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Post-Programme Surveillance Report

Ireland, Autumn 2019

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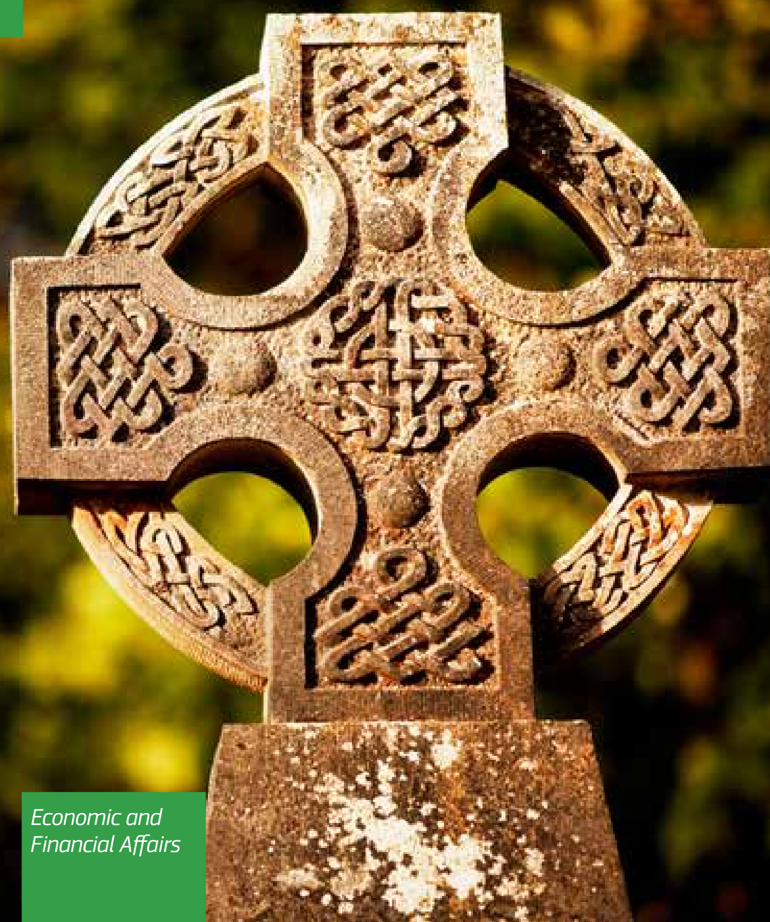
EUROPEAN ECONOMY



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European Commission
Directorate-General for Economic and Financial Affairs

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Institutional Paper 122

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This report reflects information available up until 9 January 2020.

([1]) The report was adopted as Commission Communication C(2020)591 on 30 January 2020, 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

CBD	Consolidated banking data (database)
CBI	Central Bank of Ireland
CCyB	Counter-cyclical capital buffer
CET1	Common Equity Tier 1
CRE	Commercial real estate
CSO	Central Statistics Office Ireland
DoF	Department of Finance
ECB	European Central Bank
EFSF	European Financial Stability Facility
EFSM	European Financial Stabilisation Mechanism
ESRB	European Systemic Risk Board
ESRI	Economic and Social Research Institute
GDP	Gross Domestic Product
GNI*	Modified Gross National Income
HICP	Harmonised Index of Consumer Prices
ICT	Information & Communication Technology
LTI	Loan-to-income
LTV	Loan-to-value
NPLs	Non-performing loans
NTMA	National Treasury Management Agency
PBO	Parliamentary Budget Office
PPS	Post-programme surveillance
RDF	Rainy Day Fund
SME	Small and medium sized enterprises
y-o-y	Year-on-year

EXECUTIVE SUMMARY

Staff from the European Commission, in liaison with staff from the European Central Bank, visited Dublin from 19 to 21 November 2019 for the twelfth post-programme mission to Ireland. This was coordinated with an International Monetary Fund Staff Visit. 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, albeit subject to substantial domestic and external risks. Although uncertainty has recently been weighing on business and consumer sentiment, strong employment growth and rising wages continue to support household income and private consumption. Construction investment is expanding at a solid pace, though still from a low base. The tight labour market, rising net inward migration and diminishing spare capacity point to an economy possibly operating above its potential. Increases in property prices have recently abated, but their levels remain high. Significant uncertainty continues to surround the economic outlook, in particular as regards the future relationship between the UK and the EU, as well as changes in the international taxation and trade environment.

