b>	<b><u>2014</u></b>
	€m	€m
<b><u>Current Revenue</u></b>		
Tax Revenue	40,090	40,040
Non-Tax Revenue	<u>1,870</u>	<u>1,980</u>
<b>Current Revenue</b>	<b>41,960</b>	<b>42,020</b>
<b><u>Current Expenditure</u></b>		
Net Voted	39,695	38,385
Non-Voted	<u>10,770</u>	<u>10,755</u>
<b>Net Current Expenditure</b>	<b>50,465</b>	<b>49,140</b>
<b>CURRENT BUDGET BALANCE</b>	<b>-8,505</b>	<b>-7,120</b>
<b><u>Capital Receipts</u></b>	<b>1,690</b>	<b>1,690</b>
<b><u>Capital Expenditure</u></b>		
Net Voted	3,005	3,000
Non-Voted	<u>1,160</u>	<u>1,160</u>
<b>Net Capital Expenditure</b>	<b>4,165</b>	<b>4,160</b>
<b>CAPITAL BUDGET BALANCE</b>	<b>-2,475</b>	<b>-2,470</b>
<b>EXCHEQUER BALANCE</b>	<b>-10,980</b>	<b>-9,590</b>
<b>UNDERLYING GENERAL GOVERNMENT BALANCE</b>	<b>-9,842</b>	<b>-8,165</b>
<b>% of GDP</b>	<b>-5.8</b>	<b>-4.8</b>

Sources: Department of Finance & Department of Public Expenditure and Reform.

Notes:

- Rounding can affect totals.

- The current and capital expenditure savings are consistent with the aggregate figures as per the Expenditure Report 2014.

<sup>3</sup> A further €0.53 billion in revenues arising from measures introduced previously (the “carry-over”) are estimated to benefit 2014. In addition, expenditure measures introduced previously will contribute a further €0.1 billion to consolidation. €0.6 billion of the budgetary adjustment comes from additional resources and savings elsewhere. Adding all of these to the €1.85 billion in new policy measures outlined above gives a total adjustment package of €3.1 billion in 2014.

## **Fiscal outlook 2014**

In addition to positioning the State to exit the EU/IMF Programme successfully, Budget 2014 represents the penultimate step in bringing Ireland's deficit below the 3% of GDP target. Over the last number of years, Ireland has continued with steadfast implementation of necessary fiscal consolidation and structural reforms. 2014 represents a return to normality whereby Ireland will be funding itself from the markets and will not be reliant on external funding arrangements. The importance of Ireland's successful exit from the programme cannot be overstated. It is in this context that this Budget package has been constructed, both to reassure markets and support to the greatest extent possible, the emerging economic recovery and the continued creation of jobs.

The April Stability Programme Update made a technical assumption about fiscal policy resulting in a general government deficit in 2014 of 4.3% of GDP. Based on the assessment of the economy at that stage the anticipated technical deficit forecast afforded considerable headroom in terms of meeting the agreed Excessive Deficit target of 5.1% for 2014. However, on foot of a number of adverse developments, principally a weaker than expected economic outlook, this is no longer the case. In terms of forecast nominal GDP, the SPU forecast of €174bn has now been reduced to €171bn. Setting aside the negative impact on the revenue growth associated with this, the denominator effect alone adds over 0.1 percentage points of GDP to the deficit reduction requirement.

An underlying general government deficit of 4.8% of GDP is forecast for 2014. Achievement of this target is predicated on a consolidation package of €2.5 billion complemented with €0.6 billion of additional resources and savings.

Tax revenue is expected to grow by 5.8% in 2014, based on nominal GDP growth of 2.9% and the impact of both new and carryover revenue measures. Table 8 sets out the year-on-year growth rate for 2014 of the individual tax heads based on the estimated end-2013 outturn. Looking at the individual tax heads, of particular note is the significant increase in income tax of just over 8%. This is driven by a combination of a recovering labour market, with modest growth in wages and continuing expansion of employment, and the impact of budgetary measures. Offsetting this, the maintenance of the VAT rate at 9% in the tourism and hospitality sector is expected to cost the Exchequer about €290m in 2014 and €350m in a full year, the figures which underpinned previous budgetary arithmetic.

**Table 8: Exchequer Tax Revenues 2013-2014**

	<b><u>Estimated</u></b> <b><u>Outturn</u></b> <b><u>2013</u></b> €m	<b><u>Budget</u></b> <b><u>Forecast</u></b> <b><u>2014</u></b> €m	<b><u>Forecast</u></b> <b><u>Y-on-Y</u></b> <b><u>Change</u></b> %
Customs	250	255	+1.4
Excise Duty*	4,720	4,815	+2.0
Capital Gains Tax (CGT)	390	400	+3.2
Capital Acquisitions Tax (CAT)	405	380	-5.9
Stamp Duty	1,310	1,475	+12.6
Income Tax	15,730	17,045	+8.3
Corporation Tax	4,355	4,380	+0.6
VAT	10,365	10,740	+3.6
Local Taxes	300	550	+83.3
<b>Total</b>	<b>37,825</b>	<b>40,040</b>	<b>+5.8</b>

Source: Department of Finance.

Figures are rounded to the nearest €5 million. Year-on-year changes reflect actual figures.

\*Excise duties include carbon tax and revenues from the recent increases in motor tax rates

The gross voted current expenditure of Government Departments is now forecast at under €50 billion in 2014, a reduction of 3% on the 2013 provision set out in the *Revised Estimates for Public Expenditure 2013*, but still some €9.6 billion more than will be collected in tax revenues next year. In light of the need to continue to reduce expenditure to bring it more in line with available resources, reductions will be implemented right across the board and in virtually all Ministerial Vote Groups.

Changes will also be made to the voted capital expenditure envelope for 2014. Gross voted spending is estimated at just over €3.3 billion in 2014, which includes the previously announced stimulus package of €110 million and a further provision for investment spending of €200 million funded from the proceeds of the sale of the National Lottery licence. All told there is provision for some 2.4% of GNP to be spent on capital projects next year.

Central fund services (non-voted current expenditure) in 2014 are broadly unchanged at a headline level compared to 2013. However, while the impact of the payout under the ELG scheme associated with the IBRC liquidation will not be repeated next year, debt servicing costs will increase in 2014. This increase reflects the higher stock of national debt outstanding as well as the full year costs of the borrowing undertaken in 2013, including EU/IMF Programme draw-downs as well as the €25 billion in Government bonds issued to replace the IBRC Promissory Notes.

In terms of non-tax revenues, there is a substantial fall of 22% expected relative to 2013. There are a number of reasons for this, most prominently the fall of nearly €400m in fees received from the ELG scheme. This was to be expected following the successful closing of the scheme for new liabilities in March of this year. In terms of dividends, lower surplus income from the Central Bank and commercial semi-state bodies account for a further fall of c.€200m. Overall, about €2bn is expected to be collected from non-tax revenues.

Capital receipts are also projected to decline in 2014. The State's sale of Bank of Ireland contingent capital notes and Irish Life in 2013 boosted capital receipts by €2.3bn. A repetition of this level of one-off receipts is not envisaged.

Encouragingly, 2014 marks the first time since 2007 that an underlying general government primary surplus is forecast, albeit a modest one. This means that, excluding debt service costs, revenues are sufficient to meet expenditures. This is a key metric in assessing the underlying sustainability of Ireland's public finances and is a necessary first step towards lowering our debt levels.

### **Fiscal Outlook 2015-2016**

The fiscal outlook in 2015 remains broadly unchanged from that which was set out in the SPU in April of this year. The Government remains committed to bringing the deficit below the 3% of GDP deficit target as set out in the Excessive Deficit Procedure. Further consolidation will be necessary to achieve this target in Budget 2015 but given the magnitude of previous budgetary adjustments, the required consolidation will not be as large. However this reduced fiscal effort is contingent on a continuation of growth, which is subject to a number of risks which are outlined elsewhere.

