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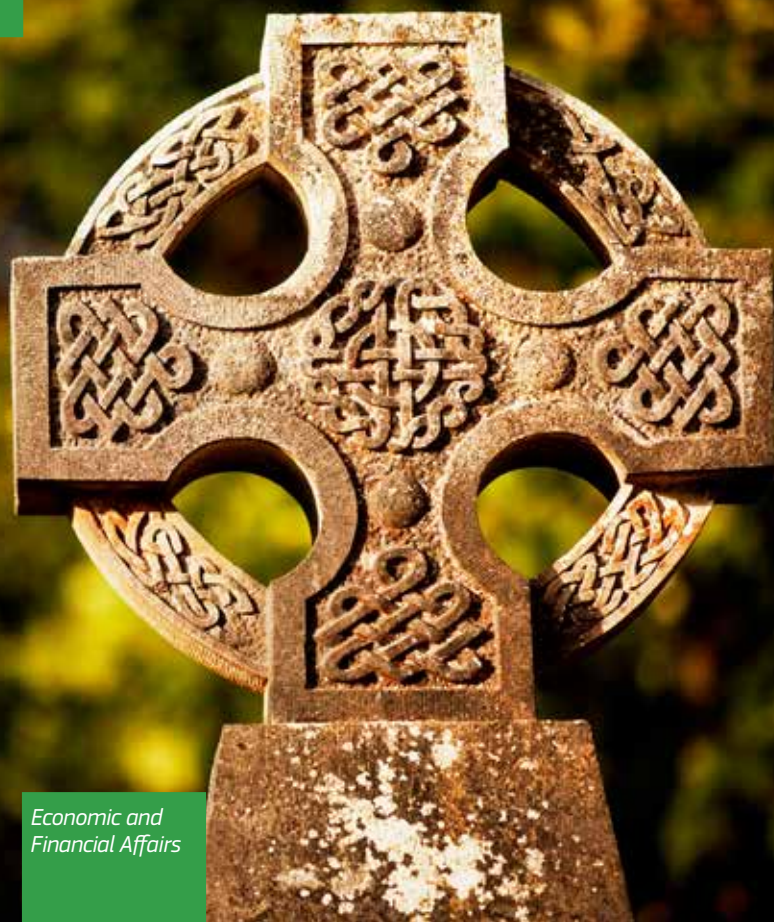
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# Post-Programme Surveillance Report

## Ireland, Spring 2024

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European Commission  
Directorate-General for Economic and Financial Affairs

## **Post-Programme Surveillance Report**

Ireland, Spring 2024

## ABBREVIATIONS

CBI	Central Bank of Ireland
CCyB	Countercyclical capital buffer
CET1	Common Equity Tier 1
CRE	Commercial Real Estate
CSO	Central Statistics Office Ireland
ECB	European Central Bank
EFSF	European Financial Stability Facility
EFSM	European Financial Stabilisation Mechanism
ESM	European Stability Mechanism
GDP	Gross Domestic Product
GNI*	Modified Gross National Income
HICP	Harmonised Index of Consumer Prices
ICT	Information and Communication Technology
MBF	Market-based financial sector
NBLs	Non-bank lenders'
NFCs	Non-Financial Corporations
NPL	Non-performing loan
NTMA	National Treasury Management Agency
O-SII	Other Systemically Important Institutions
PPS	Post-programme surveillance
q-o-q	Quarter-on-quarter
RoA	Return on Assets
RoE	Return on Equity
SME	Small and medium-sized enterprises
VAT	Value Added Tax
y-o-y	Year on year

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## EXECUTIVE SUMMARY

**The 20th post-programme surveillance (PPS) mission to Ireland took place from 11 to 14 March 2024.** This mission involved European Commission staff in liaison with European Central Bank (ECB) staff. European Stability Mechanism (ESM) staff participated on aspects relating to the ESM's Early Warning System.

**The Irish economy slowed following a period of robust growth, with the moderation being attributable to the weakening performance of some multinationals.** Private consumption continued to grow in 2023 supported by strong employment growth. However, households faced challenges due to rising price levels, higher interest rates and declining real wages, moderating private consumption growth. Modified investment, which removes the volatile aircraft leasing and R&D intellectual property components, declined in 2023, primarily reflecting a technical base effect after the completion of strong one-off investments in recent years. Modified investment is expected to remain subdued in 2024 as a result of tight financial conditions and global uncertainties. Post-pandemic normalisation, global headwinds and sector-specific developments led to a fall in net exports in 2023. However, a recovery in the global trade outlook, along with recent large-scale investments are expected to bolster exports in the coming years. Ireland's real gross domestic product (GDP) is expected to grow by 1.2% in 2024 and by 3.6% in 2025. Modified domestic demand, which better reflects Ireland's underlying domestic economic activity, is expected to grow by 1.7% in 2024 and 2.4% in 2025. After significant easing in recent quarters, inflation is expected to stand at 1.9% in 2024 and 1.8% in 2025.

**The outlook for public finances is benign, though certain risks on fiscal sustainability persist.** Ireland is projected to achieve a general government surplus both in 2024 (1.3% of GDP) and 2025 (1.2% of GDP). General government revenue growth was solid at about 7% in 2023, albeit lower than the double-digit increases of the previous two years. Government expenditure increases are driven by wage increases in the public sector and measures to offset cost-of-living pressures. The government debt-to-GDP ratio is projected to decrease over the forecast horizon. Certain risks on fiscal sustainability persist, such as the impact of an ageing population on the costs of the pension system. The establishment of saving funds could mitigate long-term fiscal sustainability risks.

**The Irish financial sector proved resilient in 2023 as Irish retail banks posted strong results on the back of higher interest margins and limited impairment charges.** Banks' high profitability levels improved their organic capital generation. However, capital levels somewhat declined in 2023, as banks stepped up their distributions to shareholders and onboarded assets and deposits from the two banks exiting the Irish market. The deposit base remained stable, with banks reporting ample liquidity levels. Asset quality remained sound, with Ireland's non-performing loans ratio declining to its lowest level since the financial crisis. Despite these positive developments, the credit quality of non-financial corporate exposures has deteriorated since the end of the pandemic and significant vulnerabilities have emerged in the commercial real estate sector. Ireland's large non-bank financial sector maintains limited interlinkages with the domestic economy, mostly related to activities of property funds and non-bank lending to small and medium-sized enterprises.

**Ireland retains the capacity to service its debt.** Despite a number of challenges, its economic, fiscal and financial situation is sound overall. According to the Commission's debt sustainability analysis, Ireland is assessed to face low risks in the short and medium-term, while long-term risks appear to be medium. Government gross financing needs are low thanks to large cash balances. Ireland's first EFSF payment is scheduled in 2029 and EUR 2.4 billion of EFSM repayment are due in 2025. Ireland continues to enjoy favourable financing conditions as its market presence and perception by investors are positive.

# 1. INTRODUCTION

**From 11 to 14 March 2024, staff from the European Commission, in liaison with staff from the European Central Bank (ECB), undertook the twentieth post-programme surveillance (PPS) mission to Ireland.** Staff from the European Stability Mechanism (ESM) participated in these meetings on aspects related to the ESM's Early Warning System. Under PPS, the Commission carries out regular review missions to euro area Member States that have had a financial assistance programme. The objective of the PPS missions is to assess the economic, fiscal and financial situation to ensure the Member State maintains its capacity to service its debt <sup>(1)</sup>.

