An Roinn Airgeadais
Department of Finance

The Irish economy
- cyclical and structural developments

Presentation to Global Government Finance Summit

John McCarthy

Dublin, 6th June 2024

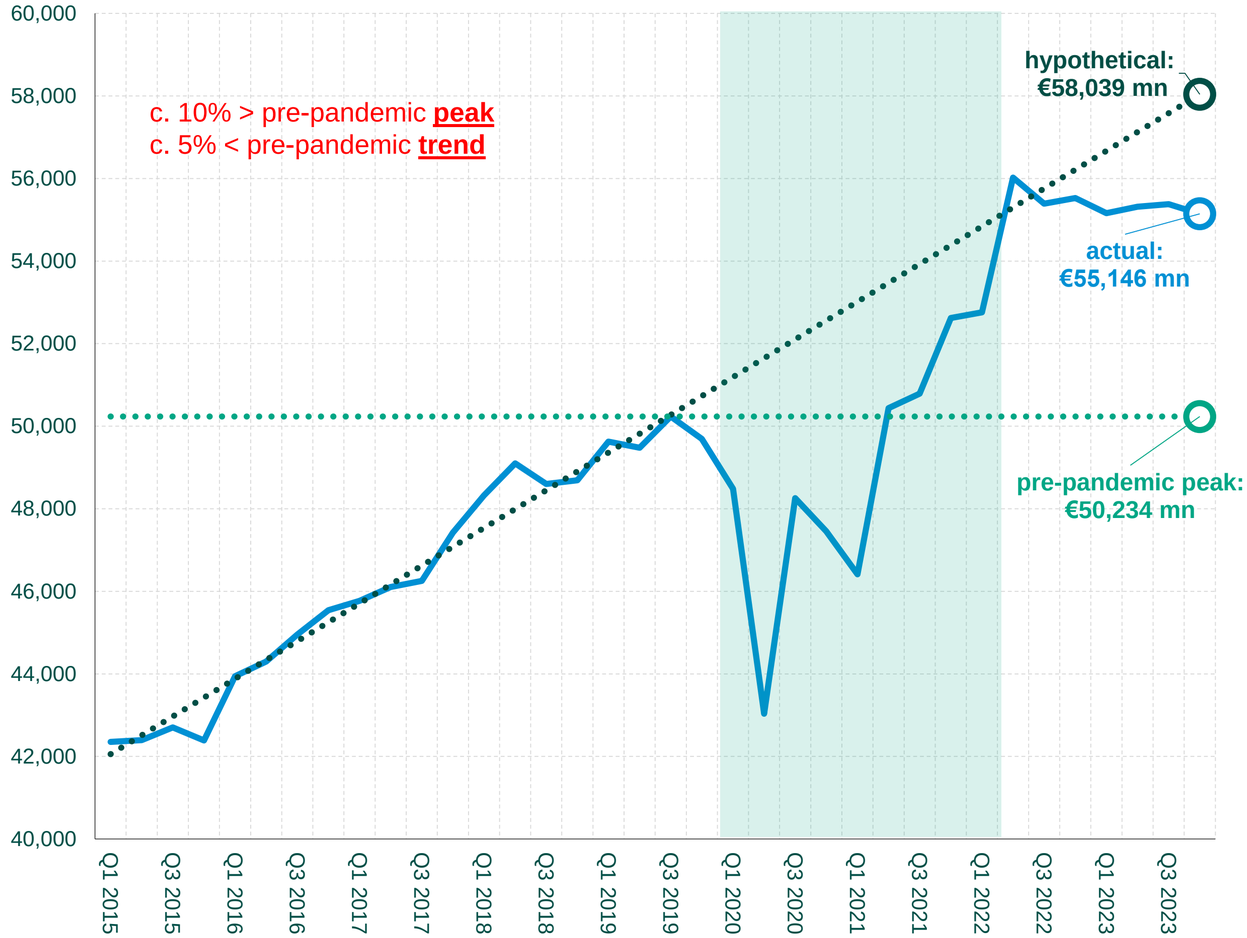
Setting the scene

- Irish economy – short-term cyclical developments
- Horizon scanning – structural changes (the “4Ds”)
  - Demographic headwinds
  - Decarbonisation – role and impact on the economy / public finances
  - Digitisation – headwind or tailwind ?
  - De-globalisation ?
- Conclusion

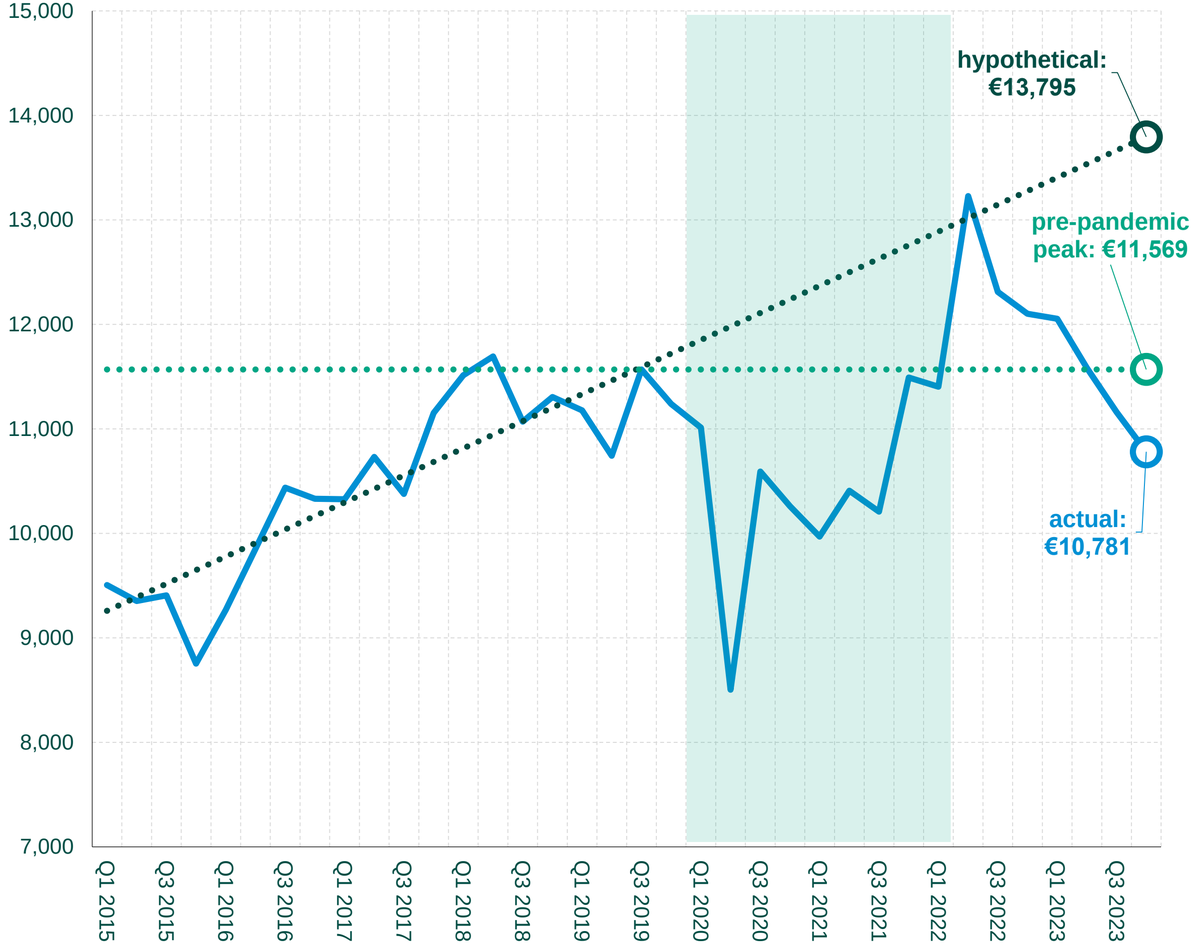
Irish economy: short-term cyclical developments

