Ireland - Stability Programme

December 2002 Update

Foreword

This document updates Ireland's Stability Programme and includes macroeconomic projections to 2005. It also takes account of the measures adopted in Budget 2003.

This Update has been prepared in conjunction with Budget 2003 and is being presented to Dáil Éireann on Budget Day, 4 December 2002. As such it also provides an economic background to Budget 2003.

It has been prepared in accordance with Council Regulation (EC) No 1466/97 which sets out the rules covering the content of Stability Programmes, and conforms with the revised Opinion on the content and format of Stability and Convergence Programmes agreed by the EU Economic and Financial Committee in June 2001.

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Chapter 1 - Overall Policy Framework and Objectives

Government Objectives

The Government's economic and budgetary strategy is designed around the aim of sustaining economic growth and maintaining full employment as the basis for building a fair society of equal opportunity and sustained prosperity. The key strategic objectives of the Government in this regard are:

- concentrating resources, within budgetary constraints, on improving the quality of public services and delivering further real improvements to pensioners and people on low incomes;
- addressing the infrastructural deficit in a coherent and structured way; and
- sustaining the public finances in a healthy state while pursuing a fiscal policy stance that safeguards the competitive position of the economy

while honouring Ireland's commitment to respect the Stability and Growth Pact, which provides the overall framework for the Government's budgetary policy.

Economic Outlook

The international economic outlook – critical to the progress of Ireland's open economy - remains characterised by a high degree of uncertainty. The economic upturn which had been anticipated to take hold through this year has not materialised. A broadly-based economic upturn now appears unlikely to set in before mid-2003, and even then the risks as to its timing and pace remain clearly on the downside.

Reflecting the prospect of a delayed global economic recovery, Irish GDP is forecast to increase at an annual average rate of 4.2% over the three years 2003-2005 compared with estimated annual growth of 6.7% in 2000-2002. GNP growth, a more accurate reflection of national income in Ireland, is anticipated to average 3% over the forecast period.

Employment may increase by more than 1% on average over 2003-2005, compared with a 2.9% average over the last three years. Unemployment is expected to be $5^1/_4$% next year, but to decline towards 5% by 2005. Consumer price inflation is forecast to remain broadly unchanged next year at 4.8% - and with easing domestic price pressures in particular, to decline to around $2^1/_2$ % by 2005. As measured by the EU's HICP, inflation should ease by about half a point, to $4^1/_4$%, next year.

Budgetary Stance

The projected budgetary position over the period 2003-05 reflects an expectation of more limited increases in the overall revenue yield, combined with a desire to sustain infrastructural investment focussed on improving the productive capacity of the economy, and to target expenditure increases otherwise at social concerns and at enhancing the quality of key public services. The outlook (summarised in Table 1 below) is for a "headline" General Government budget deficit of 0.7% GDP in 2003 followed by deficits of 1.2% of GDP in both 2004 and 2005. The underlying (structural) budget balance, improving from a small deficit in 2003 to a small surplus in 2005, respects the terms of the Stability and Growth Pact. Consistent with the need to maintain a focus on the longer term – and the consequences of ageing societies - the budgetary strategy also envisages that the ratio of Debt to GDP will remain below 35%.

Table 1 - General Government Balance and Prospective Debt Ratio (% of GDP)

% of GDP	2002	2003	2004	2005
General Government Balance	-0.3	-0.7	-1.2	-1.2
Cyclically-adjusted Balance	-1.0	-0.4	-0.2	+0.1
Debt Ratio (year end)	34.1	34.0	34.5	34.9

Source: Department of Finance

Chapter 2 - Economic Outlook

2.1 Summary[1]

Against the background of a weak global economy, GDP growth this year is estimated at this stage at 4.5%, and GNP at 1.8%, with the pace of expansion remaining sluggish through the year.

GDP is forecast to expand by 3.5% next year, with GNP growth picking up to 2¼%. Relatively moderate growth is anticipated in the first half of the year, followed by some acceleration in the second half in line with an assumed improvement in global economic activity. There are, however, significant downside risks attached to this forecast. For instance, the assumed international recovery may be more muted or may occur later than currently forecast.

Employment is forecast to rise by little more than $^1/_2$% in 2003, a significantly lower rate of increase than in recent years. Some increase in unemployment appears to be in prospect since the labour force will continue to expand, albeit more slowly than hitherto. Inclusive of the budget's impact, consumer prices as measured by the CPI are forecast to increase by 4.8% although, on the HICP measure, inflation is projected to decline by about $^1/_2$% to $4^1/_4$%.

2.2 The Economy in 2002

Against the background of a weak global economy, the moderation in Ireland's growth which began during the second quarter of 2001 continued this year. Quarterly National Accounts show that GNP rose by 2.0%, year-on-year, in the first half of 2002. Available data and survey indicators for the period since then are consistent with a continuation of weak growth in the second half of the year.

Table 2 - Economic and Budgetary Indicators: 1997-2002

	1997	1998	1999	2000	2001	2002
% volume change (except where otherwise stated)						
GNP	9.5	8.2	8.8	10.7	4.6	1.8
GDP	10.9	8.8	11.1	10.0	5.7	4.5
Personal consumption	7.2	7.6	9.3	9.0	5.1	2.8
Public consumption	5.3	6.5	6.6	7.5	10.8	8.9
Fixed investment (including stocks)	21.0	17.0	6.9	8.1	-2.1	-0.4
Exports of goods and services	17.4	21.0	15.2	20.6	6.7	4.6
Imports of goods and services	16.8	25.8	12.0	21.2	6.1	3.3
Consumer prices (% change) ^	1.5	2.4	1.6	5.6	4.9	4.7
GDP deflator (% change)	4.1	6.2	4.1	4.2	5.2	4.9
Unemployment (% of labour force)	10.3	7.6	5.6	4.3	3.9	4.5
Employment (% change)	3.9	8.3	6.3	4.7	2.9	1.0
Employment change ('000)	51.4	114.6	95.2	76.7	49.1	18.0
General Gov. Balance (% GDP) *	1.2	2.4	2.1	4.4	1.6	-0.3
General Gov. Debt (% GDP)	65.0	54.9	49.3	39.3	36.7	34.1

^ Consumer Price Index.
* Deficit (-) / Surplus (+).
Labour market data for 1997 - 98 refer to April. For later years, full - year data are used.
Source: CSO and Department of Finance

Given Ireland's deep integration into the global economy, the international slowdown was the most important factor influencing the pace of growth. This in turn reflected a number of factors, including political uncertainty and associated rising oil prices, concerns about corporate governance and the related difficulties in global equity markets, a deterioration in consumer confidence and continued

[1] The analysis here is based on data available up to end-November 2002. The forecasts are based on the technical assumption of unchanged interest rates and exchange rates. International trends over the forecast period are based on the European Commission Autumn 2002 forecasts.

excess capacity in the ICT sector. The ongoing difficulties in the ICT sector, given its importance in Ireland, have particularly affected confidence and employment here.

External Developments

2002 was a difficult year for the world economy, with all major regions experiencing below trend growth. In the US, while consumer demand was buoyed up by low interest rates employment declined marginally and, reflecting geo-political uncertainty and the adverse impact of weak equity markets, private investment contracted for a second year. The European Commission estimates GDP growth in the US at 2.3% for the year as a whole. The muted expansion in the US spilled over into the rest of the global economy. Weak domestic demand, combined with an appreciation of the euro against the dollar in particular, and against sterling, resulted in a deceleration in growth in the euro area to an estimated 0.8% in 2002. At the same time, the economic difficulties in Japan showed little sign of dissipating. In the UK, the destination for a significant proportion of Irish exports, particularly from the indigenous sector, GDP expanded by an estimated 1.6% in 2002. The OECD economy as a whole is estimated to have grown by 1.5% in real terms in 2002.

In an environment of slowing world demand growth, a deterioration in competitiveness due to a combination of continued relatively high wage and price growth and the appreciation of the euro, the rate of export growth in Ireland slowed markedly from those experienced in recent years. While merchandise export volumes were 1.3% higher over January-August than in the same period of last year, a large part of this growth was attributable to a small number of mainly chemical-related sectors where very strong rates of increase were recorded. Elsewhere, very weak – and in some cases negative – growth was recorded. Exports of services remained relatively strong, rising by 24% in value, year-on-year, in the first half of 2002. In the same period, the volume of goods and services exports rose by 5.2%. Leading indicators of export performance point to no significant improvement in the second half of 2002, so that the volume of goods and services exports is estimated to rise by 4.6% over the year as a whole.

