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COMMISSION OPINION

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GENERAL CONSIDERATIONS

1. Regulation (EU) No 473/2013 sets out provisions for enhanced monitoring of budgetary policies in the euro area for ensuring that national budgets are consistent with the economic policy guidance issued in the context of the Stability and Growth Pact (SGP) and the European Semester for economic policy coordination.

2. Article 6 of Regulation (EU) No 473/2013 requires Member States to submit annually to the Commission and to the Eurogroup a Draft Budgetary Plan presenting by 15 October the main aspects of the budgetary situation of the general government and its subsectors for the forthcoming year.

CONSIDERATIONS CONCERNING IRELAND

3. On the basis of the Draft Budgetary Plan for 2017 submitted on 17 October 2016 by Ireland, the Commission has adopted the following opinion in accordance with Article 7 of Regulation (EU) No 473/2013.

4. The Commission opinion is to be seen in light of the latest economic and budgetary data. In this context, as indicated in the Commission recommendation for a Council Recommendation on the economic policy of the euro area as well as in the Commission Communication 'Towards a positive fiscal stance for the euro area', it is important that the aggregate fiscal stance of the euro area is positive and supports the ongoing recovery, while ensuring the long-term sustainability of national public finances.

5. Ireland is subject to the preventive arm of the SGP and should ensure sufficient progress towards its medium-term budgetary objective (MTO), a structural deficit of 0.5% of GDP. In particular, the Council on 12 July 2016 recommended Ireland to achieve an annual fiscal adjustment of 0.6% of GDP towards the MTO in both 2016 and 2017. As the debt ratio was 78.6% of GDP in 2015 (the year in which Ireland corrected its excessive deficit), exceeding the 60% of GDP reference value, during the three years following the correction of the excessive deficit (2016-2018), Ireland is also subject to the transitional arrangements as regards compliance with the debt reduction benchmark. In that period it should ensure sufficient progress towards compliance.

6. The macroeconomic scenario underlying the Draft Budgetary Plan is plausible. It assumes that economic growth will remain robust but moderate compared to the scenario underlying the April 2016 Stability Programme. It mainly reflects subdued economic growth in key export markets and a more cautious assessment of domestic demand, reflecting heightened global and regional economic uncertainty. The scenario assumes that no additional changes to corporate strategies would affect the composition or volume of GDP over the forecast horizon. The Commission 2016 autumn forecast is based on similar assumptions. It projects real GDP to grow by 3.6% in 2017, slightly more than in the Draft Budgetary Plan scenario, mainly on account of a more positive outlook for net exports and investment. The Commission

forecast is however more prudent as regards private consumption in 2017 in light of the heightened uncertainty of the economic outlook. Both the Commission forecast and the Draft Budgetary Plan scenario expect inflation to recover in 2017 and sustained employment creation. Overall, the macroeconomic scenario underlying the Draft Budgetary Plan is plausible.

7. Ireland complies with the requirement of Regulation (EU) No 473/2013 that the draft budget must be based on independently endorsed or produced macroeconomic forecasts. The macroeconomic forecasts underlying the 2017 Draft Budgetary Plan of Ireland have been endorsed by the Irish Fiscal Advisory Council (IFAC). The IFAC is a statutory body mandated to monitor public finances; its independence is formally guaranteed by law.

8. The Draft Budgetary Plan projects a general government deficit of 0.9% of GDP in 2016, slightly less than the 1.1% of GDP predicted in the 2016 Stability Programme and in line with the Commission 2016 autumn forecast. The slight improvement compared to the 2016 Stability Programme reflects two opposing developments: (i) the mechanical effect of the large revision to 2015 GDP on the deficit-to-GDP ratio; and (ii) the additional expenditure adopted in June 2016, mainly to address emerging overruns in the health sector. As in 2015, larger-than-expected corporate tax receipts will partly offset spending increases in 2016. Due to the positive macroeconomic outlook, public finances are expected to improve further in 2017. The Draft Budgetary Plan targets a general government deficit of 0.4% of GDP in 2017, in line with the target included in the 2016 Stability Programme, prepared on a no-change-policy basis. The recalculated structural deficit is estimated at 1.2% of GDP in 2017, down from 2.0% of GDP in 2016 and slightly above than the estimated level derived from the 2016 Stability Programme (0.9% of GDP).

Ireland's general government debt-to-GDP ratio is projected to continue declining, having peaked at almost 120% in 2012. The Draft Budgetary Plan estimates the gross debt ratio to fall to 76.0% of GDP in 2016 and to reach 74.3% in 2017, contingent on robust GDP growth and the realisation of primary budget surpluses. The improvement (by around 12 percentage points.) compared to the projections in the 2016 Stability Programme is primarily due to the arithmetic effect of the large revision to 2015 GDP in the July 2016 National Accounts. However, the stock of debt remains very high and is projected to increase by nearly EUR 13 billion over the period 2016-2019, leaving little room to increase borrowing in an adverse scenario of a significant drop in tax revenues.

