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Post-Programme Surveillance Report

Ireland, Spring 2019

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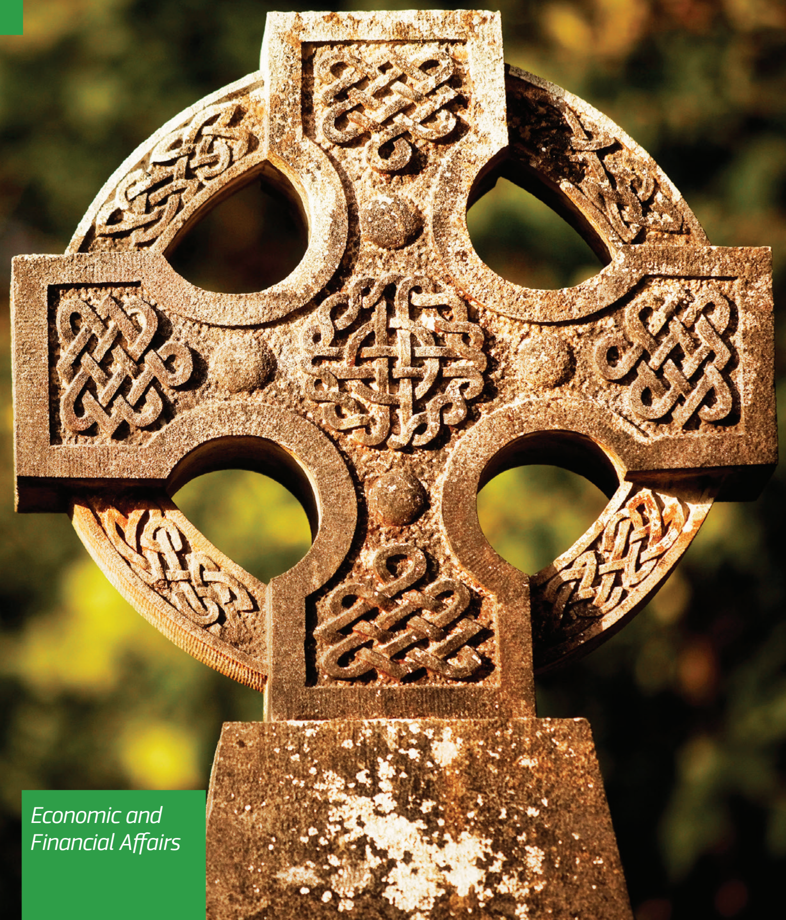
EUROPEAN ECONOMY



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European Commission
Directorate-General for Economic and Financial Affairs

Post-Programme Surveillance Report

Ireland, Spring 2019

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Institutional Paper 112

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This report reflects information available up until 20 June 2019.

([1]) The report was adopted as Commission Communication C(2019)6391 on 29 August 2019, accompanied by a Staff Working Document.

([2]) ECB Staff participated in this mission, and in the drafting of this report, in accordance with the ECB's competences and thus provided expertise on financial sector policies and macro-critical issues, such as headline fiscal targets and sustainability and financing needs.

ABBREVIATIONS

AIB	Allied Irish Banks
BTL	Buy-to-let
BTR	Build-to-rent
CBD	Consolidated banking data (database)
CBI	Central Bank of Ireland
CCyB	Counter-cyclical capital buffer
CET1	Common Equity Tier 1
CSO	Central Statistics Office Ireland
CSR	Country Specific Recommendation
DHPLG	Department of Housing, Planning and Local Government
ECB	European Central Bank
EFC	Economic and Financial Committee
EFSF	European Financial Stability Facility
EFSM	European Financial Stabilisation Mechanism
ESB	Electricity Supply Board
ESM	European Stability Mechanism
ESRI	Economic and Social Research Institute
FTB	First-time buyer
GDP	Gross Domestic Product
GNI*	Modified Gross National Income
GNP	Gross National Product
HBFI	Home Building Finance Ireland
HICP	Harmonised Index of Consumer Prices
ICT	Information & Communication Technology
IFAC	Irish Fiscal Advisory Council
IFRS	International Financial Reporting Standard
IMF	International Monetary Fund
IMHO	Irish Mortgage Holders Organisation
IP	Intellectual property
LFS	Labour Force Survey
LTI	Loan-to-income
LTV	Loan-to-value
MIP	Macroeconomic Imbalance Procedure
MTO	Medium-Term Objective
MREL	Minimum requirements for own funds and eligible liabilities
NESC	National Economic and Social Committee
NPLs	Non-performing loans
NTMA	National Treasury Management Agency
OECD	Organisation for Economic Co-operation and Development
PBP	Parliamentary Budget Office
PDH	Primary Dwelling Home
PRS	Private rented sector
PPS	Post-programme surveillance
SCSI	Society of Chartered Surveyors Ireland
SME	Small and medium sized enterprises
SOLAS	An tSeirbhís Oideachais Leanúnaigh agus Scileann (Further Education and Skills Service)
SSM	Single Supervisory Mechanism
SyRB	Systemic risk buffer
USC	Universal Social Charges
VAT	Value added tax
y-o-y	Year-on-year

EXECUTIVE SUMMARY

Staff from the European Commission, in liaison with staff from the European Central Bank (ECB), visited Dublin from 21 to 24 May 2019 for the eleventh post-programme surveillance (PPS) review for Ireland. The main objective of PPS is to assess the country's capacity to repay the loans granted under the former EU-IMF financial assistance programme and, if necessary, to recommend corrective actions. Staff from the European Stability Mechanism participated in the meetings in the context of its Early Warning System.

The short-term outlook for the Irish economy is for solid growth, but external risks are significant. Strong employment growth, in conjunction with increasing wages, continues to support household income and private consumption. Construction investment is expanding at a solid pace, though still from a low base. The tightening of the labour market and diminishing spare capacity point to an economy possibly operating above its potential. Significant uncertainty continues to surround the economic outlook. This uncertainty mostly relates to the future relationship between the UK and the EU, as well as to changes in the international taxation and trade environment.

Public finances have further improved on the back of a strong economy, but vulnerabilities remain. The public debt ratio has declined, but Ireland is still running high levels of debt, which limits the room to respond to negative economic shocks. Risks to the fiscal outlook remain skewed to the downside, mainly reflecting uncertainty as regards the economic outlook, the sustainability of the current level of some sources of government revenue, notably corporate tax, and over-spending within the health sector. Given the favourable cyclical position and the buoyant corporate tax revenue, building fiscal buffers, inter alia, by strengthening the rainy day fund, and broadening the tax base would increase the resilience of public finances to adverse shocks.

Non-performing loans have further declined, but the level of long-term arrears remains relatively high. Following a slowdown in the reduction in non-performing loans (NPLs) in 2017, the pace picked up during 2018, supported by sales. This brought the aggregate NPL ratio to 7.8% at the end of the third quarter. Although banks seem to be on track to meet their NPL target, significant heterogeneity continues to exist among Irish banks. The pace at which long-term arrears are being reduced is, however, significantly lower. Capital positions of Irish banks have increased further from relatively high levels, but provisioning continues to remain low relative to euro area averages, even after considering the high capital positions. In the current environment where some of the Irish banks are producing low returns, their internal capital generation remains weak. This, combined with the low provisioning levels, may create obstacles for banks in their efforts to reduce non-performing loans further.

Increases in property prices and rents have recently abated, but their levels remain high. Overall, housing supply remains below the level required to address long-term housing demand. While non-professional landlords continue to dominate, institutional investors are increasingly present in the private rental market, apparently contributing to housing supply. The construction sector faces cost pressure amidst existing skill shortages.

Risks for Ireland's capacity to service the European Financial Stability Mechanism and European Financial Stability Facility debt remain low. The sovereign's financing situation is comfortable and the National Treasury Management Agency plans to maintain strong cash buffers in advance of peak redemptions in 2020. Market access conditions for the Irish sovereign remain favourable. The debt sustainability analysis shows that, while improving, public debt remains vulnerable to adverse economic shocks.

The next PPS mission is planned to take place in autumn 2019.

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1. INTRODUCTION

Staff from the European Commission, in liaison with staff from the ECB, visited Dublin from 21 to 24 May 2019 for the eleventh post-programme surveillance mission to Ireland. Under PPS, the Commission undertakes regular review missions to EU Member States, which previously had an EU-supported financial assistance programme. The objective of the PPS mission is to assess the economic, fiscal and financial situation to ensure the Member State maintains its capacity to service its debt to the EFSM, EFSF and bilateral lenders.([3]) Acting upon a proposal from the Commission, the Council could recommend corrective measures. As per Regulation (EU) 472/2013, the results of the PPS mission have to be communicated to the competent committee of the European Parliament, the Economic and Financial Committee, and the Irish Parliament.

([3]) Ireland has already repaid the outstanding bilateral loans from Denmark and Sweden, early and in full. Under Regulation (EU) No 472/2013, PPS will apply until at least 75% of the financial assistance received under the programme has been repaid. Under the current repayment schedule, PPS will last until 2031 at the earliest.