Signalling properties of GDP are limited in Ireland – use MDD

MDD: rapid rebound but flat-lined…

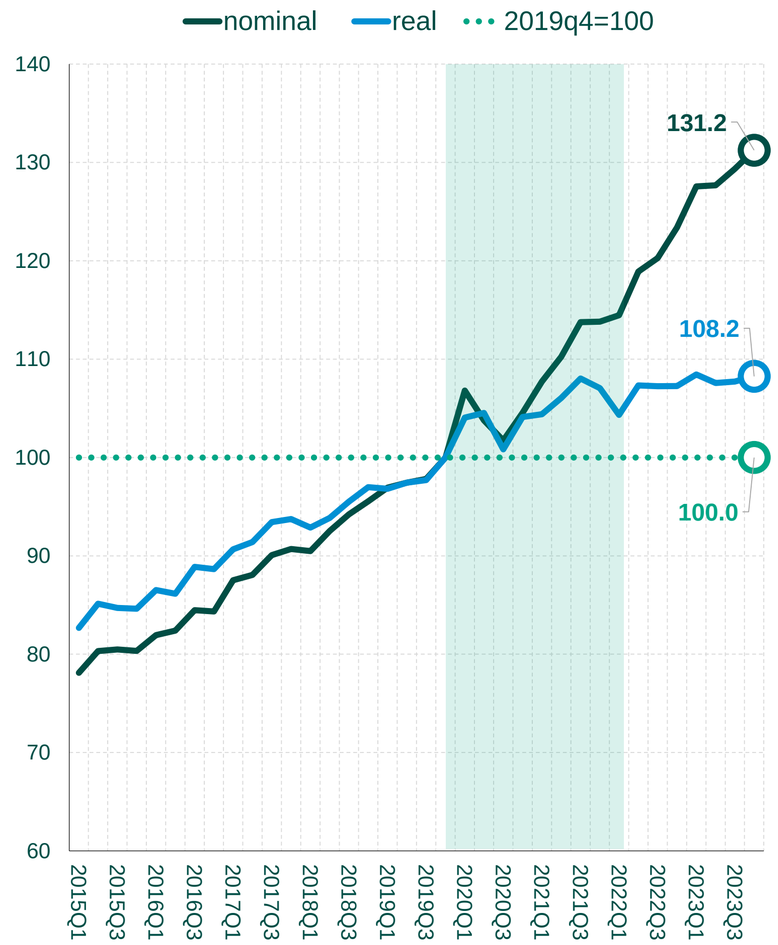


…partly due to weaker investment spending

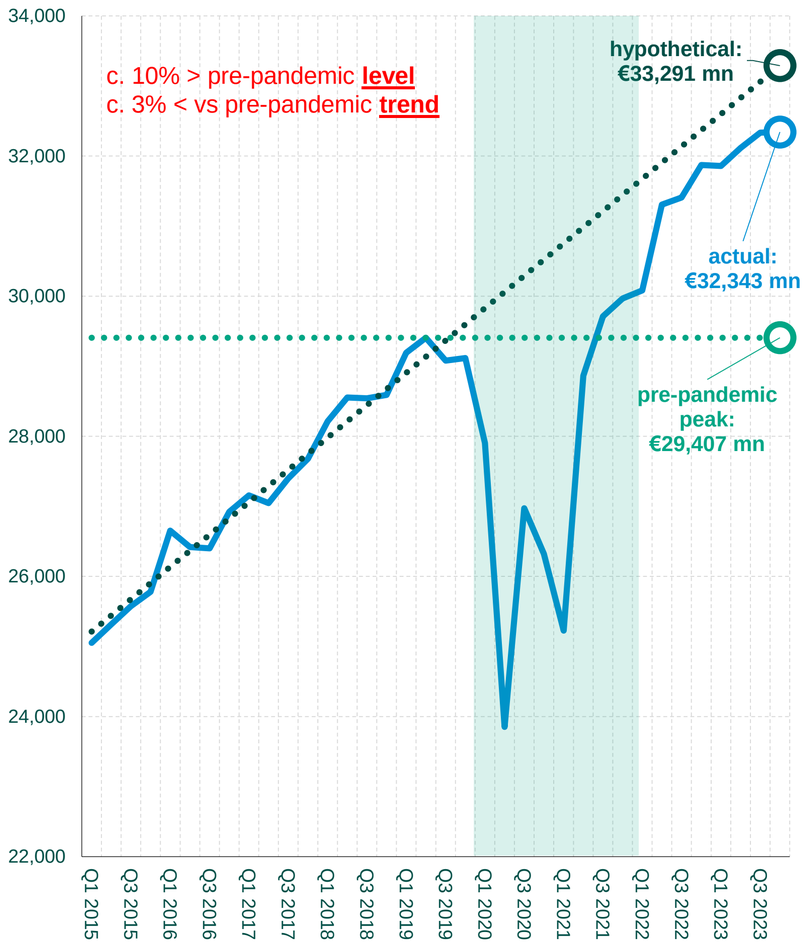


Overlapping price shocks – erosion of real incomes

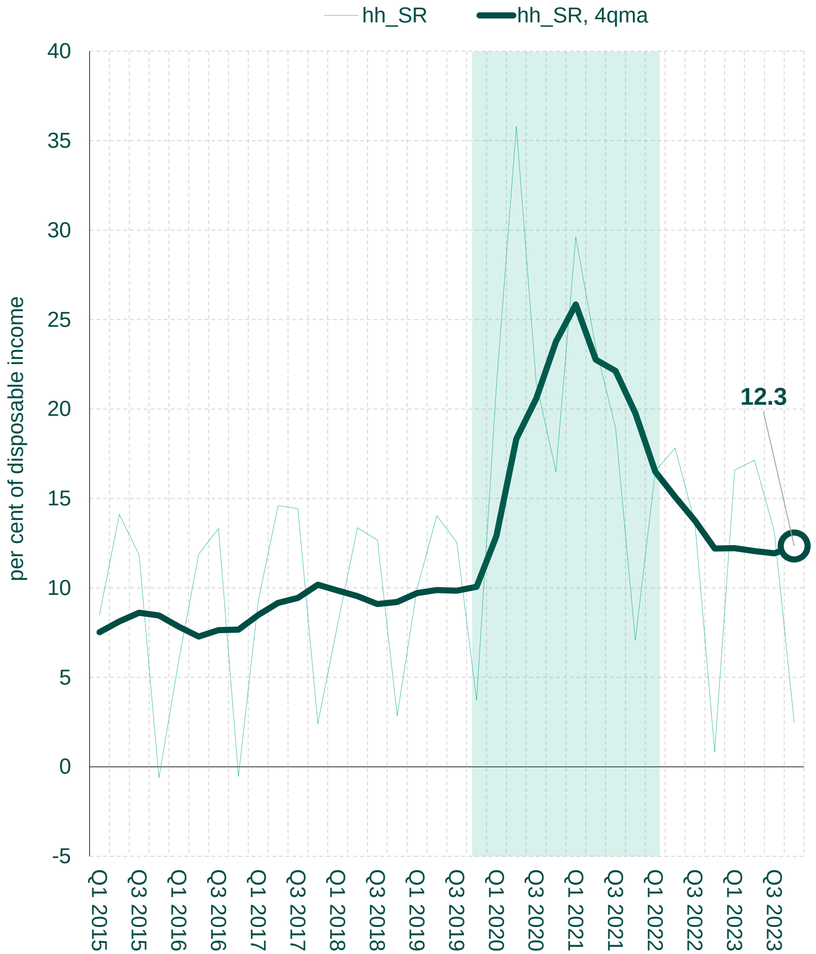
HH disposable income, 2019q4 = 100



Consumer spending