**From 2011 until the end of 2013, the euro area and the International Monetary Fund (IMF) provided financial assistance to Ireland.** The economic adjustment programme for Ireland included a joint financing package of EUR 85 billion for the period 2010-2013. In December 2013, Ireland successfully completed the financial assistance programme.

**This report reflects information available and policy developments that have taken place up to 30 April 2024.** The macroeconomic and budgetary projections, including those underlying the debt sustainability analysis, are in line with the Commission's 2024 Spring Economic Forecast released on 15 May 2024 (with cut-off date 30 April 2024).

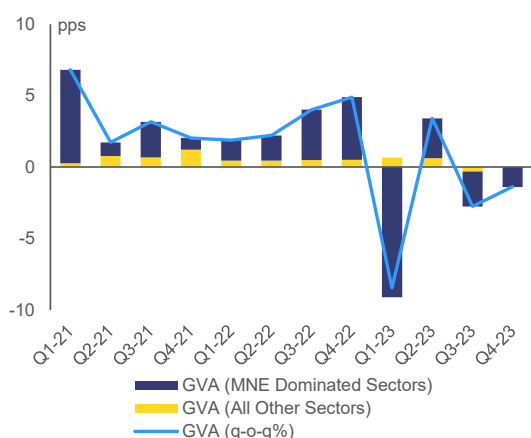
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<sup>(1)</sup> Under Regulation (EU) No 472/2013, PPS will continue until at least 75% of the financial assistance received under the programme has been repaid. Under the current repayment schedule, PPS on Ireland will last until 2031.

## 2. ECONOMIC DEVELOPMENTS

**Ireland's economic growth is set to resume.** Ireland's GDP declined by 3.2% in 2023, primarily driven by weakness in sectors dominated by multinationals headquartered in Ireland (Graph 2.1). Global headwinds and a normalisation of activity following exceptionally strong activity in previous years adversely affected physical exports, notably in the pharmaceutical and chemicals sector, as well as in contract manufacturing. The domestic economy continued to grow, albeit more moderately, affected by elevated price levels and tight financial conditions. Modified domestic demand<sup>(2)</sup> saw a modest uptick of 0.5% in 2023, driven by consumption and residential investment. Looking ahead, the gradually improving external environment and lower headline inflation suggest a positive outlook for Ireland in 2024 and 2025, although geopolitical risks and industry-specific risks create considerable uncertainty.

Graph 2.1: **Gross value added quarterly growth by sector**

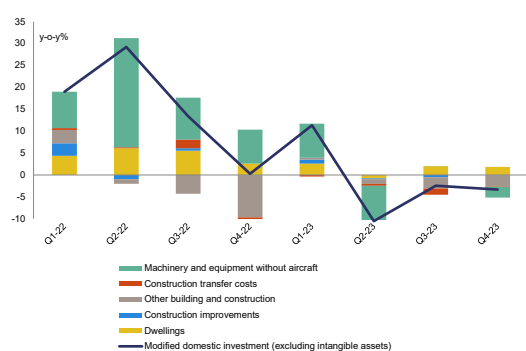


Source: Central Statistics Office (CSO).

**Domestic investment declined in 2023 and is expected to remain subdued.** Headline investment figures continue to be affected by volatile intangible and aircraft investments. Total investment increased by 2.9% in 2023, driven by increases in R&D-related services imports and intellectual property transactions in the final quarter of the year<sup>(3)</sup>. By contrast, modified investment, which strips out aircraft leasing and intellectual property transactions, declined by 7.1% in 2023. This primarily reflects a technical base effect after the completion of strong one-off investments in recent years (Graph 2.2). While modified investment remains high by historical standards, global uncertainties, tight financing conditions and continued normalisation from elevated activity levels are expected to weigh on investment growth in 2024. An assumed improvement of financial conditions and the implementation of the National Development Plan

suggest a more positive investment outlook for 2025.

Graph 2.2: **Contributions to modified domestic investment**



(1) Expenditure on GNP

Source: CSO.

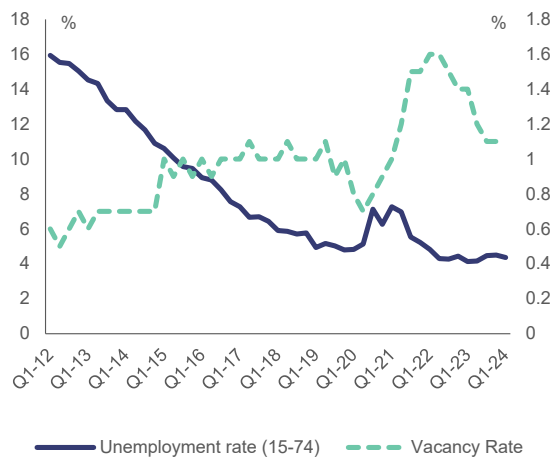
**Private consumption has continued to grow amidst signs of moderation.** Household spending increased by 3.1% in 2023, supported by a robust labour market and government support measures. However, growth has slowed down in recent quarters as elevated price levels, higher interest rates and declines in real wages led to a reduction in the real purchasing power of households. Consumer sentiment and retail sales data indicate there has been a modest pick-up in consumer demand in the first few months of 2024. Going forward, the combination of easing inflation, strong employment growth and recovery in real disposable incomes suggests favourable conditions for consumption in the coming years.

<sup>(2)</sup> Modified domestic demand aims to exclude large transactions by foreign corporations that do not have a big impact on the domestic economy.

<sup>(3)</sup> The surge in intellectual property investment was matched by a rise in intellectual property imports. These two impacts largely offset each other, and therefore, have a broadly neutral first-round impact on GDP.



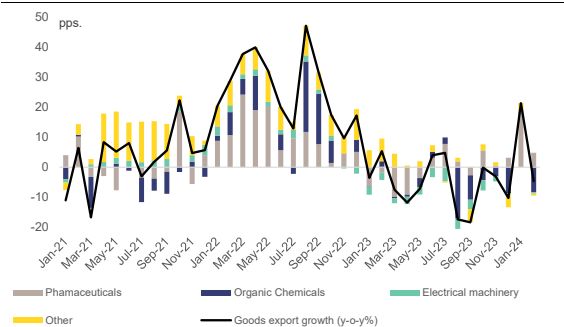
Graph 2.3: Unemployment and vacancy rates



(1) Six-month moving average

Source: CSO.

Graph 2.4: Drivers of export growth



Source: CSO.

of the year. Looking ahead, net exports are expected to contribute positively to growth, supported by a return to growth in pharmaceutical trade and a more favourable external environment. Even with these expected positive developments, Ireland's high concentration of exports in a few sectors and companies exposes it to growth volatility. It also increases its exposure to a downturn in global demand, industry- and company-specific changes and the acceleration of geoeconomic fragmentation.