2. RECENT ECONOMIC DEVELOPMENTS AND OUTLOOK

2.1. MACROECONOMIC TRENDS

The outlook for GDP growth remains positive, albeit subject to heightened uncertainty. In 2018, Ireland's real GDP grew by 6.7%, well above the euro area average, while the GNP increased by 5.9%. GDP growth is expected to remain robust, although moderating in 2019 and 2020, due to a less benign external environment, including increased uncertainty.

The domestic economy is continuing apace propelled by consumption and construction investment. While the headline national accounts figures remain distorted by the activities of multinational companies, the underlying performance of the economy remains strong, too. *Modified domestic demand*, a measure of domestic activity that strips out some of the effects of multinationals, grew by 4.5% in 2018, driven by private consumption and construction investment.

Underlying investment performs strongly. In 2018, headline investment grew by 9.8%. Building and construction activity increased by 15.8%, though still from a low base, and is expected to maintain its momentum, supported by various government measures. However, headline investment remains heavily influenced by the large swings in imports of intellectual property (IP) services and purchases of aircraft. Underlying machinery and equipment investment (i.e. excluding planes) increased by 11.5% in 2018, although it has moderated somewhat at the end of 2018. However, this moderation was not matched by capital goods imports in monthly trade data, suggesting caution in the interpretation of the recent slowdown in underlying machinery and equipment investment, which can be prone to large revisions.

Employment shows no sign of slowdown, despite heightened external uncertainty. The unemployment rate continues to decline, reaching 5.0% in the first quarter of 2019. With skill and labour shortages emerging, non-Irish nationals are increasingly contributing to the labour supply. Migrants are notably hired in sectors with elevated vacancy rates, such as information and communications technology (ICT) and professional and scientific activities.([4]) Overall employment is expected to increase further, although at a moderating pace, in line with the projected slowdown in activity.

Growth in compensation per employee picked up in 2018 and is forecast to increase further, supporting household disposable income. In the year to the first quarter of 2019, average hourly earnings increased by 2.3%. Although stronger pressures occur in highly productive sectors dominated by multinationals, such as ICT and financial services, wage pressures also build up in domestic-oriented activities, such as construction, retail or transportation. In most sectors, increases in average earnings were larger in enterprises with less than 250 employees, which are typically less productive.([5]) As growth in nominal labour cost is well above the inflation rate, increasing real wages could dampen the competitiveness of domestic firms. Rising rental prices (see section 2.4) and the shortage of affordable housing could also exert upward pressures on wages and impact the attractiveness of Ireland as a destination of foreign direct investment.

Modest inflation supports household disposable income. HICP inflation reached 1.1% on average in the first five months of 2019, after 0.7% in 2018. Core inflation remains subdued, although it has increased in the first five months of 2019, boosted by the price of services. In particular, the price of restaurant and hotel services picked up in 2019, partly reflecting the impact of the VAT rate increase on tourism activities, while rental prices keep contributing significantly to inflation. By contrast, the downward trend in industrialised goods prices, which partly reflects the impact of quality measurement([6]), keeps dragging on the price of goods. Inflation is thus projected to remain moderate in 2019.

Net exports remain strong despite the less favourable global trade environment. Net exports contributed 4.3 pps. to GDP growth in

([4]) Central Bank of Ireland, Quarterly Bulletin 02, April 2019.
([5]) European Commission (2018), 2018 SBA Fact Sheet-Ireland.
([6]) J. Keating and M. Murtagh (2018), Quality adjustment in the Irish CPI, CSO meeting of the Group of Experts on Consumer Prices Indices, 7-9 May 2018.

2018. Exports increased by 8.9%, driven by pharmaceuticals and computer services, while imports increased by 7.0%, largely driven by aircraft for leasing and R&D services. Despite the less favourable global trade environment, net exports are expected to keep contributing positively to GDP growth, as exports of pharmaceuticals and ICT services, which make a significant share of Irish exports, are less sensitive to changes in the overall global demand. However, headline trade figures may continue to be influenced by contract manufacturing.

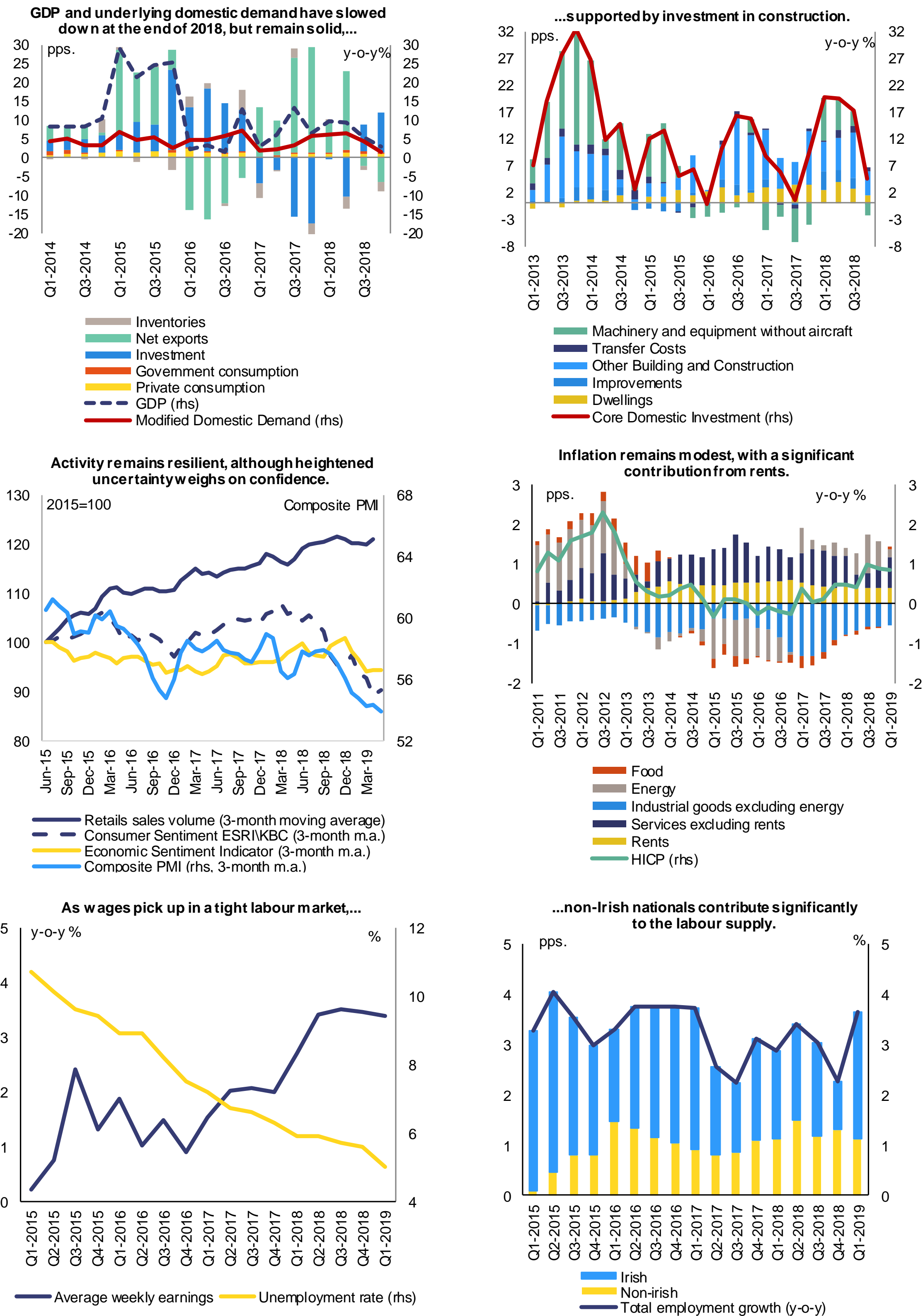
The macroeconomic outlook is clouded by uncertainty. This uncertainty mainly relates to the terms of the UK's withdrawal from the EU, an escalation in international trade tensions as well as to changes in the international taxation environment. The repatriation of profits by US multinationals following the US Tax Cuts and Jobs Act of December 2017 had a significant impact on Ireland's Balance of Payments in 2018. These financial flows are primarily linked to US multinationals' tax optimisation activities, and likely had a limited impact on physical capital and underlying economic activities.([7]) There is no evidence so far of a relocation of productive activities from Ireland to the US. Other possible changes in the international tax environment, such as digital taxation, could affect Ireland. More generally, the difficult-to-predict activities of multinationals could drive headline growth in either direction.

In the absence of major negative external shocks, the risk of overheating could increase in the coming years. The tightening of the labour market and diminishing spare capacity point to an economy possibly operating above its potential. Although residential construction remains of critical importance in the context of persistent housing undersupply, a further acceleration of construction activity could fuel overheating pressures against the background of increasing capacity constraints in the sector. The use of volatile and potentially short-lived foreign-company sourced corporation tax receipts to stimulate domestic demand could also fuel overheating.([8])

([7]) Central Bank of Ireland, Quarterly Bulletin 02, April 2019.