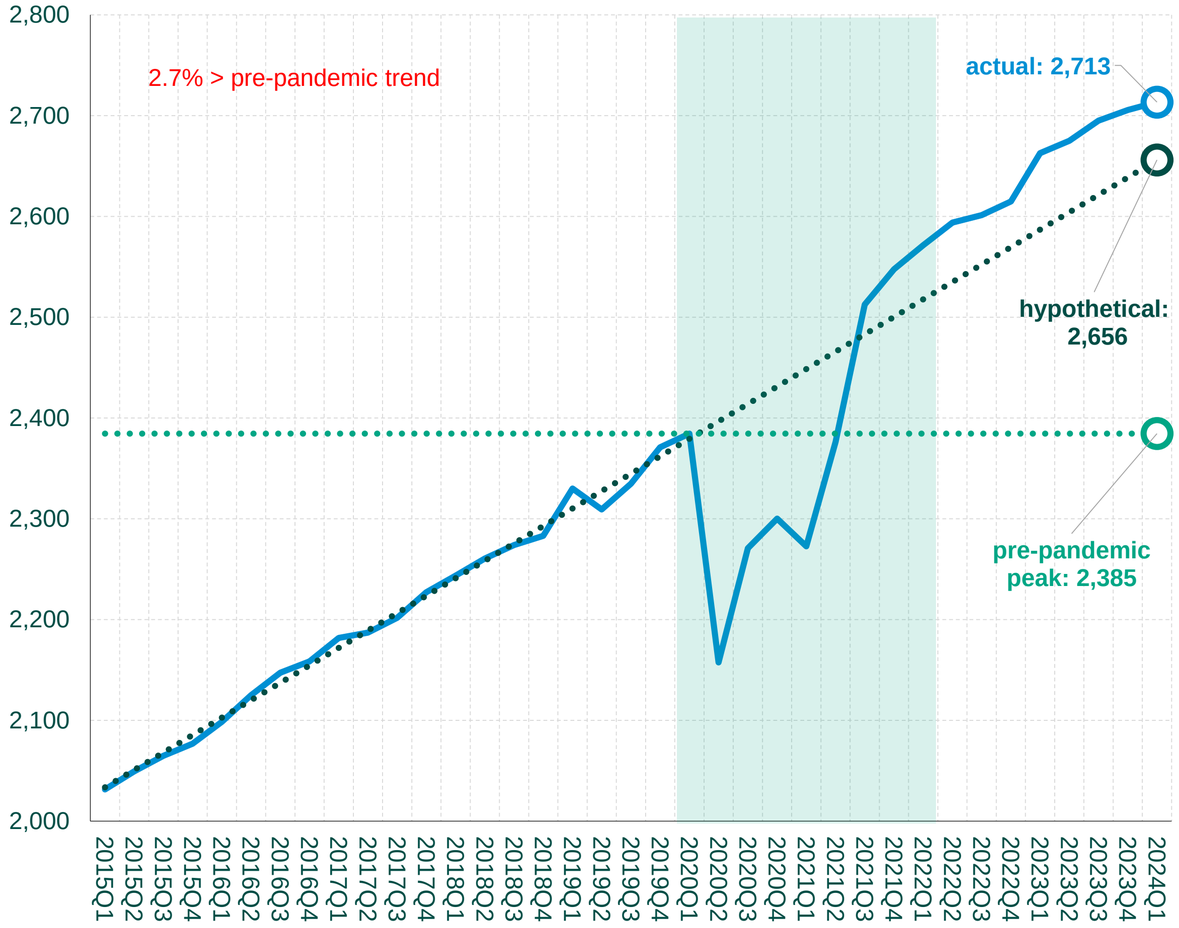


Re-normalisation of HH savings rate

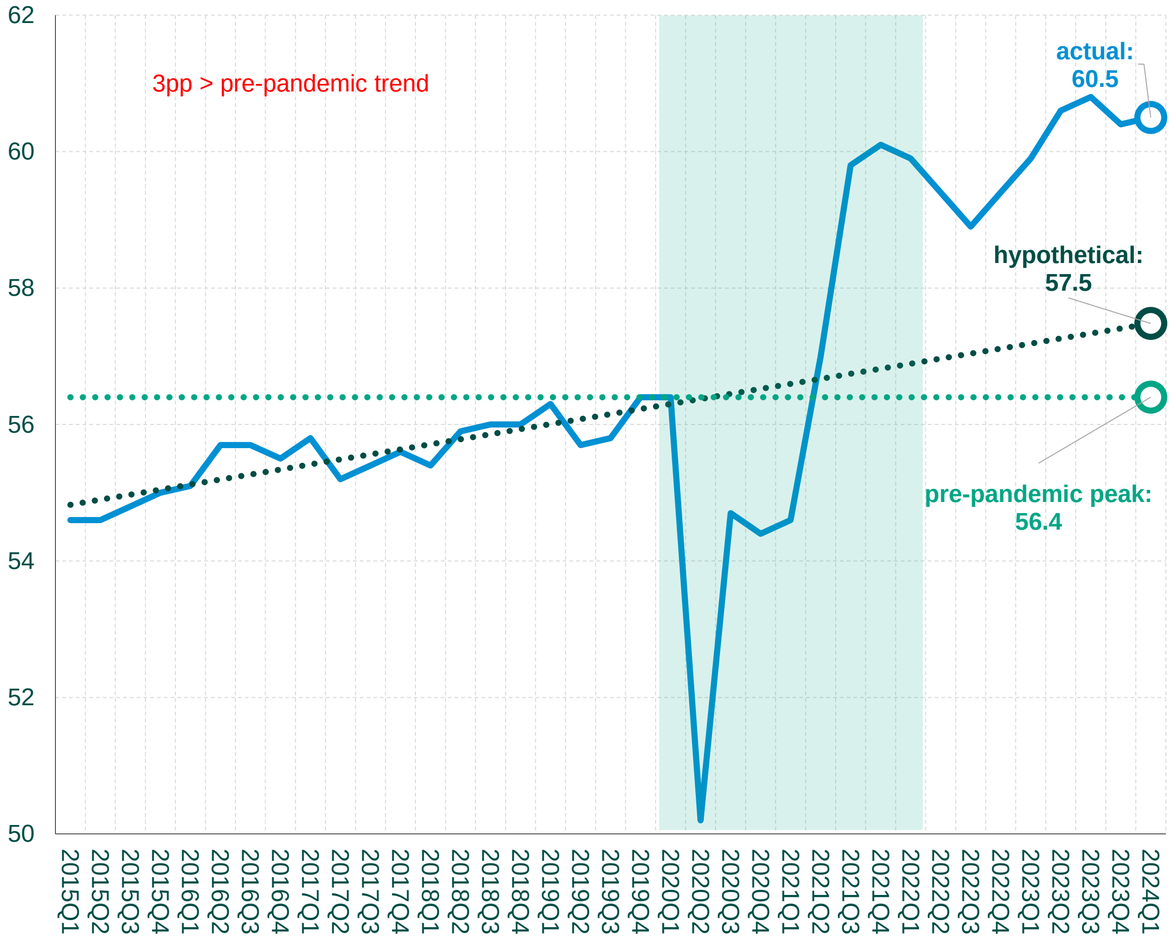


Employment v. strong – supported by positive supply-side developments

1-7 currently employed were not so on eve of pandemic

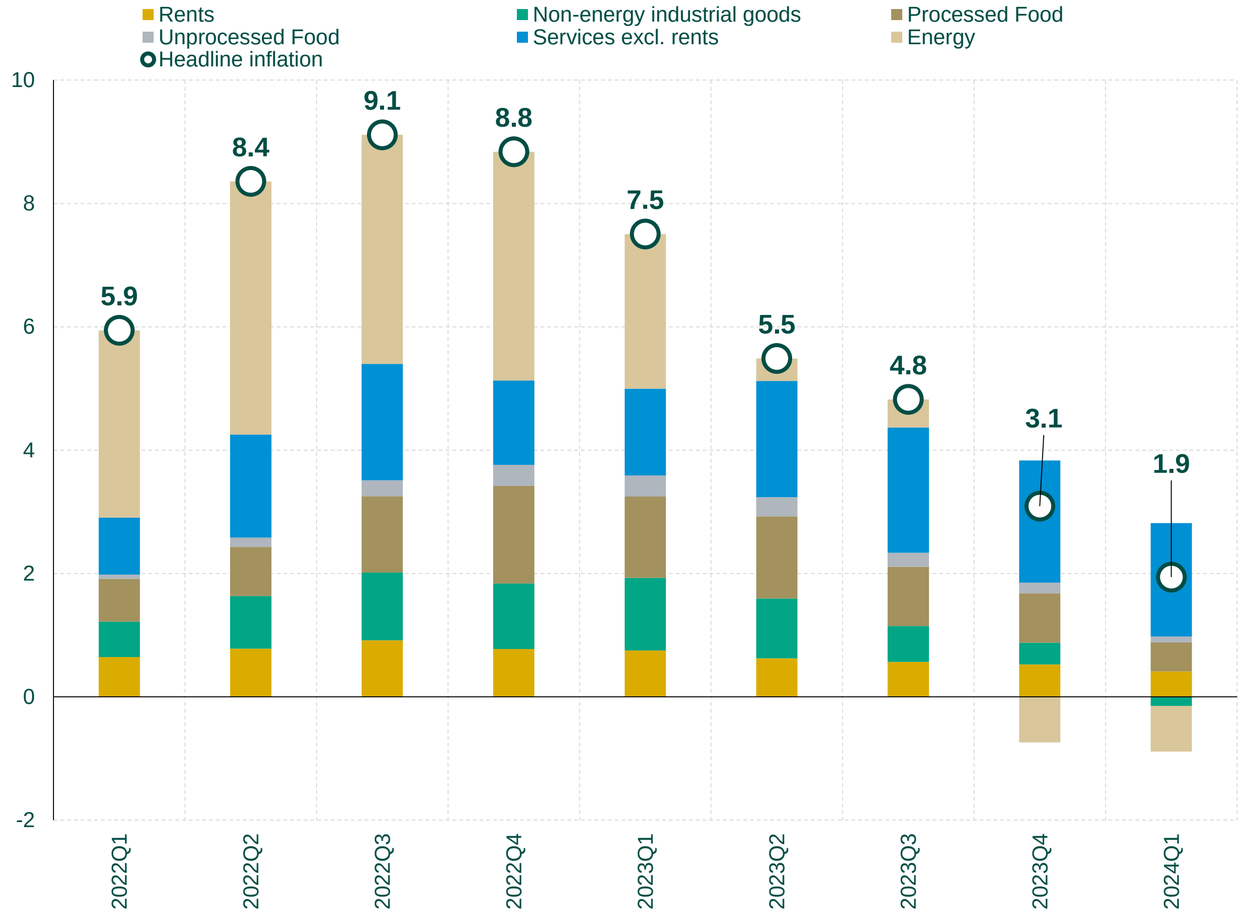


Female participation rates, per cent, s.a.

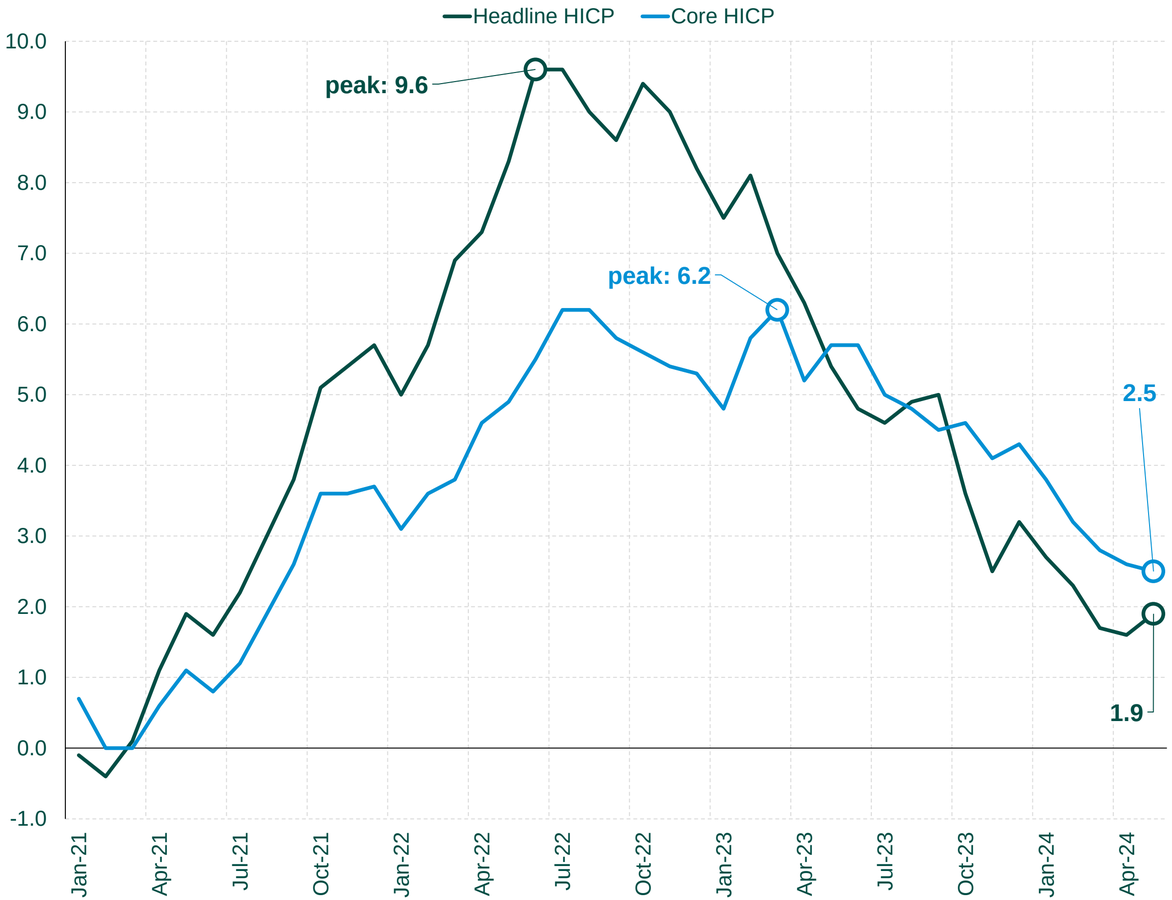


Price dynamics – last mile a problem ?