Domestic Demand

Quarterly National Accounts point to a further moderation in the growth of personal consumption this year. Household expenditure rose by just under 3.0% year-on-year in real terms over January-June. This compares to growth of 5.3% in the first half of 2001. A number of factors appear to have weighed on consumer expenditure this year. In particular, a decline in consumer sentiment associated with a number of high profile job losses and a small rise in unemployment, is likely to have been a major factor underlying slower personal consumption growth. Slower employment growth and lower growth in real disposable incomes have also contributed. Available indicators point to further moderate growth in personal consumption in the second half of this year. Retail sales data, for instance, show that the volume of retail sales in the third quarter was 2.3% higher than in the same period a year earlier. New car sales, after declining over the first half, remained at the same level as in 2001 in the third quarter. But consumer sentiment remains weak. Taking all of these factors into account, personal consumption is estimated to rise by 2¾% in 2002.

Labour market conditions were somewhat less favourable than in recent years. Employment rose by 1.5% in Q1 to Q3 of 2002 from last year, much more slowly than in recent years, with a noticeable deceleration as the year advanced. Moreover, a significant proportion of this year’s growth was concentrated in the public sector. In the important manufacturing sector employment declined by 13,000 (4%), year-on-year, in the same period. For the year as a whole, employment growth is likely to average 18,000 (1.0%). Slower employment growth led to a small rise in unemployment, albeit from a very low level, with unemployment averaging 4.4% over the first three quarters. The unemployment rate is estimated to average 4½% this year, compared to 3.9% in 2001.

Sectoral earnings data point to a slowing in the rate of wage increases this year. The most pronounced deceleration thus far occurred in the business and distribution services sector, where weekly earnings were 2.7% higher, year-on-year, in the first half (compared to a rise of 8.0% for the full year 2001). Available data suggest that the rates of increase in earnings have not slowed to the same extent elsewhere. Nevertheless, they are expected to moderate over the second half of the year, in line with the slowdown in demand growth and the easing of labour market conditions.

Available data are consistent with essentially unchanged investment this year. Quarterly National Accounts show that total investment in the first half was nearly 3% lower in real terms, year-on-year, than in 2001. The components of investment, however, show divergent trends. Building and construction investment continued to expand, reflecting continued implementation of the National Development Plan and a 5.2% annual increase in house completions over January-June. Investment in machinery and equipment, however, remains very weak, reflecting the uncertain global environment and, possibly, domestic cost developments. Capital goods imports – a useful proxy for imports of machinery and equipment – were very weak, declining by 10.8% in value in the year to July. Primarily based on building trends, investment is estimated to decline slightly, perhaps by ¼%, over the year as a whole.

Final Demand and Imports

Taking developments in all of these components together, final demand is estimated to increase by almost 3% in 2002, compared to 5.5% in 2001. The volume of goods and services imports rose at an annual rate of 1.6% in the first half of 2002. Merchandise import volumes rose by 1.8%, year-on-year, to end-August. For the year as a whole, imports of goods and services are estimated to increase by 3¼%, a sharp deceleration from the 6.1% increase of 2001.

Balance of payments figures for the first half of the year show a marginal current account deficit of just €2 million, with a merchandise surplus of €19,080 almost equal to the invisibles deficit. In relation to the latter, income outflows in the first half rose very strongly compared to the same period in 2001. For the year as a whole, a current account deficit of the order of ½% of GNP is projected.

Gross Domestic Product and Gross National Product

On this basis, GDP is estimated to expand by about 4½% in 2002. Given that a significant part of this growth is attributable to a few sectors dominated by foreign-owned multinationals, the associated profit outflows are likely to result in a significant gap with the GNP measure, which is estimated to increase by 1¾% in 2002.

Table 3 – Economic Indicators 2002: Budget Forecast and Estimated Outturn

	2002 Forecast (Dec' 2001)	2002 Outturn (Dec' 2002)
GNP (% volume change)	3.5	1.8
GDP (% volume change)	3.9	4.5
Consumer prices (% change)	4.2	4.7
Unemployment rate (% labour force)	4.7	4.5
Employment growth ('000)	24	18
Employment growth (%)	1.4	1.0

Source: Department of Finance

2.3 Macroeconomic Projections: 2003 -05

As a small country which is highly integrated into the global economy in terms of trade and investment links, economic conditions in Ireland are crucially determined by the international economic environment and our ability to trade in this environment. The forecasts for Ireland over the period 2003-05 in this Stability Programme Update are based on a scenario in which the global economy picks up during next year. They incorporate the technical assumptions that interest and exchange rates stay at present levels and the expectation that Ireland, by maintaining its international competitiveness, remains positioned to take advantage of the anticipated pick-up in global economic activity.

External Outlook
The international economy is assumed to develop as forecast by the European Commission in its latest forecasts. While there is considerable uncertainty about the timing and extent of a recovery in global economic activity, the consensus view – which the Commission shares – is that activity will pick up during 2003. The Commission's forecasts for GDP growth in key economies are set out in Table 4 below. It projects that demand in Ireland's export markets will grow by 5.6% next year, compared to an estimated 1.4% this year. Bearing in mind, however, that rising investment is a key element in the foreseen international pick-up and that capital goods production is not a mainstay of manufacturing here, this export market growth is unlikely to be fully reflected in Irish export performance. Accordingly, exports of goods and services are forecast to rise by 5% next year. Export growth is assumed to accelerate through 2003, in line with the assumed recovery in our main trading partners.

Table 4 – Real GDP Growth in Ireland's Main Trading Partners

	2002	2003	2004
Germany	0.4	1.4	2.3
France	1.0	2.0	2.7
Italy	0.4	1.8	2.4
Euro area	0.8	1.8	2.6
UK	1.6	2.5	2.7
EU15	1.0	2.0	2.6
US	2.3	2.3	2.8
Japan	-0.6	1.2	1.4

Source: European Commission Autumn 2002 Economic Forecasts

Domestic Demand
The outlook for investment is more uncertain than in recent years. While some pick-up in machinery and equipment investment seems likely after this year's decline, the uncertainty surrounding the global economic outlook means that there is little prospect of a strong recovery. In the building and construction sector, housing output is expected to moderate from the very strong level of output emerging this year. Continued implementation of the National Development Plan will support construction activity to some extent, but overall output from the sector is likely to decline by 2% or more next year. Total investment, therefore, is forecast to contract by close to 1% in 2003.

Public consumption will expand very modestly following a strong expansion in 2002. Personal consumption is forecast to rise by close to 3% in 2003, based on a further moderation in both employment growth and wage developments combined with improving confidence as global conditions improve. In these circumstances, employment growth is forecast at little more than ½%, a significantly lower rate of increase than in recent years. The labour force seems likely to continue expanding and, as a result, the unemployment rate appears likely to rise – perhaps to 5¼%. These slightly less favourable labour market conditions, allied to the slower evolution of demand growth, should result in a moderation in wage increases next year.

Final Demand and Imports
Final demand is forecast to increase by 3½%. Imports of goods and services are projected to rise by about 3½% also. Taking into account a further decline in current transfers from the EU, and slower growth in profit repatriations by the foreign-owned multinational sector in the context of a better-balanced export performance, the current account of the balance of payments is not forecast to record a deficit much different from this year's – at a little above ½% of GNP.

GDP, GNP and Risks
Taking all these components together, GDP is forecast to grow by 3½% in 2003. On the basis of more balanced growth in the export sector and, accordingly, slower growth in net factor outflows, GNP is forecast to expand by 2¼%. Relatively moderate growth is anticipated in the first half of the

year, followed by some acceleration in the second half in line with the assumed improvement in global economic activity.

Economic activity should pick up over the later years of the forecasting period, as the assumed global recovery matures and facilitates strengthening investment in, and exports from, Ireland – with the prospect that growth will be returning to its potential rate in the later part of the period. On this basis, GDP growth is projected to average 4½% over 2004/05 with GNP expanding by close to 3½% on average.

There are, however, very significant downside risks attached to this forecast. For instance, the assumed recovery in the global economy may be more muted or may occur later than currently forecast. International developments could impact on oil prices, or business and consumer sentiment. In addition, there remains a risk that Ireland could lose some of its ability to supply goods and services to, or to secure inward investment from, the rest of the world, due to adverse competitiveness developments. This could occur, for example, if expectations in relation to wages fail to adapt to the less favourable economic climate. Moreover, a sudden sharp appreciation of the euro exchange rate could pose significant difficulties for many firms, particularly those in the indigenous sector, which is more labour intensive than the high-technology sector.