### **Inflation based on the Harmonised Index of Consumer Prices (HICP) is easing, but domestic drivers of inflation persist.**

Inflation has been easing rapidly since the last quarter of 2023, reaching 2.2% in the first quarter of 2024. This is primarily attributable to lower energy prices (Graph 2.5), as the decline in wholesale prices is gradually passed on to consumers. Non-energy industrial goods inflation also sharply declined in the first few months of 2024 while inflation of processed and unprocessed food items slowed down but remains elevated. The impacts of past monetary policy tightening and strong base effects are expected to lead to continued moderation of inflation. However, domestic drivers are increasingly affecting inflation, with services inflation expected to remain high due to strong domestic demand and a tight labour market. Price pressures are generally expected to moderate, and HICP inflation is projected to be 1.9% in 2024 and 1.8% in 2025. At the same time, risks remain, including adverse weather effects affecting food prices, further increases in energy prices and escalations of geopolitical tensions leading to more fragmented supply chains. Additional risks relate to higher-than-expected labour costs and a chronic undersupply of housing.

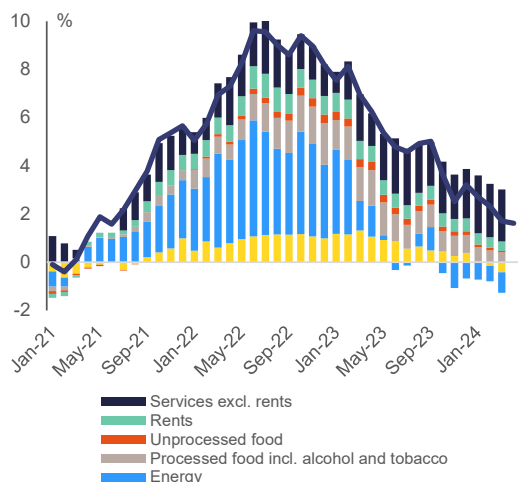
### **Vacancies are declining while unemployment remains steady at low levels.**

The labour market remains strong, but shows signs of moderation. Job vacancies have been steadily decreasing from their peak in 2022 (Graph 2.3), pointing to some softening of excess labour demand. Notable decreases in vacancies are observed in sectors such as the financial and insurance activities sector, the professional, scientific and technical activities sector, the information and communication sector and the construction sector. Despite this, the unemployment rate remained stable in 2023, at 4.4% in the first quarter of the year, indicating a still-tight labour market. Looking ahead, while the vacancy rate is in gradual decline, the unemployment rate is expected to remain low, averaging 4.4% in 2024 and 2025. Employment is expected to increase further over the forecast horizon, but more moderately, in line with the projected normalisation of economic activity.

### **Net exports have moderated following a period of robust growth.**

A negative contribution from net exports was the primary reason behind Ireland's GDP decline in 2023, due to a combination of slowing external environment and sector- and product-specific effects. A key contribution to this decline was the normalisation of chemicals and pharmaceutical exports following the COVID-related boost to these sectors' output (Graph 2.4). Semiconductor trade also weakened, likely due to company-specific issues and the impact of US trade policies. Contract manufacturing, a major contributor to net exports in previous years, also declined in 2023. By contrast, services exports remained strong, though moderating in the final quarter

Graph 2.5: HICP inflation components



Source: Eurostat.

**The rate of new housing supply is increasing.** New housing completions continued to increase in 2023 to almost 33 000, an increase of 10.0% from 2022, and are expected to rise further. Increased government spending counterbalanced the increase in the cost of construction materials and capital. However, looking ahead, while inflationary pressures and financing costs have started to decrease, raising construction capacity further to meet demand will take time and test the limits of Ireland’s infrastructure.

**House price growth has started to pick up.** In nominal terms, house prices have started to increase again after a year of subdued growth, even as mortgage interest rates have remained high by historical standards. Yearly house price inflation increased to 5.4% in January 2024. Although house price inflation is still higher outside Dublin, momentum has been strong in the capital over recent months.

Accumulated supply shortages and strong population growth, as well as the prospect of interest rate cuts in the second half of the year, are expected to support prices over the medium term.

**Residential rental prices continued to show strong growth in 2023 as the market remained very tight.** According to rental platform data, the number of properties available for rent remains below half of pre-pandemic levels <sup>(4)</sup>. Rental prices have increased at a considerably higher rate in rural areas, as hybrid working possibilities and housing shortages have been driving some demand out of urban areas. Preliminary evidence for Dublin shows that new rental stock is increasing on a net basis, but the availability of affordable housing remains a key challenge and is hindering the recruitment of skilled labour from abroad.

**The office rental market is facing a downturn and vacancy rates have increased considerably, but spillover risks remain limited for domestic banks.** The shift to hybrid working has led to a decrease in office space needed, while a pre-pandemic investment boom caused excess supply. This poses significant risks, particularly for non-prime office space. The vacancy rate for offices in Dublin increased from less than 8.5% in the fourth quarter of 2021 to 16.7% in the fourth quarter of 2023, but remains below the 20%+ rates seen during the global financial crisis <sup>(5)</sup>. However, the potential negative impact on domestic banks appears contained given their relatively limited exposures (see Section 4).

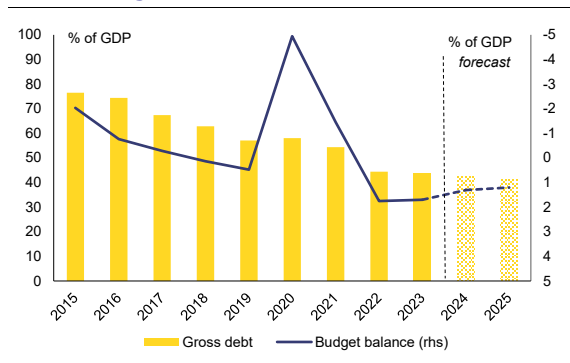
<sup>(4)</sup> Daft.ie (2024) Q4 Rental Price Report.

<sup>(5)</sup> Coldwell Banker Richard Ellis (2024) Dublin Office Market Q4 2023.

### 3. PUBLIC FINANCE DEVELOPMENTS

**The outlook for public finances is benign.** On a general government basis, Ireland achieved a surplus of EUR 8.3 billion in 2023, equivalent to 1.7% of GDP and 2.9% of GNI\* <sup>(6)</sup>. General government revenue growth was solid at 6.7% in 2023, albeit lower than the double-digit rates of the previous 2 years. Income tax growth was resilient at about 6%, thanks to the strength of the labour market, while VAT receipts growth slowed down to around 5% despite resilient private consumption. Once again, the level of corporate tax receipts was high at around EUR 24 billion, though its annual growth also moderated. The fast growth in corporation tax receipts has been visible since 2014, with an acceleration between 2020 and 2022. While in the first quarter of 2024 there were signs of a slowdown, with corporate tax receipts down by almost 25% relative to the same period a year before, the sharp decline in March that caused this might reflect a timing issue, and a catch-up is likely throughout 2024. Government expenditure increased by 8% in 2023, driven by wage increases in the public sector and support measures to alleviate cost-of-living pressures. According to the Commission's 2024 Spring Economic Forecast, Ireland's general government surplus is projected to be 1.3% of GDP in 2024, and 1.2% in 2025 (Graph 3.1). On 22 April 2024, the Irish government published a Stability Programme. The Irish authorities project surpluses of 2.8% of GNI\* in 2024 and 3.0% in 2025.