‘First-round’ effects from energy price shock are unwinding

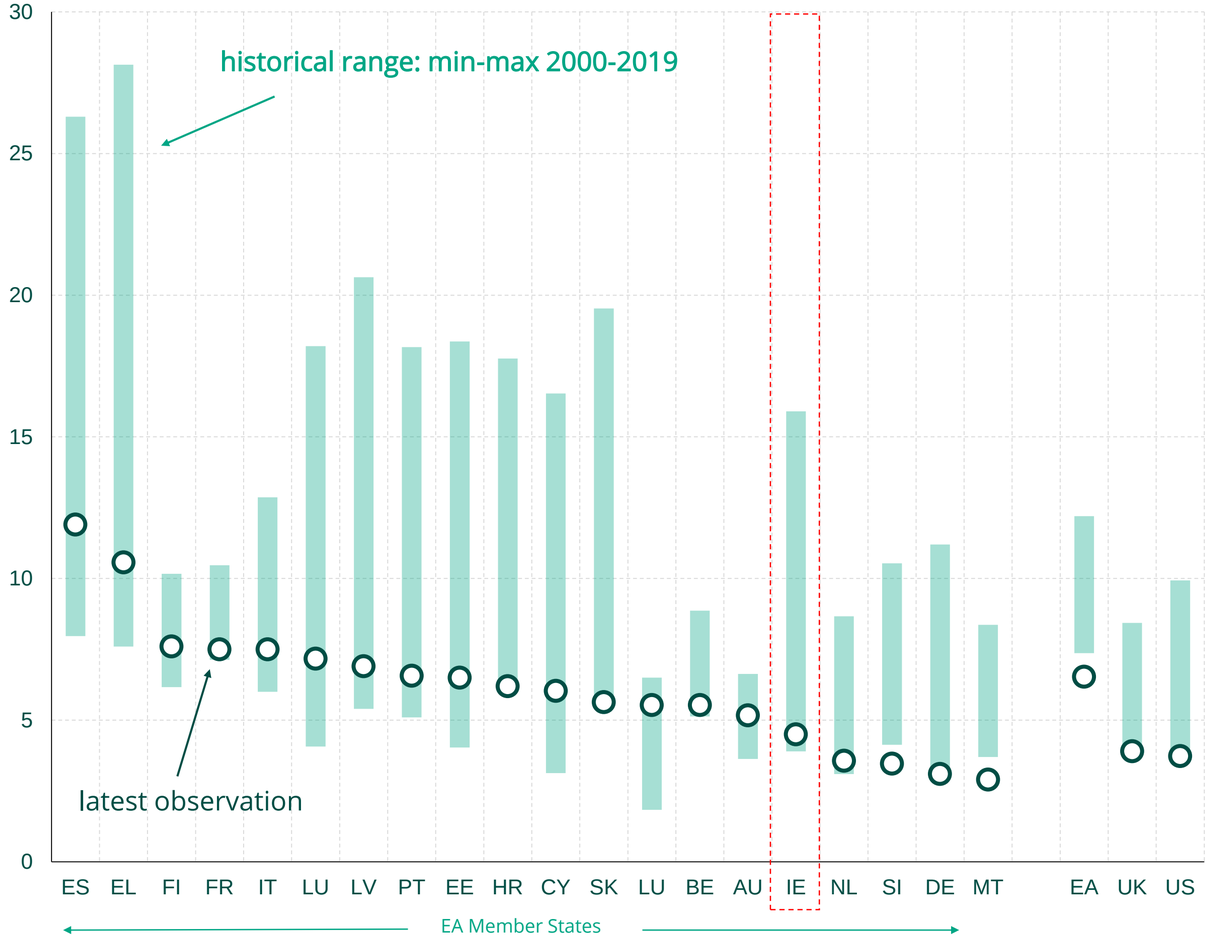


Reducing (not eliminating) risk of ‘second-round’ effects

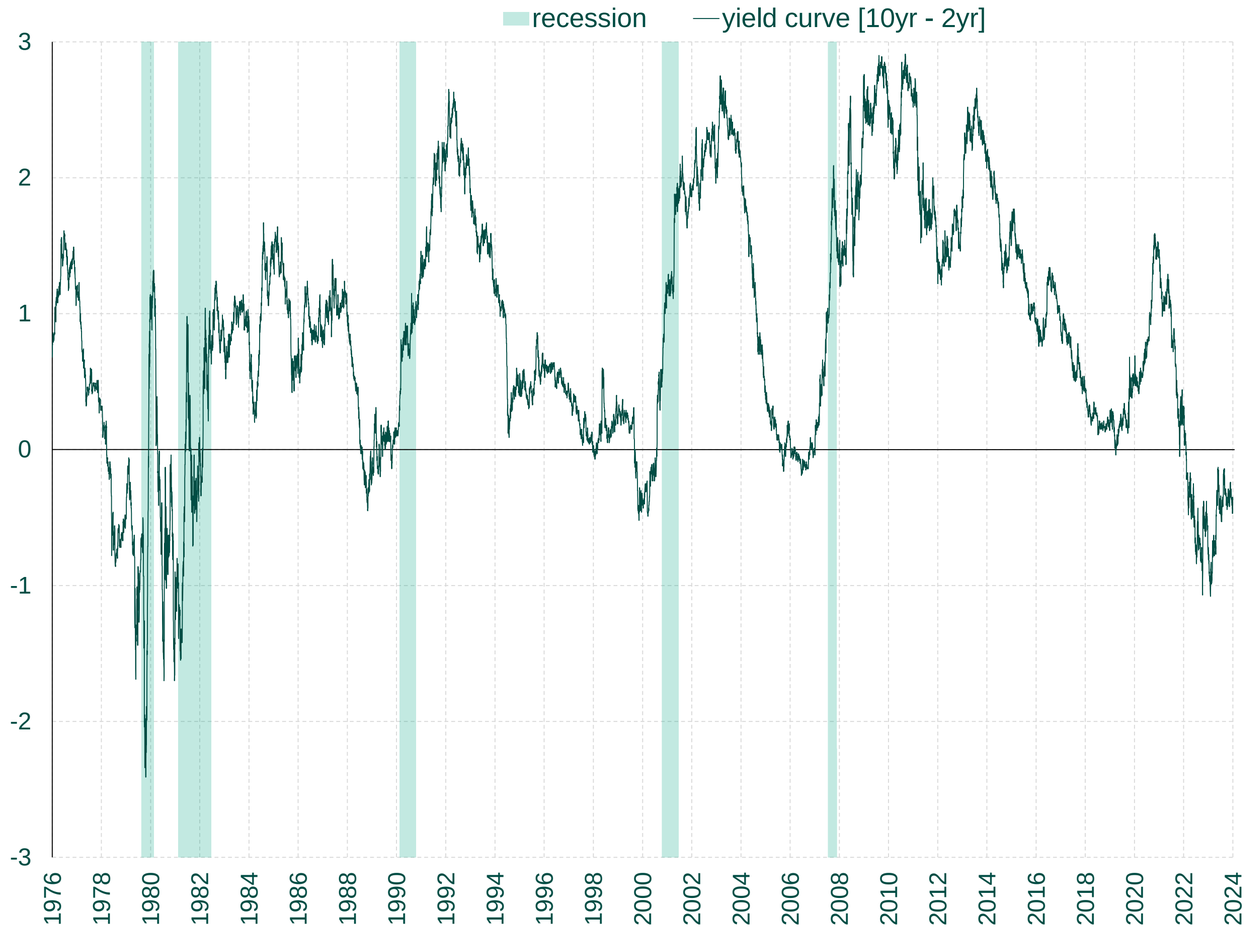


Some dynamics that are out-of-kilter with economic theory and practice…

Economic costs of aggressive monetary tightening = limited



Signalling power of the (US) yield curve

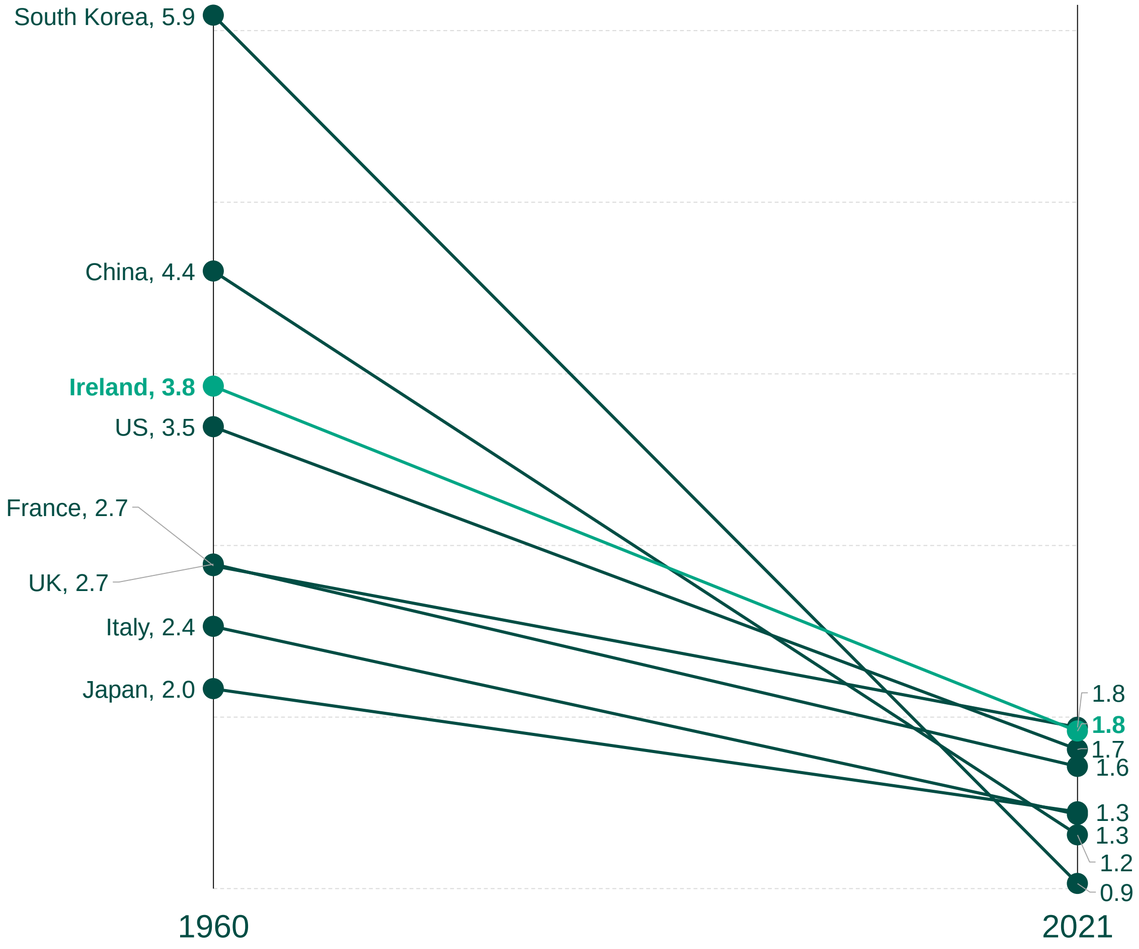


Horizon scanning – structural change (the “4Ds”)