Ireland is on track to bring the headline deficit below 3% of GDP by 2015; in other words, to correct the excessive deficit. Once the excessive deficit is corrected, it will be necessary to make rapid progress towards achieving our medium term budgetary



objective (MTO), which is for a balanced budget once allowance is made for the impact of the economic cycle on the public finances. It is important to highlight that in Ireland, where the potential growth rate of the economy remains relatively good, improvements in the structural budgetary position can be achieved without necessarily involving additional taxation increases or expenditure reductions. For instance, maintaining expenditure growth below the nominal growth rate of the economy – as provided for in the so-called ‘expenditure benchmark’ (a tool which complements the assessment of progress towards the MTO) – would, in the absence of additional consolidation, result in an improvement in the structural fiscal position.

**Table 9: Fiscal Forecasts 2013-2016**

€ million	2013	2014	2015	2016
<b>CURRENT BUDGET</b>				
<b>Expenditure</b>				
Gross Voted Current	51,145	49,605	48,250	48,600
Non-Voted Current (Central Fund)	10,995	10,755	11,390	11,810
<b>Gross Current</b>	<b>62,140</b>	<b>60,360</b>	<b>59,640</b>	<b>60,410</b>
less Receipts and Balances (including PRSI)	10,945	11,220	11,580	11,875
<b>Net Current</b>	<b>51,195</b>	<b>49,140</b>	<b>48,060</b>	<b>48,535</b>
<b>Receipts</b>				
Tax Revenue	37,825	40,040	42,285	43,985
Non-Tax Revenue	2,555	1,980	1,930	1,820
<b>Net Current Revenue</b>	<b>40,380</b>	<b>42,020</b>	<b>44,215</b>	<b>45,805</b>
<b>CURRENT BUDGET BALANCE</b>	<b>-10,815</b>	<b>-7,120</b>	<b>-3,845</b>	<b>-2,730</b>
<b>CAPITAL BUDGET</b>				
<b>Expenditure</b>				
Gross Voted Capital	3,430	3,335	3,250	3,255
Non-Voted Capital	1,500	1,160	855	840
<b>Gross Capital</b>	<b>4,930</b>	<b>4,495</b>	<b>4,105</b>	<b>4,095</b>
less Capital Receipts	335	335	335	340
<b>Net Capital</b>	<b>4,595</b>	<b>4,160</b>	<b>3,770</b>	<b>3,755</b>
<b>Capital Resources</b>	<b>4,120</b>	<b>1,690</b>	<b>1,590</b>	<b>3,575</b>
<b>CAPITAL BUDGET BALANCE</b>	<b>-475</b>	<b>-2,470</b>	<b>-2,180</b>	<b>-180</b>
<b>EXCHEQUER BALANCE</b>	<b>-11,300</b>	<b>-9,595</b>	<b>-6,020</b>	<b>-2,915</b>
<b>UNDERLYING GENERAL GOVERNMENT BALANCE</b>	<b>-12,140</b>	<b>-8,165</b>	<b>-5,205</b>	<b>-4,385</b>
<i>% of GDP</i>	<b>-7.3%</b>	<b>-4.8%</b>	<b>-2.9%</b>	<b>-2.4%</b>
<b>UNDERLYING GENERAL GOVERNMENT PRIMARY BALANCE</b>	<b>-4,495</b>	<b>25</b>	<b>3,550</b>	<b>4,845</b>
<i>% of GDP</i>	<b>-2.7%</b>	<b>0.0%</b>	<b>2.0%</b>	<b>2.6%</b>
<b>Nominal GDP (rounded to nearest €25m)</b>	<b>165,875</b>	<b>170,600</b>	<b>176,950</b>	<b>184,675</b>

Source: Department of Finance, Department of Public Expenditure & Reform & NTMA

Notes:

- Figures rounded to the nearest €5m.

- Rounding may affect totals.

- The non-voted capital expenditure projections in table 9 do not include any 1% of GNP Exchequer contribution to the NPRF in any year.

- The underlying balance: the net lending of general government adjusted for the effect of certain expenditures into the financial sector, which may be excluded for the purposes of assessing adherence to EDP targets. For further detail see tables A1 and A2.2 in the Additional Fiscal and Statistics Tables section.

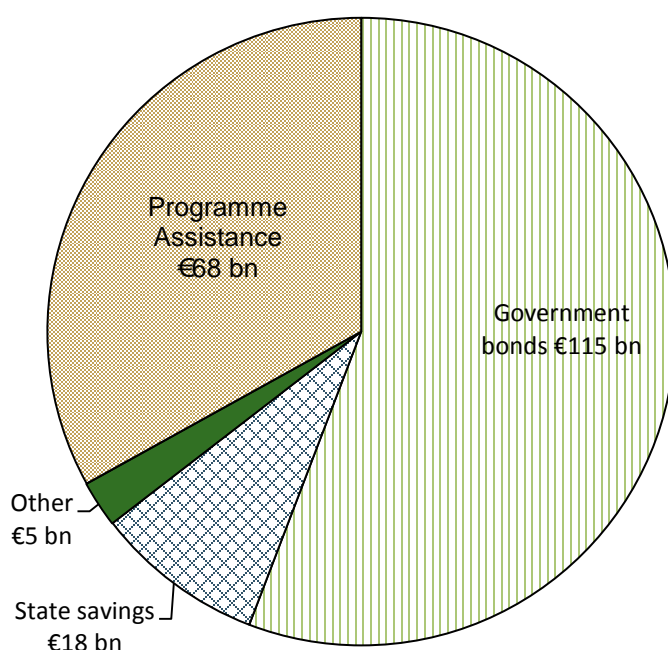
- For an explanation of the "walk" from Exchequer Balance to General Government Balance, see table A1 in the Additional Fiscal Statistics and Tables section.

## Debt Analysis and Funding Position

### Debt level and developments

The general government debt to GDP ratio has increased substantially in recent years. This has been due in part to: support for the financial sector, a series of primary deficits and a contraction in GDP which pushes up the ratio. Ireland's general government debt for 2012 is estimated to have been €192 billion or 117% of GDP. General government debt is expected to peak at approximately €205.9 billion or 124% of GDP this year. The main components of the projected debt for 2013 are shown in Figure 2.

**Figure 2: Breakdown of projected general government debt at end-2013**



Source: Department of Finance and NTMA

The evolution of general government debt for Ireland over the period 2012 to 2016 is shown in Table 10. General government debt is expected to peak at 124% of GDP this year.

**Table 10: General government debt 2012-2016**

<i>€ billion</i>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>
General government debt	192.5	205.9	204.7	209.4	211.6
Debt-to-GDP Ratio	117.4%	124.1%	120.0%	118.4%	114.6%

Source: Department of Finance & CSO

At 124% of GDP, the forecast debt ratio for this year is slightly higher than the 123% estimated in April's Stability Programme Update. The debt ratio is mechanically sensitive to its denominator and as the nominal debt level for 2013 has decreased by over €1 billion since the April projection, the higher debt ratio is therefore wholly attributable to a

downward revision to the forecast GDP for this year. General government debt is expected to fall to 120% of GDP in 2014 and to continue to decline to just under 115% of GDP by 2016. In the context of debt sustainability, Ireland is expected to record a small primary surplus in 2014; the first such primary surplus since 2007.

The increase in the stock of debt since 2007 has been accompanied by an inevitable increase in the cost of servicing the debt. In 2012 general government interest expenditure as a percentage of general government revenues amounted to 10.9%, compared to just 2.8% in 2007. By 2016, based on current assumptions regarding the evolution of revenues, debt levels and interest rates on government borrowing, the equivalent of around 14.3% of general government revenues will be required for debt servicing. While this is high, it is still lower than in the 1980s. Crucially adhering to the path of prudent budgetary management will allow debt levels to decline, freeing up expenditure for other uses.

