Fiscal Assessment Report, June 2023

Supporting information sections

The following sections provide supporting information and analysis related to various parts of the Council's mandate and its assessments. This section includes key analytical areas that the Council routinely assesses. The insights provided by these sections are an essential part of how the Council thinks through how the economy and public finances are evolving.

S1. Endorsement process

Endorsement timeline

The key dates underpinning the Council's endorsement of the Department of Finance's macroeconomic projections for *SPU 2023* are set out in Table S1a.

Table S1a: Timeline for Endorsement of *SPU 2023* Projections

3 March	The CSO released its Quarterly National Accounts estimates for Q4 2022.
6 March	The Council's Secretariat and Department staff met with the CSO to clarify technical details of latest Quarterly National Accounts estimates.
23 March	The Department sent the Council preliminary forecasts in line with Memorandum of Understanding requirements.
27 March	The Department presented its preliminary forecasts to the Council's Secretariat.
29 March	The Department sent updated forecasts.
31 March	The Department of Finance presented its latest forecasts to the Council and Secretariat and answered questions. After the meeting the Council had a preliminary discussion on its endorsement decision.
6 April	The Council finalised a decision on the endorsement. The Chairperson of the Council wrote a letter to the Secretary General of the Department of Finance endorsing the set of macroeconomic forecasts underlying *SPU 2023*.
18 April	The Department's forecasts were published in *SPU 2023*.

Council's Benchmark projections

Below is a summary of the Council's Benchmark projections, which were an input to its endorsement exercise. The Council finalised these projections on Thursday 23rd March before receiving the Department of Finance's preliminary forecasts.

Table S1b: The Council's Benchmark projections

% change in volumes unless otherwise stated

	2022	2023	2024	2025	2026	2027	2028	2029	2030
Demand									
GNI*[a]	6.5	3.1	2.7	2.8	3.2	3.1	2.8	2.6	2.4
...of which (p.p. contributions)									
Modified domestic demand[b] (p.p.)	6.9	1.8	-0.5	2.7	3.2	3.1	2.8	2.4	2.2
CA* (p.p.)	-4.4	1.4	3.2	0.1	0.0	0.0	0.1	0.2	0.3
Other, incl. stocks (p.p.)	3.9	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Modified domestic demand[a]	8.1	2.1	-0.6	3.3	3.8	3.7	3.3	2.9	2.5
Consumption	6.5	2.9	3.3	3.2	2.9	2.9	2.6	2.4	2.4
Government	0.6	0.5	0.8	2.0	2.4	2.5	2.5	2.5	2.5
Modified investment[a]	19.8	1.5	-10.5	4.8	7.3	6.6	5.5	4.1	2.8
CA*	-39.1	21.4	42.7	1.1	0.3	-0.2	0.7	2.0	2.9
Supply									
Potential output	-1.6	3.7	-0.1	1.2	4.2	4.4	4.2	3.8	3.8
Output gap (% potential output)	-4.6	-3.1	1.3	1.3	0.7	0.9	1.2	1.3	1.3
Labour Market									
Labour force	1.9	1.3	2.0	1.4	0.9	0.9	0.9	0.9	0.7
Employment	12.5	1.7	1.4	1.4	1.1	0.9	0.9	0.8	0.7
Unemployment rate (% labour force)	4.9	4.6	5.1	5.1	5.0	5.0	5.1	5.1	5.1
Prices									
HICP	8.0	4.7	2.5	2.2	1.9	1.7	1.7	2.0	2.0
Personal consumption deflator	6.5	5.2	3.4	2.9	2.6	2.6	2.5	2.3	2.3
GNI* deflator	6.3	2.4	2.4	1.8	1.9	1.8	1.8	1.7	1.6
Other									
Nominal GNI*	13.2	5.6	5.1	4.7	5.1	4.9	4.7	4.3	4.1
Nominal GNI* (€ billion)	264.2	279.0	293.3	307.2	322.9	338.9	354.7	369.9	385.1
CA* (% GNI*)	7.7	7.6	9.9	9.3	8.5	7.7	7.0	6.5	6.1
Savings ratio	19.3	19.0	17.9	16.8	16.0	15.6	14.8	14.5	14.6

[a] Modified (final) domestic demand and modified investment exclude aircraft for leasing and research and development service imports and trade in intellectual property.
[b] Modified contributions to real GNI* growth rates in percentage points.

