

Ireland – Stability Programme Update

December 2009

Foreword

This document updates Ireland's Stability Programme. The previous update and the related Council Opinion were presented and discussed at the Dáil Select Committee on Finance and the Public Service on 11 June 2009.

This Update takes account of Budget 2010 and includes macroeconomic projections up to and including 2014. The Update is being presented to Dáil Éireann and submitted to the European Commission on Budget Day, 9 December 2009. As such, it also provides an update of the economic background to Budget 2010.

This document has been prepared in accordance with Council Regulation (EC) No.1055/2005 amending regulation 1466/97, which sets out the rules covering the content of Stability Programmes, and conforms to the revised Opinion on the content and format of Stability and Convergence Programmes agreed by the Economic and Financial Committee of the EU in September 2005.

The Stability Programme should be seen in conjunction with Ireland's National Reform Programme (NRP) 2008 – 2010 which outlines a broad range of policies and initiatives to promote economic growth and employment performance in the context of the Lisbon Strategy for Growth and Jobs.

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Chapter 1

Introduction and Overview - General Policy Framework

This Update of Ireland's Stability Programme ('Update' hereafter) expands on the Government's medium term strategy for economic recovery and budgetary consolidation. This strategy intends to restore strong and sustainable economic and employment growth and to place the public finances on a sound basis for the future.

Ireland is currently subject to a Council recommendation to reduce the General Government Balance below -3% of GDP in line with the terms of the Stability and Growth Pact. On 2 December 2009, the Council of European Finance Ministers agreed with the EU Commission assessment that Ireland has taken effective action to address the fiscal deterioration in response to the recommendation issued in April 2009. At that meeting, the Council, taking account of the commitments set down by the Irish authorities, granted an extension of one year in the timeframe for reducing the deficit. Consequently, the budgetary plan has now been revised to take on board this extension as well as the latest economic and fiscal data. The Government intends reducing the General Government Balance to below -3 per cent of GDP by end-2014.

This document has been prepared to coincide with the presentation of Budget 2010 to the Dáil. Since mid-2008, the Government has implemented a series of difficult but necessary budgetary adjustments which have been welcomed by the EU Commission and other international bodies and by investors. The Government is committed to continuing to meet its obligations under the Stability and Growth Pact. The Government has sought to balance the need to stabilise the public finances and the need to position the economy to take advantage of international recovery. The following chapters detail the actions taken to date and the measures being taken in Budget 2010 which will have a sizeable role in solving the fiscal imbalances over the medium-term as well as setting out the path that will bring Ireland out of excessive deficit.

The main objectives of this medium-term strategy are to:

- assist economic growth through a restoration of competitiveness
- prevent the General Government debt rising to unsustainable levels
- restore expenditure and taxation to more sustainable levels.

Economic and Budgetary Outlook

In this Update, forecasts are presented for the main economic and budgetary aggregates out to 2014 as well as identifying the main risks to this outlook.

The global economic and financial crisis, together with the correction in the domestic property market, have had a significant impact on budgetary and economic developments in Ireland in 2009. GDP is projected to decline by 7.5 per cent this year. For next year, a GDP decline of 1.3 per cent is in prospect, although annual growth is expected to turn positive during the second half of the year. More robust economic growth is projected from 2011 onwards averaging 4 per cent per annum over the 2011-2014 period. Employment growth is also projected to resume from 2011 onwards, and as a result unemployment is forecast to peak in 2010.

A General Government Balance of -11.7 per cent of GDP is now estimated for 2009 - this is an improvement from the -12 per cent of GDP estimated in the end-September 2009 Maastricht Return to Eurostat. In the Supplementary Budget last April, recognising that the economy would still be in recession in 2010, the fiscal aim was for the deficit to be stabilised at the 2009 level. Budget 2010 has delivered this budgetary objective with a General

Government Balance of -11.6 per cent of GDP forecast for 2010. Further consolidation efforts will be pursued in subsequent years to reduce the General Government Balance to below -3 per cent of GDP by end 2014. However, at this stage it is envisaged that the scale of these further adjustments will not be as large as had been thought previously.

The General Government Debt is estimated to stand at 64.5 per cent of GDP at end-2009 and at 77.9 per cent of GDP at end-2010. Table 1 below sets out the General Government Debt ratios for the forecast period. When account is taken of the value of assets in the National Pensions Reserve Fund (NPRF) and the substantial Exchequer cash balances held by the National Treasury Management Agency, it is estimated that the debt position would be improved by 25 per cent of GDP, i.e. the net debt at the end of 2009 is estimated to be 39.5 per cent of GDP.

Table 1 – General Government Balance and Prospective Debt Ratio

% of GDP	2009	2010	2011	2012	2013	2014
General Government Balance	-11.7	-11.6	-10.0	-7.2	-4.9	-2.9
Structural Primary Balance	-7.2	-6.5	-5.1	-3.0	-1.3	0.4
Debt Ratio (year end)	64.5	77.9	82.9	83.9	83.3	80.8

Source: Department of Finance

Medium-term Budgetary Framework

This Update sets out the budgetary adjustment needed in future years and in that context it is acknowledged that there will be need for ongoing monitoring and strong fiscal discipline. With this in mind, the Government intends to examine the budgetary framework that is in place with a view to strengthening it so as to complement the requirements of the Stability and Growth Pact. The further measures being considered include the allocation of any future surplus or one-off revenues to deficit reduction and consideration of the feasibility of introducing multi-annual envelopes for current expenditure.

Conclusion

Budget 2010 sets out the budgetary measures being taken to stabilise the deficit at the 2009 level in 2010 and the medium-term consolidation strategy for its progressive reduction in subsequent years.

A number of challenges are being addressed: the public finances are being put on a more sustainable path – Budget 2010 continues the essential adjustment process started in July 2008. In addition to taking action on the fiscal front, the Government is pursuing measures to restore stability to the banking system in order to facilitate bank lending to the real economy. Measures to improve competitiveness have also been implemented. The Government's budgetary proposals include a number of targeted stimulus measures for implementation in 2010 to support economic recovery and employment. Furthermore, the Government is proposing changes to public service pensions that will significantly reduce the accrued cost of these pensions for the future. All of these measures are preparing the economy to return to a more sustainable growth path over the medium term, facilitating a return to employment growth and a long term improvement in living standards, while at the same time repairing the structural weaknesses in the public finances.

Chapter 2 Economic Outlook

2.1 Economic Developments in 2009

This year has been the most difficult one for the Irish economy in living memory, with the deterioration in the external environment and the fall-out from the correction in the house-building sector having a major impact on living standards. GDP has fallen by an estimated 7.5 per cent, the sharpest rate of decline since records have been compiled. Employment has fallen by around 7.8 per cent, with the construction, retail and manufacturing sectors being the worst affected. Unemployment has risen to its highest rate since the mid-1990s, and the indications are that the increase would have been higher but for a resumption of outward migration. On a harmonised basis, consumer prices have fallen by an estimated 1.7 per cent, providing some support to disposable incomes and living standards. (A more detailed discussion of macro-economic developments this year is contained in the Pre-Budget Outlook, published in mid-November, available at www.finance.gov.ie)

Table 2 – Economic Indicators 2009: Budget Forecast and Estimated Outturn

	2009 Forecast (April 2009)	2009 Estimate (December 2009)
GDP (% volume change)	-7.7	-7.5
Consumer prices - HICP (% change)	-1.4	-1.7
Consumer prices – CPI (% change)	-3.9	-4.4
Unemployment rate (% labour force)	12.6	11.8
Employment ('000)	-165	-164
Employment (%)	-7.8	-7.8

Source: Department of Finance.

2.2 Macroeconomic Projections 2010 – 2014

External Developments

While tentative signs of optimism have emerged in recent months, the outlook for the global economy remains uncertain. This is particularly the case for many of Ireland's main export markets where, in some cases, recent better-than-expected growth figures partly reflect fiscal stimulus and other temporary factors. The forecasts for demand in our trading partners in this document are based on the EU Commission's autumn 2009 forecasts (table 3). Following the sharp declines recorded this year, activity is projected to expand next year in our main export markets, albeit at rates which are relatively modest by historical standards.

Table 3 – GDP Growth in Ireland's Main Trading Partners

	2009	2010	2011
Euro area	-4.0	0.7	1.5
- Germany	-5.0	1.2	1.7
- France	-2.2	1.2	1.5
- Italy	-4.7	0.7	1.4
UK	-4.6	0.9	1.9
US	-2.5	2.2	2.0
Global economy	-1.2	3.1	3.5

Source: EU Commission Autumn 2009 European Economic Forecast.

There is likely to be some lag between global recovery and an improved export performance in Ireland, given the deterioration in competitiveness in recent years. The current elevated level of the euro exchange rate is also likely to weigh on exports next year. All of these developments suggest that export growth will be modest next year. An improvement in the

rate of export growth is forecast for later years, in line with the assumed recovery in our export markets and well as the assumption of continued competitiveness improvement.

Revisions vis-à-vis the Pre-Budget Outlook

There are modest differences between the estimates contained in this Stability Programme Update and those in the Pre-Budget Outlook. The PBO was based on an indicative package of €4 billion next year; the specifics of this have now been decided and their economic effects assessed. In addition, the external data that have become available since the PBO suggest that the global outlook continues to improve, so that the forecast for exports has been revised upwards. Stronger export growth and a slightly better outlook for the labour market (with positive implications for confidence, and by extension the savings rate) means that the outlook for personal consumption is somewhat better.

Domestic Demand

Household incomes are likely to fall once again next year, given the outlook for employment, wages and other components of personal income. In addition, falling consumer prices will not provide the same level of support to real incomes as was the case this year, given the projected profile for inflation. Even allowing for some reduction in the household savings rate, personal consumption is expected to fall once again next year, probably by around 3 per cent. Thereafter, rising employment and earnings, and further downward adjustment of household savings rates are assumed to underpin positive consumption growth. However, a number of factors – including the need for households to reduce debt to more sustainable levels – mean that consumption growth in later years will be relatively modest.

Public consumption is projected to fall by 3 per cent in real terms next year. This reflects reduced public sector employment achieved through natural attrition as well as reduced purchases of non-labour goods and services.

On the basis of housing start data, completions next year will amount to around 12,000 units (compared with around 25,000 units this year), with other components of building and construction – including commercial activity – also projected to record a decline next year. Ongoing economic weakness is assumed to restrain investment in machinery and equipment. These considerations point to a decline in investment of around 19 per cent next year.

Over the medium term, new housing output levels are expected to gradually revert back towards 30,000 units per annum (the tentatively-estimated sustainable level over the medium term). This will result in fairly strong annual growth rates in this component of demand, but will not contribute significantly to GDP growth given that its relative importance in overall activity has declined substantially in recent years. Investment in machinery and equipment should recover in line with the improvement in economic conditions.

Final Demand and Imports

Imports of goods and services are projected to decline by 2.8 per cent next year, in line with the assumed fall in final demand. Lower import volumes together with modest export growth should contribute towards some further improvement in the current account of the balance of payments, which is expected to move into positive territory over the course of next year. Imports are expected to increase over the forecast horizon as final demand improves.

Gross Domestic Product and Gross National Product

All of these developments point to a GDP contraction of around 1.3 per cent next year (a GNP fall of 1.7 per cent). Positive annual growth is expected to return by the second half of next year, and on a full-year basis by 2011.

The forecasts covering the period 2011 – 2014 are based on an assessment of the economy's potential growth rate. Taking into account the underlying growth in labour supply and productivity, it is tentatively estimated that the Irish economy can expand at an average rate of 3 per cent per annum (there is, of course, considerable uncertainty surrounding this estimate given the openness of the Irish economy). Given significant under-utilised capital and labour at present (i.e. a negative output gap), the economy can grow above trend as these under-utilised resources are brought back into productive use (i.e. as the output gap closes). In these circumstances, an annual average growth rate of 4 per cent over the period 2011 – 2014 is assumed.

Labour Market

The labour market has been hit hard by the recession, with the construction, retail and manufacturing sectors amongst the worst affected sectors. Following an estimated decline of 7.8 per cent this year, employment is forecast to fall once again next year. A decline of 3.4 per cent is in prospect. Over the medium term, employment is assumed to begin rising as economic activity improves, although inherent lags mean that productivity growth will be relatively strong over the next year or so.

The rate of increase in unemployment has slowed since the beginning of the summer, although this may, to some extent, reflect falling labour supply (including outward migration) rather than any improvement in labour demand. For this year, an annual average unemployment rate of 11.8 per cent is expected, with an average of 13.2 per cent in prospect for next year. The unemployment rate is forecast to fall over the medium term, as employment growth resumes, although it is not expected to return to pre-2008 levels for some time, given the structural change within the economy.

Inflation

Consumer prices on an EU harmonised basis are expected to fall by 1.2 per cent next year following an average decline of 1.7 per cent this year. Continuing weak demand and exchange rate appreciation are the main factors behind this projected fall in prices next year. As these temporary factors fade, low but positive price inflation is projected from 2011 onwards. The Consumer Price Index is forecast to decline by 0.8 per cent next year. The forecasts for both price indices take into account the various budgetary measures.