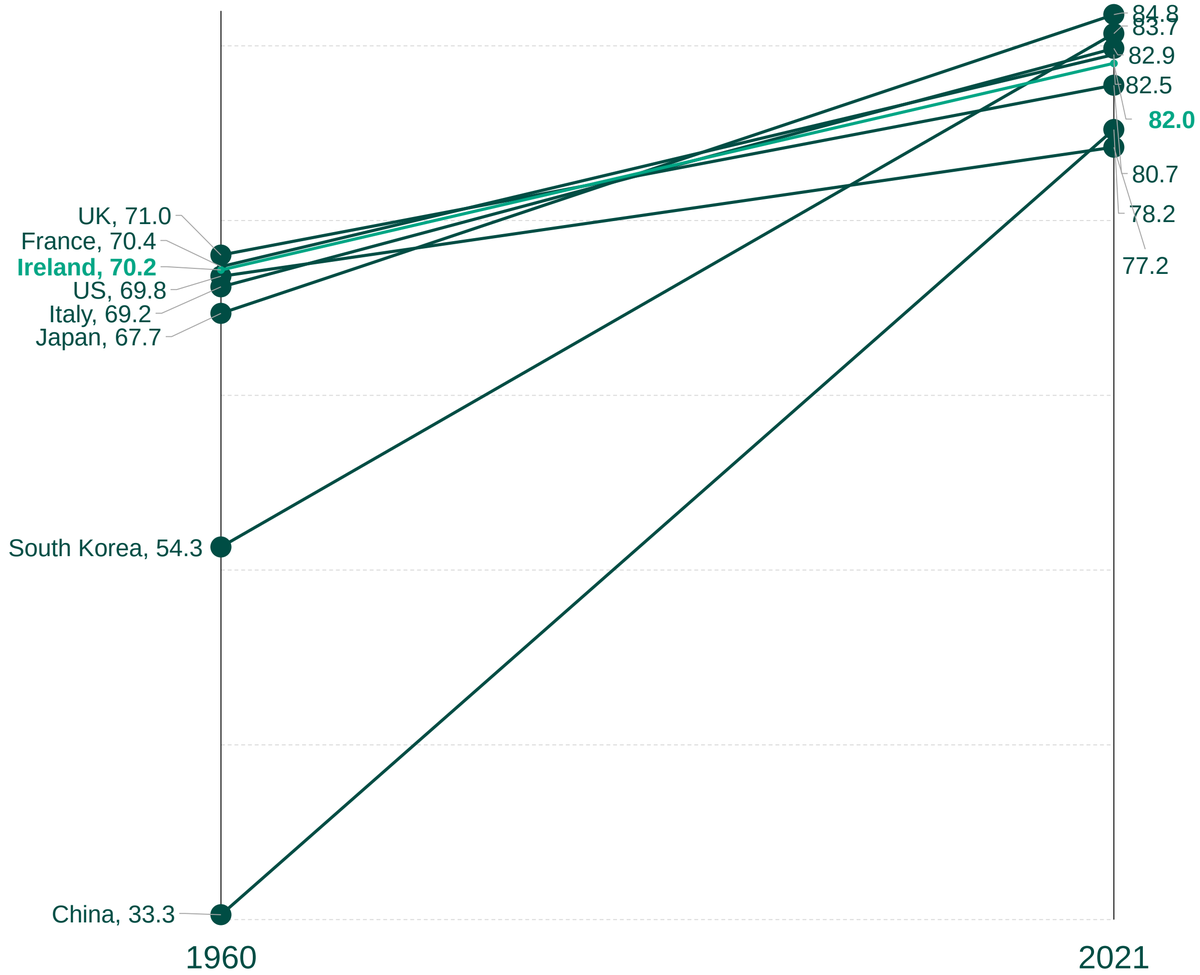
Structural trend #1: Demographic change

Demographic tipping points on the horizon

Fertility rates below population replacement rates…



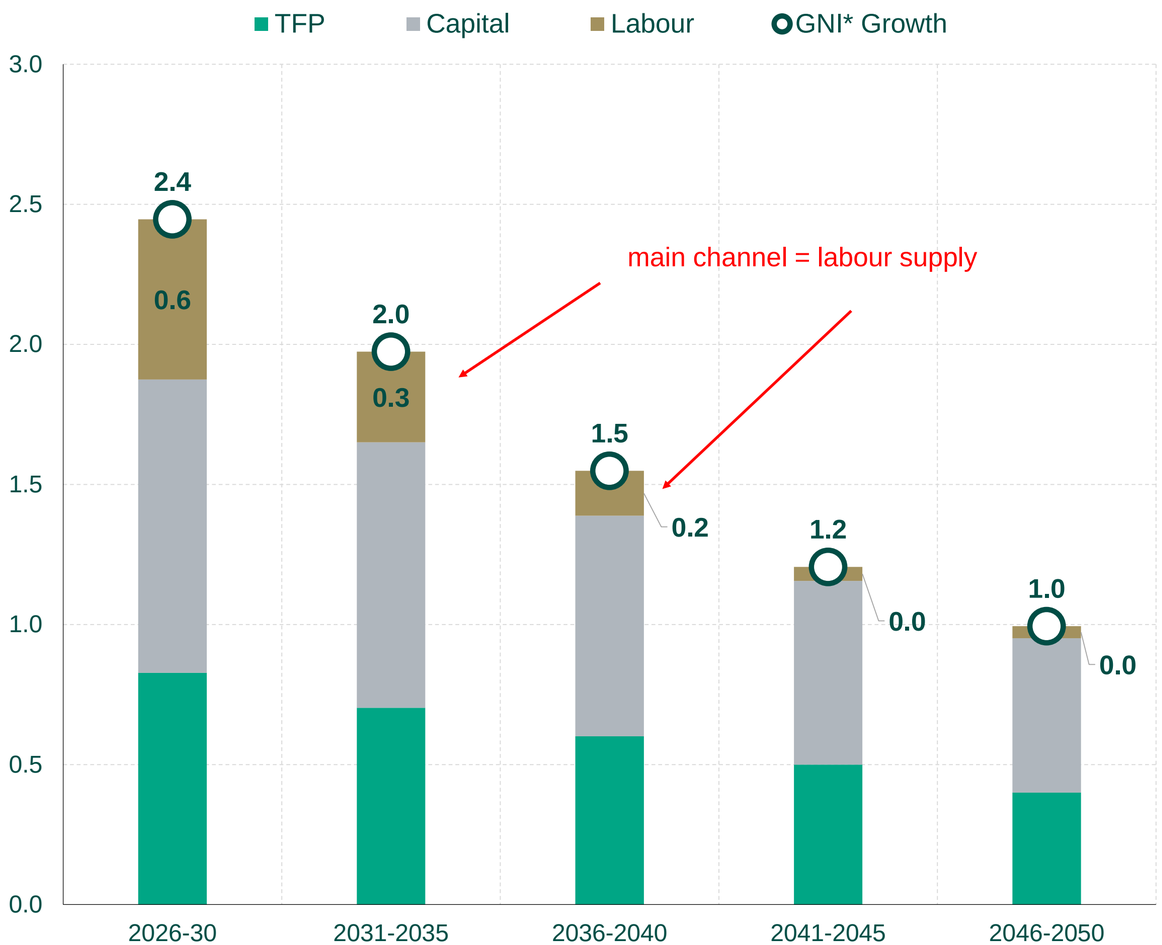
…while life-expectancy (at birth) has increased



Irish population structure is changing…with economic implications

Ireland's population pyramid set to invert…

...slowing the trend growth rate of the economy

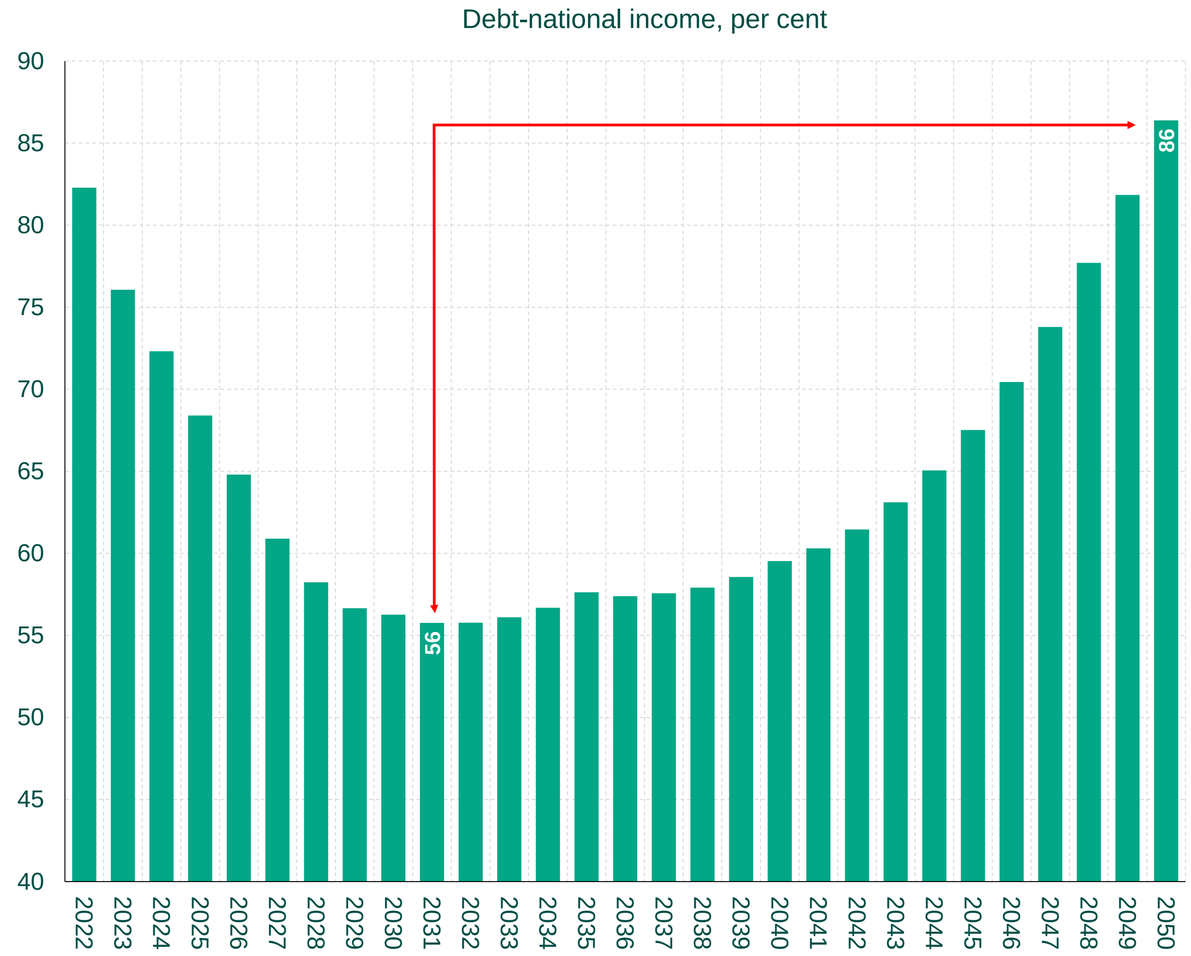


Unchanged policies involve large fiscal costs

With major fiscal costs…

Annual age-related expenditure projections 2022-2050, per cent of GNI*				
	2022	**2030**	**2050**	**Δ 2050-22**
Pension costs	7.0	7.6	11.0	**4.0**
Health Care	7.6	8.0	9.3	**1.7**
Long-term care	2.3	2.5	3.6	**1.3**
Education	5.2	4.5	4.2	**-1.0**
Total age-related	**22.0**	**22.7**	**28.0**	**6.0**

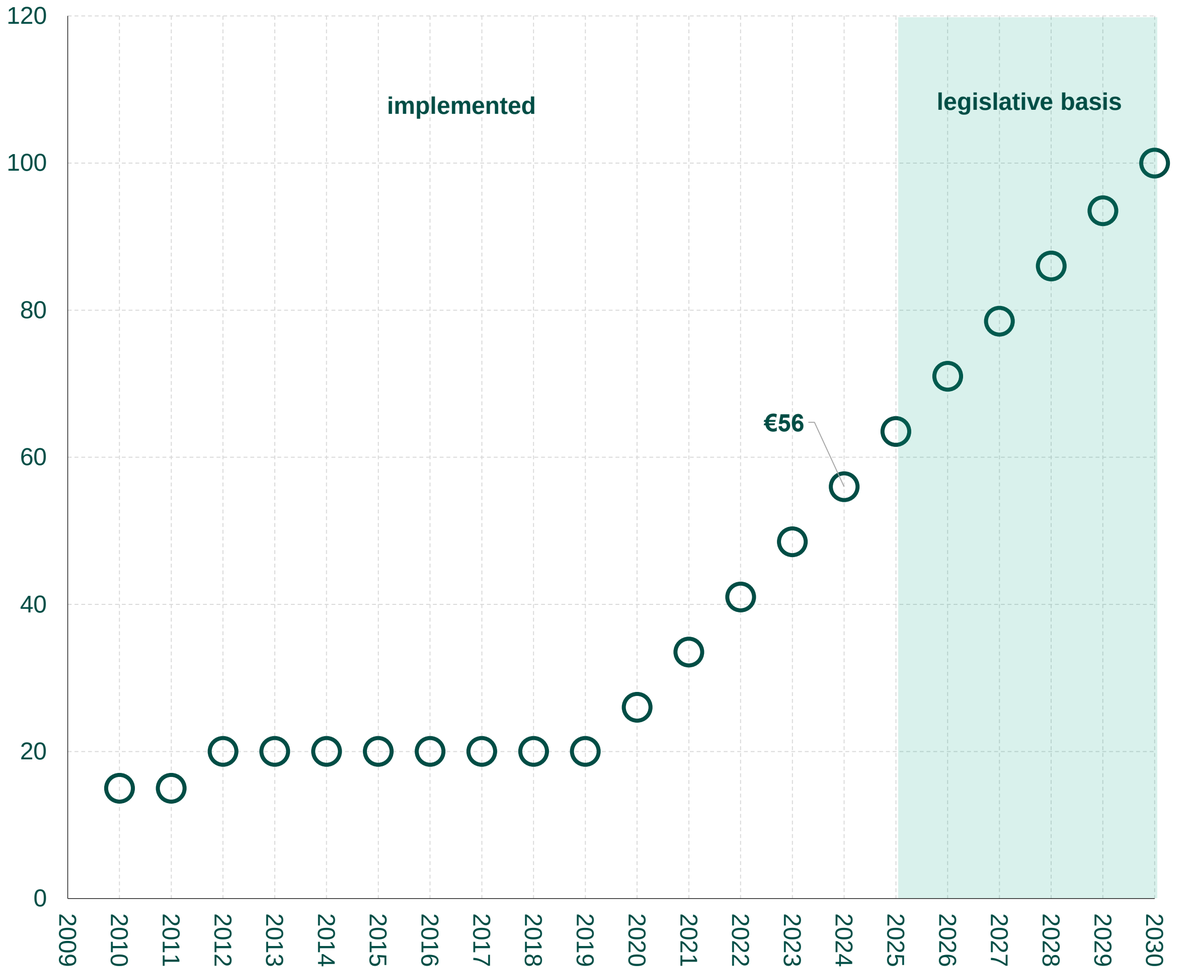
…with rising debt-income on unchanged policies