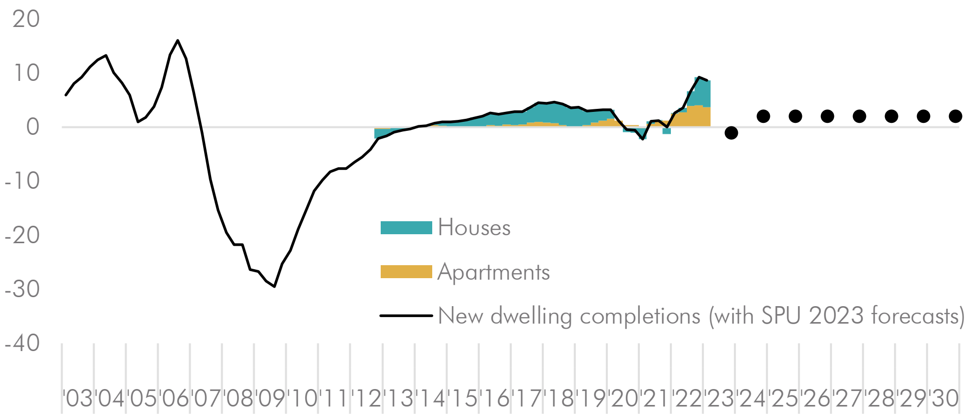
S2. Imbalances

This section looks at a selection of imbalances indicators assessed by the Council for the Irish economy. The Council monitors varios indicators on an ongoing basis, of which these are a subset. Among the aspects of the Irish economy presented below are data related to the construction sector, mortgage lending, house prices, and rents.

Completions increased considerably in 2022, with new-built apartments accounting for more than half of the increase. While apartment completions increased in the first quarter on a seasonally adjusted basis, house completions fell. This resulted in a slowdown in the annualised increase in new dwelling completions. *SPU 2023* forecasts that this will continue throughout 2023, before increases of 2,000 per year take place between 2024 and 2030.

Annualised change in new dwelling completions

Thousands

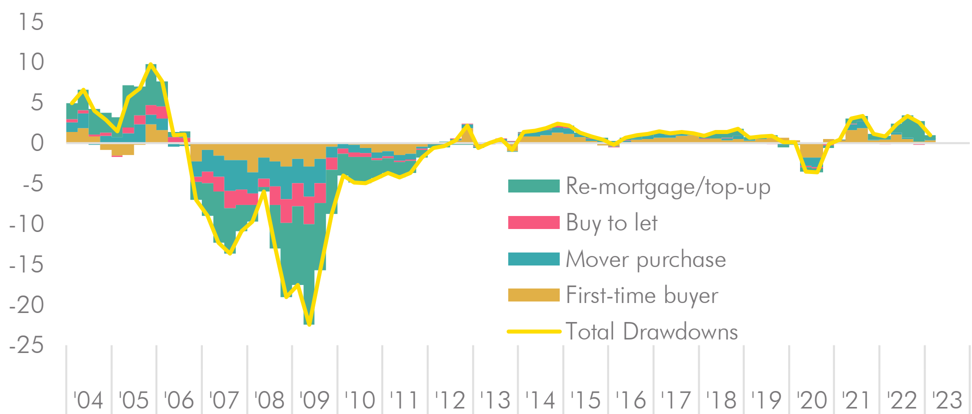


Sources: CSO; and Fiscal Council workings.
Notes: Prior to 2011, connections to the electricity grid are used as a proxy for new dwelling completions.

