

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 level¹.

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 websites². 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

¹ 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>

² <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