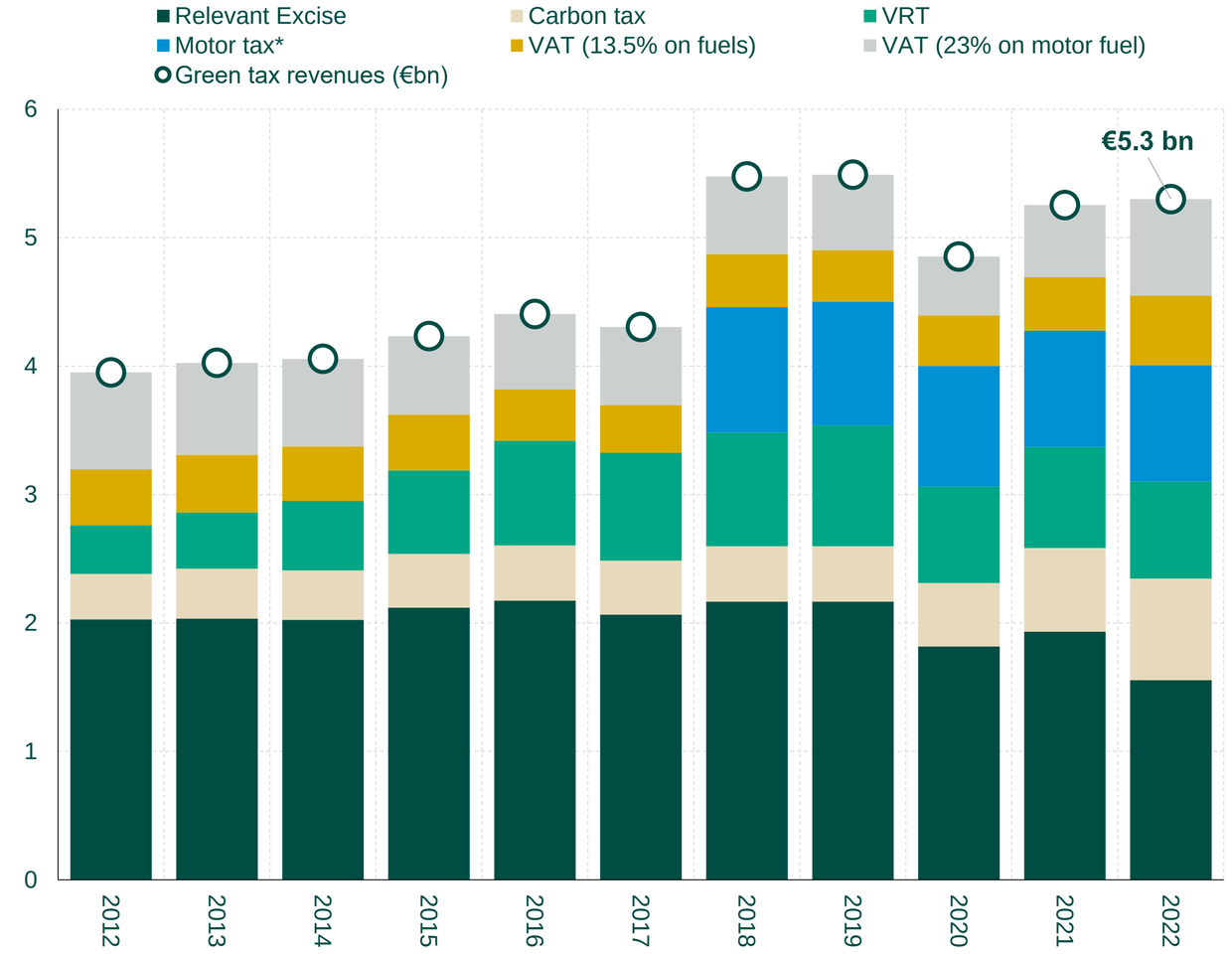
Structural trend #2: De-carbonisation

De-carbonisation – impact on public finances

Carbon pricing – pathway to €100 per tonne



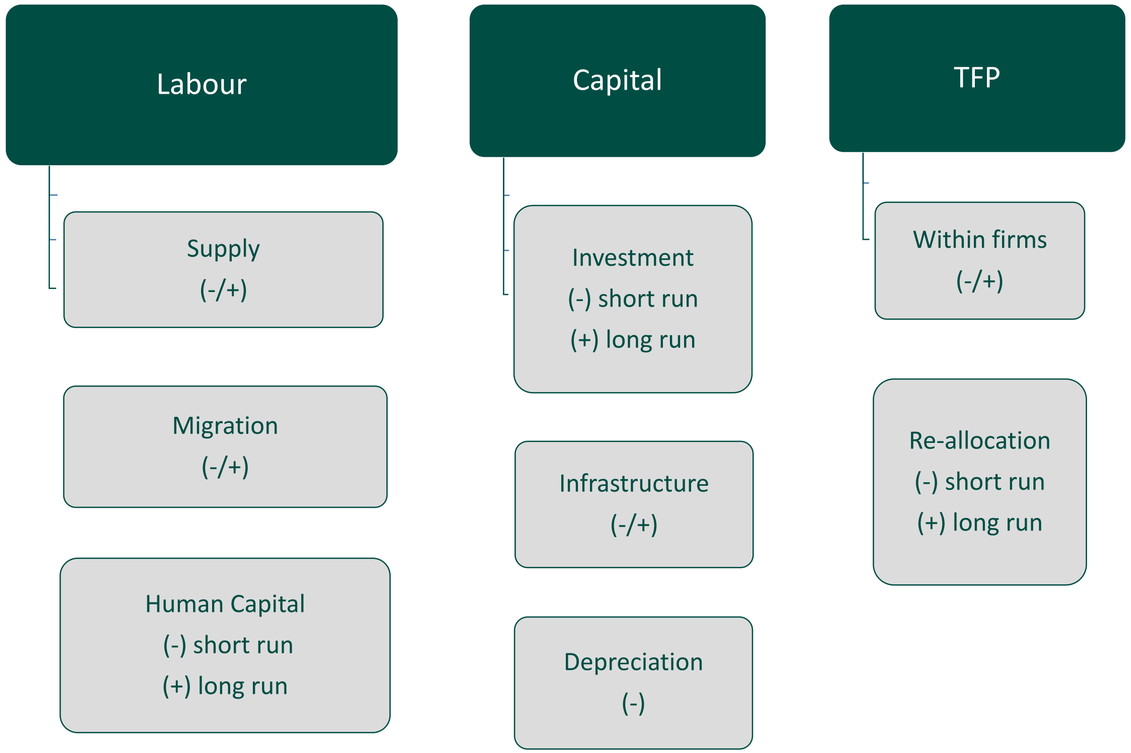
Transition to carbon neutrality: Need to mobilise new revenue streams



* motor tax part of exchequer since 2018

De-carbonisation – impact on economy

Transmission channels to K,L,TFP

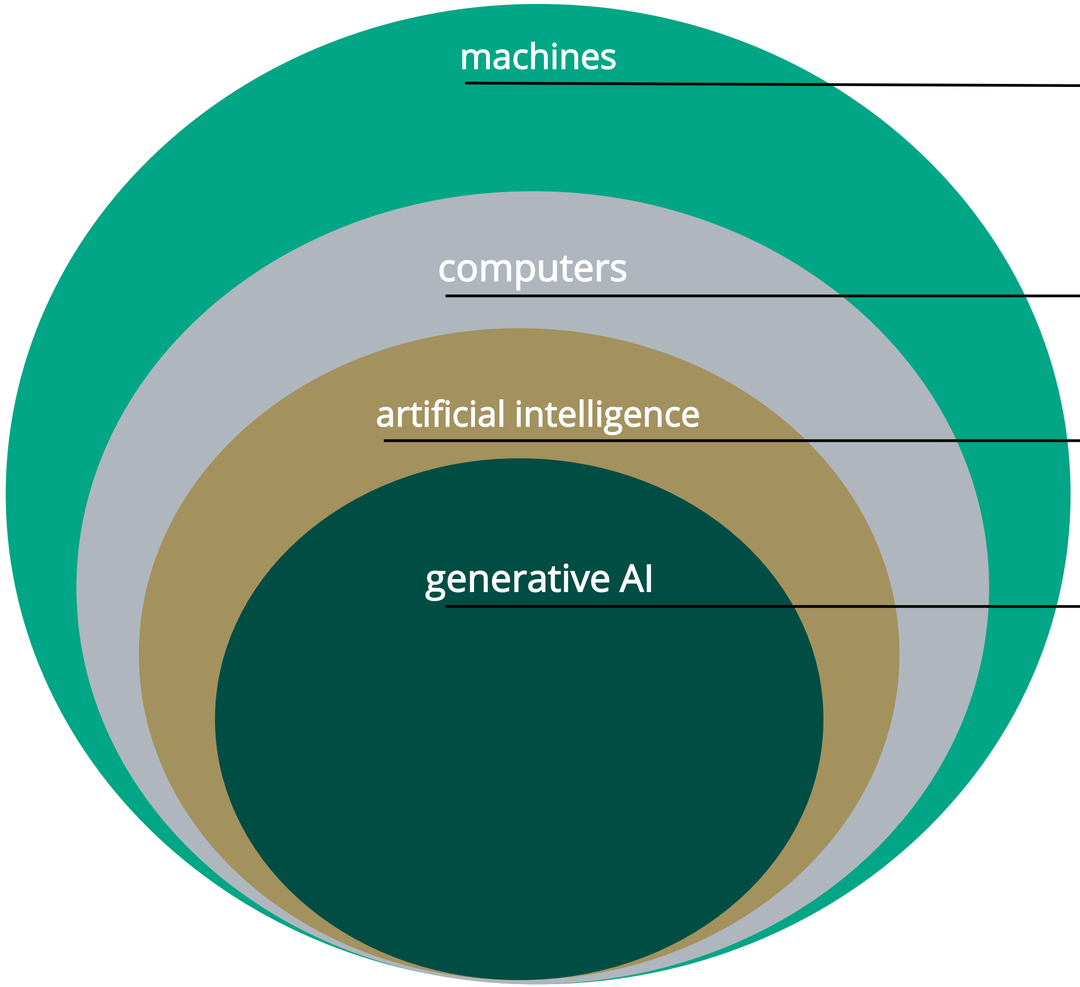


Mobilising the evidence: 'green budgeting'

	Climate positive		Climate negative		Climate budgetary impact
	Revenue	Tax expenditure	Revenue	Tax expenditure	Total
Extension ACA for energy efficient equipment		7			
Electricity micro generation		4.5			
Zero VAT rate for audiobooks and ebooks		3			
Zero VAT rate for solar panels for schools		0.5			
Extension of 9 per cent VAT rate for gas and electricity				-315	
Extension of MOT rate reduction to end-March 2024				-122	
Extension of relief for battery electric vehicles		30			
Original market value deduction for certain categories of vehicles				-	
Relief for battery electric vehicles		-			
Carbon tax	152				
Total €m	**152**	**45**	**0**	**-437**	**-240**

Structural trend #3: Digitalisation

Artificial Intelligence: the next wave of automation ?