Mortgage drawdowns increased by €0.4 billion in Q1 2023 compared to Q1 2022, down from annual increases of €1 billion for the past three quarters. This reflects lower borrowing for top-up and re-mortgaging, which had been at its highest in 14 years.

Annual change in mortgage drawdowns

€ billion year-on-year change



Sources: Banking and Payments Federation of Ireland; and Fiscal Council workings.

S3. Macro-fiscal risks

This section outlines the major risks envisaged for the Government's official economic and budgetary forecasts. The risks shown are primarily those noted in *SPU 2023*, but with additional risks identified by the Council.

Macroeconomic Risks Matrix

Likelihoods and impacts are as assessed by the Council

Likelihood	Impact	
Medium	Medium	**War in Ukraine escalates**: economic activity would suffer as a result of broader conflict.
Medium	Medium	**Lower FDI**: a partial reversal of foreign direct investment in Ireland is likely due to higher interest rates and potential international corporation tax reform; given the importance of FDI for the Irish economy, this is a significant negative development for high-skill job creation in Ireland.
Medium	Medium	**International stagflation**: if aggregate demand remains greater than aggregate supply for a sustained period, it is possible that higher inflation will prove more prolonged, with potential implications for slower international economic growth. This would reduce demand for Ireland's exports from its main trading partners. However, features of the Irish economy including the presence of multinational firms in less-cyclical sectors (such as pharmaceuticals and ICT) could potentially avert a recession for Ireland.
Medium	High	**Faster energy and food price declines**: leading indicators of energy and food prices appear to be more benign than SPU 2023 forecasts, and if prices fall faster than forecast, this increases the likelihood of faster economic growth relative to forecasts.
Medium	High	**De-globalisation and supply-chain disruption**: the pandemic could result in more permanent shifts away from trade and globalisation, exacerbating previous trade tensions and trends, with adverse implications for Ireland's small and open economy.
Low	Low	**Brexit**: renewed frictions between the EU and the UK could harm growth prospects, although the likelihood and impacts of this appear now to be greatly reduced.
Medium	High	**Higher investment in dwellings**: although housing starts have slowed in 2022, a greater medium-term response for housing supply could be encouraged by excess household savings, or the Central Bank of Ireland's loosening of its macroprudential rules for house purchases, or due to successful delivery of the National Development Plan. This could provide a boost to economic activity in excess of official estimates, although housebuilding In Ireland has been highly cyclical (see S2, and Conroy, Casey, and Jordan-Doak (2021)).
Medium	Medium	**Lower output from MNCs**: While the impact on GDP may be significant, the main benefits to the Irish economy of MNCs include wages paid to employees (including income taxes), corporation taxes paid to the Exchequer, and direct-business or ancillary benefits to domestic firms. While the impact of lower output from MNCs could affect corporation tax, which is highly concentrated, the effects of this on underlying domestic economic activity in Ireland would not be large.
Low	High	**Extreme weather events**: given the experiences of other countries, as climate change continues, It Is possible that extreme weather events with economically significant implications will occur more frequently.

Sources: Department of Finance (Budget 2023); and Fiscal Council assessments.