Table 4 – Macroeconomic Prospects

% change (unless otherwise indicated)	2009	2010	2011	2012	2013	2014
GDP growth at constant market prices	-7.5	-1.3	3.3	4.5	4.3	4.0
GDP at current market prices (€m)	164,600	160,925	169,900	181,250	192,975	204,800
GNP growth at constant market prices	-10.4	-1.7	3.0	4.1	3.9	3.6
GNP at current market prices (€m)	133,175	129,100	135,375	143,750	152,275	160,700
Components of real GDP						
Private consumption expenditure	-7.2	-3.0	2.6	3.4	3.3	3.2
Government consumption expenditure	-0.6	-3.0	-0.5	-0.5	-0.5	-0.5
Gross domestic fixed capital formation	-33.9	-19.2	4.5	7.8	8.5	7.8
Exports of goods and services	-2.7	0.4	3.4	4.0	3.8	3.5
Imports of goods and services	-9.0	-2.8	2.6	2.9	3.0	2.8
External position						
Current account (% GDP)	-2.0	0.6	1.2	1.6	1.6	1.3
Price developments						
HICP	-1.7	-1.2	1.0	1.7	1.8	1.8
CPI	-4.4	-0.8	1.8	2.0	2.0	2.0
Labour market developments						
Unemployment (% of labour force)	11.8	13.2	12.6	11.8	10.8	9.5
Employment	-7.8	-3.4	1.0	2.3	2.5	2.3
Labour productivity (GDP/person employed)	0.4	2.3	2.3	2.1	1.7	1.7

Note: Tables 2a, 2b, 2c and 2d as set out in the guidelines are enclosed at Annex 2.

Source: Department of Finance.

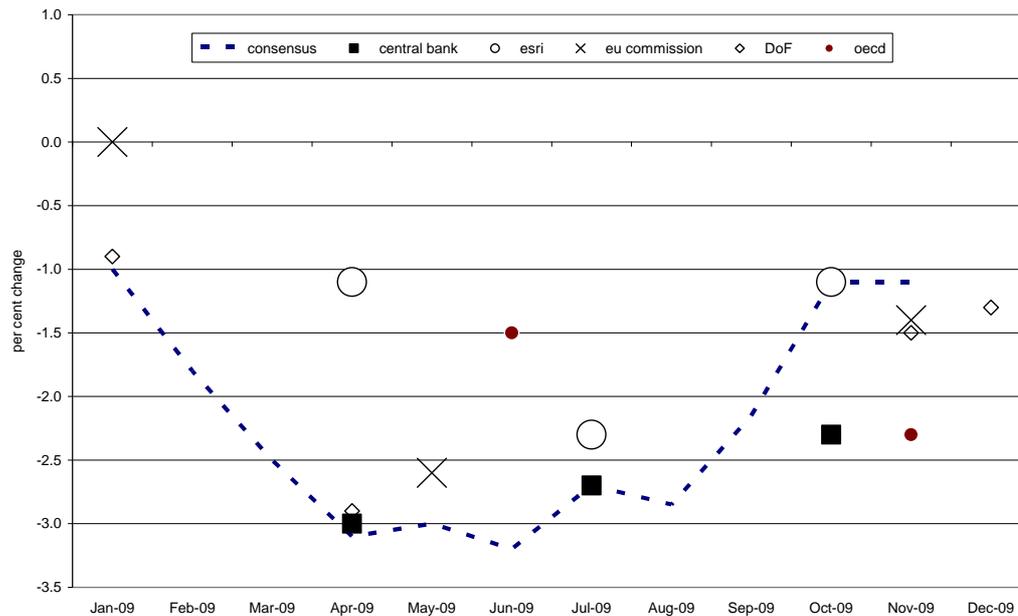
2.3 Range of Forecasts

Since the onset of the global financial crisis, economic forecasts – domestically and internationally – have been subject to even greater uncertainty than normal. This was especially the case for Ireland given how globalised the economy is. To take account of this uncertainty, the Department of Finance has complemented its various forecasts this year by publishing the consensus forecast (a monthly publication by *Reuters* based on a survey of around 10 private sector institutions in Ireland) alongside its own projections.

The graph below shows the consensus forecast for 2010 and how this has evolved since the beginning of this year. The forecasts of some other organisations are also shown; in making comparisons, it should be borne in mind that the assumptions underpinning the forecasts may be different.

In the early part of this year, when uncertainty was greatest, projections for 2010 were continually being revised downwards. From April, a period of stability became evident. The outlook has improved significantly since the summer, with the end-November *Reuters* consensus forecast for a GDP decline of 1.1 per cent next year. The Department of Finance forecast in this Update is for GDP to contract by 1.3 per cent next year.

Figure 1: Comparison of GDP Forecasts for 2010



Source: Department of Finance and institutions cited.

The current range of forecasts for the main macro-economic variables is shown in the table below.

Table 5 – Comparison of Macroeconomic Forecasts for Ireland for 2010

Institution	Publication	Annual % change			
		GDP	GNP	HICP	Employment
Department of Finance	<i>Budget 2010</i>	-1.3	-1.7	-1.2	-3.4
Central Bank of Ireland	<i>Bulletin No.4, Oct 2010</i>	-2.3	-3.1	-0.5	-4.4
ESRI	<i>QEC Autumn 2010</i>	-1.1	-1.7	-0.7	-4.1
EU Commission	<i>Autumn 2009 Forecasts</i>	-1.4	n.a.	-0.6	-3.9
OECD	<i>Economic Outlook, November</i>	-2.3	n.a.	-0.7	n.a.
Consensus	<i>Reuters poll, end-November</i>	-1.1	-1.9	-0.4	n.a.

Source: Institutions cited.

2.4 Risks to forecasts

While there are some signs of stabilisation, the outlook over the short- and medium-term remains subject to considerable uncertainty. Over the past eighteen months or so, the risks to the macroeconomic projections were skewed to the downside (and in many cases the risks actually materialised). However, upside risks to the outlook have also become apparent in recent months. The most significant of these relate to (internationally) the possibility of stronger world growth and (domestically) the possibility of a more rapid restoration of confidence with positive implications for consumer spending through a reduction in the very high savings rate. Nevertheless, downside risks remain prevalent and the main factors which could cause weaker growth than assumed are:

International

- A further weakening of demand in our main export markets (if, for instance, policy stimulus was withdrawn too quickly);
- A renewed bout of turbulence in international financial markets;
- Further exchange rate appreciation, especially versus sterling;
- Commodity price increases, especially oil.

Domestic

- Households maintain savings rates at current very high levels, representing a continued constraint on personal consumption;
- The necessary domestic competitiveness adjustment does not materialise;
- At some stage over the medium term interest rates will return to more 'normal' levels, raising the cost of borrowing for all.

2.5 Sensitivity analysis

In order to consider the sensitivity of the public finances to a different growth trajectory, the ESRI's macro-econometric model (HERMES) was used to simulate a situation in which output growth was 1 per cent different from baseline arising from (a) changes in interest rates or (b) changes in world demand.

(a) change in interest rates

These estimates suggest that a 1 percentage point lower growth rate resulting from higher interest rates would lead to deterioration in the general government balance (GGB) of about 0.6 percentage points of GDP by 2014 (see table below). This finding is broadly symmetrical, in that higher growth as a result of lower interest rates would improve the GGB by a similar amount.

(b) change in world demand

A 1 per cent higher growth rate resulting from stronger world demand would improve the GGB by 0.3 percentage points of GDP by 2011. Again, this effect is symmetrical.

The estimates should be seen as indicative and are subject to considerable uncertainty. Also, it is assumed that there is no fiscal policy response to the changed budgetary position over the period. In reality such a response would occur if desirable in the interests of economic or budgetary sustainability.

Table 6 - Impact on the Budget Balance of a 1 per cent change in the rate of growth

Baseline GDP and GGB		2010	2011	2012	2013	2014
Budget day GDP	Growth (%)	-1.3	3.3	4.5	4.3	4.0
Budget day GGB	(% GDP)	-11.6	-10.0	-7.2	-4.9	-2.9
<i>1 percentage point change in the rate of growth due to a change in interest rates</i>						
Cumulative impact on GGB	(% GDP)	Up to 0.2	Up to 0.4	Up to 0.5	Up to 0.5	Up to 0.6
GGB Range		-11.8 to -11.4	-10.4 to -9.6	-7.7 to -6.7	-5.4 to -4.4	-3.5 to -2.3
<i>1 percentage point change in the rate of growth due to a change in world growth</i>						
Cumulative impact on GGB	(% GDP)	Up to 0.2	Up to 0.3	Up to 0.3	Up to 0.3	Up to 0.3
GGB Range		-11.8 to -11.4	-10.3 to -9.7	-7.5 to -6.9	-5.2 to -4.6	-3.2 to -2.6

Source: Department of Finance calculations on basis of ESRI macro-econometric model.

2.6 Comparison with Previous Budget Forecasts

Table 7 – Divergence from April Supplementary Budget Forecasts

	2009	2010	2011	2012	2013	2014
Real GDP growth (%)						
Previous forecast	-7.7	-2.9	2.7	4.2	4.0	n/a
Current forecast	-7.5	-1.3	3.3	4.5	4.3	4.0
Difference	0.2	1.6	0.6	0.3	0.3	n/a
General Government balance (% of GDP)						
Previous forecast	-10.7	-10.7	-8.5	-5.5	-3.0	n/a
Current forecast	-11.7	-11.6	-10.0	-7.2	-4.9	-2.9
Difference	-1.0	-0.9	-1.5	-1.7	-1.9	n/a
General Government Gross Debt (% of GDP)						
Previous forecast	59.0	73.0	78.0	79.0	77.0	n/a
Current forecast	64.5	77.9	82.9	83.9	83.3	80.8
Difference	5.5	4.9	4.9	4.9	6.3	n/a

Source: Department of Finance

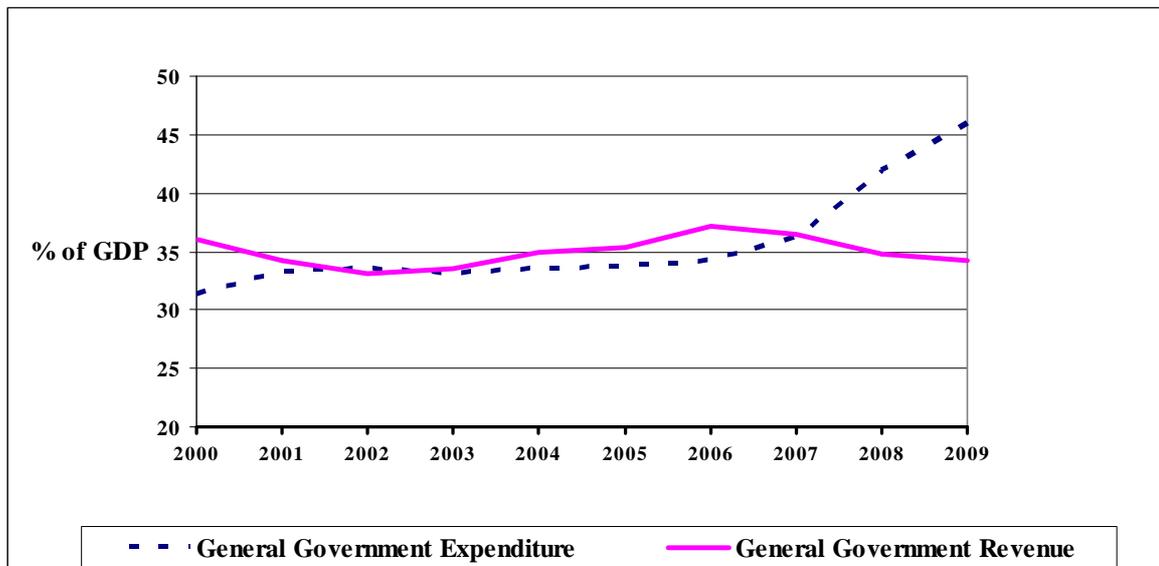
Chapter 3 The Public Finances: General Government Balance and Debt

3.1 Summary

The current outlook is for a General Government Balance of -11.7 per cent of GDP in 2009. This follows a General Government Balance of -7.2 per cent of GDP in 2008 and surpluses in ten of the previous eleven years. It is forecast that the General Government Balance in 2010 will be stabilised at the 2009 level and on the assumption that further measures are introduced, the General Government Balance will, through a series of further policy measures and controls, be reduced to less than -3 per cent of GDP by end-2014.

The Irish public finances, in particular tax receipts, have been very severely impacted by the sharp deterioration in the economic environment over the last eighteen months. However, the deterioration in the public finances also reflects the increase in government spending in recent years. Over the past decade, government revenues had moved within a relatively narrow range of 34 to 37 per cent of GDP. Following the introduction of tax changes in Budget 2009 and in the Supplementary Budget of April 2009, revenue's share of GDP is expected to rise over the next few years. Expenditure as a share of GDP has risen from 36 per cent of GDP in 2007 to a projected 46 per cent in 2009. Following the introduction of adjustment measures, including those announced in Budget 2010, this ratio is expected to fall over the coming years.