### **Gross debt and net debt**

General government debt, as defined under the Excessive Deficit Procedure (EDP) regulation, is a gross measure and consists of certain liabilities that require payment by the debtor to the creditor at a date or dates in the future. A net general government debt figure (obtained by deducting the corresponding financial assets to those liabilities used in the calculation of general government debt) is reported in Table 11.

**Table 11: General government debt and net general government debt 2012 and 2013, % of GDP**

End-year	2012	2013
<i>% of GDP</i>		
General government debt (gross)	117.4	124.1
EDP debt instrument assets	24.7	25.4
Net debt position	92.7	98.7

*Source: Department of Finance, NTMA, CSO*

### **Market Return**

Following Ireland's successful re-engagement with the international debt markets in 2012, the National Treasury Management Agency (NTMA) issued a further €7.5 billion in medium and long-term Government bonds in 2013.

In January the NTMA issued €2.5 billion of the existing 5-year benchmark bond maturing in 2017. The funds were raised at a yield of 3.316% with overseas investors taking 87% of the bonds on offer. Along with funding activity in 2012, the "funding cliff" represented by what had, at one point, been an €11.9 billion bond repayment due in mid-January 2014 was eliminated.

In March, the NTMA sold €5 billion of a new 10-year benchmark bond, at a yield of 4.15%. This was the first new 10-year issuance since January 2010, prior to Ireland's entry into the EU/IMF Programme and again there was strong investor demand in the issue with over 400 investors submitting bids.

The success of these deals demonstrates that Ireland has rebuilt a diversified investor base across many key geographic areas and, importantly, with a broad range of investor types.

Having re-entered the Treasury Bill market in July 2012 the NTMA continued with a regular schedule of Treasury Bill auctions in 2013. The most recent, in September, saw the annualised yield demanded by investors for the three month maturity at 0.18%. By contrast, in July 2012, it was 1.8%.

In addition to these market transactions, the NTMA issued eight new Floating Rate Treasury Bonds to the Central Bank of Ireland in February 2013 to replace the Promissory Notes previously held by IBRC. A total amount of €25 billion was issued. The bonds have maturities ranging from 25 to 40 years and pay interest every six months (June and December) based on the six month Euribor interest rate plus an interest margin which averages 2.63% across the eight issues.

### **Cash Balances**

At end-September 2013, €25.6 billion was available to the Exchequer in cash and other short-term cash management balances, including deposits.

In view of this relatively healthy funding position, the NTMA announced, on 1 October, that it was suspending its monthly Treasury Bill auctions for the final quarter of 2013. The NTMA has also deferred consideration of any further medium or long-term bond issuance until early 2014.

Taking account of the remaining EU/IMF Programme disbursements, the State is now well positioned to have approximately €21½ billion on hand in Exchequer cash and other short-term cash management balances at end-2013. This is deemed sufficient to meet all known Exchequer requirements up to the early part of 2015 and is consistent with the stated aim of having 12-15 months of advance Exchequer funding to hand when the EU/IMF Programme reaches its conclusion.

### **Credit Rating**

In September 2013, Moody's revised its outlook on Ireland's sovereign credit rating to stable from negative but left the rating unchanged. While welcoming the revision to the outlook, the NTMA expressed its disappointment that Moody's did not upgrade the rating from its current sub-investment grade rating to investment grade.

The revision to the outlook by Moody's follows a similar revision by Fitch in late 2012 and a revision to positive outlook, in July 2013, by Standard & Poor's (S&P). This positive move reflects the continued progress Ireland is making in restoring sustainability on the fiscal side and the improved access to capital markets.

Importantly, Ireland maintains an investment grade rating with both Fitch and S&P as well as with the two other main rating agencies – DBRS and R&I.

### **Funding Requirements**

The February 2013 IBRC Promissory Note transaction and the agreed extension of EFSF and EFSM loan maturities provide a strong underpinning to Ireland's return to the capital

markets by reducing the amount that will have to be borrowed over the next decade by around €40 billion. This is a positive development.

Despite the progress made in restoring sustainability to the State's public finances, there remains a sizeable gap between day-to-day revenues and expenditure. The 2014 EBR is estimated at €9.6 billion.

Together with maturing debt which must be repaid, the funding requirement for 2014 is estimated at around €16½ billion.

This will be financed in part through new borrowing but also through a reduction in the cash balances which have been built up by the NTMA. This "stock-flow" adjustment will aid in a reduction in the General Government debt-to-GDP ratio in 2014.

While the EBR is projected to decline over the forecast horizon, to €2.9 billion by 2016, there are significant bond maturities, particularly in 2016, which must be adequately and prudently funded.

In addition the process of repaying the loans borrowed under the EU/IMF Programme will begin in mid-2015, starting with the amortisation of the loans from the IMF.

Following the agreed extension of EFSF and EFSM loan maturities, the first EFSF loan maturity will be in 2029. Although the revised maturity dates of individual EFSM loans will only be determined as they approach their original maturity dates, it is not expected that Ireland will have to refinance any of its EFSM loans before 2027.

## Statement of Risks and Sensitivity Analysis

### Summary

Risks to the short- and medium-term outlook stem from a number of sources. The emerging recovery is fragile in key trading partners and there is a risk that assumptions for key international variables could prove to be optimistic. Domestically, the high level of household indebtedness poses a risk to the private consumption profile should deleveraging accelerate. Upside risks include any increase in economy-wide investment from its current very low levels, as well the potential for any unanticipated increase in global demand resulting in improved export prospects for Ireland.

### Background

The macroeconomic and fiscal outlook presented earlier in this document is the Department of Finance's baseline scenario for the period 2013-2016. Near-term economic forecasts are, by construction, conditional forecasts; they rely upon assumptions regarding key inputs (demand in our main trading partners, likely movements in commodity prices, exchange rates, interest rates, etc.). In addition, forecasts involve making assumptions regarding the likely future behaviour of domestic households and firms (for instance, how will households allocate their disposable income between consumption and savings).

An obvious question that arises is the impact on the projection of relaxing any of the underlying assumptions that underpin the baseline scenario. For instance, what would be the impact on the economy if there were changes to the international growth outlook or if households were to alter their consumption versus saving decisions?

Model simulations presented in the sensitivity analysis below attempt to quantify the impact on the Irish economy and the public finances of relaxing some of the assumptions that underpin the current baseline scenario. Before turning to this, the main risks – both downside and upside – to the outlook are discussed in the next section.

### Risks to the forecasts

#### Economic Risks

Risks to the central forecast emanate from both external and internal sources, and appear to be tilted to the downside. Externally, it is clear that the recovery in our main export markets is fragile and subject to downside risk. Weaker-than-assumed external growth would have negative implications for our exporting performance.

Domestically, Ireland's household indebtedness remains high, and any unexpected increase in interest rates and/or an acceleration in the pace of debt reduction could impact negatively on domestic demand. In addition, product-specific developments are affecting exports of the pharma-chem sector and any acceleration of this process has the potential to put downward pressure on trading activity.

There are also sources of upside potential. For example, a stronger-than-assumed global recovery would have a beneficial impact on output in Ireland. Economy-wide investment – currently at around 12 per cent of GDP – remains very low both in historical and cross-country terms, and a return to more normal levels of investment could add considerably to baseline GDP projections. Finally, greater certainty regarding future prospects could reduce the need for households to maintain precautionary savings at elevated levels, potentially leading to stronger domestic demand than is currently assumed.

## **Fiscal Risks**

Fiscal risks can arise from specific events or the broader economic environment and may affect the fiscal outlook. The decision whether to include likely fiscal risks in future forecasts is complicated by issues around the likelihood, timing or magnitude of potential events.