Notwithstanding continued improvement in public finances, vulnerabilities remain. While the general government debt to GDP ratio is estimated to have fallen below 60% in 2019, public debt remains high based on more tailored metrics. This limits the room to respond to negative economic shocks. Risks to the fiscal outlook are tilted to the downside. They mainly reflect uncertainty surrounding the economic outlook, in particular regarding the future relationship between the UK and the EU, the sustainability of the amount of corporation tax receipts and over-spending within certain sectors. The mission emphasised that, in view of these risks and the favourable cyclical position including buoyant corporate tax revenue, the resilience of public finances to adverse shocks should be further enhanced by strengthening fiscal buffers. This could be achieved by firming up the rainy day fund, reducing public debt and broadening the tax base. It also highlighted that more prudence on the spending side is warranted in view of the pattern of spending overruns in recent years, in particular in the healthcare sector.

Further sales of non-performing loans have improved banks' asset quality, but the level of long-term arrears remains relatively high and persistent. While there is significant heterogeneity among Irish banks, they all have successfully engaged in sales and securitisations of non-performing loans. Recently announced or concluded non-performing loans transactions will further support their balance sheet repair. The stock of long-term arrears in the financial system remains significant, reflecting a number of obstacles to their resolution. Irish banks are well capitalised and liquid, but longer-term challenges related to profitability and costs remain. In the current environment where some of the Irish banks are producing low returns, their internal capital generation remains weak. This, combined with the slightly lower than average provisioning levels, renders the banks more vulnerable to adverse shocks. Capital- and borrower-based macro-prudential measures put in place by the Central Bank of Ireland are strengthening the resilience of both banks and households.

Risks for Ireland's capacity to service the European Financial Stability Mechanism (EFSM) and European Financial Stability Facility (EFSF) debt remain low. Market access conditions for the Irish sovereign remain favourable. The debt sustainability analysis shows that the debt-to-GDP ratio is expected to decrease further in the medium-term but remains vulnerable to unfavourable shocks. The National Treasury Management Agency held cash buffers of EUR 16.5 billion at year-end 2019 in advance of peak redemptions in 2020.

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1. INTRODUCTION

Staff from the European Commission, in liaison with staff from the ECB, visited Dublin from 19 to 21 November 2019 to conduct the twelfth post-programme surveillance (PPS) mission for Ireland. This was coordinated with an International Monetary Fund staff visit. Staff from the European Stability Mechanism participated in the meetings in the context of its Early Warning System. 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

Real GDP growth remains strong but the outlook is surrounded by heightened uncertainty. In the first three quarters of 2019, Ireland's real GDP grew by 5.9% y-o-y, well above the euro area average. Headline national accounts figures were again bloated by the activities of multinational companies. GDP growth is expected to remain robust, but to moderate in 2019 and 2020, on the back of the worsening outlook for global trade and lingering uncertainty regarding the terms of the UK's withdrawal from the EU. The European Commission Autumn 2019 forecast projects real GDP to grow by 5.6% in 2019, 3.5% in 2020 and 3.2% in 2021.

Domestic activity is moderating but remains robust. Private consumption and the construction of dwellings were the main drivers for growth. *Modified domestic demand*, a measure of domestic activity that strips out some of the effects of multinationals, grew by 1.5% year-on-year in the first three quarters of 2019. Early indicators, such as business and consumer sentiment, suggest slowing growth in the second half of the year due to the lingering uncertainty, particularly in relation to the UK's terms of exit from the EU. Economic sentiment substantially weakened since mid-summer across all the major surveyed categories, although there was a turnaround of the mood in November, when markets re-assessed that the risk of a 'no-deal' Brexit has diminished. The unwinding of uncertainty regarding the future relationship between the UK and the EU could therefore effectively bolster modified domestic demand.

The strong labour market suggests that the Irish economy is operating at or above its potential. Driven by robust employment growth, the unemployment rate has continued to decline to 4.8% in October and stabilised in November. The share of part-time workers has also contracted, indicating increasing labour supply constraints ([4]). Net inward migration somewhat alleviates this problem, but structural obstacles, notably a lack of childcare facilities, housing and transport, limit the possibilities to attract and retain employees. Reportedly, these capacity constraints have already started to impact firms' investment decisions, with moderating effect on growth in the future. Earnings kept rising in a tight labour market, which, together with higher employment, is bolstering household disposable income. Average hourly earnings accelerated to 4.0% y-o-y in the third quarter. Rising income, nevertheless, did not fully translate into consumption increases. Precautionary motives led Irish households to increase their savings, as reflected by an accelerating rise in deposits over the recent months.