Table 5 - Growth and Associated Factors

	2002	2003	2004	2005
GNP growth at constant market prices	1.8	2.2	2.9	3.8
GNP level at current market prices (€)	103,900	110,300	117,600	125,600
GDP growth at constant market prices	4.5	3.5	4.1	5.0
GDP level at current market prices (€)	125,600	134,600	144,600	155,800
GDP deflator	4.9	3.5	3.3	2.6
HICP change	4.7	4.2	3.0	2.1
CPI Change	4.7	4.8	3.5	2.6
Employment growth	1.0	0.6	1.3	1.6
Unemployment Rate	4.5	5.3	5.3	5.1
Labour productivity growth [2]	0.9	1.7	1.7	2.4
	% Volume Change			
Private consumption expenditure	2.8	2.9	3.6	4.0
Government consumption expenditure	8.9	0.6	0.5	0.3
Gross fixed capital formation	-0.3	-0.7	1.5	3.1
Exports of goods and services	4.6	5.0	6.1	6.8
Imports of goods and services	3.3	3.6	5.2	5.6
	Contributions to GDP growth			
Final domestic demand	2.5	1.3	2.1	2.6
Change in stocks	0.2	0.2	0.2	0.2
External balance of goods and services	1.8	1.9	1.7	2.2

Source: Department of Finance

2.4 Inflation

Developments in 2002

Inflation, as measured by annual changes in the Consumer Price Index (CPI), remained very high this year despite the moderation in demand growth. A number of factors impacted on price developments, including higher oil prices reflecting political uncertainty and administered price increases in a number of sectors. Services sector inflation continued high and contributed disproportionately to the increase in the CPI. In the first ten months of the year, inflation averaged 4.6%. For the year as a whole, CPI inflation is likely to average 4.7%. As measured on the EU harmonised basis inflation in

[2] Growth of GNP at constant prices per person employed

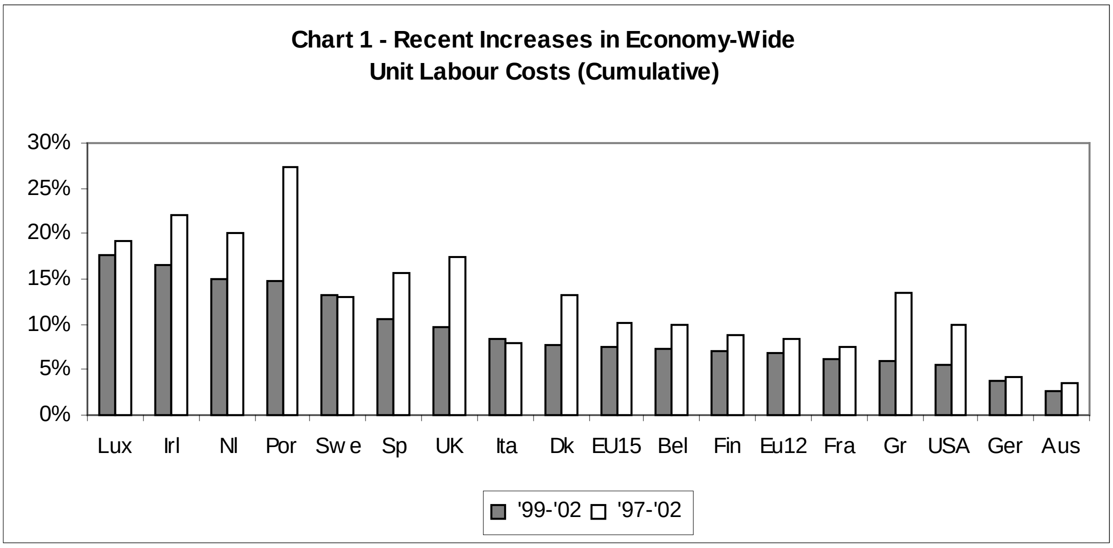
Ireland, at an estimated 4.7%, was the highest in the euro area in 2002 with the Irish rate exceeding the euro area average by around 2.4 percentage points.

Prospects for 2003 and Beyond

While the outlook is for a marginal increase in the CPI next year, to 4.8%, consumer price inflation as measured by the EU HICP is expected to fall by ½% to 4¼% - and the CPI exclusive of the impact of this year's tobacco excise increase is also projected to decline by ½% to about 4.2%. These projections make the technical assumption of unchanged interest and exchange rates and commodity prices (see table 5). A number of factors support this analysis. On the external front, assuming unchanged exchange rates, import prices are likely to benefit somewhat from the lagged effect of the appreciation this year of the euro against both sterling and the dollar. In addition, the overhang of global excess capacity this year is likely to result in muted external inflationary pressures into next year. On the domestic front, reflecting the projected loosening of labour market conditions and the more moderate evolution of demand, service sector inflation is forecast to ease somewhat, although it is expected to continue to exceed the headline figure.

The Government is committed to supporting and maintaining competitiveness and to enhancing the conditions for economic growth through structural reform of product, capital and labour markets, details of which are set out in the 2002 Progress Report on Reforming Product and Capital Markets[3] and the 2002 National Employment Action Plan[4].

Competitiveness issues will also be a key concern in the negotiations on a new social partnership agreement which are now under way. National pay policy has been set within the context of national agreements with the Social Partners since 1987, during which time Ireland has experienced rapid economic growth and development. Any new agreement will need to recognise the changed economic and budgetary environment since the last national agreement was negotiated, and the need to avoid a loss of competitiveness. This is all the more crucial in the light of the developments of recent years when, as illustrated in Chart 1, Irish costs rose more rapidly than those of all of our main trading partners.



Source: European Commission Autumn 2002 Economic Forecasts

[3] Available at http://www.finance.gov.ie
[4] Available at http://www.entemp.ie

Independent Forecasts

The following table compares the Department of Finance forecasts with those of other organisations. In some instances the assumptions underpinning the forecasts may be different, and this must be borne in mind when making comparisons.

Table 6 – Comparison of Macroeconomic Forecasts for Ireland in 2003

Annual % change	GDP	GNP	CPI	Employment
Department of Finance (Budget 2003)	3.5	2.2	4.8	0.6
European Commission (Autumn 2002)	4.2	--	3.8*	1.4
OECD (November 2002)	3.6	2.5	4.3*	--
Central Bank of Ireland (Autumn 2002)	4.75	4.25	4.25	1.2
ESRI (October 2002)	4.2	3.3	4.0	1.4

*HICP

Chapter 3 - General Government Balance and Debt

3.1 Summary

The Government's economic and budgetary strategy is designed around the aim of sustaining economic growth and maintaining full employment as the basis for building a fair society of equal opportunity and sustained prosperity.

Reflecting the very gradual nature of the international recovery, the outlook is for a "headline" General Government budget deficit of 0.7% GDP in 2003 followed by deficits of 1.2% of GDP in both 2004 and 2005. The underlying (structural) budget balance, improving from a small deficit in 2003 to a small surplus in 2005, respects the terms of the Stability and Growth Pact. The debt/GDP ratio is projected to remain below 35% to end-2005, far below the present EU average debt level of around 62% of GDP.

3.2 Policy Strategy

Following national elections, a new Government took office on 6 June 2002[5]. The new Government Programme[6] restates the commitment to respect the Stability and Growth Pact which, the Programme states, "provides the overall framework" for the Government's budgetary policy.

The three key objectives of the new Government with regard to budgetary and economic policy are:

- concentrating resources, within budgetary constraints, on improving the quality of public services and delivering further real improvements to pensioners and people on low incomes;

- addressing the infrastructural deficit in a coherent and structured way; and

- sustaining the public finances in a healthy state while pursuing a fiscal policy stance that safeguards the competitive position of the economy.

3.3 Actual Balances and Implications of Forthcoming Budget

A deficit of 0.3% of GDP on the general government finances is currently projected in 2002, compared with a surplus of 1.6% in 2001 and a planned surplus of 0.7% for 2002 at the time of last year's Budget. The 2002 Broad Economic Policy Guidelines called on Ireland to ensure that the budgetary stance for 2002 is broadly neutral and to ensure continued compliance with the close to balance requirement of the Stability and Growth Pact after 2002. While the outturn now foreseen is 1% below the Budget 2002 expectation, a Eurostat decision that proceeds associated with the change-over to the euro should be excluded in determination of government balances accounted for about 0.5% of GDP of the deterioration. The adverse revenue effects of slower domestic demand growth, largely attributable to the effects of the international economic slowdown on the Irish economy, accounted for the balance of the difference between the planned general government balance and the outcome.