Fiscal Risks Matrix

Likelihoods and impacts are as assessed by the Council

Likelihood	Impact	
High	High	**Humanitarian assistance.** Expenditure forecasts in *SPU 2023* do not incorporate any costs associated with assistance for Ukrainian refugees beyond 2023. It seems likely that significant costs would arise next year and beyond.
High	High	**Health overruns**. Beyond the immediate pressures of the pandemic, spending pressures in the health area remain a significant risk. Sláintecare reforms could also add significant costs. This risk is added by the Council.
High	Medium	**Corporation tax: policy change**. Adverse impacts of a changing international environment could be substantial. However, *SPU 2023* forecasts already incorporate a significant impact (€2 billion). *SPU 2023* forecasts do not incorporate any additional revenue from introducing a higher rate of corporation tax (15%) on firms with a global turnover in excess of €750 million. As a result, a medium impact may be more appropriate over the forecast horizon considered. There is high uncertainty about the outcomes in this area.
High	Medium	**Other spending pressures/overruns**. Some obvious spending pressures have not been budgeted for. Costs associated with the planned autoenrollment pension scheme have not been incorporated into SPU projections. In addition, the Christmas Bonus has not been budgeted for 2023 or beyond, despite having been paid in every year since 2014. This risk is added by the Council.
High	Medium	**Climate change and renewable energy targets**. *SPU 2023* says "climate policy and the corresponding actions needed to reduce emissions by 50% by 2030 and transition to net-zero by 2050 will have macroeconomic and fiscal implications." The Council assesses this risk to be medium impact over the *SPU 2023* forecast horizon (2023-2026).
High	Medium	**Population ageing**. There is a risk that the costs of ageing could be larger than allowed for under *SPU 2023* forecasts. Stand-Still costs in the coming years are significant, mostly due to inflation, but partially due to population ageing.
Medium	High	**Corporation tax: concentration risk:** As has been previously documented, corporation tax revenue is concentrated amongst a small number of payers. Cronin (2023) shows that the concentration risks could be even larger than previously understood. Firm specific factors (or factors that impact on a number of these firms) could have a significant impact on corporation tax receipts.
Medium	Medium	**Cost overruns in capital projects.** Large capital projects in Ireland have a history of significant cost overruns. Given that capacity constraints are already a factor in the construction sector, there is a risk that capital projects exceed their projected cost. This risk is added by the Council.
Medium	Medium	**Contingent liabilities**. Significant loans and guarantees to support sectors during the pandemic. Losses could arise if firms are unable to repay. The Council assesses this risk to be medium likelihood and impact.
Medium	Medium	**Litigation or one-off measures**. Any unexpected litigation against the state could lead to additional expenditure. Redress schemes, while inherently one-off in nature could have significant costs (Mica homes redress and mother and baby homes survivors scheme). No expenditure on the Defective Concrete Blocks Redress scheme has been incorporated into SPU expenditure forecasts beyond 2023. As a result, the Council assesses this to be of high impact.
Medium	Medium	**One-off revenue receipts.** One-off revenue windfalls could come from issued by the Irish Data Protection Commission. Since the publication of the SPU another fine of €1.2 billion has been issued, which is likely to be appealed. There is also potentially large, but less likely, revenue from the Apple tax case.
Medium	Low	**Borrowing costs**. Borrowing conditions have been favourable in recent times. These have since changed and will impact on Irish borrowing costs, particularly given the high debt levels. However, given the low gross financing needs in the coming years, the Council assesses this risk to be low impact within the forecast horizon covered by *SPU 2023*.

Sources: Department of Finance (*SPU 2023*); and Fiscal Council assessments.

S.4 Detail on fiscal outturns and forecasts

This section sets out key budget figures on spending, taxes and the budget balance based on recent outturns and latest forecasts.