Automation wave [1800s, 1870-1920]
- industrial revolution 1.0
- industrial revolution 2.0

decoupling production / consumption
mechanisation of agriculture
mass production
automation of routine tasks
unskilled workers

Automation wave [1970-]
- industrial revolution 3.0

ICT adoption
automation of semi-skilled tasks
semi-skilled workers

Expansion of ICT wave [1970-]
- machine leaning

1997: 'Deep Blue' defeats chess grand master

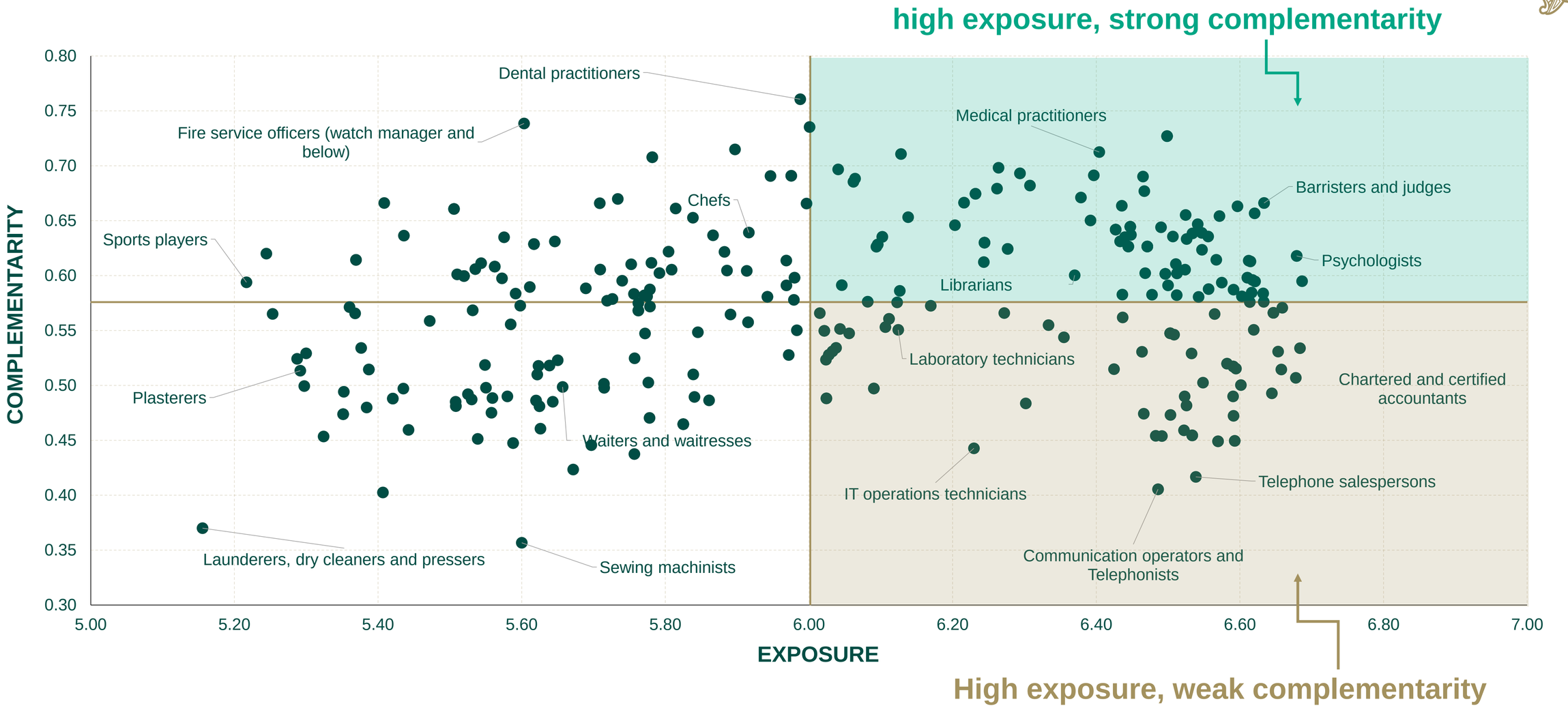
Automation wave [2022-]
- industrial revolution 4.0 ?

automate of non-routine tasks
skilled workers

The economics of A.I. – important and open questions

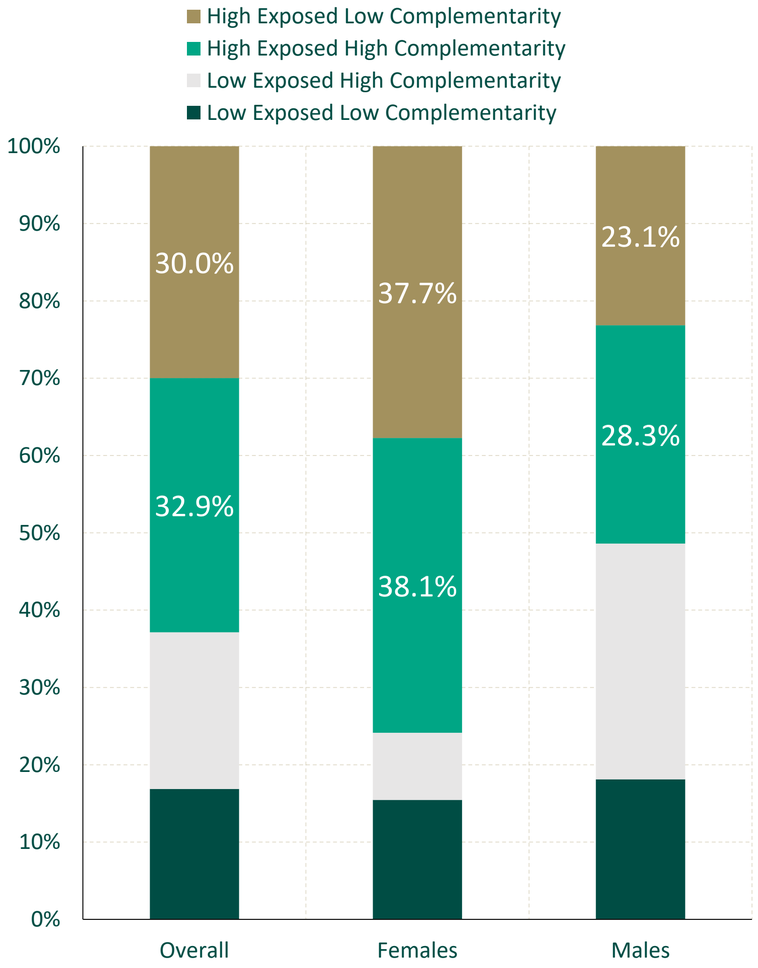
MACRO-ECONOMIC ISSUE	OPEN QUESTION	MACRO-ECONOMIC CHANNEL
LABOUR MARKET	COMPLEMENT	RAISES AGGREGATE PRODUCTIVITY / LIVING STANDARDS
	OR	
	SUBSTITUTE	ZERO SUM / UNEMPLOYMENT
INCOME DISTRIBUTION / POLARISATION	FLATTEN	INCREASES SUPPLY OF SKILLED LABOUR AND BOOSTS DEMAND FOR UNSKILLED LABOUR
	OR	
	SKEW	INCREASES THE WAGE PREMIUM ASSOCIATED WITH SKILLED LABOUR
RETURNS TO K, L	HIGHER RETURNS TO K	OWNERS OF CAPITAL CAPTURE GAINS FROM LABOUR-SAVINGS TECHNOLOGIES
	OR	
	HIGHER RETURNS TO L	RETURNS TO LABOUR ARE IN LINE WITH PRODDUCTIVITY GAINS
MARKET CONCENTRATION	MORE COMPETITION	HELPS LEVEL THE PLAYING FIELD
	OR	
	LESS COMPETITION	GENERATES WINNER-TAKES-MOST DYNAMICS
CONSISTENCY WITH OTHER POLICY OBJECTIVES	ENHANCES CONSISTENCY	FACILITATES ACHIEVEMENT OF OTHER MACRO OBJECTIVES – LIVING STANDARDS
	OR	
	INCONSISTENT	COMPROMISES OTHER MACRO OBJECTIVES – CLIMATE / GEOPOLITICAL / MACRO STABILITY