A "headline" General Government deficit of 0.7% of GDP is planned for 2003, with deficits of 1.2% of GDP anticipated for each of 2004 and 2005. The corresponding structural (cyclically adjusted) General Government balances, estimated in accordance with the methodology of the Commission, are -0.4% of GDP in 2003, -0.2% in 2004 and +0.1% in 2005.

The gross debt/GDP ratio is expected to remain below 35% out to 2005. Not less than 1% of GNP will continue to be set aside annually for the pre-funding of pension liabilities, building up assets to help address costs associated with ageing in future decades. This pre-funding does not affect the General Government Balance.

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[5] The new Government is composed of Fianna Fáil and the Progressive Democrats, the same political parties that were in coalition Government since the last national elections in 1997

[6] See: Agreed Programme for Government between Fianna Fáil and the Progressive Democrats, June 2002

In response to the infrastructural needs of the economy, capital expenditure will average 5% of GNP over the Programme period, in line with the National Development Plan. The provisions for day-to-day spending will, at the same time, underpin substantial progress across the broad range of social and other objectives. More detailed information in relation to Government expenditure and revenue issues is set out in Chapter 5.

Table 7 - General Government Budgetary Developments in % of GDP

	2001	2002	2003	2004	2005
General government balance	1.6	-0.3	-0.7	-1.2	-1.2
Central government	1.1	0	-0.7	-1.4	-1.4
Local government	-0.1	-0.1	-0.2	-0.2	-0.2
Social security funds	0.6	-0.2	0.2	0.3	0.5
Total receipts	35.8	35.0	34.4	33.5	32.9
Total expenditures	34.2	35.3	35.1	34.7	34.1
Budget balance	1.6	-0.3	-0.7	-1.2	-1.2
Net interest payments	0.2	0.2	0.3	0.4	0.4
Primary balance	3.1	1.2	0.9	0.3	0.4
		Components of Revenue:			
Taxes	25.3	24.5	24.6	24.0	23.8
Social contributions	6.1	6.1	5.9	5.9	5.8
Interest income	1.4	1.3	1.3	1.1	1.1
Other	2.9	3.1	2.7	2.5	2.3
Total receipts	35.8	35.0	34.4	33.5	32.9
		Components of Expenditure:			
Collective consumption	5.5	5.8	6.0	5.9	5.7
Individual consumption	9.2	9.6	9.8	9.7	9.5
Social transfers in kind	1.3	1.4	1.4	1.4	1.3
Social transfers other than in kind	8.6	9.1	9.1	9.2	9.3
Interest payments	1.6	1.5	1.6	1.5	1.5
Subsidies	1.1	0.9	0.8	0.8	0.7
Gross fixed capital formation	4.3	4.4	4.1	4.1	4.0
Other	2.6	2.5	2.3	2.1	2.0
Total expenditures	34.2	35.3	35.1	34.7	34.1

Source: Department of Finance; preliminary ESA'95 basis; rounding may affect totals.

3.4 Structural Balance and Fiscal Stance

By subtracting the estimated cyclically induced variation in the Budget from the observed budget balance, the Cyclically-Adjusted Budget Balance (CABB) can be calculated. Comparing Cyclically-Adjusted Balances from year to year can give an indication of the discretionary changes in the Government's fiscal position but the precision of CABB changes in estimating the overall fiscal stance is subject to the caveats expressed in previous updates.

Estimates of the cyclically-adjusted balance are presented overleaf. The estimates are based on the economic and budgetary projections set out in this Stability Programme Update, and use the methodology of the European Commission. Calculated on this basis, as indicated in Table 8, the cyclically-adjusted balance points to an expansionary fiscal stance in 2002. However, on the basis of the technical assumptions underpinning the budgetary position going forward (which include contingency provisions of 0.4% and 0.8% of GDP for 2004 and 2005, respectively), the methodology points to a fiscal tightening over the period ahead - with the cyclically-adjusted balance estimated to improve from a deficit of 1.0% of GDP this year to a surplus of 0.1% in 2005.

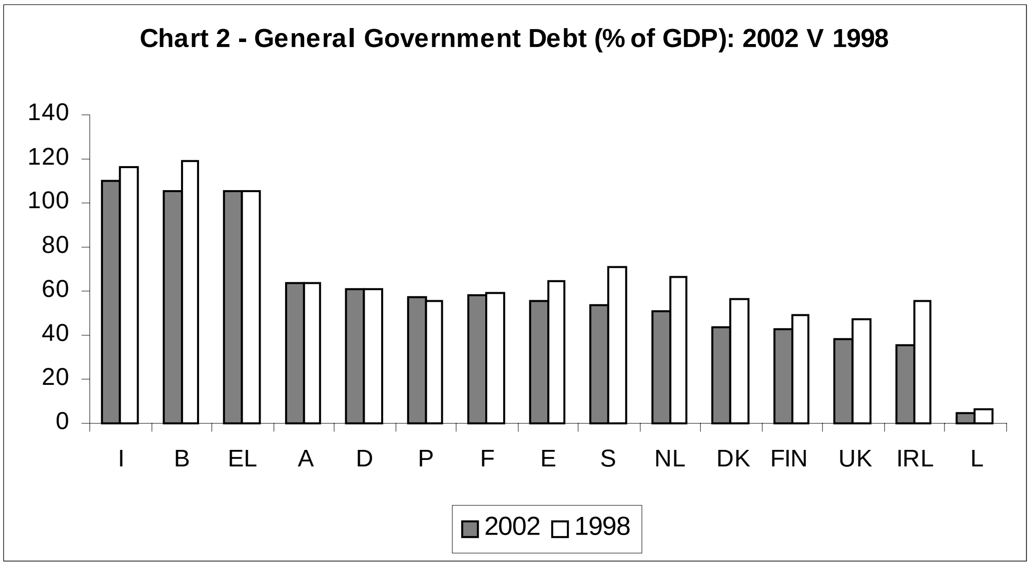
Table 8 - Cyclical Developments

% of GDP	2001	2002	2003	2004	2005
GDP growth at constant prices	5.7	4.5	3.5	4.1	5.0
Actual balance	1.6	-0.3	-0.7	-1.2	-1.2
Potential GDP growth	7.5	7.0	6.5	6.3	5.8
Output gap (% potential output)	4.4	2.0	-0.9	-2.9	-3.7
Cyclically-adjusted balance	0.1	-1.0	-0.4	-0.2	0.1
Change in Cyclically adjusted GGB	--	-1.1	0.6	0.2	0.3

Source: Department of Finance

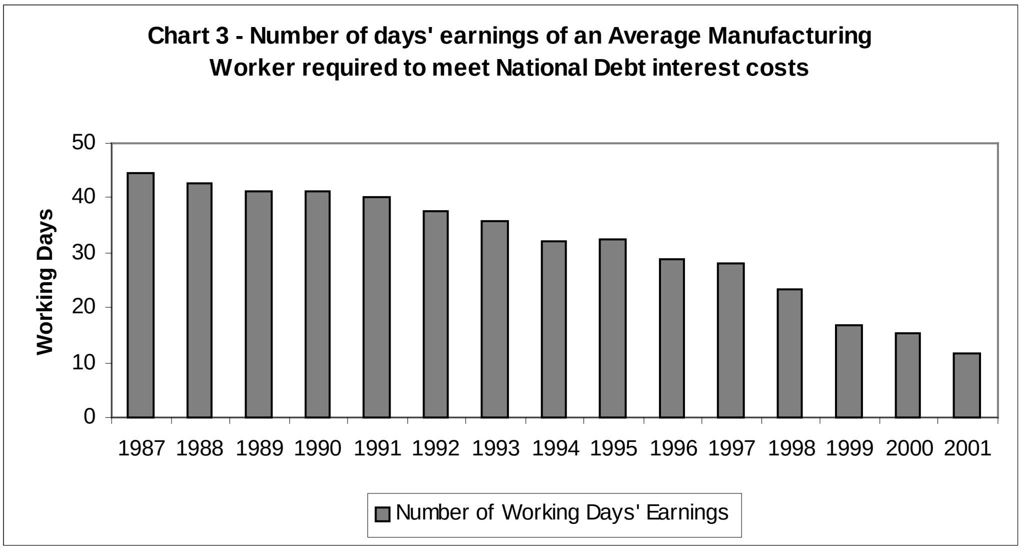
3.5 Debt Level and Developments

As indicated by Chart 2, Ireland has one of the lowest debt/GDP ratios in the EU, and has achieved the greatest reduction in its debt/GDP ratio between the onset of stage 3 of EMU in 1998 and 2002.