The information and communication technology (ICT) sector continues to drive growth and employment. Dominated by multinationals, the ICT sector has a high job vacancies rate and fast rising earnings. Vacancies were also trending upward in other rapidly expanding sectors, such as professional, scientific and technical activities. Hourly earnings accelerated in wholesale and retail trade, administrative and support services, and the accommodation and food sector. Wage levels in different sectors, however, vary substantially.

Headline investment surged, but heightened uncertainty dragged down underlying domestic investment. Headline investment figures remain driven by volatile intangible and aircraft investment. In the first three quarters of 2019, headline investment sharply increased, driven by intellectual property investment in the second quarter of 2019 ([5]). By contrast, modified investment ([6]), which excludes some of the activities of multinationals, decreased by 1.5% y-o-y over the same period. Investment in construction increased by 3.2% y-o-y in the first three quarters of 2019 and is expected to remain robust, as housing supply is still catching up with

([4]) The share of part-time workers, one fifth of the total labour force, remains sizable.

([5]) 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.

([6]) Modified investment corresponds to investment in construction, machinery and equipment excluding aircraft related to leasing and intangible assets excluding research and development service imports.

demand. By contrast, investment in machinery and equipment has weakened in recent quarters ([7]).

Exports remain robust despite global trade weakness. In the first three quarters of 2019, exports increased by 12.2% y-o-y, driven by pharmaceuticals and computer services. Strong imports of royalties, licenses and R&D services in recent quarters are expected to support export growth in ICT services in the future. Hence, despite the worsening external environment, exports are expected to remain robust, as trade in pharmaceuticals and computer services, which represent a significant share of Irish exports, is less sensitive to changes in the overall global demand than trade in other sectors.

Inflation remains modest. Higher wages have not passed through to consumer price inflation yet. HICP inflation was 0.9% y-o-y on average in the first three quarters of 2019. Rents and catering have bolstered services prices. Services are expected to continue to be the main inflation driver, consistent with strong domestic demand. By contrast, prices of non-energy industrial goods keep decreasing, which reflects high global competition, the impact of Sterling depreciation and a downward bias related to quality adjustments ([8]). HICP inflation is projected to remain low, at 0.8% in 2019, 1.1% in 2020 and 1.4% in 2021.

Country-wide residential price inflation has continued declining. In September, annual residential price inflation moderated to 1.1%. It even registered negative values (-1.3%) in Dublin for the second consecutive month.

Housing rental inflation is still high due to a persistent rental supply gap. In the second quarter of 2019, the annual price increase in the rental market for new or renewed tenancies was 7.6% on average outside Dublin, which is 1.2 pps. higher than in the same period in 2018. In Dublin housing rent inflation was 7.1% in the same period, down from +9.2% in the second quarter of 2018. The evolution of rental prices reflects changes in housing rental supply, with the number of properties available for rent increasing by 10% to 1 500 in Dublin in the year to August while the availability decreased countrywide. In Dublin, the stock of rental houses is expected to increase by 20% between 2019 and 2023, with 26 281 units currently in the pipeline. A large part of the supply consists of built-to-rent developments with around 22 000 units being planned in Dublin and Cork and close to 3 600 being currently under construction in Dublin. Newly created units are largely targeting middle to high income professionals and therefore might be unaffordable for students or lower income groups ([9]).

Price and rent increases in the commercial real estate market have moderated in recent years. In the first quarter of 2019, commercial real estate (CRE) yields remained well above sovereign bond yields. However, while higher than in other European locations ([10]), they remain low by historical standards ([11]). In the second quarter of 2019, CRE capital values and rents were 2.3% and 0.9%, respectively, higher year-on-year. This compares with increases by 30% and 20%, respectively, at the end of 2014 ([12]). Following a broadly declining trend since 2016, sentiment indices for tenant and investment demand were approaching negative territory in the first quarter of 2019 ([13]). While demand for office and industrial rental continued increasing during this period, albeit at a slower pace, tenant demand declined in the retail sector after having stagnated for three quarters.