Figure 2: General Government Revenue and Expenditure



Since mid-2008, very significant action has been taken across the spectrum of taxation and expenditure to restore sustainability to the public finances. These actions have not only stemmed the decline in the budgetary situation in the years in which they were introduced but much more importantly have provided a necessary structural improvement to the public finances. The consequence of this can be seen by the fact that when account is taken of the measures announced in Budget 2010, the deficit has now been stabilised, albeit at a very high level. Furthermore, the path that has been set out to bring Ireland out of excessive deficit has been adhered to in terms of the identified correction for 2010, i.e. adjustments amounting to €4 billion or 2½ per cent of GDP have been delivered in Budget 2010. The scale of future adjustments will not now be as large as previously thought. For 2011, it is estimated that the necessary adjustments will be of the order of €3 billion, with €1 billion already identified and incorporated into the capital expenditure forecasts taking account of revised investment priorities reflecting the changed economic environment. The remaining €2 billion will be

achieved through a series of further expenditure and taxation measures as signalled by the Minister for Finance in his Budget day speech.

3.2 Policy Strategy - Medium-Term Objectives

The strategy behind Ireland's medium-term economic and fiscal plan is based around three inter-related issues -

- Restoring economic competitiveness, the basis of future economic growth, by taking responsible action on fiscal and incomes policies;
- Inspiring confidence, both internationally and domestically, that the deterioration in the public finances has been arrested;
- Restoring Government expenditures and revenues to more sustainable levels, thus ensuring that debt does not rise to unsustainable levels.

Recognising that a large part of Ireland's deficit is permanent, or structural, which would not be eliminated without action, significant adjustments designed to yield about 5 per cent of GDP in 2009 were introduced between July 2008 and the Supplementary Budget in April 2009. These included both expenditure-reducing measures and revenue-raising measures.

In framing Budget 2010, the Government focused on curbing spending as expenditure needs to adjust to the revenue base which has been reduced as a result of the overall contraction of the economy and the loss of certain income streams. In addition, in formulating policy the Government took on board evidence from international organisations, such as the EU Commission, the OECD and the IMF, as well as the relevant economic literature which indicates that consolidation driven by cuts in expenditure is more successful in reducing deficits than consolidation based on tax increases. Past Irish experience also supports this view and suggests that confidence is more quickly restored when adjustment is achieved by cutting expenditure rather than by tax increases.

The adjustments that have been delivered to date have been wide-ranging and have impacted on all sectors of society. These are summarised in Table 1a in the Supplementary data accompanying this document. Chapter 4 also sets out in greater detail the measures on expenditure and taxation that have been taken to improve the sustainability of the public finances.

3.3 Budgetary Outlook 2009

In the end-September Maastricht returns, it was anticipated that the General Government Balance in 2009 would stand at -12 per cent of GDP, largely due to the weakness in tax revenues and ongoing spending pressures from the worsening labour market. A General Government Balance of -11.7 per cent of GDP is now forecast for 2009.

On the expenditure side of the account there has been some savings, largely due to the slowdown in the rate of increase in the Live Register which will yield savings for this year, and more importantly, in future years. In addition, there will be some savings on servicing the national debt.

Taxation receipts in 2009 have remained weak. The Supplementary Budget in April 2009 forecast that €34.4 billion in tax revenue would be collected in 2009, a deterioration of 15½ per cent on the 2008 yield. Based on data to end-November, tax revenue in 2009 is now expected to be in the region of €32.6 billion, a shortfall of €1.8 billion. This represents a decline of over 30 per cent on the level of taxes received in 2007. Tax revenues are now at the levels received in 2003. All tax-heads have experienced declines in their yield over the last two years with the decline particularly noticeable in the performance of the capital taxes (Capital Gains Tax, Capital Acquisitions Tax and Stamp Duty). In 2006, €7.2 billion was

collected from capital taxes, almost 16 per cent of total tax revenue in that year. In 2009, it is estimated that about €½ billion will be collected from capital taxes, representing less than 5 per cent of total taxes. It is not expected that a resumption of economic growth will restore the previous levels of capital taxes. As a result, 95 per cent of tax receipts are accounted for by four tax heads – VAT, Income Tax, Excise Duties and Corporation Tax.

While taxation is now back at 2003 levels, current expenditure by Government Departments and Offices (known as voted expenditure) in 2009 is about 70 per cent above the level it was in that year. It is this large gap between day-to-day revenues and expenditure that is being further addressed by budgetary policy.

3.4 Budgetary Outlook 2010

The Supplementary Budget of April 2009 included multi-annual budgetary plans for the first time. The target set for 2010 was the stabilisation of the General Government Balance at the 2009 level, following the introduction of a €4 billion adjustment.

Budget 2010 has delivered the €4 billion adjustment in 2010 and a General Government Balance of –11.6 per cent of GDP is forecast for 2010, thereby stabilising the deficit. This means that the next key milestone set out for fiscal policy in the Supplementary Budget has been delivered. Furthermore, there are signs emerging that a corner is being turned in the public finances – the decline in tax receipts has moderated, the cost of borrowing has reduced in recent months and expenditure pressures have eased in 2009 largely due to the slowdown in the rate of increase in unemployment.

The focus of Budget 2010 is on addressing the deficit situation on the expenditure side of the account. The specific expenditure and taxation measures are outlined in the Summary of Budget Measures which is published by the Department of Finance on Budget day. Taking corrective action of €4 billion imposes short-term costs because taking money out of the economy (by reducing spending or raising taxes) has a dampening effect on activity and employment, all other things being equal. Quantifying the impact of these measures on economic activity is an inherently uncertain exercise and requires a combination of econometric model simulations and judgement. Table 8 below sets out the estimated loss in tax revenue of €97 million associated with the introduction of the budgetary package in 2010. This loss in revenue has been factored into the overall budgetary arithmetic. As against that, reducing the projected Exchequer Borrowing Requirement leads to a saving of the order of €200 million on estimated debt servicing costs.

Table 8: The Impact of the Budget on the Fiscal Position 2010

	White Paper €m	Budget €m
<u>Fiscal Measures</u>		
Current Expenditure Savings identified in White Paper Budget Day Measures²	243	
Current Expenditure		2,847
Capital Expenditure		961
Taxation		17
Total Budget Day Measures		3,825
Total Package		4,068
<i>of which: expenditure</i>		<i>4,051</i>
<i>taxation</i>		<i>17</i>
Impact on Tax Projections of Budget Day Measures =		-897
<hr/>		
	White Paper €m	Budget €m
<u>Current Expenditure</u>		
Net Voted Expenditure	43,068	40,191 ³
Non Voted Current Expenditure	7,132	6,932
Total Net Current Expenditure	50,200	47,123
<u>Current Revenue</u>		
Tax Revenue	31,930	31,050
Non Tax Revenue	2,355	2,355
Total Current Revenue	34,285	33,405
CURRENT BUDGET BALANCE	-15,915	-13,718
CAPITAL BUDGET BALANCE	-6,023	-5,062
EXCHEQUER BALANCE	-21,938	-18,780

Note: Rounding may impact on totals

² Details of the expenditure and taxation measures are set out in the Summary of Budget Measures Section of the Budget day documentation.

³ Includes Departmental Balances of €30m. Departmental Balances are those amounts issued from the Exchequer Account for Departmental spending in one year which remain unspent at year-end and are carried forward to be used in the next year.

While there are undoubtedly short-term costs from correcting the deficit, it is necessary to take action now as delaying adjustment damages domestic confidence and ultimately hinders growth. The window of opportunity to take action to stabilise the deficit is now – at a time of falling prices and low interest rates the impact of reducing spending is lessened. Delaying the adjustment until a time when inflation has returned to the economy would mean that the adjustment would be even more difficult and that its impact would be more severe.

In 2010, it is forecast that tax revenues will be just over €31 billion, a 4.7 per cent decline on 2009 reflecting the continued weakness in the economy. Gross current expenditure is projected at just under €55 billion in 2010, a year-on-year decline of 1.8 per cent. Gross current spending is divided into three main areas – 38 per cent on Social Welfare spending, 34 per cent for public sector pay and pensions and 28 per cent on other programmes.

Gross Voted Capital Expenditure is projected to remain high at €6½ billion, or 5 per cent of GNP, in 2010. The reduction from the levels seen in previous years must also be assessed in the context of prevailing prices. Reductions in construction prices mean it is now possible to deliver capital projects more cheaply. This sustained high level of expenditure on capital projects will continue to enhance Ireland's productive capacity and ensure future improvements in living standards.

During 2010 the Exchequer will make a contribution to the Social Insurance Fund (SIF). Expenditure on social welfare payments in Ireland is funded from the SIF and from the Exchequer - the overall impact on the General Government Balance is the same whether the funding comes from the Exchequer or the SIF. The SIF is used to fund social insurance/security related benefits whereas the Exchequer funds means-tested allowances and payments. The SIF is financed by employee and employer social security contributions. When necessary the Exchequer acts as a residual financier of the Fund. The tripartite funding arrangement (employee, employer and State) has been in place since 1953.

Between 1997 and 2007 the Social Insurance Fund accumulated a surplus. In 2008 this position reversed, expenditures exceeded income and over the course of 2008 and 2009 the operational surplus has been gradually wound down due to the increasing costs of unemployment, state pensions and other benefits paid out of the Fund. This surplus will be exhausted during 2010. This will require the Exchequer to make a financial contribution to the Fund starting next year. As a result more of Social Welfare spending will come from the Exchequer and less from the SIF. However, as stated above, this change in the composition of spending will have no impact on the overall General Government Balance.

3.5 Public Finances 2011-2014

Over the period 2011-2014, it is expected that growth will return to the Irish economy on an annual basis and that growth in tax revenues will resume. However the tax base is now much reduced and is heavily concentrated in the four main tax areas - Value Added Tax, Excise Duties, Income Tax and Corporation Tax. In addition, when economic growth resumes it will be export-led growth, which is not as tax rich as the domestically driven growth of the mid-part of this decade. Without additional policy changes, it is estimated that tax revenues will still be below €40 billion by the end of the forecast period, which is less than the amount collected in 2008. Consequently the expected pick-up in tax revenues based on existing policies will not bridge the significant gap that has emerged in the public finances.

In keeping with the Supplementary Budget, further adjustments in the fiscal position will be required over the coming years so that there will be a return to the position in which day-to-day spending is funded out of day-to-day revenues. The budgetary projections for the forecast period include an estimated future consolidation package. The scale and nature of these future measures will be reviewed in the context of future Budgets and will very much depend on the strength of the economic cycle at the time. An indicative path is contained in this

update that will have to be periodically reviewed in the light of later developments. It is currently envisaged that the scale of these measures, while still significant, will not be as large as the measures introduced to date. See Table 9 below.

Table 9: Additional Annual Measures to be delivered in 2011 and 2012

	2011	2012
Additional adjustment	€3 billion	€3 billion
Capital already identified and incorporated into the base	€1 billion	€1 billion
Current adjustment to be made up by tax and expenditure measures	€2 billion	€2 billion

Current projections indicate that a €3 billion adjustment will be needed in 2011 as part of the process to restore the public finances to stability. This is an improvement on the position identified in the Supplementary Budget when it was estimated that a €4 billion adjustment would be needed in 2011. However, as in the Supplementary Budget, it is planned that €1 billion of the adjustment will come from capital expenditure and this has now been taken account of in the capital allocation as shown in Table 10 below. That leaves €2 billion of measures to be identified next year. In 2012 a further €2 billion current adjustment will also be needed. Tables 10 and 11 set out the public finance projections for 2009-2014. For the purposes of Table 11 - General Government Budgetary Prospects - the future fiscal consolidation has been technically distributed. While the nature of the measures to be introduced will be a matter for the annual budget, a number of policies have been identified for future consideration, including reforming the income tax and social security system, further public sector pension reform, property taxation etc.