Graph 3.1: **General government budget balance and gross debt forecast**



Source: European Commission.

**The government debt-to-GDP ratio is projected to decrease in the short term.** At end of 2023, the debt ratio was 43.7% of GDP and 75.9% of GNI\*. The Irish authorities project a debt-to-GNI\* ratio of 72.1% in 2024 and 69.7% in 2025, to provide a measure of the debt burden which is more informative in relation to the domestic economy. Ireland's gross general government debt-to-GDP ratio is projected to decrease to 42.5% in 2024 and 41.3% in 2025, according to the Commission's 2024 Spring Economic Forecast.

**Certain risks on fiscal sustainability persist.** According to the Commission's debt sustainability analysis, Ireland's fiscal sustainability challenges appear low over the short and medium term, and medium over the long term (Annex 2). The impact of an

ageing population on the costs of the pension system remains a risk. The proportion of the population over 64 relative to the working-age (20-64) population is projected to more than double between 2022 and 2070, and pension system expenditure is estimated to increase by 2.8 percentage points of GDP in the same period, making Ireland one of the EU Member States with a higher future cost of ageing. Ireland is taking steps to safeguard the pension system by increasing pay-related social insurance (PRSI) contributions. It increased the PRSI rate by 0.1 percentage points from 1 October 2024 and announced further increases in all PRSI rates between 2025 and 2028. These measures are in line with the suggestion of the independent actuarial review, commissioned by Ireland's Department of Social Protection, which suggested increasing PRSI rates by 0.08 percentage points a year up to 2076.

**The establishment of saving funds could mitigate long-term fiscal sustainability risks.** The Irish Stability Programme envisages yearly transfers to a new Future Ireland Fund of approximately EUR 4 billion between 2024 and 2027. The fund will support the inter-generational smoothing of the fiscal costs associated with structural change in the Irish economy. A second fund will be the Infrastructure, Climate and Nature Fund, for which planned instalments are EUR 2 billion a year as of 2025. Draft legislation to establish these funds' statutory basis was published in the first half of 2024.

<sup>(6)</sup> Modified gross national income (GNI\*) reflects the income standards of Irish residents more accurately than GDP. It differs from actual GNI in that it excludes, for example, the depreciation of foreign-owned, but Irish-resident, capital assets (notably intellectual property and assets associated with aircraft for leasing) and the undistributed profits of firms that have redomiciled to Ireland.

## 4. FINANCIAL SECTOR DEVELOPMENTS

**Irish banks have performed well since autumn 2023, maintaining strong capital ratios (7).** Rising interest rates in particular have boosted their profitability in the past year while credit quality has remained steady. Organic capital generation continued to improve in 2023, in line with higher profitability levels. However, the onboarding of loans acquired from the two banks exiting the Irish market have negatively affected capital levels. The transitional total capital ratio stands at 20.1% at the end of 2023, a decline of 191 basis points since the end of 2022, which can be primarily attributed to a significant increase in risk-weighted assets (RWAs), which rose by EUR 9.9 billion to reach EUR 124 billion. This, combined with higher capital requirements from an increase in both the national and the UK countercyclical capital buffer rates, has reduced capital headroom.

**The rise in interest rates helped domestic retail banks to increase interest margins and significantly improve their profitability in 2023.** Aggregate profits increased to EUR 3.7 billion in 2023, from EUR 1.8 billion a year earlier. Annualised return on equity reached 13.9% in the year to September 2023, up from 7.0% in 2022. Meanwhile, the annualised return on assets was 1.3%, compared to 0.7% in 2022. Improved profitability was largely thanks to higher net interest income, which increased by EUR 3.2 billion in 2023 to EUR 8.2 billion, driven by higher loan volumes and higher yields on loans, widening lending margins, and the large amount of excess liquidity held on deposit with the ECB. Net fee and commission income also grew, while operating costs increased at a much slower pace than revenues. The increase in operating costs can mainly be attributed to staff expenses but banks also reported the highest loan loss provisions since 2020. The profitability outlook appears less bright given the potential pressure of higher deposit rates and the risk of adverse credit developments. Banks' capacity to effectively curb their structural costs will be critical for ensuring sustainable future profitability, especially in a lower interest rate environment.

**Retail banks maintain large stocks of liquid assets despite having used some excess cash to acquire assets from the two banks exiting the Irish market.** The retail banks liquidity coverage ratio and the net stable funding ratio slightly decreased in 2023, but remain well above the regulatory minima of 100%, at 199% and 158% respectively at the end of 2023. Deposits continued to grow in 2023, especially retail deposits, in part attributable to the capture of deposits from the two banks exiting the Irish market. Nevertheless, growth in deposits slowed somewhat in the second half of 2023. The loan-to-deposit ratio for the sector increased slightly from 72% at the end of 2022 to 76% at the end of 2023.

**Retail banks managed to reduce their non-performing loans (NPLs) to their lowest level since the financial crisis.** At end-2023 the NPL ratio was 2.1% (8), 20 basis points (bps) lower than a year earlier and well below its pre-pandemic value of 4.3% at the end of 2019. NPLs on household lending stood at 2.4%, unchanged from the previous year, after steady declines in earlier years due mainly to sales and restructurings. So far, higher interest rates have not significantly affected the credit quality of mortgages, as risks were mitigated by the decreasing proportion of variable rate mortgages in Ireland and the mortgage measures in place. Loans to non-financial corporations (NFCs) were affected more severely by the pandemic, but asset quality improved over the course of 2023, with NPLs declining from 5.5% at end-2022 to 4.7% at end-2023, albeit remaining well above pre-pandemic levels (4.0% at end-2019). Retail banks increased their impairment charges in 2023 (EUR 595 million). Provisioning levels remain well below the EU average, especially for NFCs (28.8% vs 43.9%, in December 2023). These lower provisioning levels can partly be attributed to the higher proportion of loans secured by collateral and possibly by the use of calendar provisioning, i.e. deducting expected future losses directly from regulatory capital, rather than increasing reported provisions.

(7) The focus of this analysis is the three retail banks in Ireland that remain after the withdrawal of two foreign owned banks.

(8) The NPL ratio refers to total loans and advances, including to central banks, governments, credit institutions and other financial corporations, NFCs and households.