The macroeconomic outlook is clouded by heightened external uncertainty. External risks relate to an escalation of international trade tensions as well as to changes in the international taxation environment. Furthermore, in the context of Brexit, trade barriers, currency volatility and lower demand from the UK could severely affect Irish exporting sectors, such as agri-food, fisheries, indigenous manufacturing and tourism. Delays to the transit of goods at the UK border following the introduction of new customs requirements could

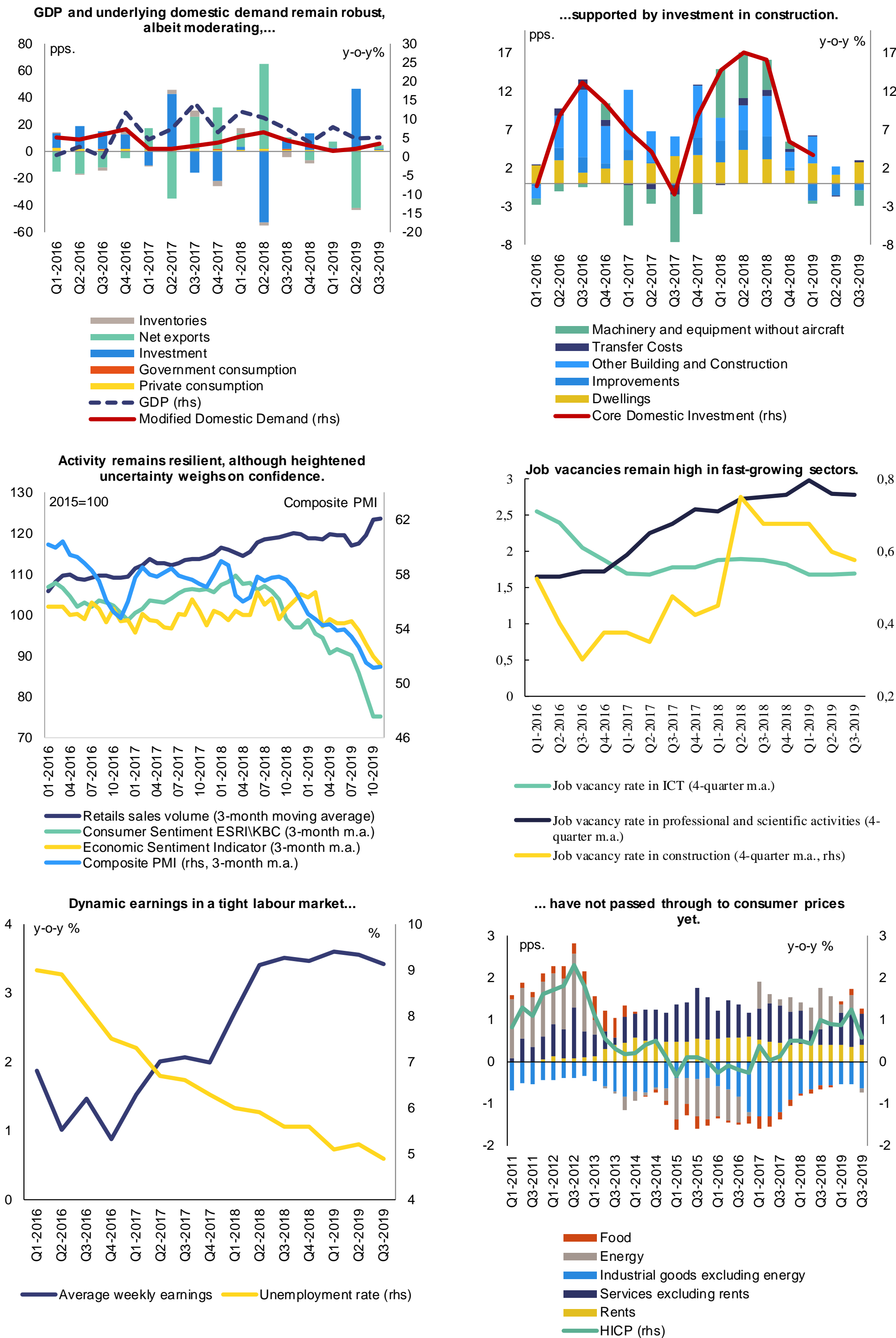
([7]) The CSO did not publish machinery and equipment investment figures for the second quarter of 2019 for confidentiality reasons.
([8]) J. Keating and M. Murtagh (2018), Quality adjustment in the Irish CPI, CSO meeting of the Group of Experts on Consumer Prices Indices, 7-9 May 2018.
([9]) Daft (2019), Irish Rental Report Q2 2019.
([10]) CBRE (2019), Real State Market Outlook 2019.
([11]) Central Band of Ireland (2019), Financial Stability Review. 2019-1.
([12]) JLL (2019), JLL Irish Property Index- Q2 2019.
([13]) Society of Chartered Surveyors Ireland and RICS (2019), Q1 2019: Ireland Commercial Property Monitor.