Table 10: Projections for the Public Finances 2009 - 2014*Rounding may impact on totals*

	2009	2010	2011	2012	2013	2014
	€bn	€bn	€bn	€bn	€bn	€bn
<u>CURRENT BUDGET</u>						
<u>Expenditure</u>						
Gross Voted Current Expenditure	55,957	54,940	55,183	54,854	54,910	54,971
Non-Voted (Central Fund) Expenditure	5,152	6,932	8,335	9,430	10,246	10,796
Gross Current Expenditure	61,108	61,872	63,518	64,284	65,156	65,768
less Expenditure Receipts and Balances	15,589	14,748	13,829	14,366	14,846	15,331
Net Current Expenditure	45,520	47,123	49,689	49,918	50,311	50,437
<u>Receipts</u>						
Tax Revenue	32,570	31,050	32,800	34,950	37,200	39,500
Non-Tax Revenue	834	2,355	1,093	1,085	1,105	955
Net Current Revenue	33,404	33,405	33,893	36,035	38,305	40,455
<u>Current Adjustment in future years</u>						
Annual			2,000	2,000	1,500	1,000
<i>Adjustment from previous years</i>				2,000	4,000	5,500
<u>CURRENT BUDGET BALANCE</u>	-12,116	-13,718	-13,797	-9,883	-6,506	-3,482
<u>CAPITAL BUDGET</u>						
<u>Expenditure</u>						
Gross Voted Capital ⁴	7,216	6,445	5,500	5,500	5,500	5,500
Non-Voted Expenditure	4,836	825	824	824	823	802
Payment to the NPRF ⁵	3,000	-	-	726	1,523	1,607
	15,052	7,270	6,324	7,050	7,846	7,909
less Capital Receipts	443	536	476	474	474	474
Net Capital Expenditure	14,609	6,734	5,848	6,576	7,372	7,435
Capital Resources	1,464	1,672	1,629	1,610	1,577	1,612
<u>CAPITAL BUDGET BALANCE</u>	-13,145	-5,062	-4,218	-4,966	-5,795	-5,823
<u>EXCHEQUER BALANCE</u>	-25,260	-18,780	-18,015	-14,850	-12,300	-9,305
<u>GENERAL GOVERNMENT BALANCE</u> ⁶	-19,260	-18,720	-17,030	-12,970	-9,450	-6,010
<i>% of GDP</i>	<i>-11.7%</i>	<i>-11.6%</i>	<i>-10.0%</i>	<i>-7.2%</i>	<i>-4.9%</i>	<i>-2.9%</i>

⁴ A multi-annual capital investment programme of over €39 billion from 2010 to 2016 has been agreed by Government. For each year from 2011 a sum of €5.5 billion is provided.

⁵ The 2010 payment to the NPRF was frontloaded into 2009. Payments in subsequent years are offset by the transfer in 2009 and 2010 to the NPRF of the assets of the pension funds of third level universities and certain non-commercial semi-state bodies. A partial payment will be made in 2012 and from 2013 onwards a payment of 1% of GNP per annum has been provided.

⁶ See Table 1c in Annex 1 for explanation of net difference between the Exchequer Balance and General Government Balance.

Table 11: General Government Budgetary Prospects

<i>Rounding may impact on totals</i>	2008	2008	2009	2010	2011	2012	2013	2014
	€m	% of GDP						
Net Lending by sub-sector								
1. General Government (=2+4+5) (=8)	-13,038	-7.2	-11.7	-11.6	-10.0	-7.2	-4.9	-2.9
2. Central Government	-12,451	-6.8	-10.2	-10.8	-9.9	-7.1	-4.8	-2.8
4. Local Government	-333	-0.2	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1
5. Social Insurance Fund	-254	-0.1	-1.3	-0.7	0.0	0.0	0.0	0.0
General Government								
6. Total Revenue (=16)	63,294	34.8	34.2	35.2	35.5	36.3	36.7	37.1
7. Total Expenditure (=24)	76,331	42.0	45.9	46.8	45.5	43.5	41.5	40.0
8. Net lending/borrowing (=6-7) (=1)	-13,037	-7.2	-11.7	-11.6	-10.0	-7.2	-4.9	-2.9
9. Interest expenditure (=20)	1,879	1.0	2.1	2.9	3.4	3.8	3.9	3.9
10. Primary balance (=8+9)	-11,158	-6.1	-9.6	-8.8	-6.6	-3.4	-1.0	1.0
11. One-off & temporary measures	-1,409	-0.8	0.4	0.6	0.0	0.0	0.0	0.0
Selected components of revenue								
12. Total taxes	43,040	23.7	21.4	20.9	22.1	23.1	23.6	24.3
a. Taxes on production & imports	22,149	12.2	11.0	11.0	11.5	11.8	12.0	12.3
b. Current taxes on income & wealth.	20,560	11.3	10.2	9.8	10.4	11.0	11.5	11.8
c. Capital taxes ⁷	331	0.2	0.2	0.1	0.2	0.2	0.2	0.2
13. Social contributions	12,501	6.9	7.7	8.2	8.1	8.0	7.9	7.8
14. Property Income⁸	2,426	1.3	1.5	1.9	1.6	1.6	1.7	1.7
15. Other	5,327	2.9	3.6	4.1	3.7	3.7	3.5	3.4
16. Total Revenue (=12 to 15) (=6)	63,294	34.8	34.2	35.2	35.5	36.3	36.7	37.1
Tax Burden⁹	56,025	30.8	29.4	29.4	30.4	31.3	31.7	32.1
Selected components of expenditure								
17. Compensation of Employees + 18. Intermediate Consumption	30,884	17.0	18.7	16.7	15.8	15.0	14.4	14.0
19. Total social payments	25,181	13.8	16.3	17.8	17.3	16.6	16.1	15.6
a. Social transfers in kind	2,853	1.6	1.7	1.7	1.7	1.6	1.5	1.5
b. Social transfers other than in kind	22,328	12.3	14.6	16.0	15.6	15.0	14.5	14.1
20. Interest Expenditure (=9)	1,879	1.0	2.1	2.9	3.4	3.8	3.9	3.9
21. Subsidies	1,083	0.5	0.5	0.6	0.6	0.5	0.4	0.5
22. Gross fixed capital formation	9,814	5.4	4.8	4.5	3.8	3.8	3.7	3.6
23. Other	7,730	4.3	3.5	4.3	4.6	3.8	3.0	2.4
24. Total Expenditure (=17 to 23) (=7)	76,331	42.0	45.9	46.8	45.5	43.5	41.5	40.0
Government Consumption	32,189	17.7	19.1	17.2	16.8	15.9	15.5	14.9

⁷ Capital Acquisitions Tax only. Capital Gains Tax is included in 12.b Current Taxes on Income, Wealth, etc', and Stamp Duty is included in 12.a Taxes on Production and Imports'.

⁸ Interest, dividends, rent, etc.

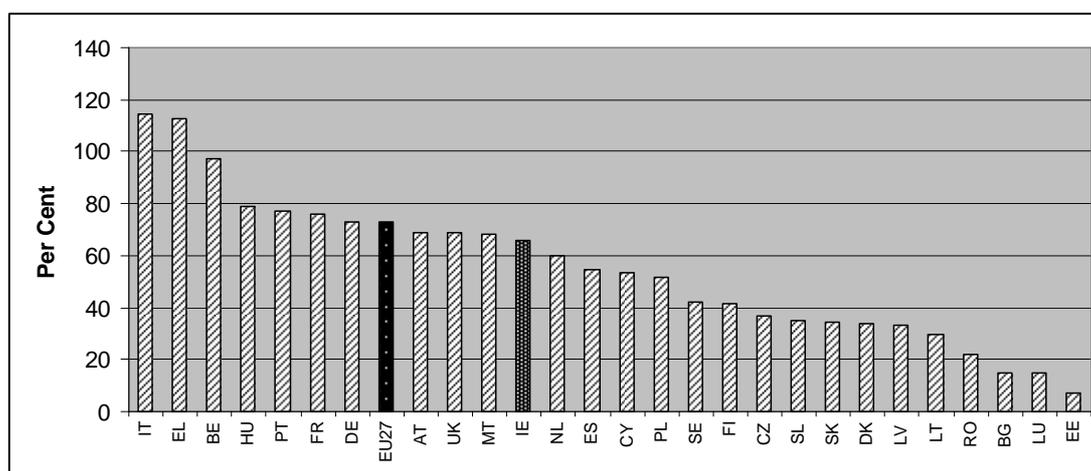
⁹ Total Taxes plus Social Contributions plus taxes paid directly to EU.

3.6 Debt Level and Developments

Ireland's debt to GDP ratio fell dramatically over the last two decades against a background of a favourable economic situation and budgets which, generally speaking, were balanced or in surplus. At end-2007, the General Government Debt stood at 25 per cent of GDP, well below the European average. Largely as a consequence of running large deficits in 2008 and 2009, this ratio has increased and is now forecast to stand at 64.5 per cent at end-2009. This ratio has however also been impacted by other factors including the decline in the value of GDP.

General Government Debt is the standard measurement of gross indebtedness used for comparative purposes within the EU. It includes the debt of the Exchequer, the extra-budgetary funds, and the non-commercial state-sponsored bodies, as well as the debt of local authorities. It does not allow the offset of liquid assets (e.g. Exchequer deposits) held at year end. During 2008 and 2009 the National Treasury Management Agency (NTMA) has maintained large cash balances to assist with liquidity management and planning the timing of bond auctions. It is estimated that these balances will stand at approximately €20 billion at end-2009. When account is taken of the value of these cash balances and the assets in the National Pensions Reserve Fund (NPRF), it is estimated that the net debt position will be 39.5 per cent of GDP at end 2009.

Figure 3 – 2009 General Government Gross Debt as % of GDP in the EU27



Source: European Commission Autumn Forecasts 2009

Table 12 below shows the evolution of the gross debt to GDP ratio over the forecasting period. The debt ratio is likely to remain within the range experienced by many other euro area sovereigns.

Table 12 – General Government Debt Developments

% of GDP	2009	2010	2011	2012	2013	2014
Gross debt¹⁰	64.5	77.9	82.9	83.9	83.3	80.8
Change in gross debt ratio	20.4	13.4	5.0	1.0	-0.6	-2.5
Contributions to change in gross debt ratio						
General Government Balance	-11.7	-11.6	-10.0	-7.2	-4.9	-2.9
Primary balance	-9.6	-8.8	-6.6	-3.4	-1.0	1.0
Interest expenditure	2.1	2.9	3.4	3.8	3.9	3.9
Stock-flow adjustment¹¹	4.1	0.3	-0.9	-0.9	-0.3	-0.6
Nominal GDP	4.6	1.5	-4.1	-5.2	-5.1	-4.8
Net Receipts of Social Security Funds	0.9	-0.2	0.6	1.0	1.5	1.5
Other factors influencing the debt ratio:						
Privatisation receipts	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Increase in local authorities' debt	0.1	0.1	0.1	0.1	0.1	0.1
p.m. implicit interest rate on debt	4.2	4.3	4.7	4.8	4.9	5.0

Note that rounding can affect totals.

The NTMA successfully raised over €5 billion of long-term borrowing in 2009, to fund the Exchequer and to refinance a €5 billion bond which fell due for repayment in April. About €5 billion of the amount raised in 2009 represents pre-funding for 2010. In 2010 the refinancing requirement will be about €1 billion. Taking into account the lower refinancing requirement and the pre-funding already achieved, the overall funding requirement in 2010 will be significantly lower than in 2009 – less than €20 billion. It is estimated that the interest costs on the National Debt will amount to €4.4 billion in 2010, €5.7 billion in 2011 and €6.6 billion in 2012.

A feature of the Irish debt market in the last eighteen months has been the higher premium that has had to be paid relative to German Government bonds. This “spread” rose sharply in the early part of 2009 as a result of a number of factors, including heightened risk aversion in the capital markets, the deterioration of the public finances in Ireland, concerns regarding the outlook for the economy and uncertainty about the cost to the Exchequer of restructuring the Irish banking sector. Over the course of the year, confidence improved following the measures introduced in the Supplementary Budget to restore stability to the public finances and the setting up of the National Asset Management Agency. In addition the NTMA undertook a number of initiatives to diversify the investor base and improve liquidity. As a result, demand for Irish debt from international investors has increased and markets have improved. The spread on Irish bonds, while still high, has narrowed considerably over recent months.

3.7 Structural Budget Balance

The most meaningful benchmark for assessing fiscal developments is, in principle, the structural budget balance, that is, the fiscal position adjusted for the economic cycle. However, unlike the headline deficit, the structural position cannot be measured directly and therefore must be estimated.

In terms of assessing Ireland’s fiscal position within EMU, the cyclical position of the economy is determined on the basis of the harmonised, production function methodology

¹⁰ The General Government debt ratio is measured on a gross basis, so liquidity held at year end will affect the gross debt. This debt ratio does not take into account the value of the funds in the NPRF or the cash balances held by the NTMA.

¹¹ Stock-flow adjustment is calculated as the change in gross debt ratio, less the GG Balance as % of GDP, less the contribution of nominal GDP growth.

developed jointly by the EU Commission and the Member States. Under this approach the first step is to determine potential output by reference to the available quantities of capital and labour together with estimates of trend total factor productivity (TFP). This enables the difference between aggregate demand and aggregate supply to be estimated. This difference – the output gap – establishes the cyclical position of the economy. The elasticity of the budget balance with respect to the economic cycle is estimated to be 0.4. (For a fuller explanation see Annex 3 of the Pre-Budget Outlook, November 2009.)

On the basis of this approach, the General Government Balance is decomposed into its cyclical and structural components in the table below, which shows that a significant part of the deficit next year is structural. If interest expenditure is excluded from the calculations, the resulting structural primary balance next year is estimated at -6.5 per cent of GDP.

In practice, all estimates of the structural position are subject to considerable uncertainty, and these uncertainties are heightened in an Irish context (difficulties in measuring the supply-side in a very open economy such as Ireland have been identified in previous Updates). Nevertheless, it is clear that erosion of the tax base and structural change within the economy (with the result that it may take a long time for unemployment to revert to pre-crisis levels), mean that a significant part of the deficit is structural and will not be eliminated with cyclical recovery.