Table 4.1: Financial soundness indicators

in %	Ireland									Euro area	EU
	Q4-2017	Q4-2018	Q4-2019	Q4-2020	Q4-2021	Q4-2022	Q1-2023	Q2-2023	Q3-2023	Q3-2023	Q3-2023
Non-performing loans	12.1	7.3	4.3	5.1	3.5	2.3	2.2	2.3	2.4	1.9	1.9
o/w NFC sector	15.3	8.1	4.0	7.6	7.7	5.5	5.1	5.1	5.2	3.4	3.3
o/w HH sector	12.8	8.1	5.5	6.1	4.3	2.4	2.4	2.5	2.6	2.1	2.1
Coverage ratio	30.3	28.8	27.9	31.4	31.7	32.8	32.8	31.6	30.1	44.0	43.9
Return on equity <sup>(1)</sup>	7.3	6.8	3.2	-6.3	6.3	7.0	11.4	12.6	13.9	9.8	10.3
Return on assets <sup>(1)</sup>	0.8	0.8	0.4	-0.6	0.6	0.7	1.1	1.2	1.3	0.7	0.7
Total capital ratio	21.1	20.2	20.8	21.6	23.2	21.9	19.9	20.4	20.1	18.9	19.1
CET 1 ratio	18.3	17.8	17.7	17.1	18.1	16.9	15.1	15.6	15.4	15.5	15.8
Tier 1 ratio	19.1	18.5	18.9	19.2	20.1	19.1	17.2	17.7	17.4	16.7	16.9
Loan to deposit ratio	94.4	94.5	92.6	80.1	75.2	71.8	75.5	75.9	78.0	92.3	94.6

(1) For comparability reasons, annualised values are presented.

The figures in the table refer to all domestic banking groups and stand-alone banks in Ireland. These figures may differ from those reported in the text, which generally refer exclusively to the three main domestic retail banks.

Source: ECB - Consolidated banking data; own calculations.

**Despite overall improvements in credit quality and insolvency rates below their historical average, some business sectors display significant credit risks.** Overall, the credit quality of NFC loans kept improving in 2023, as some of the sectors hardest hit by the pandemic saw large reductions in their risk levels (in the hospitality sector, for example, the share of stage 2 and 3 loans declined from 56.27% to 28.39% and from 12.87% to 7.11%, respectively). These improvements were partly counterbalanced by a deterioration in the real estate sector, which remains the largest NFC sub-sector. Overall, at the end of 2023, 23.95% of loans to NFCs were classified as stage 2 and 4.73% as stage 3 (respectively 0.19 pps and 0.78 pps below their levels at the end of 2022). These positive developments in banks' exposures to the NFC sector were supported by low levels of bankruptcies in Ireland. Over the course of 2023, the number of registered insolvencies (0.27%) remained below the historical average of the past 19 years (0.52%) and pre-pandemic levels (0.36% in 2019), but they have been steadily increasing since 2021 (0.14%).

**The quality of mortgages remains solid, but the commercial property sector continues to face strong headwinds.** As described in Section 2, the Irish residential property market remains very tight, with supply shortages pushing up house prices and mitigating, together with the borrower-based macroprudential measures in place, banks' risks on outstanding mortgages. However, the increase in interest rates of the past two years has added pressure to many mortgage borrowers' debt-servicing capacity. In 2023, banks recorded a slight uptick in the share of stage 3 mortgages, from 2.0% to 2.2%, while the share of stage 2 mortgages was stable at 8%. The commercial real estate (CRE) sector, offices in particular, is still squeezed amid subdued demand, with offices recording price drops of over 15% in 2023. Irish banks' CRE loan book is worth EUR 16.3 billion compared to EUR 101.7 billion for the residential real estate sector. It represents 31% of exposures to NFCs, and its share of stage 2 and 3 loans increased, over the course of 2023, from 34% to 40% and from 6% to 7%, respectively. CRE loans have been granted under more conservative lending standards than before the global financial crisis, which should limit banks' losses in case of borrowers' defaults. However, continuous scrutiny is necessary as adverse CRE market developments may continue in the future.

**The broad stability of lending in the face of higher interest rates attests the strength of the Irish economy.** A slight increase in overall credit to the domestic non-financial private sector in 2023 was driven by mortgage lending to private households, which grew by 0.9% to EUR 84.2 billion. This increase can be attributed to growth in house prices and mortgage sizes, as the number of residential mortgage accounts decreased over the same period. Meanwhile, loans to Irish companies continued to contract, with outstanding amounts hitting a new low of EUR 52.5 billion at the end of 2023, 1.4% lower than a year before. Business lending had already been retreating for years, as the Irish business sector deleveraged after the financial crisis. This is especially true for Irish small and medium-sized enterprises (SMEs), half of which report not owing any debt. Outstanding loans to SMEs continued to decline, but new lending has been nearly stable in the past few years, averaging EUR 4.1 billion in the 4 years since 2019. For many SMEs, bank financing has been supplemented by non-bank lenders. Between December 2022 and December 2023 lending rates on new mortgages rose by 143 bps and lending rates on new NFC loans by 99 bps. From a financial stability

perspective, the proportion of variable rate loans has declined in recent years, reducing the burden of interest rate risks on households. In mortgages for main residences, the proportion of fixed rate loans was 64.3% in September 2023, compared to 34.5% at the end of 2019.

**Financial stability risks in the investment fund sector come mainly from liquidity mismatches and leverage, but links to the domestic economy are limited.** Ireland's market-based finance sector consists of investment funds, money market funds (MMF) and special purpose entities (SPE). Its investment fund sector is the EU's second biggest, with EUR 3.6 trillion in assets<sup>(9)</sup>. Leverage and liquidity mismatches are the biggest sources of risks in this sector. High leverage could lead to forced fire sales of assets in the event of adverse shocks, potentially leading to spillovers to systemically important parts of the financial system. Most investment funds' shares are held by international investors and invested mostly outside Ireland, making their links to the Irish economy quite tenuous. Irish property funds, on the other hand, have strong links to the Irish economy. They have EUR 24.4 billion of assets under management and, because of their business models, are highly leveraged (assets under management over net asset value of 191.5%) and have the highest illiquidity among fund types (3.5% liquid assets over total assets<sup>(10)</sup>). While the proportion of highly leveraged property funds (debt above 60%) was little changed at 30% and 32% in 2021 and 2022, respectively, given the price drops in the CRE sector in the past year, this has likely increased in 2023. MMF risks come mainly from maturity mismatches, which increased in early 2023. However, the sector has only limited links to the domestic economy. SPEs also have limited connections with the Irish economy and are internationally focussed. A significant and growing subgroup of SPEs are collateralised loan obligations, marketable securities backed by a pool of syndicated loans to sub-investment grade borrowers, amounting to EUR 222 billion in June 2023.

**Non-bank lenders remain a major source of credit for Irish companies, especially SMEs, but data gaps persist.** At the end of 2022, non-bank lenders (NBLs) held EUR 7.7 billion of loans to Irish SMEs. The proportion of NBLs in overall lending to SMEs, about 34% in mid-2023, has declined from its pandemic peak but remains on an upward trend. NBLs are a diverse set of institutions, with the most important types being asset finance providers, specialist property lenders, and general lenders. Their funding profiles are different from retail banks', with greater reliance on wholesale funding. On the other hand, asset finance providers are almost always funded by their group<sup>(11)</sup>. General and property lenders have a wide range of funding sources, with much of this funding from overseas. They rely chiefly on floating rate loans, exposing them to changes in financial conditions. Data gaps on non-bank lenders' activities persist, making it difficult to get a comprehensive and timely overview of this sector's lending activities and funding sources.