([8]) Irish Fiscal Advisory Council (2019), Fiscal Assessment Report, June 2019.

Graph 2.1: **Recent economic developments**



Source: European Commission, Central Statistics Office, Markit, ESRI\KBC.

2.2. PUBLIC FINANCES

Public finances are further improving. The headline government position turned from a deficit of 0.3% in 2017 to a balance in 2018 on the back of a strong economy. This is the first balanced position since 2007. Taking into account a one-off factor,[9] the underlying balance was 0.1% of GDP, an improvement of 0.4 percentage points vis-à-vis the previous year's underlying position. Tax revenues, including social security contributions, were up by 7.9% in 2018, driven by strong corporate tax revenues. Government expenditure increased compared to the previous year by 6.0%. A continued fall in the interest burden facilitated the deficit reduction.

Cash returns were broadly in line with target in the first five months of 2019. Tax receipts to end of May 2019 were up by 5.7% y-o-y but 1.1% below budget targets. The personal income tax revenue (7.8% y-o-y) is slightly (-0.6%) behind profile. Corporate taxes remain also below profile (-11.4%), but it is too early to discern trends in this category, the bulk of which is collected in June and November. Overall expenditure was up by 8.2% and 0.6% below profile. Current expenditure was up by 6.7%, broadly in line with profile. Capital expenditure (31.8% y-o-y) was 4.1% behind profile through May 2019. Healthcare spending remained behind its allocation, but the pace of spending growth accelerated in May by 9.0% y-o-y. In general, and as in previous years, the departments are likely to ensure their spending limits are fully utilised by the end of the year.

Despite the recent improvements, risks to the fiscal outlook remain. Revenues are expected to remain buoyant in 2019, with many tax headings experiencing sizeable increases. The 2019 Stability Programme Update estimates an increase in general government expenditure of EUR 3.4 billion, 4.1% higher than its 2018 level. According to the Commission spring forecast, the headline government balance is projected to remain unchanged in 2019 and to improve to a surplus of 0.3% of GDP in 2020, under a no-policy-change assumption. Acknowledging the difficulties in estimating Ireland's position in the economic cycle, after a deterioration in 2018, the structural deficit is expected to improve to about 1¼% in 2019 and further to ½% of GDP in 2020, thus reaching the medium-term budgetary objective (MTO).[10] Risks to the fiscal outlook remain skewed to the downside, mainly reflecting uncertainty as regards the economic outlook, the sustainability of the current level of some sources of government revenue (notably corporate tax) and over-spending within the health sector.

Ireland is still running high levels of debt, which limits the room to respond to negative economic shocks. The general government debt declined to 64.8% of GDP at end-2018. It is projected to fall further to 61.3% of GDP in 2019 and 55.9% in 2020. This is contingent on continued stable economic growth and positive primary balances. However, public debt remains high as a proportion of modified GNI (GNI*)[11], estimated at around 107% in 2018.[12] Although improving, public debt sustainability remains vulnerable to adverse economic shocks (Annex 2).

2.3. FINANCIAL SECTOR

Banks continue to increase their capital positions, but they also face important challenges. The CET1 ratio of the Irish consolidated banking sector, which includes both domestic- and foreign-owned banks, increased by 1 percentage point to 23.4% over the year to September 2018, placing banks well above the euro area average. Banks maintain comfortable net interest margins, which is mainly due to lower funding costs and interest rates on mortgage loans and loans to small and medium-sized enterprises. Aggregate provisioning remains low relative to euro area averages, hovering at 32%. Banks are

(9) This refers to a deficit-increasing consultants' pay settlement (0.1% of GDP).

(10) Since the previous PPS mission, the estimate of potential GDP growth has significantly changed, on the back of methodological adjustments and taking into account new data on capacity utilisation that have become available in the meantime.

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

(12) Department of Finance (2019), Stability Programme Update 2019.

moving ahead with the reduction of non-performing loans, driven by sales and securitisations. However, the share of mortgages in arrears for more than two years remains high. Property-related new lending may further increase the banks' exposure to developments in the housing market and warrants close attention. The elevated uncertainty in the external environment represents an additional challenge.

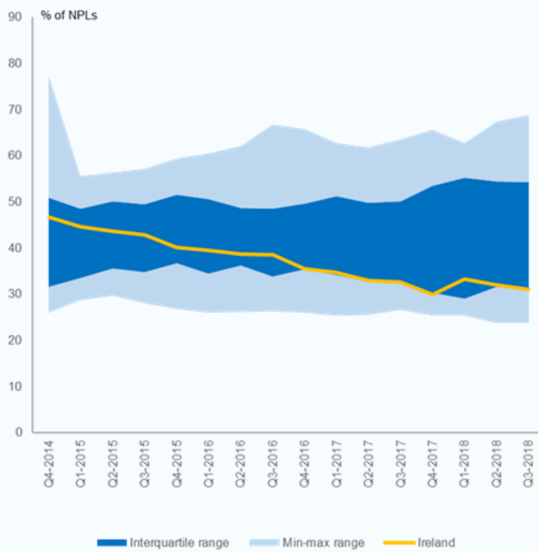
Credit growth remains subdued. Credit for primary dwellings to households has continued to expand, growing by 4.7% in 2018. This increase was completely offset by declining credit to borrowers financing buy-to-let properties and consumer loans. As a result, the stock of credit advanced to households has been broadly stable over the past year. Total credit to domestic non-financial companies (NFCs) increased very modestly towards the end of 2018, led by the pharmaceutical sector. Credit to construction and real estate companies has shown a marked decline since 2007, down from EUR 115 billion in 2008 to EUR 13 billion in 2018. The decline, however, appears to have ended in 2018. Concerning the composition of new loans, there is an increasing demand for loans with longer rate fixations. However, no bank currently offers mortgage loans with a fixation period of more than five years. Moreover, nearly three quarters of outstanding mortgage loans have floating rates or fixation periods below one year.

Aggregate provisioning has stabilised at low levels in 2018, relative to euro area average. The stabilisation follows a prolonged period of a declining coverage ratio. Still, the coverage rate of around 30% in the third quarter of 2018 compares low with the euro area average of 49%. Taking into account improving macroeconomic conditions improving macroeconomic conditions (e.g. rising property prices) and changes in the NPL portfolio (e.g. higher share of collateralised loans which carries lower provisioning), the coverage ratio is lower than that of other EU banks (see Box 1). It is important to retain prudent levels of loan loss reserves to be able to continue with reducing non-performing loans, and also in the light of new regulatory and supervisory requirements, including IFRS 9 provisioning rules that have been in place since 1 January 2018.

Box 2.1: Provisioning levels of Irish banks

The aggregate provisioning levels of Irish banks ([1]) have been declining and have stabilised at levels lower than in other European countries (Graph 1). This could be due to a number of reasons. First, there has been a significant change in the composition of NPLs held by Irish banks over the past few years. In particular, the share of NPLs of non-financial corporations (NFCs) dropped to 28% by September 2018, down from 50% of the gross NPLs at end-2014. Since NFC loans are less likely to be collateralised – and since collateralised loans tend to carry lower provisioning levels – this evolution could be driving some of the results. Second, Irish banks have been more active users of loan forbearance, which represents more than two-thirds of all NPL exposures. Assuming that these restructuring solutions have proven to be durable, i.e. not resulting in re-defaults and re-restructurings, these exposures would then carry lower provisioning levels. Third, the Irish real estate market has experienced a significant bounce-back since the depth of the crisis in the years 2010 and 2012. This could have increased collateral values and rendered part of provisioning made before those years unnecessary.

Graph 1: Provision ratios of EU banks



Note: The data includes both domestic and foreign-owned banks.
Source: *ECB, Consolidated Banking Data (CBD).*

Irish banks' low provisioning levels relate mainly to the high share of collateralised household loans. Graph 2 compares the provisioning levels of Allied Irish Banks and Bank of Ireland with the rest of the sample included in the 2018 EBA Transparency Exercise using mid-2018 data. Provisioning ratios of the two Irish banks are below the other EU banks when all exposures are considered, even after accounting for forborne loans, (Graph 2, panel a). However, the two Irish banks become comparable with the EU sample median once we focus on household exposures, which are dominated (both in Ireland and elsewhere in the EU) by home loans that are collateralised by the underlying real estate, (Graph 2, panel b). For these exposures, the provisioning levels of the two Irish banks are quite close to the EU median for *non-forborne* loans. This is also the case for one of the two banks for forborne loans, although the other bank [BOI] still has a much lower average provisioning level than the EU sample.

([1]) This box compares provisioning levels of the two largest Irish banks, Allied Irish Banks and the Bank of Ireland, with other large European banks using publicly available data from the European Banking Authority's EU-wide transparency exercises.