Receipts from individual tax-heads exhibit different degrees of volatility in relation to the level of economic activity. Property taxes are relatively stable and easier to predict while income and transaction taxes tend to reflect the level of economic activity. Although now of relatively low importance in Ireland, capital gains tax is particularly volatile and is affected by fluctuations in asset markets and the degree of flexibility that economic agents have in managing tax liabilities.

Tax forecasting is also dependent on the relationships between the economy, tax bases and tax revenues in prior years. These relationships can evolve over time and relying on accepted conventions when predicting future revenues can badly affect accuracy. The hollowing-out of the tax base during the boom years left Ireland critically exposed when transaction-based tax receipts, particularly relating to housing and property, collapsed in the wake of the financial crisis. The speed and the severity of the decline in receipts made the accurate forecasting of tax receipts extremely difficult to achieve, hampering the response of policy-makers to the crisis.

Furthermore, losses made by firms during a downturn can be used to offset taxes incurred during the recovery making the timing of corporation tax receipts difficult to predict.

A risk to the public finances comes from the timing of the Budget this year. If tax revenues in the month of November – the key month of the year in terms of revenue collection – do not perform in line with expectations, this could have consequences for the achievement of the EDP target. As of September 2012, some 71% of full-year revenues were received, with this figure increasing to 92% by end-November.

A key element in further improving fiscal forecasting ability will be the outcome of the recently published consultation on amending the pay and file dates<sup>4</sup>. This will apply to self-assessed income tax (14% of the 2012 income tax yield was collected in November of that year), capital gains tax (48% of the yield was received in December 2012) and capital acquisitions tax (an aggregate of 61% was received in the two months of October and November).

A contingent risk to the Exchequer is the potential true-up to NAMA should the value of IBRC assets be less than the value of debt owing to NAMA. This valuation process is approaching its final stages and is due for completion in the coming months. While this would represent a cash demand on the Exchequer, the European Commission have indicated that such payments made to NAMA are unlikely to be included when assessing Ireland's compliance with its EDP obligations.

## **Sensitivity analysis**

The ESRI's recently-updated HERMES 2013 model allows for the estimation of the impact of particular shocks on the economy and public finances. Results of three different

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<sup>4</sup> <http://taxpolicy.gov.ie/wp-content/uploads/2013/10/Department-of-Finance-Pay-and-File-Consultation-Documents-October-2013.pdf>



scenarios are presented below<sup>5</sup>. It should be noted that the results of each simulation are broadly symmetric – for instance the positive impact in Ireland of an improvement in world growth is broadly similar to the negative impact in Ireland of a deterioration in world activity.

**Table 12: Impact on main aggregates**

		2014	2015	2016
<b>1% Increase in World Output</b>				
GDP	% change compared with base	0.8	0.9	1.0
Total Revenue	% change compared with base	0.2	0.4	0.7
Total Expenditure	% change compared with base	-0.1	-0.1	0.0
Deficit-GDP Ratio	pp change compared with base	-0.1	-0.2	-0.2
Debt-GDP Ratio	pp change compared with base	-0.9	-1.3	-1.6
Primary Balance – GDP Ratio	pp change compared with base	-0.1	-0.1	-0.2
<b>1 Percentage Point Increase in Savings Rate</b>				
GDP	% change compared with base	-0.3	-0.3	-0.3
Total Revenue	% change compared with base	-0.3	-0.4	-0.4
Total Expenditure	% change compared with base	0.0	0.0	0.0
Deficit-GDP Ratio	pp change compared with base	0.1	0.1	0.2
Debt-GDP Ratio	pp change compared with base	0.4	0.5	0.7
Primary Balance – GDP Ratio	pp change compared with base	0.1	0.1	0.1
<b>1 Percentage Point Increase in Interest Rate</b>				
GDP	% change compared with base	-0.3	-1.1	-1.6
Total Revenue	% change compared with base	-0.5	-1.3	-1.6
Total Expenditure	% change compared with base	0.2	0.8	0.9
Deficit-GDP Ratio	pp change compared with base	0.3	0.8	0.9
Debt-GDP Ratio	pp change compared with base	1.3	2.8	4.4
Primary Balance – GDP Ratio	pp change compared with base	0.3	0.5	0.5

Source: Economic and Social Research Institute. World output shock articulated as permanent increase in UK, US, EU and OECD GDP.

The sensitivity of Irish GDP to global demand remains high, given the openness of the economy. Model simulations show that a 1 percentage point increase in world output would boost output in Ireland by a broadly equivalent amount by 2016. Simulations also show that a 1 percentage point increase in the household savings rate would reduce activity in Ireland by around ¼ percentage point via the consumption channel. Of particular note is the potential impact on the economy from interest rate changes. Simulations confirm that the impact on the economy and public finances of a shift in interest rates would be large; this is unsurprising given the high level of public and private debt.

### Range of forecasts

Table 13 compares the Department of Finance's macroeconomic forecasts for this year and next with those of other agencies, both domestic and international. Of the contemporaneous forecasts there seems to be a reasonable degree of consensus regarding the outlook for the Irish economy for this year. Omitting the Commission forecasts, which were produced prior to the publication of the second quarter National Accounts, the range of forecasts extends from a no-growth scenario to modest growth in

<sup>5</sup> Results are based on the HERMES 2013 model (Adele Bergin, Thomas Conefrey, John FitzGerald, Ide Kearney & Nusa Znuderl "The HERMES-13 macroeconomic model of the Irish economy," Papers WP460, Economic and Social Research Institute (ESRI, 2013).

the order of ½ per cent. In terms of the outlook for 2014, the range of GDP forecasts extends from 1¾ per cent to 2½ per cent.

**Table 13: Range of forecasts**

		<i>Annual % change</i>			
		<b>GDP</b>	<b>GNP</b>	<b>HICP</b>	<b>Employment</b>
<b>2013</b>					
Department of Finance	<i>Oct '13</i>	0.2	1.0	0.7	1.6
Central Bank of Ireland	<i>Oct '13</i>	0.5	0.1	0.6	1.1
IMF	<i>Oct '13</i>	0.6	0.3	1.0	0.6
Consensus*	<i>Oct '13</i>	0.0	2.3	0.7	N/A
ESRI	<i>Oct '13</i>	0.5	2.0	0.7	1.9
European Commission	<i>May '13</i>	1.1	N/A	1.3	0.1
OECD	<i>Sept '13</i>	0.0	N/A	0.9	N/A
		<i>Annual % change</i>			
		<b>GDP</b>	<b>GNP</b>	<b>HICP</b>	<b>Employment</b>
<b>2014</b>					
Department of Finance	<i>Oct '13</i>	2.0	1.7	1.2	1.5
Central Bank of Ireland	<i>Oct '13</i>	2.0	1.2	0.7	1.2
IMF	<i>Oct '13</i>	1.8	1.3	1.2	0.9
Consensus*	<i>Oct '13</i>	1.7	1.6	1.2	N/A
ESRI	<i>Oct '13</i>	2.6	2.7	1.5	1.3
European Commission	<i>May '13</i>	2.2	N/A	1.3	0.9
OECD	<i>Sept '13</i>	1.9	N/A	1.2	N/A

Source: Institutions cited.

\*The median macroeconomic forecast from a number of agencies, both international and domestic.

Notes

\*Annual average except for the Reuters Consensus which is an end-year figure (year-on-year % change unless otherwise stated).

## Budgetary Reform

The majority of the significant changes to the budgetary system which were necessary to reform and strengthen the economic governance structure have been implemented already. Part III of the Expenditure Report 2014 details Ireland's public expenditure framework, giving an international comparative perspective. With regard to budgetary reform, particular discussion must be made of the so-called 'two-pack', which came into force on 30 May of this year, includes a number of measures that have impacted our budgetary process<sup>6</sup>. The 'two pack' introduces additional budgetary coordination in the euro area including a common budgetary timeline:

- The draft budget for central government and the main parameters of the draft budgets for all the other sub-sectors of the general government must be published by the 15<sup>th</sup> of October each year; and
- The corresponding legislation to adopt or implement the Budget will have to be completed before the end of the year. This means completing the Finance Bill process, and publishing the Revised Estimates Volume; and
- The draft budget and stability programme must be based on independent macroeconomic forecasts which are defined as forecasts produced or endorsed by an independent body.