**The central bank kept its macroprudential measures steady.** In March 2024, the Central Bank of Ireland (CBI) announced that it would maintain the countercyclical capital buffer (CCyB) rate for Irish exposures at 1.5%, to be fully phased-in in June 2024. The position of the domestic banking sector remains solid, and while pockets of risk are evident (in the CRE market for example), broad systemic risks, which would warrant a reduction of the CCyB, have not crystallised at this stage. The CBI also requires supplementary capital buffers between 0.5% and 1.5% for six banks that are currently classified as other systemically important institutions. It also has a number of mortgage measures in place to ensure sustainable lending standards in the mortgage market. In November 2022, the CBI announced macroprudential policy measures for property funds. Existing funds were given until 24 November 2027 to comply with new leverage limits, but the limits already apply to all new funds. The CBI also introduced macroprudential measures for Irish GBP-denominated liability-driven investment funds, to make them more resilient to increases in yields.

<sup>(9)</sup> This group comprises equity funds, bond funds, other funds, hedge funds, GBP liability-driven investment funds, and Irish property funds.

<sup>(10)</sup> Figures from the second quarter of 2023.

<sup>(11)</sup> An example of this would be a subsidiary of a car manufacturer providing leasing services, with financing provided by the parent company.

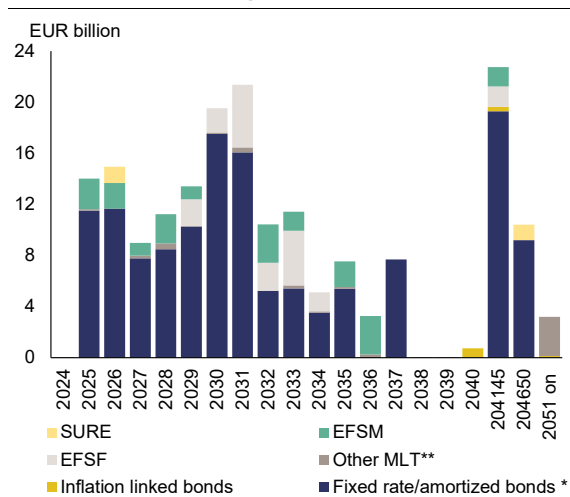
## 5. SOVEREIGN FINANCING AND CAPACITY TO REPAY

**Ireland's fiscal sustainability challenges appear low over the short and medium term, and medium over the long term.** The debt sustainability analysis shows that the government debt-to-GDP ratio is projected to continue declining over the medium term, to around 17% of GDP in 2034. Under an alternative scenario, where the interest-growth rate deteriorates by 1 percentage point of GDP compared with the baseline, the debt ratio would be somewhat higher than under the baseline by around 2 pps in 2034. However, under a scenario where the structural primary balance returns to its historical 15-year average of 2.0% of GDP, the debt ratio would be higher than under the baseline by about 34 pps. of GDP in 2034, though still below 60% of GDP. (see Annex 2).

**Ireland's cash reserves and debt structure protect it from refinancing risks.** In December 2021, the ECB began its monetary policy normalisation. Since then, it has raised its main policy rates by 4.5 pps and has kept them unchanged since October 2023. It has also ended its net purchases under the pandemic emergency purchase programme and has started to unwind the portfolio acquired under the asset purchase programme. Yields for the 10-year Irish government bond were around 2.9% at the end of April 2024, in line with the average throughout 2023. Spreads against the German benchmark were around 40 bps. Moreover, by the end of March 2024, Ireland had a liquid asset balance of more than EUR 10 billion. By the end of 2024, these balances are expected to have remained stable.

**Irish sovereign debt maintains its positive market presence and the confidence of investors.** All major rating agencies have positive rating or outlook on Ireland. Ireland issued EUR 4 billion of bonds in the first quarter of 2024, EUR 3 billion through a syndicated sale and EUR 1 billion in the first auction of the year. The funding range for the year is EUR 6-10 billion. As in previous years, the funding strategy hinges on maintaining market access and adding liquidity. Refinancing needs are low in the short term, but will be greater in the early part of the next decade. Interest expenditure on government debt is projected to be around 1% of GNI\* between 2024 and 2026, according to the Irish authorities' projections published on 22 April 2024.

Graph 5.1: **Maturity profile of medium-and long-term debt (end-April 2024)**



**Ireland retains the capacity to service its debt.** It has an outstanding debt of EUR 19.7 billion to the European Financial Stability Mechanism (EFSM) and EUR 18.4 billion to the European Financial Stability Facility (EFSF). Its first EFSF payment is scheduled for 2029 and EUR 2.4 billion of EFSM repayments are due in 2025. As of the end of 2023, official loans, Eurosystem bond holdings and domestic retail holdings – known as ‘sticky’ sources – accounted for about 60% of Irish government debt, in line with recent years. The investor base is broad, with a balanced split between non-resident and resident debt holdings. Demand for Irish sovereign debt is varied, with over half of the last syndications sold to investors from continental Europe and significant demand from the Nordics and the UK.

(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 EFSF and the EFSM.

\*Includes NTMA repo activity.

\*\* Excludes other medium and long-term loans (MLT) of EUR 5 million

Source: NTMA.

## ANNEX 1: MAIN MACROECONOMIC AND FINANCIAL INDICATORS

Table A1.1: Selected economic indicators

	2019	2020	2021	2022	2023	2024	2025
<i>Real economy</i>							
	<i>(percent change)</i>						
Real GDP	5.3	6.6	15.1	9.4	-3.2	1.2	3.6
Domestic demand incl. inventories	42.6	-10.7	-16.7	8.3	4.4	1.7	2.3
Private consumption expenditure	2.5	-10.8	8.5	9.4	3.1	2.3	3.1
Government consumption expenditure	6.2	10.3	6.6	4.5	1.9	1.1	0.8
Gross fixed capital formation	100.7	-16.5	-40.4	5.1	2.9	1.5	2.4
Exports of goods and services	11.8	11.5	15.1	13.9	-4.8	2.5	5.2
Imports of goods and services	42.3	-1.7	-7.5	15.9	0.4	3.0	4.6
<i>Contribution to growth</i>							
	<i>(percentage points)</i>						
Domestic demand (excl. inventories)	30.1	-10.9	-14.0	4.0	1.6	1.1	1.5
Foreign trade	-25.3	16.9	28.6	3.7	-6.9	0.4	2.3
Changes in inventories	0.3	0.6	0.5	1.0	1.0	0.0	0.0
<i>Inflation</i>							
	<i>(percent change)</i>						
GDP deflator	3.4	-1.2	0.5	6.6	3.0	2.6	1.9
HICP	0.9	-0.5	2.4	8.1	5.2	1.9	1.8
<i>Labour market</i>							
	<i>(percent change, unless otherwise stated)</i>						
Unemployment rate (% of labour force)	5.0	5.9	6.2	4.5	4.3	4.4	4.4
Employment	3.0	-2.8	6.0	6.6	5.4	1.6	1.5
Compensation per employee	3.8	3.7	2.6	2.7	2.7	4.4	4.1
Labour productivity	2.3	9.7	8.6	2.6	-8.2	-0.3	2.1
Unit labour costs	1.5	-5.5	-5.5	0.1	11.8	4.8	2.0
<i>Public finance</i>							
	<i>(percent of GDP)</i>						
General government balance	0.5	-5.0	-1.5	1.7	1.7	1.3	1.2
Total revenue	24.8	22.2	22.9	22.9	24.5	24.7	24.3
Total expenditure	24.3	27.2	24.4	21.2	22.9	23.4	23.2
General government primary balance	1.8	-4.0	-0.8	2.4	2.3	1.9	1.8
Gross debt	57.1	58.1	54.4	44.4	43.7	42.5	41.3
<i>Balance of payments</i>							
	<i>(percent of GDP)</i>						
Current external balance	-19.8	-6.5	13.7	10.8	9.9	9.1	9.5
Ext. bal. of goods and services	3.5	18.8	40.1	39.9	33.5	32.9	33.6
Exports goods and services	128.0	132.9	133.7	137.1	134.1	134.0	135.0
Imports goods and services	124.5	114.1	93.7	97.2	100.6	101.1	101.3
<i>(EUR bn)</i>							
Nominal GDP	356.4	375.2	434.1	506.3	504.6	524.0	553.3

Source: European Commission.