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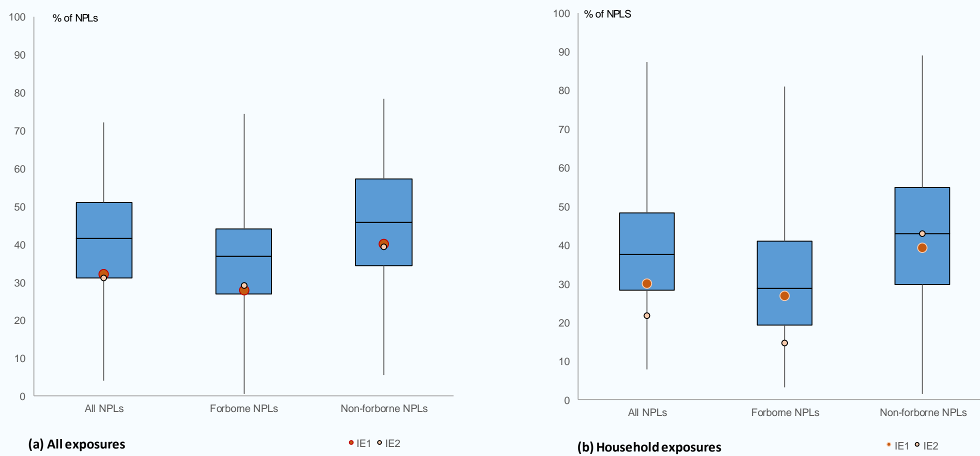
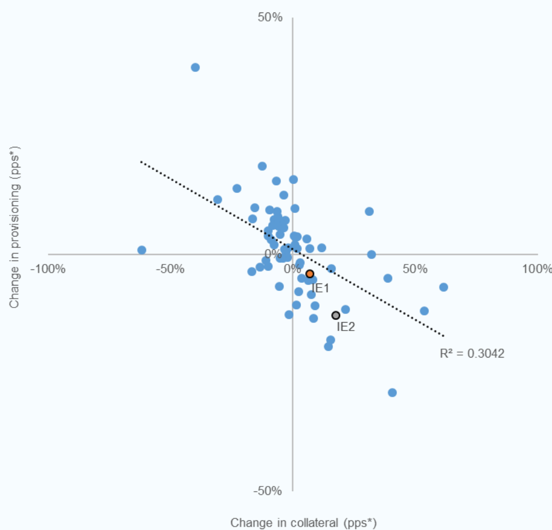
Box (continued)

Graph 2: Comparative provisioning ratios (June 2018 figures for sampled EU banks)



Note: The figures plot around 110 EU banks. The box-and-whisker plots above show the 25th and 75th percentile ranges in the blue boxes, separated by the median line, and the minima and the maxima (i.e. lines extending above and below the boxes). Banks with incomplete data were excluded from the sample, including two Irish banks, i.e. the Citibank Holdings Ireland Limited and DEPFA BANK plc.
Source: *EBA Transparency Exercise (2018), Commission Services*

Graph 3: Changes in provisioning and collateral ratios for household exposures of sampled banks (comparison of June 2018 figures to December 2014)



*Note: The figure plots around 90 EU banks that have reported their end-2014 and mid-2018 data. Some of the banks with incomplete data were eliminated. *The horizontal and vertical axes represent, respectively, the changes in collateral and provisioning ratios from end-2014 to end-2018 in percentage points (pps). Both ratios are calculated as percentages of gross non-performing loans at those dates.*
Source: *EBA Transparency Exercise (2018, 2014), Commission Services.*

(Continued on the next page)

Box (continued)

A time-series analysis confirms that the changing collateral values are also a major contributing factor to the low provisioning levels of the two Irish banks. The changes in collateral values and provisioning levels over the end-2014 and end-2018 period seem to be negatively correlated (Graph 3). Indeed, higher collateral values tend to lower the credit risks of banks. In the case of Ireland, at least one bank included in the two sampled periods showed a rise in collateral values, thanks to buoyant real estate prices. This has allowed the two banks to reduce the provisioning levels, almost at a one-to-one ratio.([2])

The declining provisioning levels of Irish banks appear to be mainly due to increasing real estate prices and the increasing share of residential mortgage loans in the pool of NPLs held by Irish banks. However, concerns about the adequacy of the provisioning levels of Irish banks remain and they are linked to collateral access. Ireland has consistently ranked among the poorest performers on World Bank's 'Doing Business' survey in terms of the strength of contract enforcement and time for resolving insolvency proceedings. The average time to enforce a contract is 650 days. For residential mortgages, the time to repossession commonly reported by authorities and stakeholders is often much higher. In addition, a significant proportion of the pool of NPLs held by Irish banks have long-term arrears, often more than five years, which tend to be more difficult to resolve. These factors alone would suggest a weaker link between real estate prices and provisioning levels.

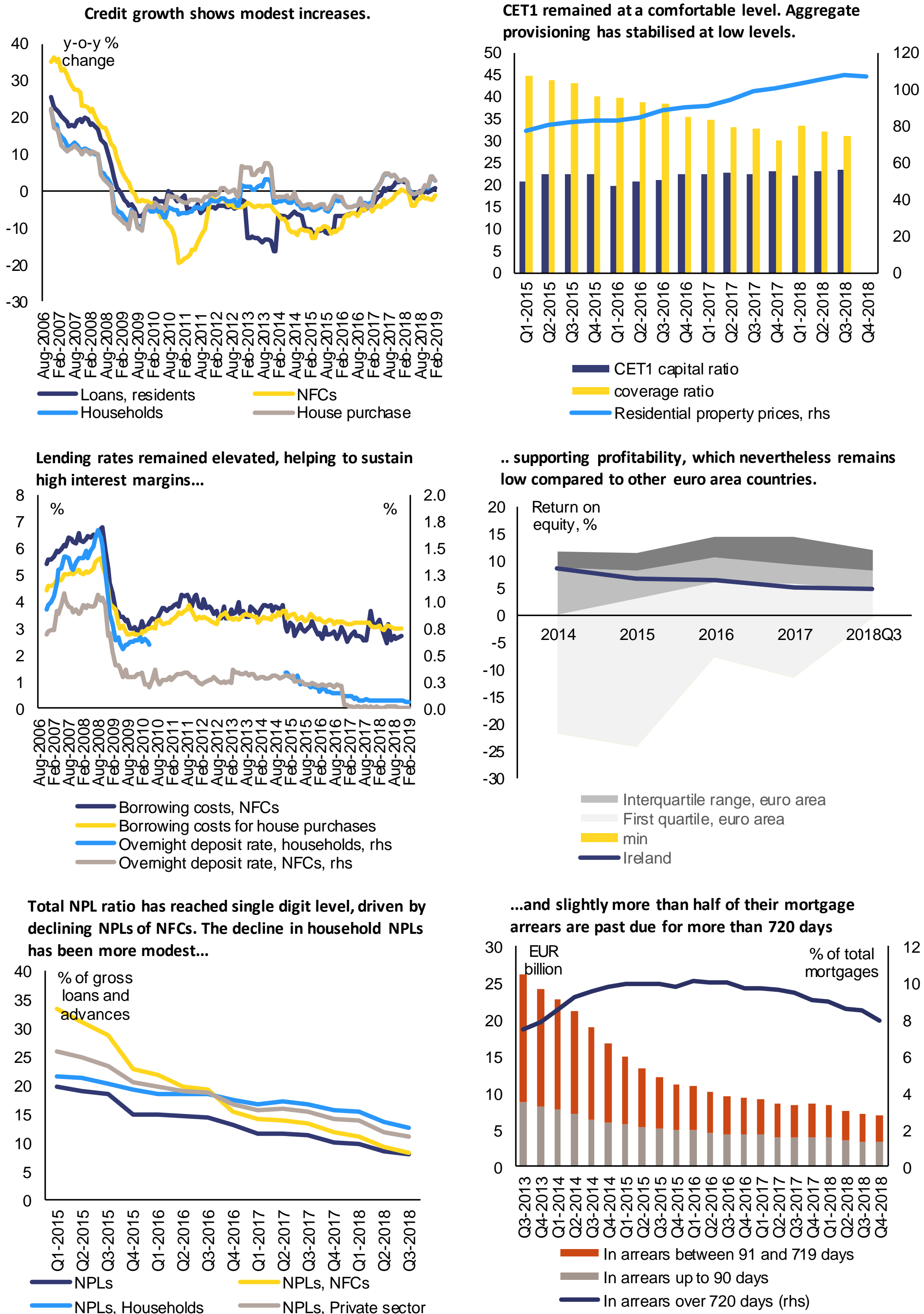
Maintaining prudent levels of provisioning would facilitate the further cleaning up of non-performing loans without putting at risk the solvency of affected banks. The recent reduction in non-performing loans has been supported by loan sales and the setup of off-balance sheet securitisation vehicles. So far, these operations have not resulted in large losses for Irish banks However, this observation does not guarantee that provisioning levels are adequate. The spot prices for NPLs on the secondary markets may exceed the book values of those assets due to a number of reasons. One reason is the newly implemented IFRS 9 standard. While the new standard requires banks to take account of the lifetime expected losses for their higher risk (i.e. Stage 2 and 3) loans, market participants often have a much shorter time horizon, resulting in a higher price.

([2]) A deeper empirical analysis (not included here) confirms that the divergences of the provisioning levels of the two Irish banks from the EU sample mean lose their statistical significance once the collateral values are taken into account. The same does not hold for any other indicators.