Table 13: Cyclical Developments

		2009	2010	2011	2012	2013	2014
<i>Economic developments</i>							
GDP growth	(1)	-7.5	-1.3	3.3	4.5	4.3	4.0
Potential GDP growth	(2)	-0.6	-1.4	-0.2	1.8	2.5	3.1
- contribution of labour		-1.7	-2.3	-1.4	0.3	0.6	0.8
- contribution of capital		0.5	0.2	0.2	0.3	0.4	0.5
- contribution of TFP		0.6	0.8	1.0	1.2	1.5	1.7
Output gap	(3)	-7.0	-6.9	-3.7	-1.1	0.6	1.5
Cyclical component of headline balance	(4) = (3)*0.4	-2.8	-2.8	-1.5	-0.4	0.3	0.6
<i>Headline fiscal developments (% GDP)</i>							
Actual balance	(5)	-11.7	-11.6	-10.0	-7.2	-4.9	-2.9
Interest expenditure	(6)	2.1	2.9	3.4	3.8	3.9	3.9
One-off and temporary measures	(7)	0.4	0.6	0.0	0.0	0.0	0.0
<i>Structural fiscal developments (% GDP)</i>							
Structural balance	(8) = (5)-(4)-(7)	-9.3	-9.4	-8.5	-6.8	-5.2	-3.5
Structural primary balance	(9) = (8)+(6)	-7.2	-6.5	-5.1	-3.0	-1.3	0.4

Source: Department of Finance calculations. The structural balance excludes one-off measures.

Note that rounding can affect totals.

Chapter 4

Quality of Public Finances

4.1 Policy Strategy

The recently published Review of the Programme for Government stated that the Government's overarching objective in the short-term is to return the economy to a sustainable position. The Government's Review is based on the plan to correct the public finances as set out in the Supplementary Budget of April 2009. The Government intend to take account of the findings of the Special Group on Public Service Numbers and Expenditure Programmes and the Commission on Taxation, while creating the room for targeted spending and taxation initiatives that can be demonstrated to promote economic renewal. However, any such plans will be implemented within the agreed overall multi-annual fiscal consolidation targets.

For the 2010 Budget, the primary emphasis has been on securing lasting, structural improvements to the expenditure base, and savings of €4 billion have been secured in this context.

The Government's guiding principles to achieve economic stabilisation are:

- Correcting the public finances
- Restoring the damaged banking system
- Regaining competitiveness
- Protecting jobs and investing in retraining those who have lost jobs

The expected improvement in the economy over the medium term will not be sufficient on its own to eliminate the gap between revenue and expenditure because of the narrow tax base and the fact that the tax content of export-led growth is less than that of domestically-driven growth. In other words, a large part of the deficit is of a permanent nature. This structural imbalance between the levels of public spending and revenue will not be eliminated without discretionary, targeted action. This is why revenue-raising and expenditure-reducing measures have been necessary and why further adjustments are unavoidable in forthcoming years.

To date, adjustments have been made on both the taxation and expenditure fronts to address this issue and some of the main efforts are set out below.

4.2 Developments on the Expenditure Side

There have been a number of developments on the expenditure side of the account to improve the efficiency and sustainability of the public finances –

- Public service savings – A number of initiatives have been introduced to reduce the cost of delivering services, including the introduction of a general moratorium on recruitment and promotion in the public service and the implementation of an incentivised early retirement scheme and career break schemes for most of the public service. These measures have resulted in a significant reduction in public service staff numbers in 2009, and this is developed and built upon by the Government's new multi-annual numbers control strategy (see below).
- The public service wage bill has been reduced through the introduction in February 2009 of a pension related deduction of an average of 7 per cent from the earnings of all public servants, and in Budget 2010 through the introduction of salary reductions averaging 6 per cent across the public service with reductions of 15 per cent for those at the most senior levels. In addition long-run pension costs in the public service should fall following

implementation of the Budget 2010 announcement of a new pension scheme which will apply to all new public servants.

- Special Group on Public Service Numbers and Expenditure Programmes – In November 2008, the Government decided to set up this independent Group to examine the current expenditure programmes in each Government Department and to make recommendations for reducing public service numbers so as to ensure a return to sustainable public finances. The Group reported in July 2009 and made a series of recommendations for savings totalling €5.3 billion in a full year and entailing staff reductions of 17,300. These recommendations have been taken into consideration in formulating Budget 2010 and will be further considered in the context of future budgets. A copy of the report is available at www.finance.gov.ie
- Capital Review – A large scale capital investment programme, averaging 4¾ per cent of GNP has been in place over recent years. A review of the capital programme was carried out in advance of Budget 2010 to ensure that this investment programme focuses on the priorities that are most appropriate to the challenges we now face and which promote economic recovery. Government decisions on capital allocations for 2010 and subsequent years have been informed by this Review. It is intended to publish this Review shortly. Capital Expenditure, at an average of approximately 4 per cent of GNP over the period 2009-2014, remains at a high level and reductions in tender prices mean it is now possible to deliver capital projects more cheaply, enabling many of the goals of the National Development Plan (2007-2013) to be more readily achieved.
- Programme expenditure - There has been a comprehensive overhaul of Government spending and all areas have been reviewed. Adjustments have been made across the board such that, if unemployment related expenditure is excluded, overall Government spending has been reduced by over 10 per cent in the period 2008-2010 in net terms.
- Public Service Numbers - The Government is implementing a new, more rigorous approach to controlling public service numbers, to drive greater efficiency and productivity from the system of public administration. This will lead to significant additional savings on a multi-annual basis, making a contribution to the progressive lowering of our deficit. The new public service numbers policy draws upon the findings of the Special Group on Public Service Numbers and Expenditure Programmes, and will facilitate a progressive reduction in staff numbers across the public service by end-2012. This is to be achieved while respecting Government commitments to maintain and improve teaching resources in primary and second-level education.
- Efficiency Review of Local Authorities – The Minister for the Environment, Heritage and Local Government is initiating a special Efficiency Review in the Local Government sector, to ensure that the local authorities are providing the very best value for money possible in the delivery of the range of services critical to communities and business at local level. The review, which will complement the exercise carried out in 2009 by the Special Group (see above), should be completed by mid-2010.

4.3 Developments on the Revenue Side

Measures have also been taken on the revenue side as part of the fiscal correction process.

- Commission on Taxation – In February 2008, the Government established a Commission on Taxation to review the structure, efficiency and appropriateness of the Irish taxation system with the intention of providing a framework within which tax policy could be set for the next decade. The membership of the Commission consisted of representatives from the Social Partners - representing the business, trade union, farming and voluntary sectors - the accounting and tax advisory sectors that advise private sector business, both

small and large, and included economic expertise and people who had wide experience in central and local government. The Report was published in September 2009 and recommends that the tax base should be widened and subject to less volatility from specific elements of economic activity such as property transactions. The report constitutes an important input to taxation policy which will inform Government actions over the medium-term to long-term. A copy of the report is available at www.taxcommission.ie

- Tax Changes – The tax base has been widened and the tax yield increased, most significantly through the introduction of a Carbon Tax in Budget 2010. In addition, Budget 2009 and the April 2009 Supplementary Budget introduced an Income Levy which has a wider coverage than Income Tax, and increased Social Security-related contributions.
- The recently published Renewed Programme for Government contains a commitment for the introduction of a property tax in line with the recommendation from the Commission on Taxation. While a great deal of preliminary work is required to underpin this tax, it is envisaged that its introduction will enhance the base-broadening nature of recent fiscal policies while also providing a sustainable source of tax revenue which is not subject to fluctuations in parts of the economy.
- Further measures for possible future implementation have been identified by the Minister for Finance as part of Budget 2010;
 - Starting in mid 2011, mortgage interest relief for principal private residences will be terminated by end-2017. There will be transitional arrangements, in particular for those who purchased their homes when prices were at their peak.
 - The introduction in 2011 of a new system of two charges on income, that is, income tax and a new universal social contribution to replace the existing levies.
- Water Metering – Proposals for the introduction of water metering for domestic properties are being prepared by the Department of Environment, Heritage and Local Government, in line with the Programme for Government commitment. The charge, together with other locally raised charges, will finance the provision of local services by Local Authorities.

4.4 Institutional Features of Public Finances

The Stability and Growth Pact (SGP) provides the basis for Ireland's medium-term fiscal planning. However, over recent years Ireland has introduced a number of further measures to strengthen the medium-term budgetary framework. These have included the introduction of the multi-annual plans in the Supplementary Budget (April 2009) to restore stability to the public finances. Other developments have been outlined in previous Stability Programme Updates and have included –

- In 2008, the OECD published a review of the Irish public service, which is an important input into the public service modernisation programme.
- Unified budgeting, whereby spending and revenue decisions are announced together on Budget day.
- Annual Output Statements were introduced in 2007 to provide a link between performance and resource allocation, and have been progressively developed and improved each year.
- The introduction of multi-year capital envelopes in 2004.
- Improved appraisal and management of capital projects, public procurement and value for money requirements.
- A programme of Agency Rationalisation was initiated in Budget 2009 and will be carried forward in the light of the findings of the Special Group on Public Service Numbers and Expenditure Programmes (see section 4.2 above).

Chapter 5

Sustainability of Public Finances

5.1 Background

Ireland's public finances will come under increasing pressure in the decades ahead as the composition of the population becomes increasingly older. Ireland's age profile – currently one of the youngest in the developed world – is set to reach European norms. This extra spending pressure will manifest itself in two ways. The first is that absolute spending on pensions, health and long-term care will have to rise. Secondly, the share of the population tasked with financing it will shrink.

Projections agreed by the EU Commission and the Member States show that public pension spending in Ireland is set to double by mid-century, one of the largest increases in the EU. In October 2009 the Commission assessed the sustainability of Ireland's public finances to be at 'high risk' due to the large age-related spending pressures that lie ahead as well as the current structural budgetary position. Ensuring the stability of the public finances on a long-term basis will require additional difficult policy choices. Among other priorities, these choices must incentivise labour supply as current needs will always have to be met from current resources.

It should be borne in mind that these challenges will not materialise in full for some time yet. Thus, we have an adequate, but by no means indefinite, period in which to take action to address them.

5.2 Long-Term Budgetary Prospects including the Implications of Ageing

The latest demographic projections from the Central Statistics Office¹² and EUROSTAT¹³ indicate that the size and composition of Ireland's population will undergo considerable change in the coming decades. The number of older people will rise considerably in both absolute and relative terms. The population aged 65 and over - which currently stands at about 11 per cent - is expected to more than double. In contrast, the share of the working age population is projected to gradually fall from around 69 per cent to below 60 per cent. There are currently about six people of working age for every older person in Ireland, which is well below European norms. This ratio will change to about two to one by mid-century.

The ageing of the population will result in increases in public expenditure as a result. Projections carried out at EU level by the Economic Policy Committee and the European Commission provide an estimate of the magnitude for Ireland. The assumptions underlying these projections (see Table 14) were agreed by spring 2008, and should be viewed in light of the economic crisis that has taken place in the meantime. Nevertheless, these projections indicate that public spending on pensions, health and long-term care will increase from 12 per cent of GDP in 2007 to 16 per cent by 2035 and to 21 per cent by 2060. Potential savings from education expenditure will contribute only a small offsetting amount. In the meantime the potential growth rate of the economy is set to slow. Labour supply growth is set to fall for demographic reasons while productivity growth will also remain lower.

Pension projections undertaken at national level as part of the Green Paper on Pensions present a similar picture of rising expenditure. Over the period to 2050, the Green Paper projects that spending on social welfare and public service pensions will increase from around 5 per cent of GDP to 13 per cent¹⁴. While the assets accumulated in the National Pensions

¹² CSO (2008) *Population and Labour Force Statistics 2011– 2041* - M2F1 scenario extended out to 2050.

¹³ EUROSTAT (2008) *EUROPOP 2008*.

¹⁴ Green Paper on Pensions (chapter 3) – www.pensionsgreenpaper.ie

Reserve Fund are expected to go some way towards easing funding concerns in this respect, it is estimated that they will fall considerably short of total future liabilities.

While technical long-run projections of the type presented here are subject to appreciable margins of error, they have considerable value in demonstrating the scale and timing of the coming fiscal challenge.

Table 14 – Long-term EU Spending Projections

	2007	2035	2060
Age-related spending projections (% of GDP) (Economic Policy Committee and European Commission)			
Public service and social welfare pensions	5.3	8.0	11.3
Health and long-term care	6.6	7.9	9.7
Other age-related spending	5.4	5.0	5.1
Total age-related spending	17.2	20.9	26.1
Underlying assumptions (Economic Policy Committee and European Commission)			
(y-o-y % change)			
Labour input	2.9	0.4	0.3
Productivity	2.2	1.7	1.7
Potential GDP	5.1	2.1	2.0

Source: Economic Policy Committee and European Commission: 2009 Ageing Report, Economic and Budgetary Projections for the EU-27 Member States (2008-2060)

5.3 Sustainability Implications of Ageing

The magnitude of the fiscal challenge Ireland faces in the decades ahead is such that the European Council and the European Commission consider Ireland to be at ‘high risk’ when it comes to the long-run sustainability of our public finances. While a number of initiatives have already been taken in this respect additional policy responses will be required if we are to safeguard the public finances into the future. In this context, we have to take advantage of the comparably favourable demographic profile and implement some or all of the following options:

- Increase taxes and/or ease age-related spending pressures;
- Raise the retirement age;
- Increase the share of the population at work;
- Improve the economy’s productive capacity and competitiveness;
- Increase private savings.