What we normally publish on Budget day in December corresponds to the definition of "draft Budget" under this Regulation, so accordingly Budget day has moved. This regulation also requires euro area Member States to submit to the Commission and the Eurogroup and make public a draft budgetary plan (DBP) no later than 15 October each year. It also requires ex-ante reporting to the Commission and Eurogroup on national debt issuance plans. In principle these are not to be disseminated publicly given the potential sensitivity of information. The DBP presents the draft budgets of Euro Area Member States in a common format to enable effective assessment by the Commission, which shall adopt an opinion on it by the end of November. The regulation also provides that the Commission may request a revised draft budgetary plan within two weeks in exceptional circumstances where it identifies particularly serious non-compliance with the budgetary obligations laid down in the Stability and Growth Pact.

Member States subject to a macroeconomic adjustment programme are exempt from the requirement to present a Draft Budgetary Plan and debt issuance report. Notwithstanding, these Member States remain subject to the common budgetary timeline. As such, Ireland must publish its draft budget on or before 15<sup>th</sup> October, but does not have to submit the Draft Budgetary Plan this year.

With regard to the independent macroeconomic forecasts, further details on the endorsement process are contained in the IFAC Endorsement section.

### Background to the latest budgetary reforms

The European Semester was implemented in 2011 and provides that EU Member States must submit their Stability or Convergence Programmes (SCPs) and National Reform Programmes (NRPs) by the end of April every year. This means that the examination of these programmes and the related EU-level discussions on fiscal policy, macroeconomic

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<sup>6</sup> REGULATION (EU) No 473/2013 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 21 May 2013 on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficits of the Member States in the euro area  
<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2013:140:0011:0023:EN:PDF>

imbalances, financial sector issues, and growth-enhancing structural reforms will now always take place before governments draw up their draft budgets. The aim of this 'upstream' policy coordination is to make the implementation of policy guidance more effective and help embed the EU dimension in national policy-making so that the policies adopted by Member States reflect jointly agreed priorities. The full implementation of the Semester enables the recommendations made at EU level to inform the national budgets adopted by member states.

### **What is the 'six-pack'**

The European Semester was further enhanced by the adoption in November 2011 of the so-called 'six pack', a body of six legislative acts that translated the initial EU reform proposals into binding rules.

The 'six-pack' has three broad goals:

- Tightening the rules of the Stability and Growth Pact (SGP), the governance regime for EU Member States to date, primarily by giving real 'teeth' to the sanctions for breaching the rules of the SGP and by making the 60% debt limit operational<sup>7</sup>;
- Introducing new surveillance of macroeconomic developments across the EU to ensure that macroeconomic imbalances, such as housing bubbles, are detected and corrected;
- Setting standards to ensure the correct and independent compilation of statistics as these data are crucial to sound budgetary policy-making and monitoring of budgets.

### **The 'two-pack'**

Following the strengthening of the SGP, a further package of budgetary regulations, the so-called 'two-pack' entered into force in May 2013.

The 'two-pack' is a further step in the reform of the economic governance regime but is applicable to euro area Member States only. The 'two-pack' focuses on improving budgetary coordination of euro area Member States and enhancing economic surveillance of those Member States in financial difficulty.

The 'two-pack' regulations build on and complement the 'six-pack' reforms to the SGP and the European Semester for economic policy coordination. Regulation 2 of the 'two pack' also stipulates that Member States will remain subject to post programme surveillance until at least 75% of assistance received is repaid.

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<sup>7</sup> If General Government Debt exceeds 60% of GDP and is not sufficiently diminishing, sanctions could be imposed regardless of whether the Member State exceeds the 3% Government deficit rule. This is a major innovation of the six-pack as prior to its enactment, it was only the 3% deficit rule which could result in sanctions.

## ADDITIONAL FISCAL STATISTICS AND TABLES

**Table A1: Explanation of net differences between Exchequer Borrowing Requirement and General Government Balance**

<i>€ millions</i>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>
	outturn		projected		
(a) Exchequer balance	-14,891	-11,300	-9,595	-6,020	-2,915
(b) Exclude equity and loan transactions	2274	-1550	320	0	-2015
(c) Adjust for interest accrual	-404	-350	65	105	-20
(d) Adjust for tax accruals	-232	110	195	140	150
(e) Adjust for other accruals	-706	370	235	-25	-115
(f) Impact of NPRF	334	575	380	400	420
(g) Transactions between government bodies	229	-205	-105	-150	-85
(h) Net lending/borrowing of non-commercial State sponsored bodies	-21	205	255	245	140
(i) Net Surplus of the Social Insurance Fund	13	0	0	0	0
(j) Net (Borrowing)/Surplus of Local Government	-90	0	0	0	0
(k) General government balance (=a to k)	-13,511	-12,150	-8,255	-5,305	-4,435
(l) Financial sector measures affecting the balance		10	90	100	50
(m) Underlying balance	-13,511	-12,140	-8,165	-5,205	-4,385
(n) Underlying balance as % of GDP	-8.2%	-7.3%	-4.8%	-2.9%	-2.4%
(o) Nominal GDP	163,938	165,875	170,600	176,950	184,675

Source: Department of Finance, Department of Public Expenditure, CSO and NTMA estimates

**Notes:**

-Rounding may affect totals

-The general government balance measures the fiscal performance of all arms of Government, i.e. central government, Local Authorities, Vocational Education Committees and non-commercial State sponsored bodies, as well as funds such as the SIF and the NPRF which are managed by Government agents. It thus provides an accurate assessment of the fiscal performance of a more complete 'government' sector.

-The general government balance does not reflect the position of commercial State sponsored bodies as these agencies are classified as being outside the general government sector. It is calculated in accordance with ESA95, a consistent standard developed by the EU to facilitate budgetary comparisons between EU Member States in accordance with their obligations under the Maastricht Treaty.

a. The Exchequer Balance is the traditional domestic budgetary aggregate which measures the net surplus or deficit position of the Exchequer account. It is the difference between total receipts into and total expenditure out of the Exchequer account of the Central Fund.

b. Equity and loan transactions are excluded from the balance on the basis that they affect the composition but not the level of assets and liabilities.

c. Interest expenditure by general government is calculated on an accruals basis and includes interest rate swaps.

d. & e. Adjustments required in respect of certain transactions recorded on an accruals basis including tax accruals, Departmental balances, EU transfers and the impact of the capital carryover.

f. This is the net lending/borrowing of the NPRF. This fund is within the general government sector and transactions within the sector do not have an impact on the general government balance.

g. Transfers between units within the general government sector do not affect the general government balance.

h, i & j. These adjustments add the net lending/borrowing of other government bodies and local government to arrive at a full concept of general government.

l. This reflects potential deficit worsening expenditure of payments into the financial sector. For the purposes of assessing adherence to EDP general government balance targets, this expenditure is therefore excluded.