The stock of NPLs continues to decline, helped by portfolio sales. According to consolidated banking data, including both domestic- and foreign-owned banks, published by the ECB (see Graph 2.2), the overall NPL ratio fell to 7.8% of gross loans in the third quarter of 2018, down from 11.2% a year earlier. The NPL ratio for the private sector, including both households and non-financial corporates, remained higher at 10.9% of gross loans at the end of the third quarter of 2018, down from 15.4% a year earlier. The decline was driven by a marked improvement in the asset quality of non-financial corporations, with a NPL ratio of 8.1% in the third quarter of 2018, down from 13.4% a year earlier. In contrast, the NPL reduction for the household sector, although significantly more than in recent years, has been more modest. The stock of household NPLs was EUR 16.9 billion (NPL ratio of 12.5%), which made up around 70% of all NPLs. Unlike recent years, where NPL reduction has been driven by restructuring activity, the recent drop is mostly due to NPL sales and off-balance sheet securitisations. Reducing household NPLs, especially for primary dwelling home borrowers, continues to be the main challenge.

Long-term mortgage arrears have declined at a slower pace and their level remains high. At the end of 2018 the total balance of mortgage loans that were more than 90 days past due was EUR 12.9 billion (representing 11.0% of all mortgages), down from EUR 15.5 billion (12.7%) a year ago. Of those mortgage loans, approximately two thirds relate to primary dwelling homes, while the remaining were related to buy-to-let properties. At end-2018, the total stock of long-term mortgage arrears (i.e. more than 720 days past due) was EUR 9.3 billion, representing 8.0% of all mortgages or 72% of all mortgage loans with arrears of 90 days or more. There are several reasons for the slow decline in long-term arrears. A substantial number of borrowers in long-term arrears are unwilling – or unable – to engage with their banks. In addition, repossession activity remains relatively limited, as banks face reputational risks when exercising collateral enforcement options, especially on vulnerable borrowers, while the length of proceedings continues to be protracted. Finally, the use of contractual write-offs is also limited.

Graph 2.2: **Recent financial sector developments**



Source: European Central Bank and Central Bank of Ireland

2.4. PROPERTY MARKET AND CONSTRUCTION

Residential price inflation eased in recent months, but price increases outside Dublin remain high. Country-wide, annual residential price inflation declined from a peak of 13.3% in April 2018 to 3.1% in April 2019, the lowest rate since July 2013. The slowdown was mainly driven by Dublin where annual inflation fell by 12.6 pps. to 0.5%. Affordability constraints and the increase in the number of properties available for sale on the market (+40% y-o-y in March 2019([13])) seem to be reasons behind the slowdown in Dublin. Outside Dublin, residential price inflation remained high at 5.6% in April 2019. Between 2016 and the first half of 2018, residential prices grew faster at the lower end of the market, by up to 15% y-o-y among the bottom three deciles compared to 6% among the top three deciles.([14])

Wages in the construction sector and prices of residential development land are driving construction costs. Labour costs in the construction sector increased by 6.1% y-o-y in the last quarter of 2018, well above the 1.2% growth experienced in the same period last year, mainly driven by skill shortages. The price of land for residential development increased by 12% in 2018. According to the Society of Chartered Surveyors, this rate could moderate to 8% in 2019, partly due to the effect of the vacant site levy.([15]) Persistent gaps in the data on residential development land and transaction volumes continue to hamper the monitoring of land prices and the impact of recent policy reforms.

Prices for building and construction materials have recently accelerated. Having moved sideways in the last quarter of 2018, prices for building and construction material have increased by 1.9% in the first four months of 2019. This could be a sign of construction supply chains approaching maximum capacity, according to a market intelligence survey carried out by Turner & Townsend in 2018.([16]) Moreover, Ireland is highly dependent on the UK for the supply of certain construction materials.([17]) This risks creating delays in accessing materials and further inflationary pressures once the UK would have withdrawn from the EU.

The rental sector continues to grow. The share of households renting privately has increased by 2 pps. to 30% in the three years to 2018.([18]) Affordability constraints and the increased number of internationally mobile workers appear to be the main factors supporting the shift from owner-occupation to private rent.

Housing rental inflation, although still high, has recently moderated. Annual private rent inflation amounted to 5.2% in April 2019, 1.4 pps. down from its last peak of 6.6% in November 2018. The rise in the number of properties available to rent nationwide, +11% y-o-y in January 2019, may have supported this recent slowdown. The increasing presence of large-scale investors in the rental market (see below) may also have contributed to the supply of rental housing. Still, rent levels continue to be high and are now 27% above their peak recorded in 2008.

Non-household buyers([19]) have become more prominent in the residential property market. Dwellings purchased by non-household buyers accounted for 16.2% of the total volume sales in 2018, i.e. 1.6 pps. more than in 2017 and 12.8 pps. more than in 2010. While the annual growth of the value of non-household transactions has been strong (+21% y-o-y in March 2019), the annual increase of household transactions moderated to 3% in March 2019, from a peak of 18% in May 2018.

Investments in the private rented sector (PRS) surged in 2018.([20]) Pure residential investments

([13]) Daft (2019), The Daft.ie House Price Report 2019 Q1.
([14]) CBI (2018), Residential property price segments and mortgage finance.
([15]) SCSI (2019) Annual Commercial Property Report.
([16]) Turner & Townsend (2018), Republic of Ireland market intelligence report. Autumn 2018.
([17]) Houses of the Oireachtas (2019), Examining the potential impacts of Brexit on Ireland's Housing Market. February 2019. According to Economic and Social Research Institute (ESRI), nearly 50% of imported plumbing and electrical fittings and prefabricated buildings and around 30% of wood products used in the Irish construction sector are imported from UK.
([18]) Calculations based on the annual average of quarterly Labour Force Survey (LFS) data.
([19]) Non-household buyers comprise private companies, charitable organisations and state institutions.
([20]) The scope of these investments is limited to transactions involving income-producing assets. Consequently, loan sales and transactions involving properties without a lease

(excluding mixed-use schemes with a substantial residential content) amounted to around EUR 1.1 billion in 2018. This represents a 250% increase with respect to 2014([21]) and 30% of last year's total property investment. Investments were concentrated in Dublin. The interest in PRS was primarily driven by pension funds trying to take advantage of the high correlation between real wages and residential rents.([22])

Build-to-rent investments are driving the activity in the PRS sector. While early movers into the PRS market were able to build up their portfolio by acquiring stalled for-sale schemes, the dry-up of standing investment opportunities together with more flexible apartment design standards([23]) may have supported the recent transition from buy-to-let (BTL) to build-to-rent (BTR) options. Among the latter, forward purchase of properties under construction has become predominant vis-à-vis alternatives such as forward funding or direct construction.([24]) Under this forward purchase option, development risks, including those associated with unexpected construction cost increases, remain with the developers and are not externalised to, often overseas, investors.

There are few non-professional individual investors entering the rental market. These investors, who usually resort to BTL mortgages, have traditionally dominated the Irish rental market. However, the BTL share of the mortgage market dropped from around 20% before 2008 to levels below 5% after 2010, and it has not recovered despite the sharp increase in rents since 2015. More stringent mortgage conditions coupled with high taxes may have discouraged individual investors to enter the rental market.

Despite the increasing presence of large-scale investors, non-professional landlords continue to be predominant. According to the Office of the Revenue Commissioners, in 2018, from the 556 000 properties registered as owned by individuals or entities with more than one property, the large majority (82.9%) belonged to owners with fewer than 10 properties and around 5.6% to owners with more than 200 properties. Figures from the Residential Tenancies Board show that the bulk of landlords in Ireland (86%) rented out one or two properties at most in 2017. However, there is no data on the concentration of ownership for new residential properties offered in the rental market.

agreement in place (including some forward commitments where lease contracts are not yet in place) are excluded.

([21]) Savills (2019), Ireland Investment Report 2019.

([22]) Knight Frank (2018), The Dublin PRS report. Higher real wages imply higher liabilities for a pension fund. Pension funds invest in the residential market to hedge against increases in real wages.

([23]) The 'Design Standards for New Apartments - Guidelines for Planning Authorities' were approved in March 2018.

([24]) Savills (2019), Ireland Investment Report 2019.

3. POLICY ISSUES

3.1. PUBLIC FINANCES

In view of the cyclical position of the economy, any windfall revenue should be used to strengthen the resilience of public finances. A balanced budget and declining debt ratio, combined with favourable near-term growth prospects, put Ireland in a good position to further strengthen its public finances. The heightened external risks imply an even stronger case for using any windfall revenue to build fiscal buffers, such as the rainy day fund, and/or reduce debt, rather than offsetting unplanned spending increases or financing current expenditure of a permanent nature.

While the overall fiscal outlook is positive, risks to the expenditure side remain. In the first five months of 2019, the increase in total expenditure was matched by a strong increase in revenue. However, in recent years, there have been frequent within-year expenditure increases towards the end of the year, in particular in healthcare, contributing to limited compliance with fiscal rules. The Irish Fiscal Advisory Council (IFAC) deemed government plans to contain spending implausible.([25]) IFAC considers that public expenditure as forecast by the government would not be enough to maintain existing levels of services and investment plans. To this end, prudent expenditure management remains crucial.