Source: European Commission 2002 Autumn Economic Forecasts

This improvement extends the long-standing decline in Ireland's debt/GDP ratio, which has seen the cost of interest payments on the national debt per person at work fall from the equivalent of 45 days' earnings for an average manufacturing worker in 1987 to 12 days' earnings in 2001, as Chart 3 shows.



Source: Department of Finance

Over the Programme period as a whole, the gross debt level is expected to remain below 35% of GDP. When account is taken of the build-up of assets in the National Pension Reserve Fund, the net debt to GDP ratio is considerably lower than the gross debt levels set out in Table 9. At end 2001, it was well below 30% of GDP.

Table 9 - General Government Debt Developments

% of GDP	2001	2002	2003	2004	2005
Gross debt level	36.7	34.1	34.0	34.5	34.9
Change in gross debt level	-2.6	-2.6	-0.1	0.5	0.4
Primary balance	-3.1	-1.2	-0.9	-0.3	-0.4
Interest payments	1.6	1.5	1.6	1.5	1.5
Nominal GDP	-4.0	-3.2	-2.3	-2.4	-2.5
Net Receipts of Social Security Funds[7]	1.7	0.8	1.1	1.3	1.4
Other factors influencing the debt ratio	1.2	-0.5	0.4	0.4	0.4
Of which: Privatisation receipts	-0.6	-0.1			
Increase in local authorities' debt[8]	0.6	0.6	0.4	0.4	0.4
p.m. implicit interest rate on debt	4.4	4.4	4.8	4.6	4.5

Source: Department of Finance

3.6 Balance by Sub-sectors of General Government

The balance by sub sectors of general government is set out in detail in Table 7. In Ireland Central Government accounts for around 90% of total Government expenditure. Ireland does not have a federal or state government system and Local Government, the Social Insurance Fund and the National Pension Reserve Fund (from which no expenditure is scheduled before 2025) account for the balance. These Funds had a combined surplus of more than 8% of GDP at end-2001, and this is expected to grow over the Programme period.

[7] Central Government transfers, contributions and investment income

[8] Substantially offset by increased mortgage assets

Chapter 4 – Sensitivity Analysis and Comparison with Previous Updates

4.1 Summary

This Chapter briefly outlines the impact on the underlying budget balance of different possible economic scenarios. It is estimated that a 1% change in the growth rate would change the General Government Balance by about ½% of GDP. In addition it is estimated that a 1% increase in interest rates could reduce economic growth by about ½% in the short-run. As a result, a 1% change in interest rates could change the General Government Balance by around ¼%.

4.2 Alternative Scenarios and Risks

A number of points should be borne in mind when examining the results of the sensitivity analysis set out below. Firstly, the estimates should be seen as indicative and are subject to considerable uncertainty. Secondly, no fiscal policy response to the changed budgetary position is assumed over the period of the Programme. In reality such a response would occur if desirable in the interests of economic or budgetary sustainability, or if required in terms of the Stability and Growth Pact.

4.3 Sensitivity of Budgetary Projections to Different Scenarios and Assumptions

In line with estimates for previous years, it is calculated that a 1% impact on the growth rate would change the General Government Balance by about ½% of GDP. The budgetary impact of a 1% change in the growth rate per annum compared with the central projection is given in the Table below.

Table 10 - Impact on the Budget Balance of 1% Change in Rate of Growth Per Annum

	2003	2004	2005
Baseline GDP Growth	3.5	4.1	5.0
GGBalance (% GDP) (including contingency)	-0.7	-1.2	-1.2
Cumulative impact of 1% change in growth per annum on GGBalance	up to 0.5%	up to 1.0%	up to 1.5%
GGBalance Range (%GDP)	-1.2 to -0.2	-2.2 to -0.2	-2.7 to +0.3

Source: Department of Finance

Interest rate changes would impact on the budgetary position in two ways. They would affect debt service costs directly; and they would have an impact on economic activity, with consequences for both revenue and expenditure.

The impact on economic activity is highly uncertain. Higher interest rates would reduce investment and consumption spending. The size of the impact clearly depends on future expectations. Interest rate changes which are seen as temporary in nature will have a smaller impact than changes that are considered to be longer-lasting. The financial balance sheets of the personal and business sectors are also important. A more indebted economy would suffer a greater impact.

Estimates by the Economic and Social Research Institute suggest that a 1% increase in interest rates could reduce growth by as much as ½% in the short-run. As a result, a 1% change in interest rates could change the General Government Balance by around ¼% of GDP. It would also directly affect debt servicing costs but, as the debt burden declines, these effects are becoming more and more marginal relative to the impact on growth and Government revenues.

4.4 Comparison with Previous Update

Table 11 compares this Stability Programme Update with the updated programme for 2001. GDP growth in 2002 was below trend, at 4.5%, although higher than anticipated in last year's Stability

Programme Update. However, at 1.8%, GNP growth (with which overall tax yields are more strongly associated) was 1¾% weaker than anticipated, reflecting relatively weak domestic demand and a strong increase in net factor outflows associated with export success in a few, largely overseas-owned, sectors. GDP growth rates for 2003 and 2004 have also been revised downwards, consistent with the global economic slowdown persisting well into 2003.

The General Government Balance in 2002 is now projected at 1.0% of GDP below the level anticipated in last year's Update. Some 0.5% of the deterioration reflects a Eurostat ruling concerning the appropriate treatment by Member States of once-off revenues associated with the changeover to the Euro. Otherwise, the forecast outturn for 2002 has been revised downward primarily because, as economic activity eased in response to the international slowdown, tax revenues rose more slowly than envisaged. This is reflected, also, in weaker General Government budgetary positions for 2003 and 2004 than envisaged a year ago. Nonetheless the General Government debt ratio, already far below the 'Maastricht' threshold, is set to remain low over the period to 2005.

Table 11 - Divergence from Previous Update

% of GDP	2001	2002	2003	2004	2005
GDP growth					
previous update	6.8	3.9	5.8	5.3	--
latest update	5.7	4.5	3.5	4.1	5.0
Difference	-1.1	+0.6	-2.3	-1.2	--
Actual budget balance					
previous update	1.4	0.7	-0.5	-0.6	--
latest update	1.6	-0.3	-0.7	-1.2	-1.2
Difference	+0.2	-1.0	-0.2	-0.6	--
Gross debt levels					
previous update	35.8	33.7	33.8	34.1	--
latest update	36.7	34.1	34.0	34.5	34.9
Difference	+0.9	+0.4	+0.2	+0.4	--

Source: Department of Finance

Chapter 5 - Quality of Public Finances

5.1 Summary

With the twin objectives of strengthening the basis for sustainable economic progress going forward and of enhancing - broadly defined - social progress, over recent years Ireland has:

- Very substantially raised the share of national resources devoted to public investment - assisted by a falling debt-service ratio associated with keeping the public finances 'close to balance or in surplus' over the period;

- Significantly improved a broad range of key day-to-day public services - by maintaining the proportion of national resources devoted to day-to-day non-interest public service provision in a rapidly expanding economy, and

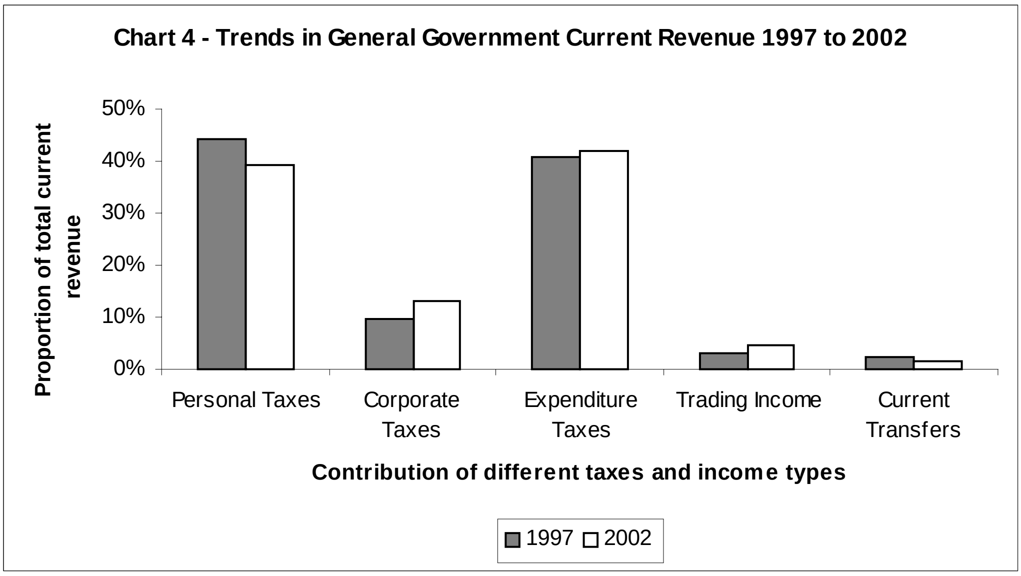
- Underpinned incentives to, and reward for, effort and enterprise with an easing of personal taxation.