**Table A.2.1: General Government Balance (GGB) Estimates 2012-2016**

	ESA	2012	2012	2013	2014	2015	2016
		€m	outturn	outturn	per cent of GDP		
		outturn			projected		
<b>Net lending (EDP B.9) by sub-sector</b>							
1. General government (=6-7)	S.13	-13,511	-8.2	-7.3	-4.8	-3.0	-2.4
p.m.: Underlying balance			-8.2	-7.3	-4.8	-2.9	-2.4
2. Central government	S.1311	-13,434	-8.2	-7.3	-4.8	-3.0	-2.4
4. Local government	S.1313	-90	-0.1	0.0	0.0	0.0	0.0
5. Social security funds	S.1314	13	0.0	0.0	0.0	0.0	0.0
<b>General government (S.13)</b>							
6. Total Revenue	TR	56,524	34.5	35.3	35.7	35.8	35.3
7. Total Expenditure	TE	70,035	42.7	42.6	40.5	38.8	37.7
8. Net lending/borrowing (=6-7)	B.9	-13,511	-8.2	-7.3	-4.8	-3.0	-2.4
9. Interest expenditure	D.41	6,135	3.7	4.6	4.8	4.9	5.0
10. Primary balance (= 1 + 9)		-7,375	-4.5	-2.7	0.0	1.9	2.6
11. One-off and other temporary measures		0	0.0	-0.4	0.2	-0.1	-0.0
<b>Selected components of revenue</b>							
12. Total taxes (12=12a+12b+12c)		39,453	24.1	25.0	25.7	26.0	25.9
12a Taxes on production and imports	D.2	17,997	11.0	11.1	11.3	11.5	11.3
12b Taxes on income & wealth	D.5	20,691	12.6	13.3	13.8	14.3	14.3
12c Capital taxes	D.91	765	0.5	0.6	0.6	0.3	0.2
13. Social contributions	D.61	9,651	5.9	6.0	6.0	6.0	5.9
14. Property Income	D.4	2,249	1.4	1.6	1.3	1.3	1.2
15. Other		5,171	3.2	2.7	2.6	2.5	2.3
16. (=6) Total revenue (=12+13+14+15)	TR	56,524	34.5	35.3	35.7	35.8	35.3
p.m.: Tax burden		49,520	30.2	31.2	32.0	32.2	32.0
<b>Selected components of expenditure</b>							
17a Compensation of employees	D.1	18,769	11.4	11.3	10.8	10.2	9.8
17b Intermediate consumption	P.2	8,428	5.1	5.0	4.8	4.7	4.6
18. Social payments (= 18a+18b)		29,018	17.7	17.1	16.3	15.1	14.5
18a. Social transfers in kind supplied via market producers	D.63	4,321	2.6	2.6	2.5	2.3	2.2
18b. Social transfers other than in kind	D.62	24,697	15.1	14.5	13.8	12.8	12.3
19=9 Interest expenditure	D.41	6,135	3.7	4.6	4.8	4.9	5.0
20. Subsidies	D.3	1,540	0.9	0.8	0.8	0.7	0.7
21. Gross fixed capital formation	P.51	3,057	1.9	1.8	1.5	1.4	1.4
22. Capital transfers	D.9	1,249	0.8	1.2	0.7	0.6	0.6
23. Other		1,838	1.1	0.8	0.9	1.1	1.1
24=7 Total expenditure (=17+18+19+20+21+22)	TE	70,035	42.7	42.6	40.5	38.8	37.7
p.m. : Government consumption (nominal)	P.3	29,432	18.0	18.7	17.8	16.7	15.0
GDP at current market prices	B.1*g	€m	163,938	165,875	170,600	176,950	184,675

Sources: Department of Finance, Department of Public Expenditure and Reform, CSO & NTMA

Notes to Table A.2.1:

- Rounding may affect totals.
- Table A.2.1 sets out the general government deficit for the years 2012 to 2016 in terms of selected components of general government receipts and expenditures.
- Item 1: Net lending by general government is identical with the general government balance.
- Item 9 & 19: Interest expenditure by general government is calculated on an accruals basis and includes interest rate swaps.
- Item 12a: Taxes on production and imports include VAT; customs, excise and stamp duty; local authority rates; the non-household part of motor tax; the stamps collected by the Risk Equalisation Fund; and the banking levy introduced in Budget 2014.
- Item 12b: Current taxes on income and wealth comprise income tax; capital gains tax; corporation tax; the household part of motor tax and of television licences; and the local property tax.
- Item 12c: Capital taxes comprise capital acquisitions tax and the pension funds levy.
- Item 13: Social contributions consist mainly of contributions to the Social Insurance Fund. Imputed social contributions are also included.
- Item 14: Property income is made up of investment or dividend income.
- Item 15: Other receipts include miscellaneous receipts such as Departmental receipts (appropriations in aid), rents and receipts from abroad, receipts by non-commercial State sponsored bodies and miscellaneous capital receipts.
- Item 17a: Compensation of Employees includes wages and salaries as well as an estimate of the amount that would have to be contributed if public sector pensions were actually funded schemes.
- Item 17b: Intermediate consumption is current spending on goods and services by government units.
- Item 19: Social transfer payments include pensions; child benefit; payments for medical goods; transfers to the rest of the world; and other unrequited payments to households. Social transfers in kind include such items as free travel on public transport and fuel allowances.
- Item 22: Gross fixed capital formation is acquisitions less disposals by government of capital formation such as construction and machinery.
- Item 23: Other expenditure includes transfer payments to non-government bodies and capital grants. It also includes acquisitions less disposals of non-produced assets such as royalties, mobile phone licences and the licence to operate the National Lottery.

Memo items:

Tax burden: the sum of total taxes (D.2, D.5 and D.91), social contributions (D.61) and EU taxes.

The underlying balance: the net lending of general government adjusted for the effect of certain expenditures into the financial sector.

**Methodological Changes in the table since April 2013 SPU**

In 2012 the CSO reclassified Irish universities out of the non-profit institutions serving households (NPISH) into the corporations sector. Fee paying secondary schools also moved from the NPISH sector to the corporations sector. See Appendix A of National Income & Expenditures 2012 (NIE).

[http://www.cso.ie/en/media/csoie/releasespublications/documents/economy/2012/nie\\_2012.pdf](http://www.cso.ie/en/media/csoie/releasespublications/documents/economy/2012/nie_2012.pdf)

The reclassification was applied in June 2013 and led to a number of classification changes in the accounts with no direct impact on the net borrowing/lending of government. These changes are discussed in table A.2.3 in the context of changes since the SPU in April 2013.

**Table A.2.2: General Government Receipts and Expenditures (nominal)**

Description	ESA code	2012	2013	2014	2015	2016
<i>Revenue</i>						
<i>€ millions</i>						
Taxes on production and imports	D.2	17,997	18,485	19,200	20,270	20,945
Current taxes on income, wealth	D.5	20,691	22,000	23,570	25,215	26,395
Capital taxes	D.91	765	935	1045	545	410
Social contributions	D.61	9,651	9,920	10,310	10,550	10,830
Property Income	D.4	2,249	2,655	2,265	2,315	2,240
Other		5,171	4,530	4,500	4,510	4,320
Total revenue	TR	56,524	58,525	60,895	63,405	65,145
<i>Expenditure</i>						
Compensation of employees	D.1	18,769	18,695	18,435	18,075	18,095
Intermediate consumption	P.2	8,428	8,305	8,130	8,365	8,560
Social payments	D.6	29,018	28,395	27,870	26,640	26,830
Interest expenditure	EDP_D.41	6,135	7,645	8,190	8,755	9,230
Subsidies	D.3	1,540	1,320	1,305	1,275	1,270
Gross fixed capital formation	P.51	3,057	2,985	2,640	2,555	2,570
Capital transfers	D.9	1,249	2,050	1,110	1,135	1,085
Other		1,838	1,280	1,470	1,910	1,940
Total Expenditure	TE	70,035	70,675	69,150	68,710	69,580
General government balance	B.9=TR-TE	-13,511	-12,150	-8,255	-5,305	-4,435
Financial Sector measures affecting the balance		0	10	90	100	50
Underlying balance		-13,511	-12,140	-8,165	-5,205	-4,385
GDP at current market prices		163,938	165,875	170,600	176,950	184,675
Underlying GGB as % of GDP		-8.2%	-7.3%	-4.8%	-2.9%	-2.4%

Sources: Department of Finance, Department of Public Expenditure and Reform, CSO & NTMA.