Given the scale of the task it will be necessary to put in place policy measures to ensure a number of these outcomes to safeguard long-term sustainability. Due regard should be given to the impact on the wider economy of the various options and their timing.

5.4 Policy Strategy

To date a range of measures designed to take account of long-term fiscal pressures, along with the welfare needs of older members of society, have been put in place. These include:

- A public service pension-related deduction was introduced in Ireland in March 2009. It is structured as a progressive tax-relieved levy on the gross pay of pensionable public servants, excluding workers in commercial State bodies. The deduction improves fiscal sustainability as it ensures that public servants make a greater contribution to the Exchequer to take account of their high-quality final-salary

pensions and comparatively secure employment. However, the deduction does not itself qualify as a pension contribution and it confers no additional pension benefits.

- The Commission on Taxation considered the structure of the taxation system, including how best the system could encourage long-term savings to meet the needs of retirement and how it could support economic activity and promote increased employment while providing the resources necessary to meet the cost of public services and other Government outlays in the medium and longer term. The report constitutes an important input to taxation policy which will inform Government actions over the medium-term to long-term.
- Partial pre-funding of future social welfare and public service pension costs through the National Pensions Reserve Fund. The value of the Fund at end-September 2009 was in the region of 13 per cent of GDP.
- Reform of public service pension provision which has, in relation to most new public servants, allowed for the raising of the minimum pension age from 60 to 65 and for the removal of a compulsory retirement age.
- The *Fair Deal*, which puts the financing of individuals' long-term care needs on a fair and equitable basis, came into effect this year.
- The April Supplementary Budget provided for Exchequer capital investment to be over 5 per cent of GNP in 2009. This will boost the long-term productive capacity of the economy.

Budget 2010 announces additional structural reforms. These include changes to the taxation system as signalled in section 4.3 earlier, which are designed to broaden the tax base.

In relation to public service pensions, the Government proposes to introduce legislation in early 2010 to implement significant reform measures. This will provide inter alia for a new single scheme for all new entrants to the public service from 2010, raising the minimum public service pension age to 66 years and setting a maximum retirement age of 70 years. The Government will consider using the CPI as the basis for post-retirement increases for both existing and future pensioners. Details of these changes are contained in the Summary of Budget Measures published with Budget 2010.

Notwithstanding the above, it is recognised that further policy responses will be required, particularly in the area of pensions. To this end, the Government is developing the framework for longer term pensions policy as a follow up to the consultation process on the Green Paper. This will be an important step in responding to the Council's invitation to '*improve the long-term sustainability of public finances by implementing further pension reforms*'.

Chapter 6

The Excessive Deficit Procedure

6.1 Background

On 27 April 2009, the Ecofin Council issued recommendations to Ireland under the excessive deficit procedure of the Stability and Growth Pact. The recommendations principally required that the General Government balance be reduced below the reference value of -3 per cent of GDP by 2013. It also set a deadline of 27 October 2009 for initial effective action to be taken in response to the recommendation. This chapter reviews the measures which have been taken and planned on foot of the Council recommendations of 27th April 2009 and the subsequent Council Recommendation of the 2nd December 2009 which are annexed to this chapter.

In November 2009, the EU Commission reported on budgetary developments and concluded that Ireland had taken initial effective action. In accordance with the Pact, the Ecofin Council of 2 December 2009 adopted revised recommendations in the case of Ireland and a number of other Member States which acknowledge the impact on budgetary developments of adverse economic circumstances and provide for an extension of one-year to the deadline for correction of the excessive deficit - in Ireland's case to 2014.

6.2 Update regarding implementation of the recommendations:-

2009 deficit – rec. 2(a)

The deficit for 2009 increased to 11.7 per cent of GDP compared to the projection of 10¾ per cent in the April Supplementary Budget due mainly to weaker tax revenues. In its recent report on effective action the Commission acknowledged that revenue fell, significantly beyond what could be expected on the basis of standard elasticities and in spite of significant consolidation measures. (Note: the assessment of the action taken by Ireland on foot of the recommendation is available on the [Commission website](#)).

Identifying the measures necessary to achieve fiscal consolidation – rec. 2(c)

The priority is to stabilise the deficit in 2010 as a prerequisite to its progressive reduction in subsequent years. As indicated elsewhere in this Stability Programme Update, budgetary adjustments totalling €4 billion have been announced for 2010. Budget 2010 also outlines the consolidation strategy for subsequent years building on the approach set out in the April 2009 Supplementary Budget.

During 2009 the reports of Government commissioned independent expert groups on public expenditure and taxation were published. Their recommendations have informed the Government's decisions for Budget 2010 and will feed into the budgetary process for future years. These reports have been widely discussed in the media and have had an important role in enhancing understanding of the underlying public finance issues.

Implement reforms to reduce current expenditure over the coming years – rec. 2(c)

As indicated in Chapter 3, there has been a comprehensive overhaul of Government spending and all areas have been reviewed. Adjustments have been made across the board, including reductions in rates of social welfare support and in public service salaries. As a result, overall net Government spending will be reduced by over 2½ per cent in 2010, bringing the cumulative decrease in net terms since 2008 to 6½ per cent. If the costs of unemployment-related supports are excluded, the overall expenditure reduction is 4 per cent in 2010 and 10 per cent cumulatively since 2008. This compares with expenditure growth averaging over 10 per cent p.a. in the previous two years.

Reconsider public investment priorities in the light of the changed economic environment – rec. 2(c)

As announced in the Supplementary Budget, a review of the capital programme was subsequently carried out in advance of Budget 2010 to ensure that the investment programme focuses on the priorities that are most important to the challenges which we now face and which promote economic recovery. Capital expenditure, at an average of around 4 per cent of GNP over the period 2009-2014 remains at a high level and above the euro area average. Reductions in construction prices are allowing the delivery of capital projects more cheaply, thereby achieving many of the goals of the National Development Plan (2007-2013) and reducing Ireland's infrastructure deficit.

Broaden the narrow Irish tax base – rec. 2(c)

Significant revenue-raising measures were introduced in Budget 2009 and in the April 2009 Supplementary Budget. In framing Budget 2010, the view of Government was that the scope for further extensive revenue measures is limited at this time. The Report from the Commission on Taxation recommended that the tax base should be made broader and less volatile and the Government has indicated that this will be an important factor in medium-term taxation policy.

Strengthen the binding nature of the medium-term budgetary framework – rec. 3

Under the reformed Stability and Growth Pact particular importance is attached to national budgetary frameworks and fiscal rules. The Government acknowledges the importance of a robust budgetary framework in ensuring that fiscal consolidation is successful and enduring. In recent years, important reforms and innovations have been made in the budgetary process and these are reviewed in the chapter on the Quality of Public Finances.

Review of Ireland's medium-term budgetary framework and proposed reforms

As part of the Excessive Deficit procedure, the EU Commission has called upon Ireland to provide greater information on the necessary medium term actions required to reduce the deficit and in particular has expressed the view that Ireland should strengthen its budgetary process. This recommendation has also been made in recent OECD and IMF assessments.

In considering improvements, it is important to note the procedures already in place. Ireland's budgetary process is already conditioned by various rules and requirements:

Under the Stability and Growth Pact,

- There are ceilings of 3 per cent of GDP for the general government deficit and 60 per cent of GDP for gross government debt.
- Medium-term budgetary objectives for the structural balance of the public finances.

Under the Excessive Deficit Procedure,

- The Irish authorities have made commitments aimed at reducing the general government deficit below 3 per cent of GDP by 2014 – with implicit strictures on taxation and expenditure.
- The Council recommendation of 2 December 2009 calls for an average annual fiscal effort of 2 per cent of GDP over the period 2010-2014. A fiscal adjustment of 5 per cent of GDP was provided for in 2009 and Budget 2010 provides for a further fiscal adjustment of the order of 2½ per cent of GDP.
- The EU's fiscal surveillance process calls for improvements in national fiscal governance arrangements capable of improving the sustainability of public finances.
- There is an obligation to make annual improvements of 0.5 per cent of GDP towards structural balance after the excessive deficit has been corrected.

National arrangements,

- Multi-year capital envelopes were introduced in 2004.
- Additions to budgeted expenditure are met from existing allocations in the first instance.
- Since 2001, there is a statutory obligation for the payment from the Exchequer of a sum equivalent to 1 per cent of GNP per annum into the National Pensions Reserve Fund.
- The April 2009 Supplementary Budget set out the aggregate annual budgetary adjustments which would be required to reduce the deficit below 3 per cent of GDP. This process is continued in Budget 2010 on the basis of the revised deadline of 2014 agreed by the Ecofin Council on 2 December 2009.
- As indicated in the Pre-Budget Outlook, the Government shares the view widely supported internationally that fiscal consolidation must rest on expenditure control in the first instance.
- Decisions on the detailed recommendations made by the Special Group on Public Service Numbers and Expenditure Programmes will inform budgetary policy – including the Group’s recommendations on strengthened multi-annual expenditure budgeting.
- Budget 2010 states that many of the structural recommendations contained in the Report of the Commission on Taxation are likely to form part of medium-term policy instruments.

Additional measures now being considered:

- (i) Any surplus or one-off revenues which might arise in future years, in particular taxes, to be used to reduce the deficit and thereby contribute to reducing the debt burden. Any surplus revenues would be examined as to the appropriateness of including them in the base for subsequent years.
- (ii) In line with the recommendations of the Special Group on Public Service Numbers and Expenditure Programmes, the feasibility of current expenditure envelopes will be examined with a view to their future introduction.

Closely monitor adherence to budgetary targets throughout the year – rec. 3

The Department of Finance publishes monthly targets for revenue and expenditure shortly after the annual Budget. Monthly data comparing these targets against the outturn is published within two working days of the end-month. In addition, a press conference is held at the end of each quarter to report on the emerging position. These arrangements provide for assessment of the extent to which targets are being adhered to during the year. The Government regularly reports to the Dáil on fiscal developments. These monitoring arrangements are kept under ongoing review.

Improve the long-term sustainability of public finances by implementing further pension reform measures – final para. Council recommendation

The Government has had detailed analysis undertaken of the expenditure implications associated with an ageing population as published in the Green Paper on Pensions. Consideration of comprehensive pension reform is at an advanced stage as set out in the Chapter on the long-term sustainability of the public finances.

Supplementary Data**The Council recommendation – issued April 2009**

The main points of the recommendation:-

(1) On the basis of the macroeconomic outlook of the Commission services' January 2009 interim forecast, the Irish authorities should put an end to the present excessive deficit situation by 2013.

(2) The Irish authorities should bring the general government deficit below 3 per cent of GDP in a credible and sustainable manner by taking action in a medium-term framework in accordance with the path for deficit reduction as specified in the January 2009 addendum to the October 2008 stability programme on which the Council gave its opinion on 10 March 2009. Specifically, to this end, the Irish authorities should:

- (a) do the necessary to ensure that the 2009 deficit target is achieved;
- (b) stand ready to implement additional annual efforts going beyond those foreseen in the stability programme addendum in the subsequent years of the correction period in order to ensure that the annual targets are respected even if downside risks to the budgetary targets were to materialise and in so doing ensure that the rise in the debt ratio is halted;
- (c) spell out the detailed measures that are necessary to achieve this consolidation path and implement them rigorously; in particular, implement reforms to reduce current expenditure over the coming years, reconsider public investment priorities in the light of the changed economic environment, broaden the narrow Irish tax base in order to create more sustainable revenue streams and align them to reduced expenditure levels.

(3) To limit risks to the adjustment, Ireland should strengthen the binding nature of its medium-term budgetary framework as well as closely monitor adherence to the budgetary targets throughout the year.

(4) The Council establishes the deadline of 27 October 2009 for the Irish government to take effective action regarding the measures to achieve the 2009 deficit target and the specification of the necessary measures to progress towards the correction of the excessive deficit. The assessment of effective action will take into account economic developments compared to the economic outlook in the Commission services' January 2009 interim forecast.

(5) The Irish authorities should report on progress made in the implementation of these recommendations in a separate chapter in the updates of the Irish stability programme which will be prepared between 2009 and 2013.

In addition, the Council invites the Irish authorities to ensure that the budgetary consolidation towards the medium-term objective for the budgetary position – a structural balance between 0.5 and 0 per cent of GDP – is sustained after the excessive deficit has been corrected. In view of the significant projected increase in age-related expenditure and also of the increase in debt expected over the programme period (albeit from a low level) the Council also invites the Irish authorities to improve the long-term sustainability of public finances by implementing further pension reform measures in addition to pursuing fiscal consolidation.