The concentration of corporate income taxes remains a significant vulnerability. Corporation tax receipts remain concentrated among a fairly small group of companies. According to Revenue Commissioners, the top ten companies accounted for 45% of corporate tax receipts in 2018, up from 39% in 2017 and 37% in 2016.([26]) Furthermore, the employees of these multinationals contribute approximately 24% to total income tax revenue, thus representing a significant concentration in income tax as well.([27]) A CBI report shows that corporate taxes have driven 40% of the total tax revenue growth since 2015.([28]) In 2018, corporate taxes were again considerably above profile, by 22%, influencing the overall performance of public finances. ESRI estimates that, if the corporate tax had been in line with its estimated profile, the government balance, as percentage of GDP, would have been 0.4 pps. lower than the actual level.([29]) IFAC assesses that between EUR 3 and 6 billion of the EUR 10.4 billion in corporate taxes collected in 2018 could be considered in excess of sustainable levels. It recommends that the government should set aside the excess receipts, above a certain threshold, into a 'Prudence Account'. It also suggest to transfer these additional receipts into the newly established rainy-day fund or use the amount to reduce the stock of public debt. In this way, the government's scope to finance within-year additional spending from the windfall gains would be limited.

Broadening the tax base and reducing the reliance on corporate tax revenues, would improve revenue stability. The high concentration of corporate taxes, their volatility and rising share in total tax receipts, from 10.3% in 2011 to 18.7% in 2018, underline the importance of further diversifying the tax base. In this respect, the Annual Taxation Report 2019 highlights that public finances are sensitive to possible shocks to corporate profitability.([30]) IFAC also raises concerns about the sustainability of the corporate taxes and the negative impact of a reversal in these receipts.([31]) The Minister for Finance is expected to announce a set of measures to address the over-reliance on corporate taxes and their concentration risk following the publication of the Summer Economic Statement.

Recent revenue measures, on balance, contributed little to broadening the tax base. The main revenue-raising measure in the 2019 Budget is an increase in the rate of value added tax (VAT) in the tourism sector from 9% to 13.5%

([25]) Irish Fiscal Advisory Council (2019), Fiscal Assessment Report, June 2019.
([26]) Revenue Commissioners (2019). Corporation Tax 2018 Payments and 2017 Returns. May 2019. https://www.revenue.ie/en/corporate/documents/research/ct-analysis-2019.pdf
([27]) Parliamentary Budget Office (2019), Preliminary Analysis of the Stability Programme Update 2019, April 2019.
([28]) Central Bank of Ireland (2019), Quarterly Bulletin, QB2, April 2019.
([29]) Economic and Social Research Institute (2019), Quarterly Economic Commentary, Spring 2019.
([30]) Department of Finance (2019), Annual Taxation Report, March 2019.
([31]) Irish Fiscal Advisory Council (2019), Fiscal Assessment Report, Box B, June 2019.

from 2019.[32] This reduces an important tax expenditure, in line with the European Semester 2018 Country-Specific Recommendations. The Department of Finance published in March 2019 the Review of Local Property Tax. The report recommends that the revaluation of local property tax takes place, as previously planned, in November 2019, and highlighted that any further delays may pose risks to the long-term sustainability of this tax.[33] However, the government decided to further postpone the revaluation to November 2020. Furthermore, besides a small change related to vehicle registration tax on diesel cars, there were no changes to fuel and carbon taxes.

A formal decision on the future of the universal social charge (USC) is pending. Budget 2019 includes further reductions in personal income tax and USC. A working group was created in 2018 to set out a plan for the amalgamation of USC and personal income tax to simplify the personal tax system over the medium term. The completion of this exercise, previously expected for June 2018, has been delayed to 2019.

The financial sustainability of the Irish healthcare system is not ensured. Over the last years, spending overruns in the Department of Health led to expenditure increases for healthcare without significant improvements in performance. The national children's hospital is also experiencing large cost overruns which could have a negative impact on the delivery of other projects set out in the National Development Plan, as highlighted by IFAC. For example, there has been a delay in relation to the A5 road project.

3.2. FINANCIAL SECTOR POLICIES

The CBI's tracker mortgages examination is being finalised. As of end-February 2019, the total redress was around EUR 665 million, with around 40 000 customers affected. Almost all potentially impacted customers have been identified and verified as having received redress. The exercise is expected to be finalised by the end of summer of 2019. Meanwhile, the Financial Services and Pensions Ombudsman (FSPO) received over 1 700 complaints on tracker mortgages during 2018, including some from borrowers who feel that they were entitled to a tracker mortgage but were refused. While the FSPO had put complaints on hold pending the outcome of the examination, the FSPO is now progressing, where possible, some previously paused complaints.

The Enhanced Mortgage-to-Rent scheme is attracting an increasing number of applications but approvals remain limited. Two mortgage associations, iCare and Homes for Life, are among the key players, offering the scheme to vulnerable households qualifying for social housing. The number of applications per quarter have increased from a low of 22 applications in June 2017 to an average of 135 applications at end-2017 following the introduction of the revised scheme. However, the approval rate continues to be extremely low, representing nearly 20 to 25% of applications. A significant number of applications are either terminated or deemed ineligible. There is also evidence of increased delays, with the total number of untreated active applications growing from 574 in September 2017 to 1 044 in March 2019.

As NPL sales pick up, there is an increasing degree of political and social hostility against home repossessions. A number of initiatives have been proposed over the past years that aim to address the social and economic impact of the NPL workout process. Some of these initiatives, like the *Mortgage-to-Rent or the Abhaile* schemes, aim to provide help and restructuring packages to vulnerable homeowners, which is welcome. Others may have unintended consequences by unduly undermining creditor's rights. This is currently the case for a recent legislative proposal, the Land and Conveyancing Law Reform Bill 2019, which has passed all legislative stages in both Houses of the Oireachtas in early July 2019. While some elements of the bill could provide protection for vulnerable households, others have the potential to undermine the progress on NPL reduction and introducing more obstacles and uncertainty to the legal repossession process. Other legislation introduced in this area includes the Consumer Protection (Regulation of Credit Servicing Firms)

(32) Along with changes in some excise duties, vehicle registration surcharge for diesel engine passenger cars, compliance measures and an increase in the National Training Fund levy.

(33) Department of Finance (2019). Review of Local Property Tax. The report of the Interdepartmental Group, March 2019. https://s3-eu-west-1.amazonaws.com/govieassets/7465/91ccbd3ddc97461898211710e2d7ec55.pdf

Act, which was adopted in December 2018, requires the authorisation of loan owners by the Central Bank. It is not yet clear how this bill might interact with existing or upcoming measures, including current insolvency rules as well as EU initiatives.([34])

Of particular concern is a recent proposal that could create significant obstacles to NPL sales or other workout methods. The so-called 'No Consent, No sale' Bill, which was proposed by the opposition party Sinn Féin in January 2019, would require an explicit borrower consent before a mortgage loan can be transferred. This would imply that such a consent would be needed for the case of a loan sale, off-balance sheet securitisation, issuance of asset-backed securities or covered bonds, and would thus severely impact the use of loans as collateral to obtain liquidity through the central bank facilities or in the wholesale market. Thus, the bill would not only reduce the availability of NPL workout options but could also increase the funding costs of banks. There is a risk that higher funding costs generated by such restrictions would be passed on to current and prospective borrowers, with potential effects on mortgage pricing and availability.

Legislation to give the central bank the power to cap standard variable rates is still on hold. Concerns remain that a draft law enabling the CBI to cap interest rates on variable rate mortgages, if enacted, could have negative implications for the transmission of monetary policy, financial stability and bank competition.

The existing macro-prudential policy parameters have not been modified. The CBI introduced in 2018 a 1% countercyclical capital buffer (CCyB), which is effective from July 2019, to increase the resilience of the financial system. In its latest November 2018 review, the CBI decided not to change any of the parameters of the residential mortgage loan-to-value (LTV) and loan-to-income (LTI) measures. More broadly, there is evidence that the residential mortgage measures have become more binding. In particular, the share of lending at or just below the LTV and LTI limits increased in 2018.

The CBI is seeking powers from the Irish government to introduce a systemic risk buffer (SyRB). The CBI's current capital buffer toolset does not cover for the so-called 'tail risks' that are independent from the macro-financial cycle. This means that if there was a structural shock that may arise due to the globalised nature of the Irish economy, the cumulative decline in economic activity may far exceed the decline due to a normal cyclical recession. This would have significant implications for the financial system. The CBI has requested to address this risk by adding the option of a systemic risk buffer (SyRB) to its toolkit, which would improve the resilience of the Irish banking system to such structural shocks. Credit supply could be further protected by switching off the SyRB should these shocks emerge. For these reasons, the power to activate the SyRB if certain conditions materialise should be granted to the CBI.