Table S4: Fiscal forecasts from *SPU 2023*

	2021	2022	2023	2024	2025	2026
General Government Revenue	98,916	115,506	123,440	129,170	134,955	142,120
Income Tax	26,665	30,730	32,830	34,905	37,035	39,220
VAT	15,440	18,600	20,435	22,350	23,825	25,350
Corporation Tax	15,325	22,645	24,305	25,060	25,450	27,190
Of which excess	5,000	10,800	11,800	11,800	11,400	12,400
PRSI	11,798	14,021	15,069	16,554	17,622	18,698
Excise	5,840	5,440	5,790	6,330	6,630	6,910
Stamp Duties	1,485	1,825	1,640	1,700	1,790	1,885
Remaining GG Revenue	22,363	22,245	23,371	22,271	22,603	22,867
General Government Expenditure	105,721	107,473	113,440	112,955	116,845	121,285
Social payments	37,285	37,133	38,625	38,435	39,520	40,765
Compensation of employees	26,631	28,859	29,805	30,860	32,010	33,290
Intermediate consumption	16,271	17,843	18,275	18,185	18,565	19,170
Capital expenditure	8,709	9,982	10,965	12,050	13,200	14,290
Interest expenditure	3,292	3,276	3,430	3,470	3,320	3,380
Subsidies	7,186	3,303	2,815	2,175	2,190	2,170
Other	6,347	7,077	9,525	7,780	8,040	8,220
Primary expenditure	102,429	104,197	110,010	109,485	113,525	117,905
Current Primary expenditure	93,720	94,215	99,045	97,435	100,325	103,615
General Government Balance excluding excess CT	-11,805	-2,767	-1,800	4,415	6,710	8,435
General Government Balance	-6,805	8,033	10,000	16,215	18,110	20,835

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

Note: Estimates for excess CT in 2020 are Fiscal Council estimates. Estimates for 2022-2026 are taken from *SPU 2023* documentation. Remaining GG revenue is calculated as a residual. It is calculated as general government revenue minus tax and PRSI revenue items which are listed above. As these specific revenue headings are on a cash basis, this residual measure may not be informative.

S5. Tax forecasts decomposed

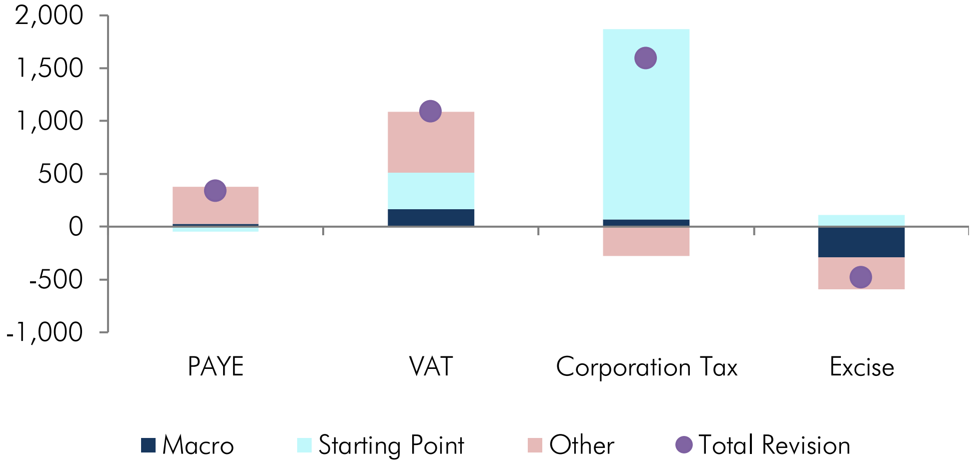
This section examines official forecasts for the main tax heads. The projected yearly changes in tax receipts are decomposed to better understand how the forecasts are arrived at.

Changes to forecasts since *Budget 2023*

This section first looks at the revisions to the Department's tax forecasts for 2023 compared to *Budget 2023* forecasts. The revisions are assessed in terms of: (1) the change in the "macro" economic outlook relevant for each tax head; (2) the error arising from an incorrect "starting point" estimate of 2022, which biases the 2023 forecast (a positive starting point means that the 2022 outturn was actually higher than expected at budget time); and (3) an "other" source of revision, caused by use of incorrect estimates of any other component of the forecast.

Tax forecast revisions in 2023

€ million, *SPU 2023* – Budget 2023



As an example of how to interpret this, the upward revision to corporation tax is entirely driven by a higher starting point (the 2022 outturn being higher than what was forecast in *Budget 2023*).