also disrupt Irish supply chains, and in turn, affect the price and availability of consumer goods. An increase in uncertainty and a further fall in business and consumer confidence could lead firms and households to hold back investment and consumption. The strong linkages between Ireland and the UK mean that a disorderly Brexit could also have a negative effect on investor sentiment towards Irish assets. On the other hand, Ireland might benefit from the relocation and diversion of FDI from the UK. However, this positive impact would likely be outweighed by the negative trade effects ([14]).

In the absence of adverse external shocks the risks of overheating on the domestic side could increase. The tight labour market, net inward migration and diminishing spare capacity all point to an economy possibly operating above its potential. The use of volatile multinational company sourced corporation tax receipts to stimulate domestic demand could also contribute to overheating ([15]). In addition, the exposure of Ireland to global value chains via some multinationals could drive headline economic growth in either direction.

([14]) A. Bergin, P. Economides, A. Garcia-Rodriguez and G. Murphy, 'Ireland and Brexit: modelling the impact of deal and no-deal scenarios', ESRI and Irish Department of Finance (2019).
([15]) Irish Fiscal Advisory Council (2019), Fiscal Assessment Report, June 2019.

Graph 2.1: Recent economic developments



(1) The breakdown of modified investment is not available for Q2 2019 as machinery and equipment investment figures were not published for confidentiality reasons.
Source: European Commission, Central Statistics Office, Markit, ESRI\KBC.

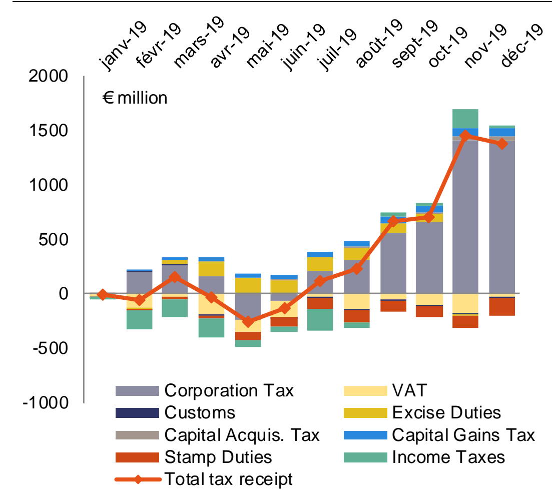
2.2. PUBLIC FINANCES

Public finances continue to improve. The headline government position turned from a deficit of 0.3% in 2017 to a small surplus of 0.1% of GDP in 2018. In the first half of 2019, the government deficit stood at -0.1% of GDP, compared with -1.5% in the same period last year ([16]). Government revenues were up by 7.2%, driven by strong corporate tax receipts while expenditure increased by 1.1%. A continued fall in the interest burden has contributed to the deficit reduction. The improvement in the non-interest budget balance since 2015 has been weaker, as pointed out by the Irish Fiscal Advisory Council ([17]).

The Exchequer position was better than expected in 2019. Tax receipts at the end of December were up by 6.8% y-o-y and 2.4% ahead budget target, reflecting a favourable economic climate. All major tax categories have performed broadly in line with, or above, expectations (Graph 2.2). Corporate tax receipts were 14.9% above profile, with an annual growth of 4.8%. Gross voted expenditure was up by 6.9% y-o-y and 1.2% above profile. Current expenditure was up by 5.2% y-o-y and 1.3% ahead of profile. Capital expenditure (+22.5% y-o-y) was 0.3% above profile. Overall, an Exchequer surplus of EUR 647 million was recorded at the end of December 2019, compared with a surplus of EUR 99 million in the same period last year.