As a result of the lower market rates and the early repayment of IMF loans, total interest payments by the general government have continued to decrease. Based on the information included in the Draft Budgetary Plan, interest expenditure in Ireland is expected to fall to 2.4% of GDP in 2016 from 2.6% of GDP in 2015 and is projected to decrease further next year, to 2.2% of GDP, well below the 4.1% of GDP recorded back in 2012, at the peak of the euro area sovereign debt crisis.

9. The Draft Budgetary Plan for 2017 includes new expansionary measures worth around EUR 1.3 billion (around 0.5% of GDP). Reductions in the Universal Social Charge (USC) account for the vast bulk of changes to government revenue. On the spending side, current expenditure increases focus on public pay rises, recruitment of additional staff and social protection initiatives, including increases in pension payments, a new universal childcare scheme and an increase of housing assistance

payments. Government capital expenditure is projected to increase by 9% compared to 2016. Investment will focus on social housing and education.

10. The Commission 2016 autumn forecast projects a general government deficit of 0.5% of GDP in 2017, 0.1 percentage point higher than in the Draft Budgetary Plan, on account of an expected less-tax-rich composition of GDP and a more dynamic forecast for government expenditure, caused by recurring overspending compared to government plans in the past several years. Public finances are expected to improve further in 2018 on the back of resilient, yet more moderate, economic growth. Risks associated with the Draft Budgetary Plan and the Commission budgetary projections mainly relate to uncertainties surrounding the macroeconomic outlook and the volatility of some sources of government revenues. On the upside, cash returns as of the end of November 2016 could further exceed expectations. Debt projections are less exposed to interest rate changes, as most of the outstanding stock of debt is at fixed rates. Therefore, downside risks to the budgetary outlook relate more to changes to the economic outlook. On the other hand, the potential sales of shares the government still retains in the three major domestic banks would reduce public debt.

11. The Draft Budgetary Plan does not include sufficient information to assess compliance with the transitional arrangements for the debt reduction benchmark. Based on the Commission 2016 autumn forecast, the structural effort is higher than the required minimum linear structural adjustment both in 2016 (0.1% of GDP vs. required -0.3% of GDP) and in 2017 (0.7% of GDP vs. required -0.5% of GDP).

12. Based on the information provided in the Draft Budgetary Plan there is a risk of some deviation in both 2016 and 2017 from the required adjustment towards the MTO. The same conclusion can be drawn on the basis of the Commission 2016 autumn forecast. The overall assessment mostly relies on the expenditure benchmark in the case of Ireland as it is deemed to provide a more stable and reliable anchor for prudent fiscal policy. In 2016, whereas the improvement of the structural balance, both on the basis of the Draft Budgetary Plan and the Commission forecast, significantly deviates from the required adjustment, the growth rate of government expenditure, net of discretionary revenue measures, is expected to be below the expenditure benchmark. Taking all factors into consideration, including a one-off transaction in 2015, the expenditure benchmark would point to a deviation from the requirement which is below but close to 0.5% of GDP. On that basis, the overall assessment points to a risk of some deviation from the required adjustment path towards the MTO in 2016. In 2017, both the Draft Budgetary Plan and the Commission forecast expect the improvement of the structural balance to be above the required structural adjustment. However, the growth rate of government expenditure, net of discretionary revenue measures, is expected to exceed the expenditure benchmark. Following an overall assessment, both the Draft Budgetary Plan and the Commission forecast point to a risk of some deviation in 2017.

13. Concerning the structural part of the 2016 fiscal recommendations issued by the Council, the Commission notes that the establishment of a rainy-day-fund, if appropriately designed, could provide a fiscal buffer during a future economic downturn and, together with the announced long-term target for the debt-to-GDP ratio to stand at 45%, could reduce vulnerability to economic fluctuations. However, the Draft Budgetary Plan also introduced a wide range of tax expenditure measures which are likely to further narrow the income tax base, thereby increasing public finances' exposure to shocks. Some progress has been made in enhancing the quality

of expenditure through a reform of the budgetary process and in prioritising government expenditure in public infrastructure.

14. Overall, the Commission is of the opinion that the Draft Budgetary Plan of Ireland, which is currently under the preventive arm and subject to the transitional debt rule, is broadly compliant with the provisions of the SGP. At the same time, the government's decision to use a large part of volatile, still uncertain, tax intakes to allocate additional expenditure in 2016 is not in line with Council recommendations in the context of the European Semester which ask Ireland to use windfall gains from better-than-expected economic and financial conditions to accelerate the deficit and debt reduction. In line with the Commission Communication 'Towards a positive fiscal stance for the euro area', the Commission invites the authorities to take the necessary measures within the national budgetary process to ensure that the 2017 budget will be compliant with the SGP.

    Furthermore, the Commission is also of the opinion that Ireland has made some progress with regard to the structural part of the fiscal country-specific recommendations issued by the Council in the context of the 2016 European Semester and thus invites the authorities to make further progress. A comprehensive assessment of progress made in the implementation of the country-specific recommendations will be made in the 2017 Country Reports and in the context of the country-specific recommendations to be adopted by the Council in 2017.

Done at Brussels, 16.11.2016

For the Commission
Pierre MOSCOVICI
Member of the Commission

CERTIFIED COPY
For the Secretary-General,

Jordi AYET PUIGARNAU
Director of the Registry
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