Notes:

- Rounding may affect totals.
- Table A2.2 is a reproduction of Table A2.1 showing the main aggregates of government revenue and expenditure at nominal values.
- Financial sector measures affecting balance: This reflects potential deficit worsening expenditure into the financial sector and the credit union sector which may be excluded for the purposes of assessing adherence to EDP targets.
- The underlying balance: the net lending of general government adjusted for the effect of certain expenditures into the financial sector.



**Table A2.2.3: Comparison of vintages of receipts and expenditures**

Document		SPU	Budget	difference	notes
		2013	2014		
		2013	2013		
<i>Revenue</i>					
Taxes on production and imports	D.2	18,875	18,485	-390	1
Current taxes on income, wealth	D.5	22,180	22,000	-180	2
Capital taxes	D.91	850	935	85	3
Social contributions	D.61	9,785	9,920	135	4
Property Income	D.4	2,775	2,655	-120	
Other		4,280	4,530	250	5
Total revenue	TR	58,745	58,525	-220	
<i>Expenditure</i>					
Compensation of employees	D.1	18,725	18,695	-30	
Intermediate consumption	P.2	8,555	8,305	-250	
Social payments	D.631, D62	28,200	28,395	190	6
Interest expenditure	EDP_D.41	8,240	7,645	-595	7
Subsidies	D.3	455	1,320	865	8
Gross fixed capital formation	P.51	3,180	2,985	-195	
Capital transfers	D.9	2,382	2,050	-332	9
Other		1,583	1,280	-303	10
Total expenditure	TE	71,320	70,675	-645	
General government balance	B.9=TR-TE	-12,745	-12,150	595	
Underlying balance		-12,645	-12,140	505	

Source: Department of Finance estimates

#### Notes

Table A2.2.3 compares the 2013 revenue and expenditure figures of general government given in the current Budget 2014 document with their equivalents at the time of the earlier Stability Programme Update 2013 publication in April 2013.

The tables are also updated in the light of new 2012 receipts and expenditure data produced by the CSO to ensure a smooth transition from outturn to forecast year.

The main items contributing to these changes explained in the notes:

1. VAT & excise receipts almost €400m lower than forecast in SPU; Stamp duties are €130m higher.
2. Income tax receipts €250m lower than SPU estimate; LPT €50m higher than SPU estimate.
3. Pension levy increased €53m.
4. Increased contributions to Social Insurance Fund.
5. Bank guarantee fees €150m; Local authority higher imputed income as a result of latest census results €100m.
6. Local authority imputed social transfers related to higher rents as in note 5.; free fees for university students reclassified €250m; and other reclassifications D.7 current transfers payable and D.6 social payments between, see 10(v) below add -€250m.
7. This reduction in interest payments reflects a more favourable interest rate environment generally and that the NTMA does not intend to engage in further market activity this year.
8. €700m of the change in subsidies relates to the reclassification of payment to universities; the remainder is due to improved data on payments relating to transport
9. -€300m capital transfers reclassified to subsidies under the reclassification of universities.
10. (i) -€350m university block grant reclassified to subsidies  
(ii) -€250m adj. for free fees to universities transposed to social payments  
(iii) Net -€300m as a result of recording the disposal of the mobile phone licence in 2013 and the national lottery in 2014.  
(iv) €300m further EU contribution payable in 2013.  
(v) €250m other reclassified transactions between D.7 current transfers payable and D.6 social payments.

**Table A.3: Projected General Government Interest Expenditure 2013-2016**

<i>€ million</i>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>
National Debt Cash Interest	7,160	8,155	8,750	9,075
<i>% tax revenue</i>	19	20	21	21
<i>% of GDP</i>	4.3	4.8	4.9	4.9
National Debt Interest Accruals	150	-50	-90	35
Consolidation and Grossing Adjustments	65	25	20	55
Accrued Promissory Note Interest	225	10	10	10
Other	45	50	65	55
<b>Total Interest on ESA95 basis</b>	<b>7,645</b>	<b>8,190</b>	<b>8,755</b>	<b>9,230</b>
<i>% total General Government revenue</i>	13	13	14	14
<i>% of GDP</i>	4.6	4.8	4.9	5.0

Sources: Department of Finance & NTMA

Notes:

- Rounding may affect totals

**Table A.4: Projected movement in general government debt 2013-2016**

<i>€ billion</i>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>
Opening General Government Debt	192.5	205.9	204.7	209.4
EBR	11.3	9.6	6.0	2.9
Change in Exchequer Deposits	3.1	-10.7	-0.6	-0.1
Net Lending of Local Government & NCSSBs	-0.4	-0.1	-0.5	-0.2
Change in collateral held	-0.5	-0.0	-0.3	-0.2
Other	0.0	0.0	0.1	-0.4
Closing General Government Debt	205.9	204.7	209.7	211.6
<b>General Government Debt-to-GDP Ratio</b>	<b>124.1%</b>	<b>120.0%</b>	<b>118.4%</b>	<b>114.6%</b>

Sources: Department of Finance & NTMA

Notes:

- Rounding may affect totals

**Table A.5: General government debt developments**

(% of GDP)	2012	2013	2014	2015	2016
Gross debt	117.4	124.1	120.0	118.4	114.6
Change in gross debt (= 1 + 2 + 3)	13.3	6.7	-4.2	-1.6	-3.8
<b>Contributions to change in gross debt ratio:</b>					
1. General Government Deficit	8.2	7.3	4.8	3.0	2.4
2. Stock-flow adjustment	5.9	0.8	-5.6	-0.3	-1.2
3. Nominal GDP contribution to $\Delta$ in debt ratio	-0.8	-1.4	-3.4	-4.3	-5.0
<b>Composition of GGB:</b>					
4. General Government Balance	-8.2	-7.3	-4.8	-3.0	-2.4
5. Interest expenditure	-3.7	-4.6	-4.8	-4.9	-5.0
6. Primary balance (= 4 - 5)	-4.5	-2.7	0.0	2.0	2.6
<b>Composition of stock-flow adjustment:</b>					
7. Change in liquid assets	3.8	1.9	-6.3	-0.4	0.0
8. Interest adjustments	-0.3	-0.2	0.0	0.1	0.0
9. Equity transactions	1.4	-0.9	0.2	0.0	-1.1
10. Accrual adjustments	-0.6	0.3	0.3	0.1	0.0
11. Impact of NPRF	0.2	0.3	0.2	0.2	0.2
12. Collateral held	0.8	-0.3	0.0	-0.1	-0.1
13. Net discounts	0.4	0.0	0.1	0.1	0.1
12. Other	0.3	-0.3	-0.1	-0.3	-0.4
<b>Memorandum item:</b>					
Implied average interest rate (%)	3.6	4.0	4.0	4.3	4.4

Source: Department of Finance

**Notes:**

- The implied average interest rate is calculated by dividing general government interest expenditure in year t by the stock of general government debt outstanding at the end of year t - 1.

- Item 9: Equity transactions in 2012 include the acquisition of share capital in Irish Life; contributions to the ESM and loans granted to the Insurance Compensation fund. Equity transactions in 2013 include the sale of Irish Life and contingent capital notes, offset somewhat by further equity injection into the ESM and further loans granted to the Insurance Compensation Fund.

**Table A.6: Requirements and path for the general government balance**

% of GDP	2011	2012	2013	2014	2015
EDP ceiling for general government balance	-10.6	-8.6	-7.5	-5.1	-2.9
Underlying general government balance*	-8.9	-8.2	-7.3	-4.8	-2.9

Source: Department of Finance.

\* excluding support for the banking sector.

Tax burden: the sum of total taxes (D.2, D.5 and D.91), social contributions (D.61) and EU taxes.