Public finances are set to further improve. The general government balance is expected to have slightly increase to 0.2% of GDP in 2019, from 0.1% in 2018, based on European Commission 2019 autumn forecast ([18]). Projections are based on an expected robust 5.7% increase in tax revenue and a 5.1% increase in expenditure. The latter includes a marked rebound of public investment (+23.7%) linked to the infrastructure projects comprised in the National Development Plan. According to the Commission 2019 autumn forecast, the general government surplus is expected to improve to 0.3% of GDP in 2020 and to 0.6% of GDP in 2021, based on a no-policy change assumption.

Graph 2.2: Differences between exchequer outcomes and profile



Source: Department of Finance, Fiscal Monitors

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, including in the context of the ongoing review of the global tax system, and over-spending within some sectors.

Budget 2020 is based on a no-deal Brexit scenario. This scenario implies a slowdown in the economic growth in 2020, which would lead to lower government revenue linked to, *inter alia*, expected weaker tax receipts. On the expenditure side, it includes contingency provisions of EUR 1.2 billion (0.35% of GDP) in 2020 for temporary and targeted expenditures that will be defined and implemented only in the event of a no-deal Brexit. This includes EUR 650 million (around 0.2% of GDP) to support the sectors identified as most affected, EUR 410 million for employment support (most of which reflecting the operation of automatic stabilisers) and EUR 160 million for necessary compliance checks at ports and customs.

Although public debt-to-GDP ratio is declining, alternative indicators suggest that Ireland is still running high levels of public debt. In 2018, the level of debt increased by approximately

([16]) Figures are reported here on accrual basis. Based on end-2019 Exchequer figures, a surplus of 0.4% of GDP is likely in 2019.
([17]) Irish Fiscal Advisory Council (2019), Fiscal Assessment Report, November 2019.
([18]) European Commission (2019), European Economic Forecast Autumn 2019, Institutional Paper 115, November 2019. The estimates do not take into account the latest Exchequer out-turn for 2019.

Table 2.1: Financial soundness indicators, all domestic and foreign banks in Ireland

	2014	2015	2016	2017	2018q1	2018q2	2018q3	2018q4	2019q1	2019q2
Non-performing loans	21.6	14.9	13.1	9.9	9.8	8.5	7.8	5.5	4.7	4.2
o/w foreign entities	18.2	10.1	9.2	7.1	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
o/w NFC & HH sectors	28.4	20.5	16.6	14.1	13.7	11.8	10.9	8.2	7.3	6.8
o/w NFC sector	37.8	22.9	15.3	11.8	11.0	9.1	8.1	5.7	5.0	4.4
o/w HH sector	22.8	19.1	17.4	15.5	15.4	13.4	12.5	10.1	8.9	8.5
Coverage ratio	46.7	40.2	35.5	29.9	33.3	32.1	31.0	28.5	28.5	27.4
Return on equity(1)	8.5	6.8	6.3	5.0	6.3	6.9	6.4	4.9	5.2	4.5
Return on assets(1)	0.9	0.9	0.9	0.7	0.9	1.0	0.9	0.7	0.7	0.6
Total capital ratio	22.6	25.3	25.0	25.2	24.3	25.2	25.6	25.4	24.6	24.3
CET 1 ratio	20.1	22.3	22.2	22.9	22.1	23.0	23.4	22.9	21.9	21.8
Tier 1 ratio	20.5	23.2	23.0	23.4	22.6	23.5	23.9	23.4	22.5	22.4
Loan to deposit ratio	98.8	98.7	93.2	95.3	91.8	88.5	88.4	90.2	90.3	89.8

(1) For comparability reasons, annualized values are presented.
Source: ECB CBD

EUR 5 billion, while the general government debt-to-GDP ratio declined to 63.6% of GDP in 2018 on the back of strong GDP growth. Based on the Commission 2019 autumn forecast, this ratio is estimated to have declined to 59.0% of GDP in 2019 and projected to further fall to 53.9% in 2020, contingent on continued economic growth and positive primary balances. However, alternative metrics show that the level of debt remains high by historical and international standards. As a proportion of modified GNI (GNI*) ([19]), the public debt ratio was at 104.3% in 2018. The interest-to-revenue ratio was also high at 6.4% ([20]). Although further improving, debt sustainability remains vulnerable to unfavourable shocks in the medium-term (see Annex 1).

