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COMMISSION OPINION

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on the Draft Budgetary Plan of Ireland

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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 2018 submitted on 16 October 2017 by Ireland, the Commission has adopted the following opinion in accordance with Article 7 of Regulation (EU) No 473/2013.
4. 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 2017, it should achieve an annual fiscal adjustment of 0.6% of GDP or more towards the MTO. In 2018, it should pursue a substantial fiscal effort, taking into account the need to ensure the sustainability of Ireland's public finances. According to the commonly agreed adjustment matrix under the Stability and Growth Pact, that adjustment translates into a requirement of a nominal rate of growth of net primary government expenditure, which does not exceed 2.4% in 2018, corresponding to an annual structural adjustment of at least 0.6% of GDP. As its debt ratio was 76.9% of GDP in 2015, during the three years following the correction of the excessive deficit Ireland is also subject to the transitional arrangements as regards compliance with the debt reduction benchmark.
5. The macroeconomic scenario underlying the Draft Budgetary Plan is plausible. It assumes that economic growth will remain robust, mostly in line with the April 2017 Stability Programme. The macroeconomic assumptions for 2017 in the Draft Budgetary Plan diverge marginally from the Commission 2017 autumn forecast, while the two are more alike for 2018 and 2019. The Commission takes a more optimistic approach as regards intangible investment and assumes that it will not decline in the second half of 2017. Risks to the macroeconomic projections underlying the Draft Budgetary Plan are tilted to the downside. The most important sources of uncertainty relate to the outcome of negotiations between the United Kingdom and the EU, as well as potential changes to United States tax and trade policies, to which Ireland is highly exposed as a small and very open economy.
6. Ireland complies with the requirement of Regulation EU No 473/2013 that the draft budget has to be based on independently endorsed or produced macroeconomic forecasts. The macroeconomic forecasts underlying the Draft Budgetary Plan have

been endorsed as within the range of appropriate forecasts by the Irish Fiscal Advisory Council.

7. The Draft Budgetary Plan projects a general government deficit of 0.3% of GDP in 2017, slightly less than the 0.4% of GDP predicted in the 2017 Stability Programme. The progress compared to the 2017 Stability Programme is mostly due to the improved output projection. For 2018, the Draft Budgetary Plan targets a general government deficit of 0.2% of GDP, slightly above the target of 0.1% of GDP included in the 2017 Stability Programme, prepared under no-change-policy assumptions. On the basis of the information provided in the Draft Budgetary Plan, the structural deficit[1] is estimated at 1.1% of GDP in 2017 and 0.6% in 2018, broadly in line with the estimate derived from the 2017 Stability Programme.

   The Draft Budgetary Plan estimates gross debt to fall to 70.1% of GDP in 2017 and to reach 69.0% in 2018, contingent on still robust GDP growth and the realisation of primary budget surpluses. The improvement (by 2.8 and 2.2 % of GDP, respectively) compared to the projections in the 2017 Stability Programme is primarily due to a combination of the carry-over effect of higher-than-previously-expected nominal GDP in 2016 and a lower absolute level of debt at the end of 2017. However, due to the impact of multinational companies on Ireland's GDP and GNP, these macro-aggregates tend to overstate the actual size of the domestic economy[2]. A range of other metrics, including a debt-to-modified GNI ratio, shows that the stock of debt remains high. Reflecting the historically low euro area sovereign bond yields, based on the information included in the Draft Budgetary Plan, interest expenditure in Ireland is expected to fall from 2.2% of GDP in 2016 to 2.0% in 2017 and to decrease further by 0.1% of GDP next year. The picture stemming from the Draft Budgetary Plan is broadly confirmed by the Commission forecast.

8. The DBP for 2018 includes some reductions to personal income tax of around 0.1% of GDP, mainly through cuts in the Universal Social Charge rates, an income tax band change and increases on certain tax credits, as well as new spending initiatives of more than 0.4% of GDP. These revenue decreasing measures will be partly financed by several revenue raising measures, including an increase in stamp duty for commercial property purchases, a reduction in capital allowances for intangible assets, an increase in excise duties on tobacco products, the introduction of a tax on sugar-sweetened beverages, and by a range of tax compliance initiatives, which reduce the overall net impact of the budgeted measures to nearly -0.2% of GDP.

9. The Commission 2017 autumn forecast projects a general government deficit of 0.4% of GDP, 0.1 % of GDP higher than in the Draft Budgetary Plan. This reflects more conservative revenue estimates given the shortfalls in the year through September cash returns. The Commission 2017 autumn forecast projects the general government deficit to fall to 0.2% of GDP in 2018, in line with the Draft Budgetary Plan estimates. Risks associated with the Draft Budgetary Plan and the Commission budgetary projections are on the downside and mainly relate to uncertainties surrounding the macroeconomic outlook and the volatility of some sources of

[1] Cyclically adjusted balance net of one-off and temporary measures, recalculated by the Commission using the commonly agreed methodology.