The Council recommendation – issued 2 December 2009

The main points of the recommendation:

- (1) Recognising that Ireland's budgetary position in 2009 resulted from the interplay of the severe recession and the free play of automatic stabilisers on the one hand and significant consolidation efforts on the other (as part of which some moderate recovery measures were taken), which is an appropriate response to the European Economic Recovery Plan, the Irish authorities should put an end to the present excessive deficit situation by 2014.
- (2) The Irish authorities should bring the general government deficit below 3 % of GDP in a credible and sustainable manner by taking action in a medium-term framework. Specifically, to this end, the Irish authorities should:
 - (a) specify consolidation measures in the budget for 2010 in line with the package announced in the April 2009 supplementary budget;
 - (b) ensure an average annual fiscal effort of 2 % of GDP over the period 2010-2014, which should also contribute to bringing the government gross debt ratio back on a declining path that approaches the 60 % of GDP reference value at a satisfactory pace by restoring an adequate level of the primary surplus;
 - (c) specify the measures that are necessary to achieve the correction of the excessive deficit by 2014, cyclical conditions permitting, and accelerate the reduction of the deficit if economic or budgetary conditions turn out better than currently expected.
- (3) In addition, the Irish authorities should seize opportunities beyond the fiscal effort, including from better economic conditions, to accelerate the reduction of the gross debt ratio back towards the 60 % of GDP reference value.
- (4) To limit risks to the adjustment, Ireland should strengthen the enforceable nature of its medium-term budgetary framework as well as closely monitor adherence to the budgetary targets throughout the year.
- (5) To reduce the risks to the long-term sustainability of public finances, the Irish authorities should pursue further reforms to the social security system as soon as possible.
- (6) The Council establishes the deadline of 2 June 2010 for the Irish government to take effective action to specify consolidation measures in the budget for 2010 in line with the package announced in the April 2009 supplementary budget and to outline in some detail the consolidation strategy that will be necessary to progress towards the correction of the excessive deficit. The assessment of effective action will take into account economic developments compared to the economic outlook in the Commission services' autumn 2009 forecast.

The Irish authorities should report on progress made in the implementation of these recommendations in a separate chapter in the updates of the stability programmes which will be prepared between 2010 and 2014.

Further, the Council invites the Irish authorities to implement reforms with a view to raising potential GDP growth. This includes reforms conducive to enhancing the quality of public finances. In particular, reforms should be geared towards broadening the narrow Irish tax base and reducing current expenditure over the coming years, while reconsidering public investment priorities in the light of the changed economic environment. In addition, Ireland is invited to foster a swift adjustment to sustainable medium-term growth by productivity-enhancing measures and adequate wage policies which will help restore competitiveness.

Table 1a - Measures Announced to Improve the Budgetary Position

	Planned Budgetary Impact
<p>July 2008: Expenditure Adjustments</p> <ul style="list-style-type: none"> ▪ Savings focused on reducing the payroll bill, introducing a range of efficiency measures across Departments and Agencies and reducing expenditure on consultancy, advertising and PR. In addition there was some re-prioritisation of capital projects. 	<p>€440 million saving in 2008 €1 billion saving in 2009</p>
<p>October 2008: Budget 2009</p> <ul style="list-style-type: none"> ▪ Revenue raising package – a significant element of which was the introduction of an income levy. ▪ Strictly contained planned expenditure for 2009. Most areas of expenditure saw reductions, with the health, education and welfare areas being the main areas where spending was allowed to increase reflecting demographic and labour market pressures. 	<p>€1.95 billion yield in 2009 (€2 billion in a full year)</p>
<p>Feb 2009: Expenditure Adjustments</p> <ul style="list-style-type: none"> ▪ Most significant measure in this package was the introduction of the public sector pension-levy which has the effect of reducing the public service pay bill. ▪ Postponed next increase scheduled under the Social Partnership <i>Towards 2016</i> pay agreement. 	<p>€1.8 billion saving in 2009 (€2.1 billion in a full year) Saving of up to €1 billion in 2010 and in a full year</p>
<p>April 2009: Supplementary Budget</p> <ul style="list-style-type: none"> ▪ Revenue raising package – main features were an increase in the income levy and changes to social security (PRSI) and health levy arrangements. ▪ Adjustments to current and capital expenditure 	<p>Tax Measures: €1.8 billion in 2009 (€½ billion in a full year) Current: €886 million saving in 2009 (€1.2 billion in a full year) Capital: €76 million saving in 2009 (€600 million in a full year)</p>
<p>December 2009: Budget 2010</p> <ul style="list-style-type: none"> ▪ The 2010 Budget delivered an overall package of €4 billion. ▪ Details of the Expenditure and Taxation measures are available as part of the Budget-day supporting documentation available at www.budget.gov.ie. 	<p>Net Current Exp: €3,090 million saving in 2010 Net Capital Exp: €61 million saving in 2010 Taxation: €17 million yield in 2010</p>

Table 1b – Exchequer Taxation Receipts 2009-2012

	2009		2010		2011	2012
	Estimated		Projection	y-on-y	Projection	Projection
	Outturn	y-on-y	€n		€n	€n
	€n					
Income Tax	11,810	-10%	11,530	-2%	12,105	13,030
Value Added Tax	10,640	-21%	10,090	-5%	10,545	11,160
Corporation Tax	3,790	-25%	3,160	-17%	3,550	3,935
Excise Duties	4,575	-16%	4,514	-1%	4,740	5,025
Stamp Duties	900	-45%	975	8%	1,040	940
Capital Gains Tax	385	-73%	340	-12%	360	380
Capital Acquisitions Tax	260	-22%	240	-8%	255	270
Customs	209	-16%	200	-4%	205	210
Levies	1		1		-	-
Total	32,570	-20%	31,050	-4.7%	32,800	34,950

Note: Rounding may impact on totals

Table 1c – Explanation of net difference between Exchequer Balance and General Government Balance

	2009 Post-Budget Forecast	2010 Projection	2011 Projection	2012 Projection
	€m	€m	€m	€m
Exchequer Balance	-25,260	-18,780	-18,015	-14,850
Interest adjustments (a)	-636	-62	-14	-17
Exclude equity and loan transactions (b)	105	-136	-29	-28
Net (Borrowing)/Surplus of non-commercial State sponsored bodies	20	26	31	36
Adjustments for Transactions between the Exchequer and Government Departments/Offices and Extra-Budgetary Funds (c)	359	-355	-60	-11
Impact of the National Pensions Reserve Fund (d)	4,384	1,844	1,014	1,850
Accrual Adjustments (e)	171	117	242	250
Anglo Irish Bank	4,000			
Net (Borrowing)/Surplus of Central Government	-16,857	-17,346	-16,831	-12,770
Net Surplus of the Social Insurance Fund	-2204	-1173	0	0
Net (Borrowing)/Surplus of Local Government	-200	-200	-200	-200
General Government Balance	-19,260	-18,720	-17,030	-12,970
Net Difference between Exchequer Balance and GGB	6,000	60	985	1,880

Figures may not add due to rounding

The Exchequer Balance is the traditional domestic budgetary aggregate which measures Central Government's net surplus or borrowing position. It is the difference between total receipts into and total expenditure out of the Exchequer Account of the Central Fund.

The General Government Balance (GGB) measures the fiscal performance of all arms of Government, i.e. Central Government, Local Authorities, Health Boards (prior to 2005 - their replacement, the HSE, is part of the Exchequer), Vocational Education Committees and non-commercial State sponsored bodies, as well as funds such as the Social Insurance Fund and the National Pensions Reserve Fund which are managed by government agents. It thus provides an accurate assessment of the fiscal performance of a more complete "government" sector.

The GGB does not reflect the position of commercial State sponsored bodies as these agencies are classified as being outside the General Government Sector.

The GGB 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) This adjustment reflects the requirement, under ESA95 rules, that changes in the assets of the Capital Services Redemption Account and capital gains or losses on foreign exchange contracts, swaps, etc., should be excluded from the interest recorded for the purposes of calculating the GGB. An adjustment for interest accrued but not paid on small savings is also included, as is an adjustment for FISIM.
- b) Equity and loan transactions are excluded from the GGB on the basis that they affect the composition but not the level of assets and liabilities.
- c) Transfers between units within the General Government Sector do not affect the GGB.
- d) The National Pensions Reserve Fund (established in 2001) is within the General Government Sector and transactions within the Sector do not have an impact on the GGB. These figures include the contributions paid from the Exchequer and a provision for income earned by the funds. These figures include the pre-funding in 2009 of the 2010 contribution, the payment into the NPRF in 2009 and 2010 of the pension funds of third level universities and semi-state bodies, and also income earned on the investments made by the NPRF.
- e) This adjustment is required in respect of certain transactions recorded on an accruals basis in calculating the GGB. The main adjustments are in respect of the accrual forward to 2005 of the full projected cost of the repayment of certain nursing home charges, Value Added Tax receipts, PAYE Income Tax receipts, Departmental Balances, EU Transfers, and the impact of the capital envelopes facility, which allows a carryover of up to 10% of Departmental capital spending into the following year in accordance with Section 91 of the Finance Act 2004.

Table 1d: SUMMARY OF NET EXPENDITURE (CAPITAL AND CURRENT)

	Ministerial Vote Group	2009 Forecast Outturn ^(a)	2010 Pre- Budget Estimate	Adjustments ^(b)	2010 Post- Budget Estimate	% Change Post-Budget Estimate over Forecast Outturn
		€000	€000	€000	€000	%
	<i>Current Expenditure Allocation:</i>					
1	Agriculture, Fisheries and Food	1,039,434	985,162	-63,996	921,166	-11.4%
2	Arts, Sport and Tourism	398,979	400,699	-35,410	365,289	-8.4%
3	Communications, Energy and Natural Resources	117,167	112,967	-16,731	96,236	-17.9%
4	Community, Rural and Gaeltacht Affairs	330,103	322,743	-18,766	303,977	-7.9%
5	Defence	972,459	967,398	-80,116	887,282	-8.8%
6	Education and Science	8,046,097	8,032,775	-459,684	7,573,091	-5.9%
7	Enterprise, Trade and Employment	976,109	1,106,099	-85,420	1,020,679	4.6%
8	Environment and Local Government	847,478	893,944	-92,333	801,611	-5.4%
9	Finance Group	1,101,840	1,195,780	-96,947	1,098,833	-0.3%
10	Foreign Affairs	755,165	732,336	-27,876	704,460	-6.7%
11	Health and Children	12,285,717	11,848,060	-1,014,936	10,833,124	-11.8%
12	Justice Group	2,294,434	2,318,722	-205,426	2,113,296	-7.9%
13	Social and Family Affairs ^(c)	10,617,847	13,589,359	-778,719	12,810,640	20.7%
14	Taoiseach's (including Legal Votes)	172,952	200,178	-23,054	177,124	2.4%
15	Transport	530,724	581,087	-66,853	514,234	-3.1%
	Pay Contingency		-219,000	+219,000	-	-
	Net Voted Current Expenditure ^(d)	40,486,505	43,068,309	-2,847,267	40,221,042	-0.7%
	<i>Capital Expenditure Allocation:</i>					
	Net Voted Capital Expenditure	6,899,005	6,869,733	-960,789	5,908,944	-14.4%
	Net Voted Total Expenditure ^(d)	47,385,510	49,938,042	-3,808,056	46,129,986	-2.6%
	<i>adjustment for estimating savings since PBO ^(e)</i>			-243,003		
	Net adjustment compared to PBO			-4,051,059		

- (a) The 2009 Forecast Outturn figures are estimated figures notified by Departments and Offices. Exchequer Issues for capital include carryover savings of €125.717 million.
- (b) These adjustments include the savings per Vote Group of €67 million and savings on payroll, fees and grants / grants in aid.
- (c) 2010 figure for the Department of Social & Family Affairs includes an Exchequer subvention of €1,451.448 million to the Social Insurance Fund; no such Exchequer subvention was required in 2009.
- (d) For comparison purposes, this figure does not include Departmental balances of €18.501 million in 2009 and €30 million in 2010. Departmental balances are those amounts issued from the Exchequer Account of the Central Fund for Departmental spending in one year which remain unspent at year-end and are carried forward to be used for the next year.
- (e) The Pre-Budget Outlook was published in November 2009.