5.2 Revenue Strategy

A primary objective of Government over the last five years has been to reform the tax and benefit systems comprehensively so as to incentivise enterprise and effort, with a particular focus on motivating higher participation in the labour force and removing those on low incomes from the tax net. Tax rates have been reduced, tax allowances have been replaced by tax credits and the standard rate tax band has been widened. These measures contributed to an increase of the order of 6% in female labour force participation (by the 15-64 age-group) over the five years to last spring, and of some 2% in male labour force participation. Overall labour force participation rose by more than 4 percentage points, marking substantial progress towards the Lisbon employment objective. The measures in Budget 2003 continue the policy of easing the tax burden on lower-paid employment.

5.3 Changing Sources of Government Revenue

The evolution of general government current revenues over the last five years is indicated in Chart 4.



Source: Department of Finance

The policy-driven easing of personal taxation, especially for those on lower incomes, led to a decline in its share in total current government revenues over the period, while the shares of net trading income arising in the government sector, and of both indirect and corporate taxes, rose - the latter despite further progress towards a unified corporate tax rate. Reflecting the continued diminution of net EU transfers to Ireland, government's net current transfer income declined in importance.

5.4 Durability of Revenue Measures

Viewed in a structural (underlying) context, there is a once-off expenditure provision, noted below, which involves significant increased outlay in 2003 but will not arise in subsequent years. A number of revenue measures that have temporary effect on 2003 tax yields (or which will not reach their full anticipated yield next year) also deserve mention, as follows:

- Hitherto, corporate taxes were paid on a "preceding year" basis, while a "current year" approach generally applies for most other taxes. Budget 2002 established a five-year time-path to bring the corporate sector's tax payments onto a broadly "current year" basis, providing additional yields over the five years 2002-2006;

- Budget 2001 provided for a scheme of savings incentives operated through the tax system, the full year effects of which are first felt in 2003. The budgetary cost of this incentive will ease through 2006 and will be minimal (if not negative) in 2007.

The latter measure, accordingly, broadly offsets the positive impact on the budgetary balance of the additional yield from the foregoing corporate tax measure, over the same timescale.

- Capital gains taxes, also, have been paid on a "preceding year" basis hitherto. Budget 2003 provides for taxes arising on gains over the first nine months of each year to be paid within that year, beginning in 2003. This measure will yield a substantial, once-off, cash-flow gain in 2003. One other measure included in Budget 2003 also yields (a minor) once-off cash flow in 2003 only.

- Recognising that talks on a new national agreement are in train, Budget 2003 provides for the cost of paying a first tranche of "benchmarking" awards in the event of a new agreement. That would include arrears from 1 December 2001 as agreed under the terms of the Programme for Prosperity and Fairness, which would not arise in subsequent years.

These two measures, also, broadly offset one another in terms of their impact on the budgetary balance.

Budget 2003 includes several other initiatives that have limited or no revenue yield in their first or early years of operation, but which promise a rising yield over the medium term as they take full effect.

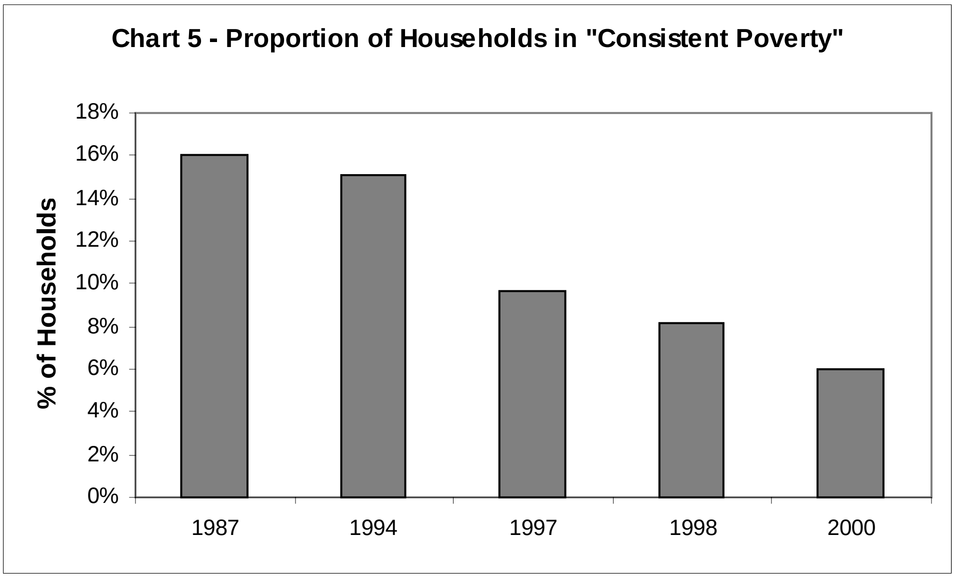
Compared with their impact in 2003, there is a net positive impact on the General Government balance from all of these measures combined by 2005, of the order of 0.4% of GDP. One further revenue measure will have effect for three years, so that the foregoing net positive impact relative to the 2003 position may reduce to 0.3% of GDP in 2006.

The recent and ongoing economic slowdown has been accompanied by a lower tax yield relative to economic growth than was experienced in the period up to the millennium year. This reflects, in particular, a lower tax-intensity in economic activity as growth slowed. This drop in tax intensity of economic activity - which appears to have been underway for two years - implies that any above-average revenues which may have accompanied past strong growth have substantially, if not wholly, unwound at this juncture.

5.5 General Government Expenditure

Against a background of strong economic and revenue growth, Ireland has been able to make considerable progress in addressing the national infrastructural deficit and improving a broad range of key public services.

Those improvements are well illustrated by advances made in addressing poverty - as defined in Ireland's National Anti-Poverty Strategy which was developed in line with similar strategies of all the EU member states - over recent times. The proportion of Irish people in poverty thus defined has fallen considerably through recent years, as illustrated in Chart 5.



Source: Economic and Social Research Institute: Reports No 34 and 45 [9]

However, more moderate growth rates and revenue flows since mid-2001 and going forward mean that Ireland cannot sustain similar levels of increase in expenditure in the years ahead. Partly in that context, the 2002 Broad Economic Policy Guidelines recommended that Ireland "improve expenditure control through setting norms and ensure in the 2003 Budget and beyond that expenditure priorities and resource generation are targeted at a sustainable budgetary and economic outcome". Public Expenditure is currently planned within an overall 3 year fiscal framework. The Irish Government is committed to framing and managing its expenditure policy, along with other fiscal policies, to achieve a sustainable match between spending and resources and meet the circumstances of the Irish economy, subject to achieving and maintaining the overall stability objectives of fiscal policy.

The record on control of public expenditure is good as is evidenced by the following data :

Table 12 - Measuring Expenditure Management: 1997-2001

Year	Variance: Budget Estimate v Outturn	Variance as a % of GNP
1997	+1.7%	+0.4%
1998	-0.8%	-0.2%
1999	+1.6%	+0.4%
2000	+1.7%	+0.4%
2001	+1.5%	+0.4%

Source: Department of Finance

[9] In the National Anti-Poverty Strategy, consistent poverty was defined as being below 50-60% of average disposable income and experiencing enforced basic deprivation. Basic deprivation refers to a set of 8 indicators, which were regarded as necessities and possessed by a majority of those in the Living in Ireland Survey conducted by the ESRI. Chart 5 uses the 60% of average disposable income measure.

Nonetheless, there is a continuing focus on improved monitoring and control of public expenditure trends. Monthly Expenditure Management Reports are now submitted to Government detailing actual expenditure and revenue receipts to date as well as overall trends in both. This affords the opportunity to take early corrective action if spending pressures emerge in particular sectors.