[2] A Modified Gross National Income (also known as GNI*), recently provided by the Irish statistical authorities, more accurately reflects the income of Irish residents than GDP. It differs from actual GNI in that it excludes inter alia the depreciation of foreign-owned, but Irish-resident, capital assets (most notably intellectual property and assets associated with aircraft leasing) and the undistributed profits of firms that have re-domiciled to Ireland.

government revenues. Exposure of debt projections to interest rate changes is limited, as most of the outstanding stock is at fixed rates. Therefore, downside risks to the debt projections relate more to changes to the economic outlook. Moreover, the planned early repayment of EUR 5.5 billion in EU-IMF Programme loans from the IMF, Sweden and Denmark has the potential to generate interest savings while providing an opportunity to further smoothen and extend the debt maturity profile.

10. The Draft Budgetary Plan does not include sufficient information to assess compliance with the transitional arrangements to make sufficient progress towards compliance with the debt reduction benchmark. Based on the Commission 2017 autumn forecast, Ireland is projected to make sufficient progress towards compliance with the debt reduction benchmark in 2017 and 2018.

11. The expenditure benchmark points to some deviation from the requirement of a real rate of growth of net primary government expenditure, which should not exceed 1.2% in 2017, based on the Draft Budgetary Plan and significant deviation based on the Commission forecast. The improvement of the structural balance, both on the basis of the Draft Budgetary Plan and Commission forecast, is above or in line with the required adjustment of 0.6% of GDP, but is positively influenced by the estimate of potential output growth. Given the very open nature of the Irish economy and the volatility of potential GDP estimates, the expenditure benchmark provides a more appropriate yardstick for fiscal policy. However, it does not capture the additional revenue linked to the continued non-indexation of income tax bands, which is considered to be of a permanent nature. Following an overall assessment of the Draft Budgetary Plan, there is thus a risk of some deviation in 2017 both based on the Draft Budgetary Plan and Commission forecast. Nonetheless, the average deviation over 2016 and 2017 taken together would still be well above the applicable significant deviation threshold of 0.25% of GDP based on the Commission forecast (0.6% of GDP), with this conclusion confirmed also after taking into account the non-indexation of income tax bands. Therefore, the overall assessment points to a risk of a significant deviation over 2016 and 2017 taken together.

    For 2018, based on the Draft Budgetary Plan, Ireland is projected to have a structural balance of -0.6% of GDP, slightly less than the MTO of -0.5%. Based on the Commission forecast, Ireland is projected to achieve the MTO in 2018. The planned growth rate of government expenditure, net of discretionary revenue measures based on the Draft Budgetary Plan, is expected to be slightly below the requirement of a nominal rate of growth of net primary government expenditure which does not exceed 2.4%. The planned change in the structural balance points to a small deviation. In turn, over 2017 and 2018 together, the expenditure benchmark pillar suggests that Ireland is at risk of some deviation from the requirements. Based on the Commission forecast, the expenditure benchmark points to some deviation in 2018. The projected improvement in the structural balance of 0.8% of GDP is above the recommended fiscal effort. Over 2017 and 2018 together, the expenditure benchmark suggests that Ireland is at risk of a significant deviation from the requirements. However, when the additional revenue from the continued non-indexation of income tax bands in 2017 and 2018 is taken into consideration, the average deviation based on the expenditure benchmark pillar is below but close to the applicable significant deviation threshold of 0.25% of GDP. Therefore, the overall assessment points to a risk of some deviation in 2018 from the required adjustment path according to the two-year average rule.

12. With regard to the structural part of the fiscal recommendations contained in the Council Recommendation of 11 July 2017[3], the Commission welcomes the use of income from the sale of government's shares in state-owned banks to reduce the debt. By the same token, the recent redemption by the National Asset Management Agency of the final EUR 500 million of the government-guaranteed debt, three years ahead of the target, marks another important step toward restoring full financial market confidence in the Irish sovereign. As for the part of the recommendation to limit the scope of the number of tax expenditures and broaden the tax base, measures outlined in the Draft Budgetary Plan are mixed. Some progress has been made in enhancing the quality of expenditure through a new spending review process which, in its first three-year cycle, has focussed on specific critical spending areas, representing around 30% of current government expenditure, such as drug costs in the health sector, disability and employment programmes in the area of social protection, and public transport.

13. 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 period to make sufficient progress towards compliance with the debt reduction benchmark, is broadly compliant with the provisions of the SGP. The Commission invites the authorities to stand ready to take further measures within the national budgetary process to ensure that the 2018 budget will be compliant with the SGP.

    The Commission is also of the opinion that Ireland has made some progress with regard to the structural part of the fiscal recommendations contained in the Council Recommendation of 11 July 2017 in the context of the 2017 European Semester and invites the authorities to make further progress. A comprehensive assessment of progress made with the implementation of the country-specific recommendations will be made in the 2018 Country Reports and in the context of the country-specific recommendations to be proposed by the Commission in May 2018.

Done at Brussels, 22.11.2017

For the Commission
Pierre MOSCOVICI
Member of the Commission

[3] Council Recommendation of 11 July 2017 on the 2017 National Reform Programme of Ireland and delivering a Council opinion on the 2017 Stability Programme of Ireland (OJ C 261, 9.8.2017, p. 26-30).