Analysing tax forecasts

The second part of this section looks at the latest official tax forecasts. It shows the yearly changes expected for receipts from VAT, corporation tax, excise duties, and the PAYE and USC components of income tax. The annual changes are attributed to a number of components:

1) "macro" is the part of the forecast driven by growth in the relevant macro driver (such as wage growth, recognising the sensitivity of income tax growth to this driver)

2) "one-offs" — non-recurring items that effect expected receipts

3) "policy" changes, such as tax cuts or tax increases. For PAYE and USC, this does not include the yield from higher wages. As a result, in 2024, 2025 and 2026, the negative impact of policy changes is shown, these policy changes are less than the estimated cost of fully indexing tax bands and credits (Section 2.4). For excise duties, the positive impacts of policy changes reflects the expected increase in the rate of the carbon tax.

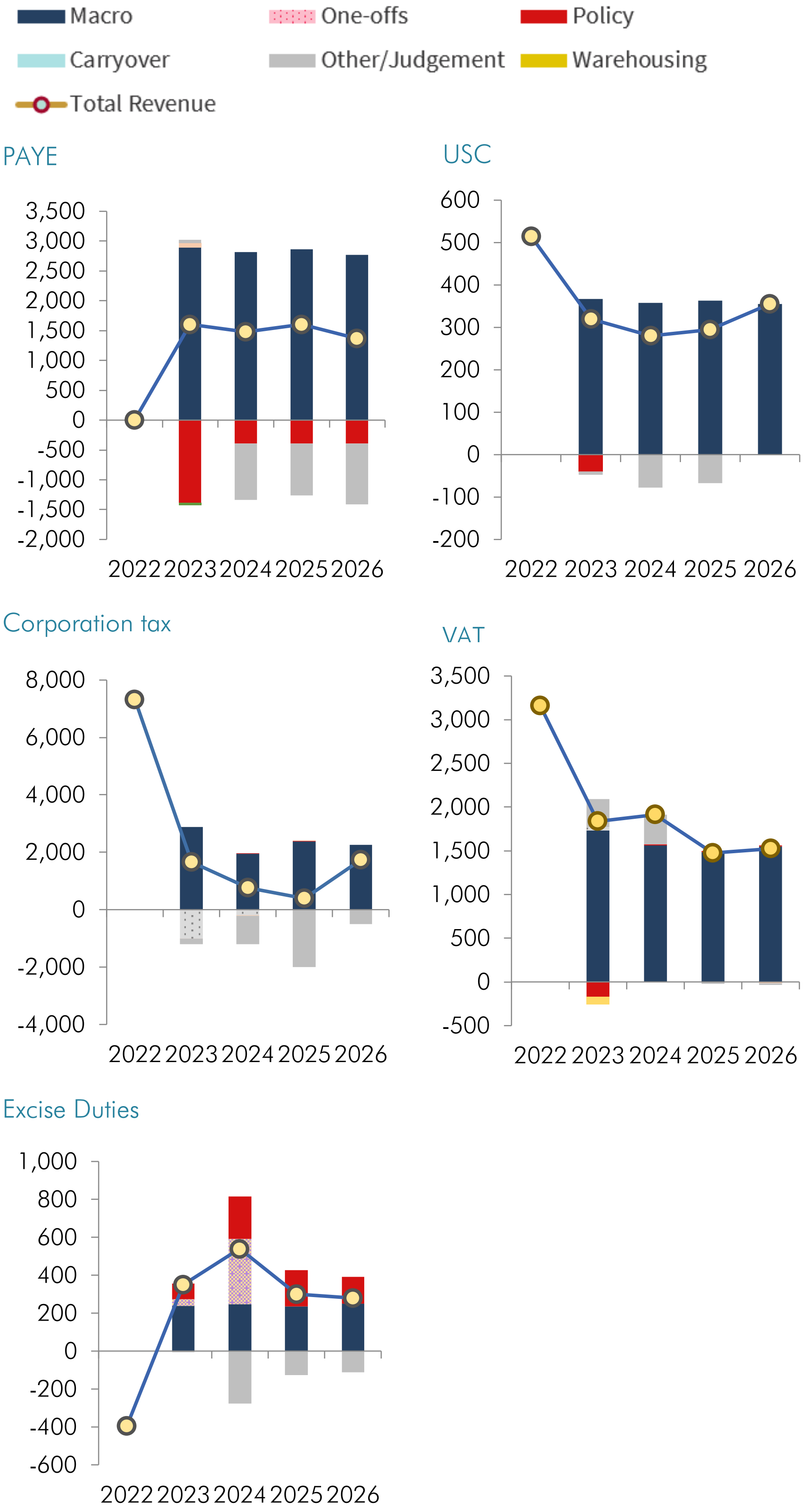
4) "warehousing" the net impact of warehousing of taxes from 2020 - 2022, with repayments from 2022-2026.