## ANNEX 2: DEBT SUSTAINABILITY ANALYSIS

**This annex assesses fiscal sustainability risks for Ireland over the short, medium and long term.** It follows the multi-dimensional approach of the European Commission's 2023 Debt Sustainability Monitor, updated based on the Commission's 2024 Spring Economic Forecast.

**1 – Short-term risks to fiscal sustainability are low.** The Commission's early-detection indicator (SO) does not point to any major short-term fiscal risks (Table A2.2) <sup>(12)</sup>. Government gross financing needs are expected to remain low in the short term at around 2% of GDP on average over 2023-2024 (Table A2.1, Table 1). Irish sovereign debt maintains its positive market presence and investor confidence. All major rating agencies have positive rating or outlook on Ireland.

**2 – Medium-term fiscal sustainability risks appear low.**

**The DSA baseline shows that the government debt-to-GDP ratio is projected to continue declining over the medium term, to around 17% of GDP in 2034.** (Graph 1, Table 1) <sup>(13)</sup>. The debt reduction is supported by the assumed structural primary surplus (excluding changes of cost of ageing) of 2.5% of GDP. This appears plausible compared with past fiscal performance <sup>(14)</sup>. The debt decline also benefits from a still favourable but decreasing snowball effect of 1.0% of GDP annually on average over 2025-2034. Government gross financing needs are expected to remain low over the projection period at 1.5% of GDP on average.

**The baseline projections are stress-tested against four alternative deterministic scenarios to assess the impact of changes in key assumptions relative to the baseline** (Graph 1). Under the *historical structural primary balance (SPB) scenario* (i.e. the SPB returns to its historical 15-year average of -2.0% of GDP) the debt ratio would be higher than under the baseline by about 34 pps. of GDP in 2034, though still below 60% of GDP. Under the *adverse interest-growth rate differential scenario* (i.e. the interest-growth rate deteriorates by 1 pp. of GDP compared with the baseline), the debt ratio would be somewhat higher than under the baseline by around 2 pps. in 2034. Under the *financial stress scenario* (i.e. interest rates temporarily increase by 1 pp. compared with the baseline) the government debt ratio would be broadly unchanged compared with the baseline in 2034. Finally, under the *lower structural primary balance scenario* (i.e. the projected cumulative improvement in the SPB over 2023-2024 is halved), the debt ratio would be slightly higher than under the baseline by about 4 pps. in 2034.

**The stochastic projections indicate low risk, pointing to a limited sensitivity of these projections to plausible unforeseen events** <sup>(15)</sup>. These stochastic simulations indicate a 20% probability that the debt ratio will be higher in 2028 than in 2023, implying low risks given the low debt level. Though, the uncertainty surrounding the baseline debt projections is medium, as 80% of the simulated debt paths lie in a wide range of 36 pps. in five years' time (Graph 2).

<sup>(12)</sup> The SO is a composite indicator of short-term risk of fiscal stress. It is based on a wide range of fiscal and financial-competitiveness indicators that have proven to be a good predictor of emerging fiscal stress in the past.

<sup>(13)</sup> The assumptions underlying the Commission's 'no-fiscal policy change' baseline include in particular: (i) a structural primary surplus, before ageing costs, of 2.5% of GDP from 2024 onwards; (ii) inflation converging linearly towards the 10-year forward inflation-linked swap rate 10 years ahead (which refers to the 10-year inflation expectations 10 years ahead); (iii) the nominal short- and long-term interest rates on new and rolled over debt converging linearly from current values to market-based forward nominal rates by T+10; (iv) real GDP growth rates from the Commission's 2024 spring forecast, followed by the EPC/OGWG 'T+10 methodology projections between T+3 and T+10 (average of 2.9%); (v) ageing costs in line with the 2024 Ageing Report (European Commission, Institutional Paper 279, April 2024). For information on the methodology, see the 2023 Debt Sustainability Monitor.

<sup>(14)</sup> This assessment is based on the consolidation space indicator, which measures the frequency with which a tighter fiscal position than assumed in a given scenario has been observed in the past. Technically, this consists of looking at the percentile rank of the projected SPB within the distribution of SPBs observed in the past in the country, taking into account all available data from 1980 to 2022.

<sup>(15)</sup> The stochastic projections show the joint impact on debt of 2000 different shocks affecting the government's budgetary position, economic growth, interest rates and exchange rates. This covers 80% of all the simulated debt paths and therefore excludes tail events.

**3 – Long-term fiscal sustainability risks appear overall medium.** This assessment is based on the combination of two fiscal gap indicators, capturing the required fiscal effort to stabilise debt (S2 indicator) and bring to 60% of GDP (S1 indicator) over the long-term<sup>(16)</sup>. This assessment is mainly driven by the projected increasing ageing costs and the favourable initial budgetary position.

**The S2 indicator points to medium fiscal sustainability risks.** The indicator shows that, relative to the baseline, the SPB would need to increase by 2.2 pps. of GDP in 2025 to ensure debt stabilisation over the long term. This result is driven by the projected increase in ageing-related costs (contribution of 4.5 pps. of GDP), which is only partly offset by the favourable initial budgetary position (-2.3 pp. pps. of GDP). In particular, the projected increase in pension expenditure (contribution of 2.6 pps. of GDP), but also of health-care and long-term care spending (+1.3 pps. and +1.1 pps. of GDP respectively) drive these results (Table A2.1, Table 2). Hence, while several investments and reforms in the RRP contribute to supporting the efficiency of the Irish health care system, additional measures may be required to further improve the efficiency and fiscal sustainability of the Irish long-term care system.

**The S1 indicator points to low fiscal sustainability risks.** The indicator shows that the country would not need to improve its fiscal position to bring its debt to 60% of GDP by 2070. This result is mainly driven by the projected increase in age-related public spending (contribution of 3.1 pps. of GDP), that is fully offset by the favourable initial budgetary position (-2.8 pps. of GDP) and the current distance of the government debt ratio from the 60% reference value (-0.4 pp. of GDP) (Table A2.1, Table 2).

**4 – Finally, several additional risk factors need to be considered in the assessment.** On the one hand, risk-increasing factors include higher interest rates, a relatively large share of short-term public debt as well as public debt held by non-residents and the negative net international investment position, though this largely reflects the presence of multinationals and the International Financial Services Centre<sup>(17)</sup>. Finally, alternative metrics to GDP suggest higher fiscal sustainability risks. On the other hand, risk-mitigating factors include relatively stable financing sources (with a diversified and large investor base), the currency denomination of debt, and historically still low borrowing costs.