Revised procedures are also being developed to further strengthen arrangements for the control and management of public expenditure:

- Publication of Departments' monthly spending profiles for 2003 to facilitate a more informed assessment of emerging spending trends;
- Improvements in risk assessment measures and the introduction of contingency planning to cater for unforeseen pressures which may emerge as the year progresses;
- Greater focus on effective management of demand-led schemes;
- Revised arrangements for managing capital spending; and
- Provision of incentives for Departments to improve efficiency and cost-effectiveness.

Slower revenue growth heightens the need to evaluate the benefits being secured from existing spending programmes as a basis for determining which areas warrant priority access to resources. A number of recent initiatives undertaken in this context, such as the Expenditure Review Initiative, the Management Information Framework and the Commission on Financial Management and Control Systems in the Health Services, are set out in detail in Chapter 7.

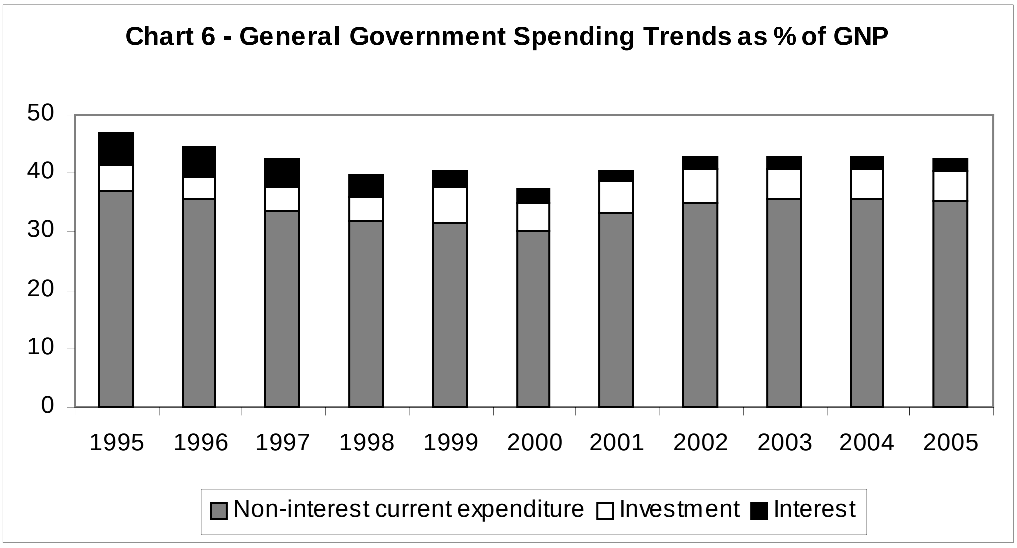
Outlook for Expenditure 2003-05

In 2003, while sustaining strong public investment, resources available to improve day-to-day services have been targeted at priority areas:

- An additional €520 million (7%) in gross current spending for health services
- An additional €240 million (5%) in gross current spending for education and science
- An additional €770 million (8%) in gross current spending for social welfare

This allocation of resources to priority areas has necessarily required a tighter approach in the allocations to other areas.

Expected trends in General Government Expenditure as a percentage of GDP are shown in Table 7. GDP includes income arising in Ireland but attributable to overseas owners of businesses located here. Accordingly, GDP ratios overstate Ireland's taxable capacity, and understate the proportion of national resources devoted to public services. GNP ratios are a truer indication of Ireland's taxable capacity, and thus measure public spending or revenue effort more accurately. Chart 6 shows the projected evolution of government expenditure as a percentage of GNP over the period 1995-2005.

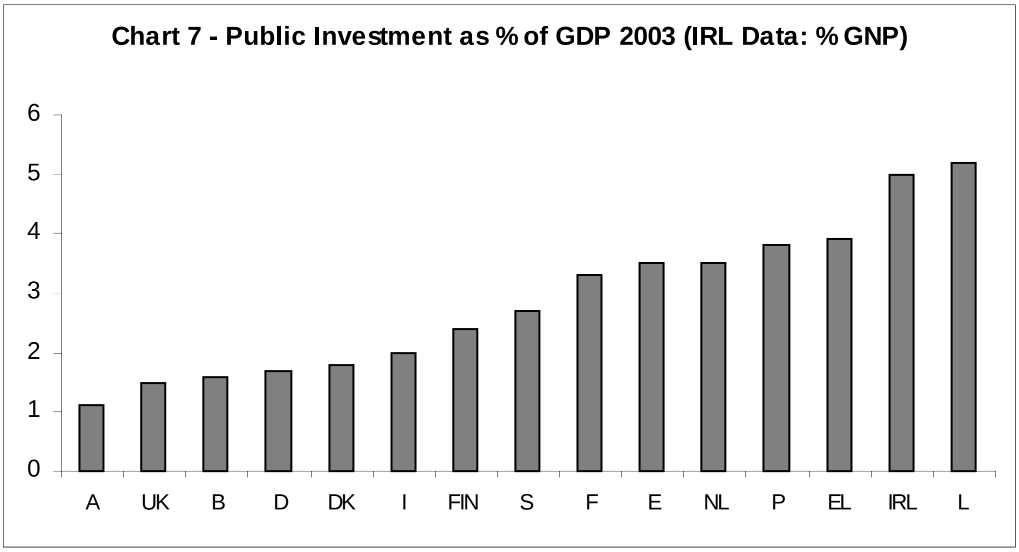


Source: Department of Finance

5.6 Infrastructural Investment

Cumulative exchequer expenditure under the National Development Plan (NDP) by end 2002 (over €8.7 billion) is ahead of target. The bulk of this planned investment in roads, public sector transport and water and sewerage services is aimed at addressing existing bottlenecks and supporting further economic growth in the years ahead.

Gross capital expenditure increased by 186% between 1997 and 2002. In 2003, consistent with the commitment to infrastructure provision and notwithstanding the tight budgetary situation prevailing, the Government has sought to maintain high levels of investment in key priority areas as illustrated in Chart 7.



Source: European Commission Autumn Forecasts 2002; Irish Data: Department of Finance

In 2002 about €3.5 billion, 3½% of GNP, was spent on developing roads, public transport, water services and health infrastructure. Investment in 2003 will be as follows:

- Roads and Transport: €1.7 billion
- Housing: €1 billion
- Water services: €0.5 billion
- Health: €0.5 billion

The investment measures contained in the Estimates, in Budget 2003 and in the NDP represent a prudent use of available resources to support sustained economic progress into the future. Their financing, despite an expected continuing reduction in EU funding, will respect the Stability and Growth Pact. With a view to maintaining investment efficiency, new approaches to public investment are underway, including a series of Public Private Partnerships.

Other Productive Investment

Over recent years, investment in Research & Development, Education, Employment Supports and Training has increased significantly. Productive investment (current and capital) in 2003 in these areas will exceed €6.4 billion (6% of GNP) as against €3.6 billion in 1997. The investment can be broken down as follows:

- Education: €5.6 billion
- Research & Development: €270 million
- Employment Supports and Training: €660 million

Chapter 6 - Sustainability of Public Finances

6.1 Long term Budgetary Prospects, including the Implications of Ageing

The EU Economic Policy Committee (EPC) report entitled “Budgetary Challenges Posed by Ageing Populations: The Impact on Public Spending of Pensions, Health and Long-Term Care for the Elderly and Possible Indicators of the Long-Term Sustainability of Public Finances” of October 2001 contained projections for public spending on pensions and health/long-term care for all Member States, including Ireland, out to 2050. On the common assumptions used, the EPC Report estimated that demographic changes could increase Irish public spending on pensions from just over 4½% of GNP in 2000 to 9% in 2050 and raise public spending on health care from just over 6½% of GNP in 2000 to more than 9% in 2050.

More recent work confirms the foregoing EPC assessment with respect to potential future public pension costs. Ireland undertakes an actuarial review of its Social Insurance Fund (SIF) periodically. The latest review, “Actuarial Review of the Financial Condition of the Social Insurance Fund”, reflecting the pension and social security contribution system as at end-2000 and assessing prospects over the period to 2056, was published in June. The report, on a scenario of uprating pensions in line with earnings and before utilising the assets of the National Pensions Reserve Fund (NPRF: see below), concludes that the existing social security (PRSI) contribution rate would require to be raised by 55.8% (almost $^{4}/_{7}$ths) for the SIF to break even over the full period to 2056. The previous assessment - the 1997 “Actuarial Review of Social Welfare Pensions” – had estimated that a 61% increase in the overall PRSI rate would be needed for the SIF to break even over the period 1996 to 2056.