Perhaps more so than the other non-bank financial sectors, the Irish insurance sector is subject to significant risks. Nearly one-quarter of the gross premium incomes of Irish insurers are written on an outwards and inwards basis between Ireland and the UK. In the event of UK's withdrawal from the EU without a deal, insurers established in Ireland would be unable to continue operating in the UK (including Gibraltar) or vice versa. The authorities have enacted temporary permissions regimes to provide additional time to insurers to complete the implementation of their restructuring plans to prepare for the UK's withdrawal from the EU. Beyond these risks, which have been temporarily offset by actions by the authorities, the Irish insurers and their UK-based parents are also exposed to the UK market through their investment portfolios. This exposes them to exchange rate and market risk in case of market valuation fluctuations. Beyond these risks, the Irish insurers are also subject to the same set of challenges borne by their peers in the EU, including the upcoming implementation of the IFRS 17 standards from 2022 and the continued low interest rate environment.

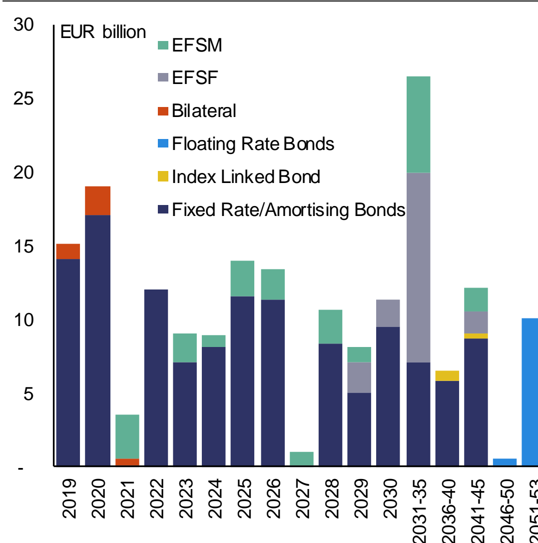
([34]) For similar concerns on these bills, see also the opinions of the European Central Bank of 5 July 2018 (CON/2018/31) and 18 February 2019 (CON/2019/8).

4. SOVEREIGN FINANCING ISSUES

Sovereign financing remains comfortable. The government had over EUR 25 billion in cash at the end of June 2019. Around EUR 7 billion of long-term debt is due to mature over the rest of this year (Graph 4.1). In the first half of 2019, the National Treasury Management Agency (NTMA) purchased a further EUR 1.5 billion of floating rate notes linked to the Irish Bank Resolution Corporation from the CBI and subsequently cancelled them. The outstanding balance stands at EUR 10 billion from an initial EUR 25 billion in 2013.

The volume of issuance in 2019 is expected to be broadly similar to 2018. The NTMA raised over EUR 17 billion in 2018. This included EUR 3 billion in its first-ever sale of green bonds to diversify the agency's issuance. The NTMA plans to issue EUR 14-18 billion in bonds in 2019, from which it already raised EUR 10.4 billion in benchmark funding by end-June. Furthermore, in March 2019, the NTMA issued EUR 300 million of new inflation-linked bonds. The principal repayment will be linked to the HICP for Ireland, excluding tobacco ([35]).

Graph 4.1: **Maturity profile of long-term marketable and official debt (end-April 2019)**



(1) The Irish programme was the second euro area assistance programme, and the first financed by two new financial assistance instruments established in 2010, the European Financial Stability Facility (EFSF) and the European Financial Stabilisation Mechanism (EFSM). EFSF loans reflect the maturity extensions agreed in June 2013. EFSM loans are also subject to a seven year extension. It is not expected that Ireland will have to refinance any of its EFSM loans before 2027. However the revised maturity dates of individual EFSM loans will only be determined as they approach their original maturity dates. The graph reflects the current maturity dates of individual EFSM loans.
(2) Bilateral loans were provided from the United Kingdom.
Source: National Treasury Management Agency

Bond market conditions have been affected by monetary policy developments. The ECB's policy measures, including the asset purchase programmes, appear to have contributed to a compression of sovereign borrowing costs and, in turn, debt servicing costs. This also appears to have had ramifications for the maturity profile of sovereign debt, which has shifted towards longer maturities.([36]) Aided by the low yields, total interest payments by the general government have continued to decrease as a share of GDP. The 10-year bond yield for Ireland remains low by historical standards, at around 0.3% in June 2019. The spread against the German benchmark has followed a downward trend in the beginning of the year but then started increasing since April. Interest expenditure in Ireland fell from 2.0% of

([35]) However, the principal is protected against a fall in the index over the life of the bond, i.e. if inflation over the bond's lifetime is negative, investors will still receive the principal amount in full.

([36]) John Larkin, PJ Anderson and Sean Furlong (2019), The Irish Government Bond Market and Quantitative Easing, Central Bank of Ireland, Quarterly Bulletin 02, April 2019.

GDP in 2017 to 1.6% in 2018 and is expected to fall further this year, to 1.5%. However, as a share of GNI*, interest expenditure amounted to 3.2% in 2017 and an estimated 2.7% in 2018.

Risks for Ireland's capacity to service the EFSM and EFSF debt remain low. At the end of 2018, public debt amounted to EUR 206 billion, of which around 90% had a maturity of more than one year. Redemptions of EFSF and EFSM loans currently extend until 2042. For EFSF, there are no maturities until 2029. The maturity of EFSM loans to Ireland can also be extended within the limit of 19.5 years of average original maturity established by the Council Decision on Union financial assistance to Ireland. EUR 3.9 billion originally due in 2018 have already been extended.([37]) It is therefore not expected that Ireland will have to repay any of its EFSM loans before 2027, unless it wishes to do so. The revised maturity dates of individual EFSM loans will be determined as they approach their original maturity dates. This Decision and the ensuing operations entail financial benefits for Ireland, linked to the EU's favourable funding conditions.

Table 4.1: **Government financing plans**

EUR billion	2018	2019
Funding requirement		
Exchequer borrowing requirement (EBR) (1)	-0.1	2.1
Bond maturities (2)	8.9	13.1
UK bilateral loan (3)	0.0	1.6
Other bond flows (4)	6.8	5.0
Total requirement	**15.6**	**21.9**
Funding sources		
Government bonds (5)	17.5	16.0
Other (6)	2.8	3.6
Use of cash & other short-term investment balances (- represents an increase)	-4.8	2.3
Total sources	**15.6**	**21.9**
Financial buffer (7)	**15.3**	**13.1**

(1) 2019 figures are estimates, as of April 2019. Rounding may affect totals.
(2) 2019 estimate as per Stability Programme Update April 2019.
(3) Includes Amortising Bonds.
(4) Includes the effect of currency hedging.
(5) Includes floating rate notes purchases, bond switching and, for 2019, general contingencies.
(6) In its 2019 Funding Statement, the NTMA announced plans to issue EUR 14 - EUR 18 bn of government bonds in 2019. EUR 16 bn is used as an indicative amount in this presentation.
(7) Includes net State Savings (Retail), net short-term paper funding and other medium/long-term funding.
(8) Exchequer cash and liquid assets. Excludes non-liquid Exchequer financial assets.

Source: NTMA

([37]) Council Implementing Decision 2011/77/EU.

ANNEX 1
Debt sustainability analysis

The public debt-to-GDP ratio is projected to continue declining. Based on the Commission 2019 spring forecast and the no-policy-change assumption beyond the forecast horizon, the debt-to-GDP ratio is projected to decrease to 49.9% in 2029, thus below the 60% Treaty reference value. The sale of government shares in the three major banks would further reduce public debt.

Gross funding needs are expected to be modest. This reflects the relatively long maturity of public debt, the government's fiscal stance, as well as high nominal GDP growth. Ireland's gross financing needs are forecast to settle around 6% by 2029, well below the estimated value for 2019 of close to 9%.([38])