Table 1e: SUMMARY OF GROSS EXPENDITURE (CAPITAL AND CURRENT) ^(a)

	Ministerial Vote Group	2009 Forecast Outturn ^(b)	2010 Pre- Budget Estimate	Adjustments ^(c)	2010 Post- Budget Estimate	% Change Post-Budget Estimate over Forecast Outturn
		€000	€000	€000	€000	%
	<i>Current Expenditure Allocation:</i>					
1	Agriculture, Fisheries and Food	1,443,787	1,373,241	-68,032	1,305,209	-9.6%
2	Arts, Sport and Tourism	404,176	405,025	-36,348	368,677	-8.8%
3	Communications, Energy and Natural Resources	355,944	360,729	-19,411	341,318	-4.1%
4	Community, Rural and Gaeltacht Affairs	342,076	330,067	-19,194	310,873	-9.1%
5	Defence	1,013,489	1,013,728	-76,517	937,211	-7.5%
6	Education and Science	8,615,260	8,657,859	-485,048	8,172,811	-5.1%
7	Enterprise, Trade and Employment	1,424,646	1,632,911	-89,949	1,542,962	8.3%
8	Environment and Local Government	867,977	915,874	-94,287	821,587	-5.3%
9	Finance Group	1,288,905	1,379,564	-100,588	1,278,976	-0.8%
10	Foreign Affairs	795,552	773,528	-28,318	745,210	-6.3%
11	Health and Children	15,582,536	15,842,730	-1,014,350	14,828,380	-4.8%
12	Justice Group	2,516,751	2,548,955	-223,342	2,325,613	-7.6%
13	Social and Family Affairs	20,419,190	21,874,969	-776,691	21,098,278	3.3%
14	Taoiseach's (including Legal Votes)	181,965	206,888	-23,815	183,073	0.6%
15	Transport	704,520	746,988	-67,664	679,324	-3.6%
	Pay Contingency		-260,000	+260,000	-	
	Gross Voted Current Expenditure ^(d)	55,956,774	57,803,056	-2,863,554	54,939,502	-1.8%
	<i>Capital Expenditure Allocation:</i>					
	Gross Voted Capital Expenditure	7,341,614	7,350,714	-905,284	6,445,430	-12.2%
	Gross Voted Total Expenditure ^(d)	63,298,388	65,153,770	-3,768,838	61,384,932	-3.0%
	<i>adjustment for estimating savings since PBO ^(e)</i>			-296,933		
	Gross adjustment compared to PBO			-4,065,771		

(a) This table includes voted expenditure and expenditure from the National Training Fund and from the Social Insurance Fund.

(b) The 2009 Forecast Outturn figures are estimated figures notified by Departments and Offices. Exchequer Issues for capital include carryover savings of €125.717 million.

(c) These adjustments include the savings per Vote Group of €67 million and savings on payroll, fees and grants / grants in aid.

(d) For comparison purposes, this figure does not include Departmental balances of €18.501 million in 2009 and €30 million in 2010. Departmental balances are those amounts issued from the Exchequer Account of the Central Fund for Departmental spending in one year which remain unspent at year-end and are carried forward to be used for the next year.

(e) The Pre-Budget Outlook was published in November 2009.

Table 1f: SUMMARY OF CAPITAL EXPENDITURE 2010

	Ministerial Vote Group	2009 Forecast Outturn ^(a)	2010 Post- Budget Estimate	% Change Post-Budget Estimate over Forecast Outturn
		€000	€000	%
1	Agriculture, Fisheries and Food	546,079	429,979	-21.3%
2	Arts, Sport and Tourism	135,491	132,342	-2.3%
3	Communications, Energy and Natural Resources	118,002	176,200	49.3%
4	Community, Rural and Gaeltacht Affairs	120,719	105,000	-13.0%
5	Defence	17,494	15,609	-10.8%
6	Education and Science	846,905	715,428	-15.5%
7	Enterprise, Trade and Employment	488,391	473,995	-2.9%
8	Environment and Local Government	1,807,257	1,506,103	-16.7%
9	Finance Group	209,546	164,067	-21.7%
10	Foreign Affairs	12,106	9,782	-19.2%
11	Health and Children	511,622	483,842	-5.4%
12	Justice Group	116,150	122,558	5.5%
13	Social and Family Affairs	13,808	10,202	-26.1%
14	Taoiseach's (including Legal Votes)	-	-	-
15	Transport	2,398,044	2,100,323	-12.4%
	Gross Voted Capital Expenditure	7,341,614	6,445,430	-12.2%
<i>Less</i>	<i>Appropriations-in-Aid</i>	442,609	536,486	-
	Net Voted Capital Expenditure	6,899,005	5,908,944	-14.4%

(a) The 2009 Forecast Outturn figures are estimated figures notified by Departments and Offices. Exchequer Issues for capital include carryover savings of €125.717 million.

Table 1g: Voted Expenditure Projections 2011 and 2012

Ministerial Vote Group		2011	2012
		€000s	€000s
<i>Current Expenditure Allocations:^(a)</i>			
1	Agriculture, Fisheries and Food	1,352,503	1,344,403
2	Arts, Sport and Tourism	365,693	363,366
3	Communications, Energy and Natural Resources	336,402	335,285
4	Community, Rural and Gaeltacht Affairs	310,310	309,600
5	Defence	927,034	927,681
6	Education and Science	8,196,958	8,303,306
7	Enterprise, Trade and Employment ^(b)	1,381,596	1,373,469
8	Environment and Local Government	819,055	817,250
9	Finance Group	1,281,283	1,305,635
10	Foreign Affairs	778,177	818,377
11	Health and Children	14,849,052	14,847,942
12	Justice Group	2,346,331	2,347,762
13	Social and Family Affairs ^(b)	21,307,811	20,879,068
14	Taoiseach's Group	213,604	177,297
15	Transport	717,280	703,375
	Gross Voted Current Expenditure	55,183,089	54,853,816
<i>less</i>	Appropriations-in-Aid	13,828,503	14,365,610
	Net Voted Current Expenditure	41,354,586	40,488,206
<i>Capital Expenditure Allocations:</i>			
	Gross Voted Capital Expenditure	5,500,000	5,500,000
<i>less</i>	Appropriations-in-Aid	475,955	473,955
	Net Voted Capital Expenditure	5,024,045	5,026,045

(a) These allocations also include further reductions resulting from anticipated Public Service numbers reductions in 2011 and 2012.

(b) Including expenditure from the Social Insurance Fund and the National Training Fund.

Table 1h: National Accounts Classification of General Government

	2008	2009 Estimated Outturn	2010 Forecast
SUMMARY	€m	€m	€m
RECEIPTS			
1. Current (15)	56,440	50,153	50,092
2. Capital (29)	3,641	2,724	2,775
3. Total Receipts (1+2)	60,081	52,877	52,866
EXPENDITURE			
4. Current (21)	60,040	63,193	63,474
5. Capital (37)	13,078	8,944	8,113
6. Total Expenditure (4+5)	73,118	72,137	71,587
7. Net Lending (+)/Borrowing (-) [3-6=40]	-13,037	-19,260	-18,720
CURRENT ACCOUNT			
RECEIPTS			
8. Taxes on income and wealth	19,136	16,364	15,428
9. Social insurance and health contributions	9,288	9,282	9,477
10. Taxes on expenditure (including rates)	22,149	18,155	17,669
11. Total taxation (excluding taxes on capital)	50,573	43,801	42,575
12. Gross trading, rental and investment income	2,426	2,540	3,040
13. Current transfers from the rest of the world	121	119	191
14. Miscellaneous Receipts	3,320	3,694	4,286
15. Total receipts on Current Account	56,440	50,153	50,092
EXPENDITURE			
16. Subsidies:	843	894	1,010
17. National debt interest	1,879	3,402	4,609
18. Current transfer payments:			
to residents	24,360	26,529	28,664
to the rest of the world	2,252	2,128	2,078
19. Current expenditure on goods and services (excluding depreciation)	25,144	25,037	22,490
20. Current expenditure on goods and services by local government	5,563	5,202	4,623
21. Total expenditure on Current Account	60,040	63,193	63,474
22. Gross Saving (+)/Deficit(-) [15-21]	-3,600	-13,040	-13,382
CAPITAL ACCOUNT			
RECEIPTS			
23. Taxes on capital	1,755	645	580
24. Loan repayments and equity sales	856	806	1,001
25. Capital transfers from the rest of the world	24	104	181
26. Other Capital receipts	1,863	1,974	2,014
27. Borrowing	14,020	20,398	19,668
28. Total receipts on Capital Account	18,518	23,927	23,443
29. Capital receipts less Financial Transactions [24. 27.]	3,641	2,724	2,775
EXPENDITURE			
30. Grants to enterprises	1,934	551	723
31. Other transfer payments	1,295	479	83
32. Debt Redemption	521	606	647
33. Loans and purchase of share capital	1,318	1,349	1,309
34. Gross fixed capital formation	9,814	7,884	7,259
35. Capital payments to ROW	35	30	48
36. Total expenditure on Capital Account	14,917	10,899	10,069
37. Capital expenditure less Financial Transactions [32. 33.]	13,078	8,944	8,113
38. Current Saving (+)/Deficit (-) [22]	-3,600	-13,040	-13,382
39. Capital Saving (+)/Deficit (-) [29-37]	-9,436	-6,220	-5,338
40. Net Lending (+)/Borrowing (-) [38+39]	-13,037	-19,260	-18,720

Explanatory Notes

1. Table 1h brings together estimates of the consolidated capital and current accounts of General Government which includes the Exchequer, various extra-budgetary funds (e.g. the Social Insurance Fund), various non-commercial semi-state bodies, the Local Authorities and the Vocational Education Committees, classified according to the definitions employed in national income accounting. The main purpose of the presentation is to provide a basis for relating the income and expenditure of General Government to such national income aggregates as saving, investment and personal income, whereas many other budgetary documents cannot be readily used in this way. The presentation thus gives a more comprehensive view of fiscal policy than would be possible on the basis of the budgetary accounts alone.
2. The figures shown for 2008 are based on published information. Figures for 2009 are provisional and are subject to revision when the Appropriation Accounts and other final accounts become available. The estimates shown for 2010 are consistent with the Budget Day projections.
3. Transactions between the various funds and accounts are eliminated so as to show the net flows between the General Government sector and the rest of the economy. Current transactions of government trading activities are omitted, but estimates of the gross surplus on these activities are included in item 12.
4. The various definitions employed are similar to those used in Table 21 of the *National Income and Expenditure* accounts published by the Central Statistics Office. It should be noted that there are some differences in presentation between Table 21 as published in the *National Income and Expenditure* and Table 1h as some of the headings used in Table 21 have been amalgamated. Additionally, items 29 (Capital receipts less Financial Transactions) and 37 (Capital expenditure less Financial Transactions) are included to facilitate the calculation of a Net Lending / Net Borrowing figure (also known as the General Government Balance (GGB)).
5. The GGB is calculated according to standardised European statistical accounting rules, the European System of Accounts 1995 (ESA95).
6. It should be noted that the GGB (item 40) varies from the Exchequer Balance shown in the Exchequer Budgetary accounts. Table 1c sets out an explanation of the differences.

Additional tables as set out in the code of conduct for stability programmes**Table 2a – Macroeconomic Prospects**

	2008	2009	2010	2011	2012	2013	2014
	€ <i>million</i>	% <i>change</i>	% <i>change</i>	% <i>change</i>	% <i>change</i>	% <i>change</i>	% <i>change</i>
Real GNP	156,760	-10.4	-1.7	3.0	4.1	3.9	3.6
Nominal GNP	154,598	-13.9	-3.1	4.9	6.2	5.9	5.5
Real GDP	183,991	-7.5	-1.3	3.3	4.5	4.3	4.0
Nominal GDP	181,816	-9.5	-2.2	5.6	6.7	6.5	6.1
Components of real GDP							
Personal consumption	91,055	-7.2	-3.0	2.6	3.4	3.3	3.2
Government consumption	27,991	-0.6	-3.0	-0.5	-0.5	-0.5	-0.5
Investment	41,766	-33.9	-19.2	4.5	7.8	8.5	7.8
Exports of goods and services	151,875	-2.7	0.4	3.4	4.0	3.8	3.5
Imports of goods and services	131,266	-9.0	-2.8	2.6	2.9	3.0	2.8
Contribution to real GDP growth							
Final domestic demand		-11.1	-4.8	1.8	2.7	2.7	2.6
Changes in stocks		-0.7	0.8	0.2	0.0	0.0	0.0
External trade balance		4.3	2.4	1.3	1.7	1.5	1.3

* Figures subject to rounding.

Source: CSO (2008), Department of Finance (2009 – 2014)

Table 2b – Price Developments

	2009	2010	2011	2012	2013	2014
	<i>% change</i>					
GDP deflator	-2.2	-1.0	2.2	2.1	2.1	2.0
Private consumption deflator	-2.1	-0.8	1.6	1.8	2.0	1.9
HICP	-1.7	-1.2	1.0	1.7	1.8	1.8
Export price deflator	1.9	0.8	2.0	1.7	1.6	1.5
Import price deflator	1.3	0.5	0.7	1.0	1.1	1.1

Source: Department of Finance (2009 – 2014)

Table 2c – Labour Market Developments

	2008	2009	2010	2011	2012	2013	2014
	(000)	%	%	%	%	%	%
Employment, persons	2,100	-7.8	-3.4	1.0	2.3	2.5	2.3
Unemployment rate (%)	6.3	11.8	13.2	12.6	11.8	10.8	9.5
Labour Productivity, per employee (GDP)		0.4	2.3	2.3	2.1	1.7	1.7

Source: CSO (2008), Department of Finance (2009 – 2014)

Table 2d – Sectoral Balances

	2009	2010	2011	2012	2013	2014
	%	%	%	%	%	%
Net lending vis-à-vis rest of world	-2.0	0.6	1.2	1.6	1.6	1.3
Net lending of public sector	-11.7	-11.6	-10.0	-7.2	-4.9	-2.9

Source: Department of Finance