5) "carryover" effects — policy impacts carried over from previous years

6) "other" — other potential elements affecting the forecasts, including judgment applied by the Department of Finance. It is calculated as the difference between the Fiscal Council's internal forecasting exercise and the Department of Finance's own forecasts.

Figure S5: Tax forecasts decomposed

€ million, year-on-year change



Sources: Department of Finance; and Fiscal Council workings.

S6. Fiscal rules

Table S6.1: Summary Fiscal Rules assessment[1, 2, 3, 4]

% of GDP unless otherwise stated. For deviations, negative values = non-compliance

	2022	2023	2024	2025	2026
Corrective Arm					
General government balance (% GNI*)[4]	3.0	3.5	5.4	5.8	6.3
General government balance	1.6	1.8	2.8	2.9	3.1
General government balance Limit	**-3.0**	**-3.0**	**-3.0**	**-3.0**	**-3.0**
General government debt (% GNI*)[4]	83.3	78.8	75.4	70.4	65.4
General government debt	44.7	40.5	38.2	35.0	32.0
1/20th Debt Rule Limit	**60.0**	**60.0**	**60.0**	**60.0**	**60.0**
Debt Rule met?	Y	Y	Y	Y	Y
Preventive Arm & Domestic Budgetary Rule					
Structural balance adjustment requirement					
MTO for the structural balance	-0.5	-0.5	-0.5	-0.5	-0.5
Structural balance	0.3	0.0	0.3	0.5	0.6
MTO met?	Y	Y	Y	Y	Y
Minimum change in structural balance required	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Change in structural balance	0.1	-0.2	0.2	0.2	0.1
1yr deviation (€ bn)	3.8	2.9	4.4	6.1	7.2
1yr deviation (p.p.)	0.8	0.5	0.8	1.0	1.1
2yr deviation (€ bn)	3.3	3.3	3.7	5.3	6.6
2yr deviation (p.p.)	0.7	0.6	0.6	0.9	1.0
Expenditure Benchmark					
(a) Reference rate of potential growth (% y/y)	2.4	2.4	2.3	2.2	2.1
(b) Convergence margin	0.0	0.0	0.0	0.0	0.0
(a-b) Limit for real net expenditure growth (% y/y)	2.4	2.4	2.3	2.2	2.1
GDP deflator used	5.3	4.0	2.3	2.2	2.2
Limit for nominal net expenditure growth (% y/y)	**7.8**	**6.4**	**4.7**	**4.4**	**4.3**
Net expenditure growth (% y/y)	6.6	4.8	-0.6	3.7	4.0
Net expenditure growth (corrected for one-offs) (% y/y)	8.7	7.7	4.0	4.0	4.2
1yr deviation (corrected for one-offs) (€ bn)	-0.8	-1.2	0.8	0.4	0.1
1yr deviation (corrected for one-offs) (% GNI*)	-0.3	-0.4	0.3	0.1	0.0
2yr deviation (corrected for one-offs) (€ bn)	-2.3	-1.0	-0.2	0.6	0.3
2yr deviation (corrected for one-offs) (%GNI*)	-0.9	-0.4	-0.1	0.2	0.1
Limit for nominal net expenditure growth (€bn)	**6.8**	**6.1**	**4.8**	**4.7**	**4.8**
Net expenditure increase (€bn)	6.3	5.0	-0.6	4.0	4.5
Net expenditure increase (corrected for one-offs) (€bn)	7.6	7.4	4.1	4.3	4.7
Current Macroeconomic Aggregates					
Real GDP growth (% y/y)	12.0	5.6	4.1	4.9	4.4
Potential GDP growth (% y/y)	3.8	1.8	2.3	2.4	2.3
Output gap	1.6	1.4	1.1	1.2	1.3
GDP deflator used (% y/y)	5.3	4.0	2.3	2.2	2.2