Table 13 - Long-term Sustainability of Public Finances

% of GNP [10]	2000	2005	2010	2020	2030	2040	2050
Old Age Pensions	4.6	4.5	5.0	6.7	7.6	8.3	9.0
Health Care (inc. care for the elderly)	6.6	7.1	7.2	7.7	8.2	8.7	9.1
			Assumptions				
Labour Productivity Growth		3.2	2.7	1.8	1.8	1.8	1.8
Real GNP Growth		4.7	3.5	2.1	2.2	1.9	1.8
Male 20-64 Participation Rates	87.9	87.5	87.1	86.3	85.7	84.9	85.6
Female 20-64 Participation Rates	56.7	56.3	56.4	56.7	61.3	65.6	73.3
Total 20-64 Participation Rates	72.3	72.0	71.7	71.6	73.6	75.4	79.5
Unemployment Rate		5.0	5.0	5.0	5.0	5.0	5.0

Source: EPC Report: Budgetary challenges posed by ageing populations 2001

Ireland submitted its National Strategy Report on the Pension System to the European Commission in September, in common with other Member States. This report acknowledged the ageing challenge that Ireland faces, and its implications for financial sustainability. It highlighted Ireland’s creation (in 1999) of a fund which would partially pre-fund future public pension liabilities, as a key – and timely - policy response. Each year 1% of GNP is required by law to be placed in the National Pensions Reserve Fund from budgetary resources. The Fund’s accumulating assets cannot be drawn upon before 2025. At the end of 2001, the assets of the fund amounted to almost 8% of GNP.

The National Strategy Report notes that crucial elements in addressing the “ageing” issue are to achieve further increases in labour force participation rates – especially among females and older age groups – to sustain unemployment at its current low level and to continue the policy of five-yearly actuarial reviews of the SIF and NPRF to keep assessment of the extent of the challenge up-to-date. It also notes Ireland’s support for the process of open co-ordination in the area of pensions policy, as a

[10] Pensions/Health Expenditure expressed as a percentage of GNP

useful basis for helping Member States to develop their own pension policies in an optimal manner through the exchange of experience, ideas and best practice.

Chapter 7 - Horizontal Issues Affecting Public Finances

7.1 Summary

This Chapter sets out a number of reform measures in relation to the public finances that have been ongoing over the last year. These include the Expenditure Review Initiative, revisions to the Estimates/Budgetary Process, the establishment of an Independent Estimates Review Committee as part of this year's Estimates process, the continued development of a Management Information Framework, the establishment of a Commission on Financial Management and Control Systems in the Health Services, the Report of the Public Service Benchmarking Body and proposals to establish a National Development Finance Agency.

7.2 Expenditure Review Initiative

The objectives of the Expenditure Review Initiative (ERI) are to analyse in a systematic manner what is being achieved by Exchequer spending and to provide a basis on which more informed decisions can be made on priorities within and between programmes. It moves the evaluation of public expenditure away from a focus on inputs (the traditional audit perspective) towards a focus on outputs and results.

The first phase of the ERI was carried out over 1997-2001. Over 70 reviews have now been completed covering about one quarter of Government's discretionary spending. In June 2001, following a review of the process by the Department of Finance (which included consideration of a value for money study by the Comptroller and Auditor General), the Government approved revised arrangements for the next phase of the ERI. This involved laying down criteria for the selection of programmes for review, the provision of central supports in terms of training and networking, arrangements for quality control and the undertaking of cross-departmental reviews.

In May 2002, the Government approved the expenditure review topics proposed for the first year of the next three-year planning horizon (2002-2004). In selecting topics for review, the emphasis was on programmes that involved significant levels of expenditure and programmes where the external environment had changed substantially since the programmes were introduced. Two topics were selected for pilot cross-departmental reviews.

7.3 Revisions to the Estimates/Budgetary Process

In framing Budget 2002, a “Budget Day spending envelope” was set aside to facilitate a more strategic and focussed approach by Government in making choices about the allocation of net extra resources among competing priority areas.

To strengthen the basis for choice among priorities, a revised system for determining multi-annual expenditure figures has also been adopted. An “Existing Level of Service” approach replaces a ‘No Policy Change Process’ of recent years. The ELS approach focuses solely on the costs of continuing to provide the existing level of service in future years. This allows a clearer distinction to be made between technical and policy adjustments, providing Government with a clearer basis for selecting priorities in the allocation of net extra resources.

7.4 Independent Estimates Review Committee

This year, the Government took a further initiative aimed at identifying programmes or projects which no longer justify their cost because of changed circumstances, programmes which could be deferred or delivered over a longer time period, and new delivery or user-charging mechanisms which could improve the management and delivery of programmes. An independent Estimates Review Committee - comprising three former senior civil servants – was appointed to make an overall assessment of spending proposals from all Departments and Offices with those objectives in view.

The Committee adopted a “whole of Government” approach in analysing expenditure and in making its recommendations. In order to deepen public understanding of the relative merits of the various public expenditure programmes, the report of this Committee is being published in association with Budget 2003. Reflecting the limitations associated with a review of expenditure on a one-year basis and in a short timeframe, the Government has decided that the Department of Finance, early next year, should initiate a similar review of expenditure in 2004 and 2005.

7.5 Management Information Framework

Management information systems need to be developed to support enhanced decision-making, performance and accountability, including through a move from a focus almost exclusively on inputs (the traditional audit perspective) towards a focus also on outputs and results in the evaluation of public expenditure. This is the goal of the Management Information Framework (MIF), a flexible system of accounts integrated with output measurement, development of which is now well under way. The aim of the MIF is to help Departments to meet their internal and external reporting requirements, to modernise their accounts systems, to report on resources consumed in producing their outputs and to produce the data required for "value for money" assessments.

7.6 Commission on Financial Management and Control Systems in the Health Services

An Independent Commission on Financial Management and Control Systems with a remit to examine, evaluate and make recommendations on relevant systems, practices and procedures throughout the health service was established in 2002. It has focussed on the financial management systems and control procedures of the Department of Health and Children and of the main service agencies of the health sector - which accounts for almost one quarter of current expenditure.

The primary objective of the Commission is to develop recommendations to enhance the timeliness and quality of financial information available to managers in the health services and to the Departments of Health and Children, and Finance. The work of the Commission is a cornerstone in the development of a modern financial framework in the health sector capable of promoting better budgetary control and securing value for money for the growing resources being channelled to that area.

It is intended that the Commission will report by the end of 2002.

7.7 Public Service Benchmarking Body Report.

The Report of the Public Service Benchmarking Body was published in July 2002.

The benchmarking process was agreed between the public service unions and employers as part of the Programme for Prosperity and Fairness. The process was to examine the pay and jobs in the public service with similar jobs and pay in the private sector and to recommend appropriate levels of pay for the grades reviewed. This marked a new and innovative approach to determining public service pay levels by comparison with the private sector.

As part of the Programme for Prosperity and Fairness, the parties agreed that the implementation of the report would be the subject of negotiations between the parties and that one quarter of any increases recommended would be paid with effect from 1 December 2001. The Report recommended that the payment of the balance of the awards should be conditional on real and verifiable outputs from a programme of modernisation and change. Talks between the parties on implementation began in July and are continuing.

The cost of implementing the Benchmarking Report's full recommendations is about €1.1bn in a full year.

7.8 National Development Finance Agency

In November, the Government published a Bill to establish a National Development Finance Agency (NDFA), under the aegis of the National Treasury Management Agency, to assist in providing cost effective finance for public investment projects. The new Agency will:

- provide advice to State Authorities, including Government Departments, to assist them in evaluating financial risks and costs of public investment projects;
- assess optimal financing for public investment projects (including Public Private Partnerships) such as those set out in the NDP and other infrastructure priorities; and
- in certain circumstances, raise finance for public investment projects.

The NDFA will help to maximise value for money for the Exchequer in a number of ways, including the identification of the best financing packages and the application of commercial standards in terms of evaluating financial risks and costs for each project.

Annex 1

Table 14 - Basic Assumptions

	2002	2003	2004	2005
Short-term interest rate (annual average)	3.4	3.3	3.3	3.3
Long-term interest rate (annual average)	4.8	4.7	5.2	5.2
USD/€ exchange rate (annual average)	0.94	1.00	1.00	1.00
World excluding EU, GDP growth	2.9	3.9	4.2	4.2
EU-15 GDP growth	1.0	2.0	2.6	2.6
Growth of relevant foreign markets	1.4	5.6	6.3	6.3
World import volumes, excluding EU	3.1	6.6	7.3	7.3
Oil prices, (Brent, US$/barrel)	24.8	24.3	24.3	24.3

Source: European Commission