The labour market: complement or substitute – a (very) preliminary first look

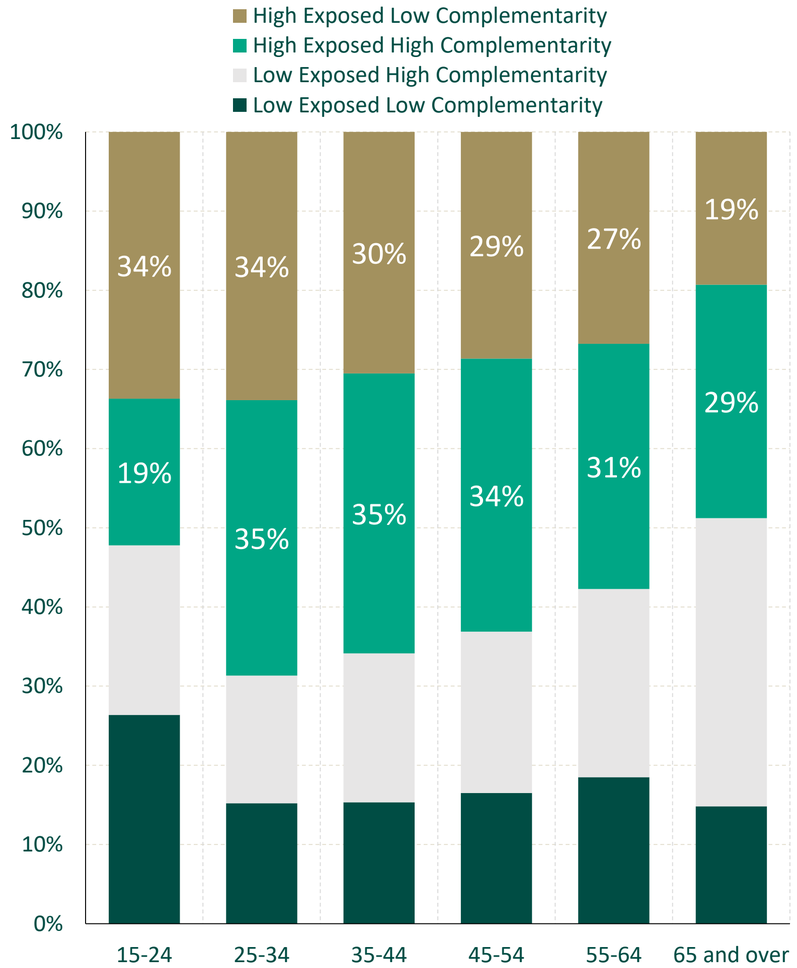


Distributional issues: along various dimensions

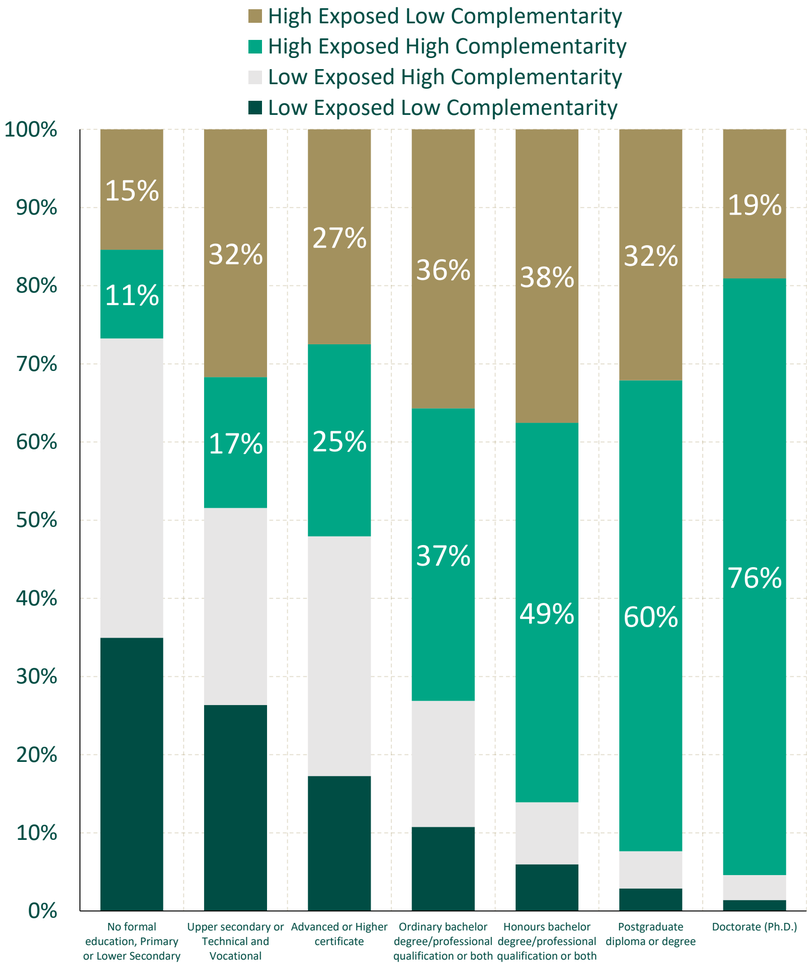
gender



age



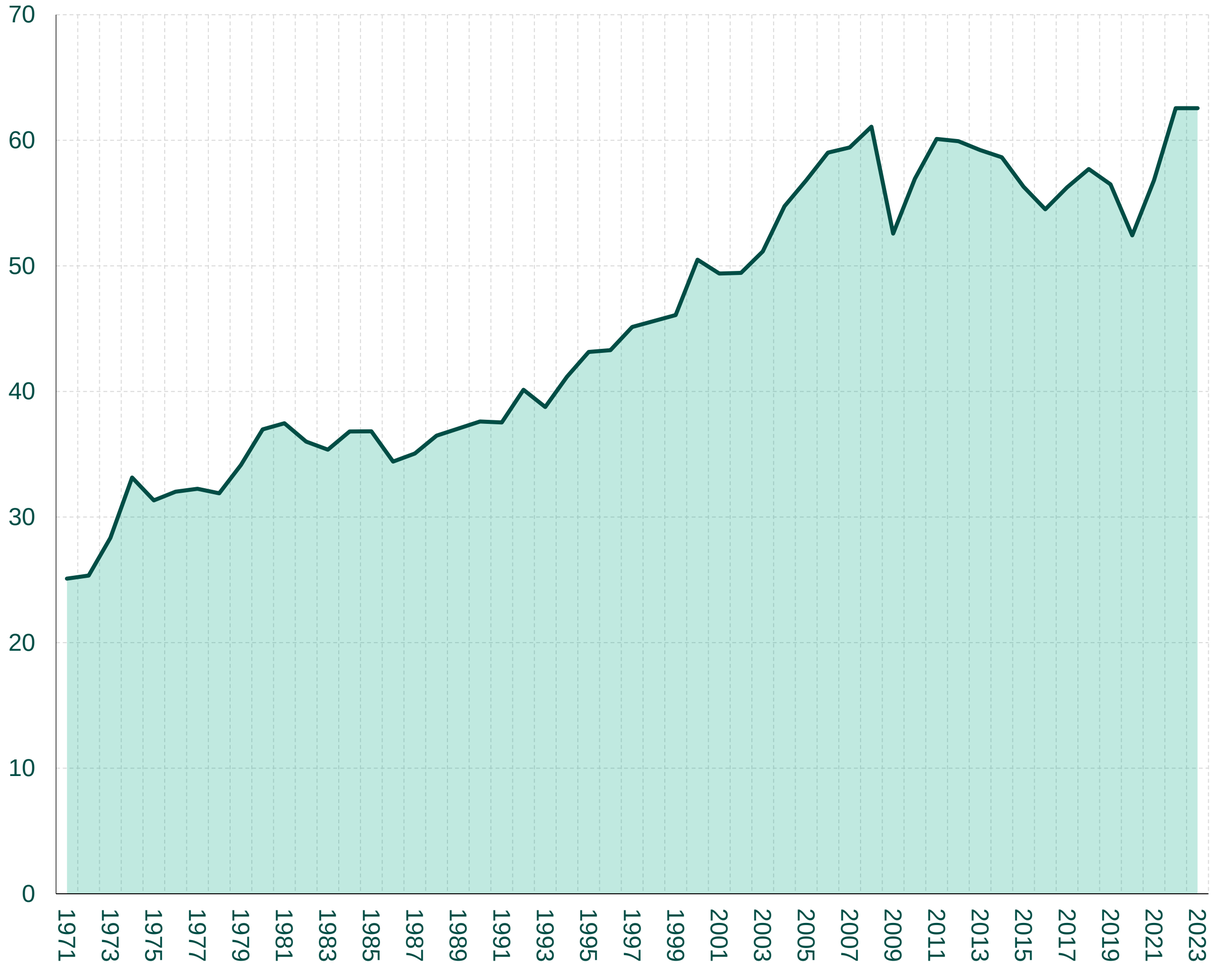
educational attainment



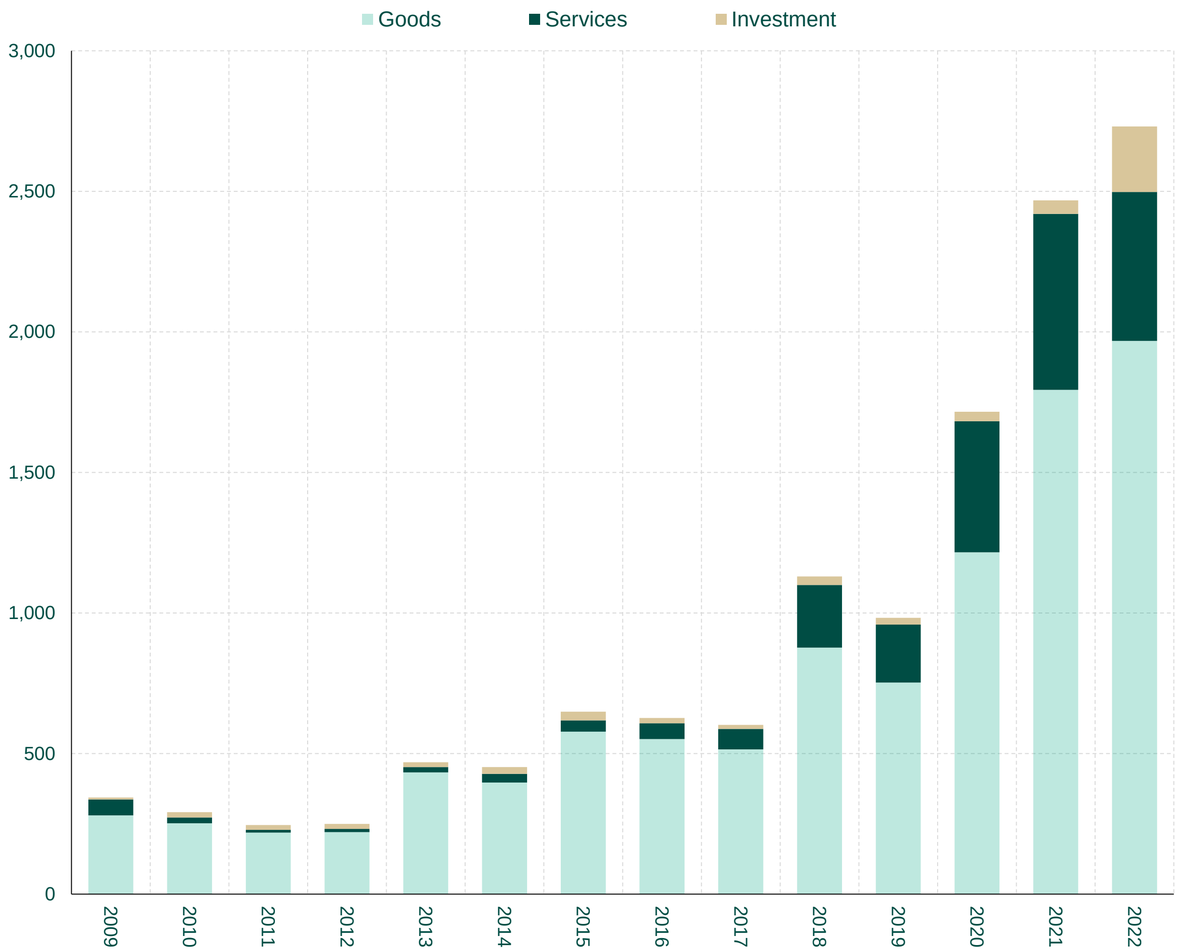
Structural trend #4: Deglobalisation

Second-best world: trade on basis of geopolitics not comparative advantage

Trade-intensity of production has stalled



Global economy: # of trade restrictions introduced



Conclusion

Summary and conclusion

- More modest growth in near-term as inflation recedes
- Intersecting with powerful structural forces
- Policy challenges
  - maximise opportunities / minimise challenges
  - boost productivity
  - fiscal resilience
- Administrative challenges [civil service / economics]
  - enhance understanding of forces at work
  - mobilise better evidence
  - scenario analysis

Disclaimer and other information:

The forecasts in this presentation are those of the Department of Finance set out in its autumn forecasts (Economic and Fiscal Outlook, April 2024). Data are as per end-May 2024

Views are those of the presenter and not necessarily those of the Minister or Department of Finance.

Outturn data are sourced from a variety of sources including the Department of Finance, Central Statistics Office, European Commission (AMECO), macrobond and Central Bank of Ireland.

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