**Table A.7: Contingent liabilities**

	2012 % of GDP
Public guarantees	70.0
<i>of which linked to the financial sector</i>	
Eligible Liabilities Guarantee	44.4
Exceptional Liquidity Assistance	7.0
National Asset Management Agency	17.8
other	0.8

Source: Department of Finance, CSO

## IFAC Endorsement – Letter and Associated Material

Economic governance in the euro area has been reformed significantly in recent years. The so-called ‘two-pack’, which came into force on 30 May of this year, provides for draft budgets to be based on economic forecasts which are either produced or endorsed by independent bodies at national level<sup>8</sup>.

In Ireland the endorsement route has been selected, and the Irish Fiscal Advisory Council (IFAC) has been assigned the task of endorsement in the Fiscal Responsibility Act 2012 and 2013. Only the forecasts for the current and following years are subject to the endorsement process.

In order to operationalise the endorsement process, a Memorandum of Understanding (MoU) between the Department of Finance and the Council was drawn up and is available on both websites<sup>9</sup>. Sections 4.1.b(ii) and 4.1.b(iii) of the MoU set out that Departmental staff share their provisional economic forecasts with IFAC staff and Council Members in advance of Budget day.

A set of macroeconomic variables was supplied to the Council on 24 September 2013 and formal presentations by Departmental staff to the IFAC were provided to the secretariat of the Council on 25 September; and to the full Council on 30 September, as provided for in the MoU. These forecasts made the technical assumption of a €3.1bn fiscal adjustment in 2014, as this was the latest articulation of government fiscal strategy at the time.

A letter of endorsement from the Chair of IFAC, issued to the Secretary-General of the Department on 4 October 2014, is included in Budget documentation. It states:

“The Irish Fiscal Advisory Council endorses as within the range of appropriate projections the set of macroeconomic projections prepared by the Department of Finance for Budget 2014 for the years 2013 and 2014 provided to the Council on 30 September 2013.”

Section 4.1.b(iii) of the MoU provides for endorsement of the “provisional final” economic forecasts, based on the aggregate measures foreseen in the Budget; it also provides for the possibility to modify the economic forecast after the completion of the endorsement process once the precise specification of the budgetary measures is made available.

In this context, the final macroeconomic forecasts that underpin Budget 2014 are slightly different from that endorsed by the IFAC. The quantum of permanent consolidation assumed in the IFAC-endorsed numbers was €3.1 bn. The Budget 2014 forecasts also assume €3.1bn in 2014 consolidation, but composed of €2.5bn in permanent measures and €0.6bn in temporary and one-off measures. It is assumed that the temporary and one-off measures, due to their composition, have no detrimental impact on the economy. Therefore, the final macro forecasts assume GDP growth of 2.0 per cent in 2014, compared with 1.8 per cent in the

<sup>8</sup> REGULATION (EU) No 473/2013 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 21 May 2013 on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficits of the Member States in the euro area

<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2013:140:0011:0023:EN:PDF>

<sup>9</sup> <http://www.finance.gov.ie/documents/publications/mou/mouaug2013fiscalcouncil.pdf>

IFAC-endorsed numbers. It is assumed that the lower impact on household income results in slightly higher personal consumption. The first-round impact is reduced somewhat by increased imports.

## IFAC-endorsed macroeconomic forecasts

**Table B1: Background assumptions**

	<u>2012</u>	<u>2013</u>	<u>2014</u>
Short-term interest rate (annual average)	0.8	0.2	0.5
Long-term interest rate (annual average)	3.6	4.3	4.1
USD/€ exchange rate (annual average)	1.29	1.32	1.34
Growth of relevant foreign markets	1.3	1.9	4.8
Oil prices (Brent, €/barrel)	86.67	82.23	77.73

*Source: European Commission, Spring forecasts, May 2013 except for oil prices (futures prices) and exchange rates which are presented as ten-day moving averages as of 30-September unchanged thereafter.*

**Table B2: Macroeconomic developments**

	<u>2012</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>
	<i>level</i>	<i>rate of change</i>		
Real GDP	162,855	0.2	0.2	1.8
Nominal GDP	163,938	0.8	1.2	2.7
<i>Components of real GDP</i>				
Private final consumption expenditure	82,634	-0.3	-0.2	1.1
Government final consumption expenditure	25,096	-3.7	-0.9	-1.9
Gross fixed capital formation	17,434	-1.0	4.9	6.8
Changes in inventories and net acquisition of valuables (% of GDP)	376	0.2	0.4	0.3
Exports of goods and services	176,735	1.6	-0.6	1.9
Imports of goods and services	136,990	0.0	-0.4	1.4
<i>Contributions to real GDP growth</i>				
Final domestic demand	125,164	-0.8	0.3	1.0
Changes in inventories and net acquisition of valuables	376	-0.4	0.2	-0.2
External balance of goods and services	39,573	1.6	-0.2	0.9

*Source: 2012 - CSO and Department of Finance calculations; 2013-14 - Department of Finance projections.*

**Table B3: Price developments**

	<u>2012</u>	<u>2013</u>	<u>2014</u>
	<i>rate of change</i>		
GDP deflator	0.6	0.9	0.9
Private consumption deflator	0.6	1.0	1.4
HICP	2.0	0.7	1.5
Export price deflator (goods and services)	4.2	0.5	0.6
Import price deflator (goods and services)	3.9	0.4	1.1

Source: 2012 - CSO and Department of Finance calculations; 2013-14 - Department of Finance projections.

**Table B4: Labour market developments**

	<u>2012</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>
	<i>level</i>		<i>rate of change</i>	
Employment, persons	1,837,000	-0.7	1.6	1.4
Unemployment rate (%)	317,000	14.7	13.5	12.6
Labour productivity, persons		0.9	-1.3	0.4
Compensation of employees		0.1	1.5	3.0
Compensation per employee		0.8	-0.1	1.5

Source: 2012 - CSO and Department of Finance calculations; 2013-14 - Department of Finance projections.

**Table B5: Sectoral balances**

	<u>2012</u>	<u>2013</u>	<u>2014</u>
	<i>% GDP</i>		
Current account	4.4	4.4	4.1

Source: 2012 - CSO and Department of Finance calculations; 2013-14 - Department of Finance projections.



04 October 2013

Dear Secretary General Moran,

The Ministers and Secretaries (Amendment) Act 2013 amends the Fiscal Responsibility Act (2012) to include a macroeconomic forecast endorsement function for the Irish Fiscal Advisory Council as follows:

The Fiscal Responsibility Act 2012 is amended in section 8 by substituting the following for subsection (4): “(4) The Fiscal Council shall— (a) endorse, as it considers appropriate, the macroeconomic forecasts prepared by the Department of Finance on which the Budget and stability programme will be based, . . .” [Ministers and Secretaries (Amendment) Act 2013, p. 5.]

The Memorandum of Understanding between the Department of Finance and the Council that sets out the agreed modalities of the endorsement function in relation to the Budget states:

“An endorsement would be provided via a formal letter from the Chair of the Council to the Secretary General of the Department of Finance, and simultaneously in electronic format. This letter would be sent after the meeting referred to in 4.1.b.(iii) and no later than five working days in advance of Budget day. This letter would be made public by the Council and the Department of Finance on Budget day, once the Minister for Finance begins speaking, and will be included in the Budget book.

The letter from the Chair of the Council would not typically contain any commentary on the macroeconomic forecasts. Any Council views regarding the forecasts or parts thereof (including any possible late modifications referred to in 4.1.b.(iii)) would be contained in the Council’s subsequent Fiscal Assessment Report.” [Memorandum of Understanding, 2013, p. 5.]

**The Irish Fiscal Advisory Council endorses as within the range of appropriate projections the set of macroeconomic projections prepared by the Department of Finance for Budget 2014 for the years 2013 and 2014 provided to the Council on 30 September 2013.**

A detailed discussion of the endorsement process and an assessment of the macroeconomic projections will be provided in the Council’s forthcoming *Fiscal Assessment Report*, which is scheduled for publication in November.

Yours Sincerely

John McHale  
Chair, Irish Fiscal Advisory Council