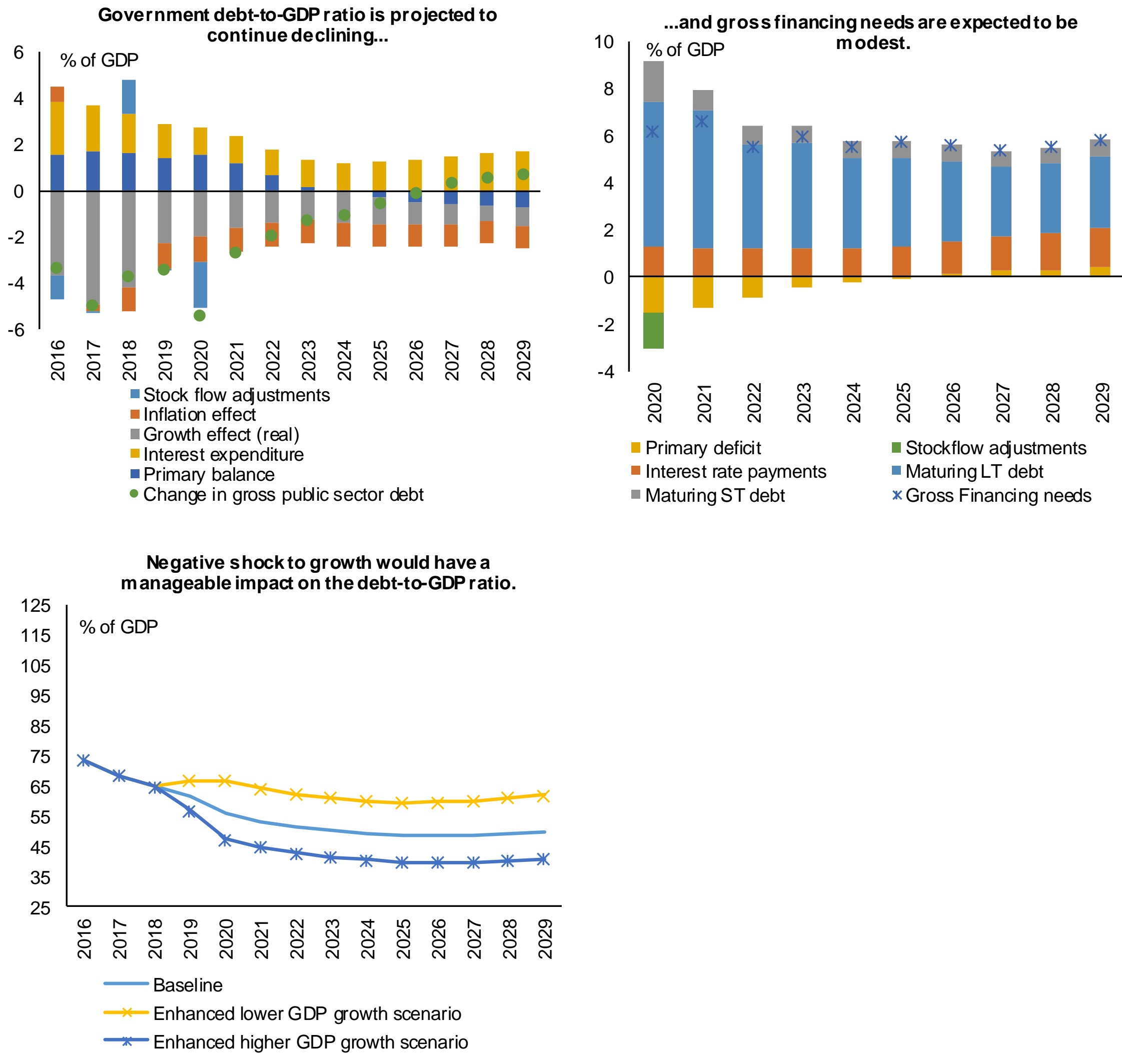
Debt sustainability risks appear to be low over the medium term. This assessment is based on the results from the baseline scenario, as outlined above, and most of the stress tests and alternative scenarios.([39]) Adverse shocks to real GDP growth – of a magnitude reflecting Ireland's historical variability of output – would increase the public debt-to-GDP ratio by 16.0 pps by 2029 compared to the baseline scenario. When debt metrics are computed relative to GNI*, standard sensitivity analysis would point to higher vulnerabilities than measured on the basis of GDP.([40])

([38]) European Commission (2019), Fiscal Sustainability Report 2018, Volume 2, Country Analysis, Institutional Paper 094/January 2019.

([39]) Sensitivity analysis includes several deterministic debt projections, as well as stochastic projections (see European Commission (2019), Fiscal Sustainability Report 2018, Volume 1, Country Analysis, Institutional Paper 094/January 2019 for more details).

([40]) See Fiscal Sustainability Report 2018, Volume 1, Box 3.1. Alternative metrics to assess debt sustainability: the use of GNI.

Graph A1.1: **Debt Sustainability Analysis**



(1) Details on the scenarios can be found in European Commission (2019), Fiscal Sustainability Report 2018, Volume 1, Country Analysis, Institutional Paper 094/January 2019.

Source: European Commission

ANNEX 2
Supplementary tables

Table A2.1: **Fiscal accounts (based on 2019 spring forecast)**

	2017	2018	2019	2020
	% of GDP			
Indirect taxes	8.4	8.0	8.2	8.0
Direct taxes	10.4	10.9	10.6	10.6
Social contributions	4.3	4.2	4.2	4.2
Sales	1.9	1.8	1.7	1.7
Other current revenue	0.7	0.5	0.5	0.5
Capital taxes	0.2	0.2	0.1	0.1
Total current revenue	**25.9**	**25.6**	**25.4**	**25.1**
Capital transfers received	0.1	0.2	0.2	0.2
Total revenue	**26.0**	**25.8**	**25.6**	**25.3**
Compensation of employees	7.0	7.0	7.0	6.8
Intermediate consumption	3.4	3.4	3.7	3.8
Social transfers in kind via market producers	2.1	2.0	1.9	1.9
Social transfers other than in kind	7.8	7.3	7.1	6.9
Interest paid	2.0	1.6	1.5	1.2
Subsidies	0.6	0.5	0.5	0.5
Other current expenditure	1.1	1.2	1.1	1.1
Total current expenditure	**23.9**	**23.1**	**22.8**	**22.2**
Gross fixed capital formation	1.8	2.0	2.3	2.3
Other capital expenditure	0.5	0.6	0.5	0.5
Total expenditure	**26.3**	**25.7**	**25.6**	**25.0**
General government balance	**-0.3**	**0.0**	**0.0**	**0.3**
General government balance net of one-offs	**-0.3**	**0.1**	**0.0**	**0.3**
	EUR billion			
Indirect taxes	24.8	25.5	27.7	28.3
Direct taxes	30.6	34.6	35.5	37.6
Social contributions	12.7	13.4	14.2	14.8
Sales	5.5	5.9	5.9	5.9
Other current revenue	2.0	1.6	1.7	1.8
Capital taxes	0.4	0.5	0.5	0.5
Total current revenue	**76.1**	**81.5**	**85.4**	**88.9**
Capital transfers received	0.4	0.6	0.6	0.6
Total revenue	**76.5**	**82.0**	**86.0**	**89.5**
Compensation of employees	20.7	22.2	23.4	24.2
Intermediate consumption	9.9	10.9	12.6	13.3
Social transfers in kind via market producers	6.1	6.5	6.5	6.6
Social transfers other than in kind	23.0	23.4	23.7	24.3
Interest paid	5.8	5.2	4.9	4.3
Subsidies	1.8	1.7	1.7	1.8
Other current expenditure	3.2	3.7	3.8	4.0
Total current expenditure	**70.4**	**73.5**	**76.7**	**78.4**
Gross fixed capital formation	5.4	6.5	7.7	8.1
Other capital expenditure	1.6	1.9	1.8	1.9
Total expenditure	**77.4**	**82.0**	**86.2**	**88.4**
General government balance	**-0.8**	**0.0**	**-0.1**	**1.2**
General government balance net of one-offs	**-0.7**	**0.2**	**-0.1**	**1.0**

Source: Eurostat and European Commission Spring 2019 forecast

Table A2.2: **General Government debt projections (based on 2019 spring forecast)**

	2017	2018	2019	2020
Government balance (% of GDP)	**-0.3**	**0.0**	**0.0**	**0.3**
Government gross debt (% of GDP)	68.5	64.8	61.3	55.9
	levels, EUR billion			
Government balance	**-0.8**	**0.0**	**-0.1**	**1.2**
Gross debt	201.4	206.2	206.0	197.8
Change in gross debt	0.7	4.8	-0.2	-8.2
Nominal GDP	294.1	318.5	336.0	353.9
Real GDP	270.6	288.6	299.5	309.6
Real GDP growth (% change)	**7.2**	**6.7**	**3.8**	**3.4**
Change in gross debt (% of GDP)	-5.0	-3.7	-3.4	-5.4
Stock-flow adjustments (% of GDP)	-0.1	1.5	-0.1	-2.0
	% of GDP			
Gross debt ratio	**68.5**	**64.8**	**61.3**	**55.9**
Change in gross debt ratio	-5.0	-3.7	-3.4	-5.4
	contribution to change in gross debt			
Primary balance	1.7	1.7	1.4	1.5
"Snow-ball" effect*	-3.2	-3.6	-1.9	-1.9
of which				
Interest expenditure	*2.0*	*1.6*	*1.5*	*1.2*
Real growth effect	-4.9	-4.2	-2.3	-2.0
Inflation effect	-0.3	-1.0	-1.1	-1.1
Stock-flow adjustments	**-0.1**	**1.5**	**-0.1**	**-2.0**
Implicit interest rate	*2.9*	*2.6*	*2.4*	*2.1*

(1) The projections assume no borrowing for precautionary contingencies foreseen in the programme's financing plan.
* Snow-ball" effect, Interest expenditure, Real growth effect and Inflation effect are derived from the Debt sustainability monitor update - Spring 2019. Snow-ball effects refer to the net impact of the counteracting effects of interest rates, inflation and real GDP growth (as well as exchange rates in some countries) on the evolution of the debt ratio ((see Debt sustainability monitor update - Spring 2019, Annex A4 for more details).

Source: Eurostat and European Commission Spring 2019 forecast

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