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<sup>(16)</sup> The S2 fiscal sustainability indicator measures the permanent SPB adjustment in 2024 that would be required to stabilise public debt in the long term. It is complemented by the S1 indicator, which measures the permanent SPB adjustment in 2024 to bring the debt ratio to 60% by 2070. For both the S1 and S2 indicators, the risk assessment depends on the amount of fiscal consolidation needed: 'high risk' if the required effort exceeds 6 % of GDP, 'medium risk' if it is between 2% and 6% of GDP, and 'low risk' if the effort is negative or below 2% of GDP. The overall long-term risk classification combines the risk categories derived from S1 and S2. S1 may notch up the risk category derived from S2 if it signals a higher risk than S2. See the 2023 Debt Sustainability Monitor for further details.

<sup>(17)</sup> The thresholds used for the fiscal sustainability risk classification can be found in Table A1.3 on pp.125 of the 2023 Debt Sustainability Monitor.

Table A2.1: Debt sustainability analysis

Table 1. Baseline debt projections	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034
Gross debt ratio (% of GDP)	54.4	44.4	43.7	42.5	41.3	37.7	34.3	31.0	28.1	25.4	22.9	20.8	18.9	17.2
Changes in the ratio	-3.7	-10.0	-0.7	-1.2	-1.2	-3.5	-3.5	-3.3	-2.9	-2.7	-2.4	-2.1	-1.9	-1.7
of which														
Primary deficit	0.8	-2.4	-2.3	-1.9	-2.0	-2.0	-2.0	-2.0	-1.9	-1.8	-1.7	-1.5	-1.4	-1.3
Snowball effect	-7.1	-7.1	0.8	-0.9	-1.5	-1.6	-1.5	-1.3	-1.0	-0.9	-0.7	-0.6	-0.5	-0.4
Stock-flow adjustments	2.7	-0.5	0.8	1.6	2.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Gross financing needs (% of GDP)	5.7	2.5	1.8	2.6	3.5	2.2	1.6	1.5	1.4	1.0	1.2	1.2	1.1	0.5

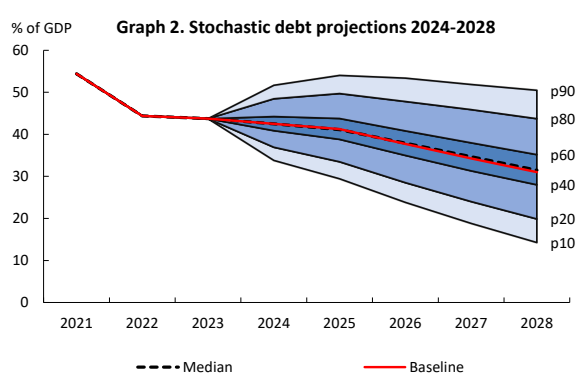
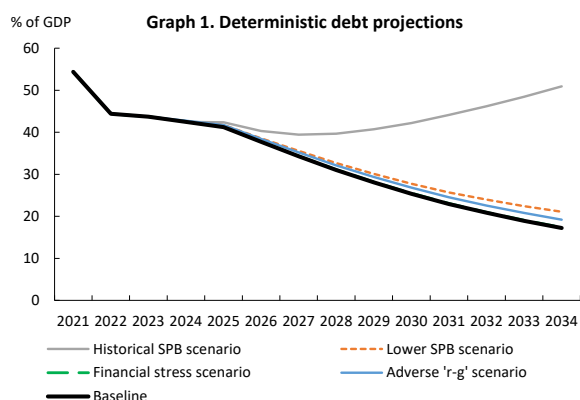


Table 2. Breakdown of the S1 and S2 sustainability gap indicators

	S1	S2
Overall index (pps. of GDP)	0.0	2.2
of which		
Initial budgetary position	-2.8	-2.3
Debt requirement	-0.4	
Ageing costs	3.1	4.5
of which		
Pensions	2.0	2.6
Health care	0.9	1.3
Long-term care	0.7	1.1
Education	-0.4	-0.5

Source: European Commission services.

Table A2.2: Heatmap of fiscal sustainability risks

Short term	Medium term - Debt sustainability analysis (DSA)							Long term			
	Overall (S0)	Overall	Deterministic scenarios					Stochastic projections	S2	S1	Overall (S1 + S2)
			Baseline	Historical SPB	Lower SPB	Adverse 'r-g'	Financial stress				
LOW	LOW	Overall	LOW	LOW	LOW	LOW	LOW	MEDIUM	LOW	MEDIUM	
		Debt level (2034), % GDP	17.2	50.9	21.1	19.2	17.4				
		Debt peak year	2024	2034	2024	2024	2024				
		Fiscal consolidation space	34%	70%	36%	34%	34%				
		Probability of debt ratio exceeding in 2028 its 2023 level									20%
							36.2				

(1) Debt level in 2034. Green: below 60% of GDP. Yellow: between 60% and 90%. Red: above 90%. (2) The debt peak year indicates whether debt is projected to increase overall over the next decade. Green: debt peaks early. Yellow: peak towards the middle of the projection period. Red: late peak. (3) Fiscal consolidation space measures the share of past fiscal positions in the country that were more stringent than the one assumed in the baseline. Green: high value, i.e. the assumed fiscal position is plausible by historical standards and leaves room for corrective measures if needed. Yellow: intermediate. Red: low. (4) Probability of debt ratio exceeding in 2028 its 2023 level. Green: low probability. Yellow: intermediate. Red: high (also reflecting the initial debt level). (5) The difference between the 90th and 10th percentiles measures uncertainty, based on the debt distribution under 10000 different shocks. Green, yellow and red cells indicate increasing uncertainty. (For further details on the Commission's multidimensional approach, see the 2023 Debt Sustainability Monitor).

Source: European Commission (for further details on the Commission's multidimensional approach, see the 2023 Debt Sustainability Monitor).

## ACKNOWLEDGMENTS

This Post-Programme Surveillance assessment was prepared in the Directorate-General for Economic and Financial Affairs of the European Commission under the guidance of Declan Costello, Deputy Director General, Isabel Grilo, Director, and Robert Kuenzel, Deputy Head of Unit for Ireland <sup>(18)</sup>.

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The report was prepared in liaison with staff from the ECB <sup>(19)</sup>. Staff from the European Stability Mechanism (ESM) also provided comments.

This report reflects information available and policy developments that have taken place until 30 April 2024. Therefore, the macroeconomic and budgetary projections, including those underlying the debt sustainability analysis, are in line with the Commission 2024 spring forecast released on 15 May 2024 (with a cut-off date of 30 April 2024).

Comments on the report would be gratefully received and should be sent, by mail or e-mail, to:

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<sup>(18)</sup> The executive summary of this report was adopted as Commission Communication C(2024)4000 on 18 June 2024. The rest of the report reflects the findings of the Staff Working Document (SWD(2024)400) accompanying this communication.

<sup>(19)</sup> European Central Bank (ECB) staff participated in this mission, and 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.

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