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

Notes: [1] All figures are presented on a general government basis. Assessments examine the *SPU 2023* revenue and expenditure plans, using the Council's principles-based approach to the Domestic Budgetary Rule and considering the Council's views on one-off/temporary measures and on Discretionary Revenue Measures. Potential output and output gap estimates are taken from *SPU 2023*. For more information on the Council's principles-based approach see Table S6.2 and Box A of the Fiscal Council's Ex-post Assessment of Compliance with the Domestic Budgetary Rule 2018 (Fiscal Council, 2019a). The MTO is assumed constant at -0.5% of GDP for each year. [2] The 1/20th Debt Rule requires that the debt-to-GDP ratio should make annual progress toward the reference value of 60% of GDP. Once the debt-to-GDP ratio falls below 60%, the requirement is to maintain a ratio below 60%.[3] Exceptional circumstances exist for 2022–2023. Therefore, deviations from the requirements for these years are allowed. [4] The general government balance and general government debt are shown here as a % of GNI* for reference purposes only. Legal compliance with the corrective arm of the SGP is assessed based on GDP ratios.

Table S6.2: Outline of the Council's principles-based approach to the Budgetary Rule

Criteria	Fiscal Council Approach	European Commission Approach
Potential Output and the Output Gap	The Department's GVA-based estimates of potential output and the output gap.	The European Commission's own CAM-based estimates of potential output and the output gap.
Reference Rate for Expenditure Benchmark	Based on the Department's latest estimates of GVA-based potential output growth (i.e. not frozen).	Based on the European Commission's CAM-based estimates of potential output, frozen in spring of year *t-1*. No reference rate is set for *t+2* or later years.
Deflator for Expenditure Benchmark	Based on the Department's latest estimates of the demand-side GVA deflator (i.e. not frozen).	Based on the European Commission's estimates of the GDP deflator, frozen in spring of year *t-1*.
Adjustment Requirement and Convergence Margin	Based on the latest estimates of distance from the MTO in year *t-1* (i.e. not frozen). No negative convergence margin applied.	Based on the European Commission's estimates of distance from the MTO that are frozen in either spring or autumn of year *t-1* (whichever is more favourable). For ex-post assessment, requirements can be unfrozen in spring of year *t+1* if these are more favourable in terms of compliance. Negative convergence margin allowed.
NAWRU	Assumed constant at 5.5%.	The Commission's latest CAM-based estimates of the NAWRU.
Margin of Tolerance	No margin of tolerance.	0.25% of GDP from the MTO.
Significant Deviation from the Expenditure Benchmark	0.5% and 0.25% of GNI* for 1-year and 2-year assessment respectively.	0.5% and 0.25% of GDP for 1-year and 2-year assessment respectively.
Budgetary Semi-Elasticity	0.52	0.522

Note: For a full explanation of the Council's Principles-based Approach (PBA) to the Domestic Budgetary Rule see Box A of Ex-post assessment of compliance with the Domestic Budgetary Rule 2018 (Fiscal Council, 2019a) and Box M of the November 2019 Fiscal Assessment Report (Fiscal Council, 2019b). As of *Budget 2022,* the Department's preferred measure of the output gap is based on their GVA based models. As a result, the Council's Principles-based Approach is now based on this preferred measure of the output gap.