2.3. FINANCIAL SECTOR

Irish banks are well capitalised and liquid. The CET1 ratio of the Irish banking sector, including both domestic and foreign-owned banks, was 21.8% as of June 2019, which is among the highest in the EU (Table 2.1). However, foreign-owned subsidiaries, which are less retail-oriented than the largest Irish banks, were responsible for most of this excess capital position ([21]). These high capital levels should help alleviate potential worsening in credit portfolios in line with some of the adverse scenarios. A countercyclical capital buffer (CCyB) rate of 1% has been implemented in July 2019, introducing an additional cushion that could be released in the event of a downturn.

Despite healthy capital levels, the banking sector faces several challenges. Brexit uncertainty and concerns over the banking systems' direct and indirect exposures to the UK have contributed to significant downward pressure on share prices of Irish banks since early 2019. Subdued credit growth along with limited investment opportunities have resulted in an adequate build-up of liquid assets, such as cash and central bank deposits. This excess liquidity, banks' reluctance to apply negative deposit rates, as well as increased competition in mortgage lending, including from the non-bank financial sector, is driving net interest margins lower, currently at 2.1% ([22]). The retail banks continue to look for ways to cut costs, including lowering staff count, as well as branches closures. All these challenges come at a time when the banks are investing heavily in updating their information technology systems. Finally, although house price growth has significantly moderated in 2019, existing vulnerabilities in the Irish residential real estate

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

([20]) Alternative metrics showing that the debt burden is high in Ireland are debt-to-revenue ratio, debt as a fraction of the national pay-bill and debt per capita (Department of Finance (2019), Annual Report on Public Debt in Ireland 2019, August 2019).

([21]) The CET1 ratio for the domestic banking groups, including the largest three Irish banks Bank of Ireland, Allied Irish Banks, and Permanent TSB, was much lower at 17.6% in June 2019, slightly down from 18.4% a year earlier.

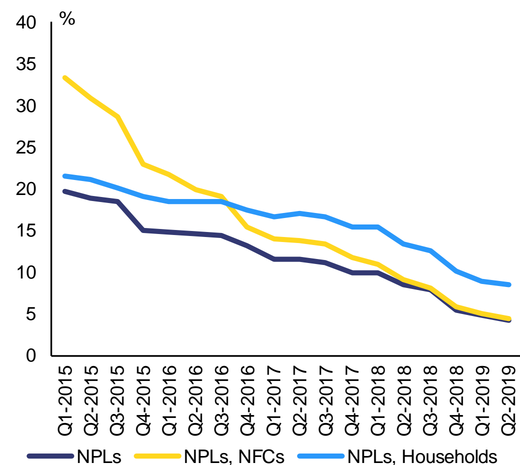
([22]) Nevertheless, Irish banks continue to have higher net interest margins than most of their euro area counterparts, which have an EU average net interest margin of 1.4% as of mid-2019, according to data from EBA's Risk Dashboard for the second quarter of 2019.

sector could have adverse effects on the banking sector, should they materialise ([23]).

Credit growth has improved in the second half of 2019, although it is too soon to determine whether this will be sustained. Growth in new mortgage loans has been significant over the past year, with the volume of new mortgage loans (excluding renegotiations) issued in the 12-month period leading to October 2019 increasing by 11% on the same period a year ago, according to CBI data. Meanwhile, new corporate loans that are below EUR 1 million, which are mostly issued to SMEs, have increased by around 10% on average over 12-months leading to October 2019. Despite this improved outlook, new credit issuance remains quite volatile and may decline substantially in the upcoming months due to external uncertainties.

Banks' asset quality has improved in recent quarters following further sales and securitisations of NPL portfolios. According to ECB data, banks have further reduced their NPL stocks, which accounted for 4.2% of total loans at the end of the second quarter of 2019, down from 8.5% a year earlier ([24]). This ratio is poised to further decline, as new NPL transactions have been announced or concluded in the second half of 2019. Retail mortgages make up 72% of the overall NPL stock. While the share of household loans that are non-performing has continuously declined over the past five years, it represented 8.5% at the end of the second quarter of 2019, which remains high in comparison to the EU average (3.1%) and to the equivalent rate for non-financial companies (4.4%). All major Irish retail banks have sold NPLs and typically encountered high buyer demand. However, the distribution of NPLs across banks remains uneven, and banks with high NPL-ratios remain more vulnerable to shocks and limited in their lending capacity. The supervisory focus pertaining to NPL workout accordingly remains high.

Graph 2.3: Non-performing loan ratios (% of gross loans)



Source: ECB CBD

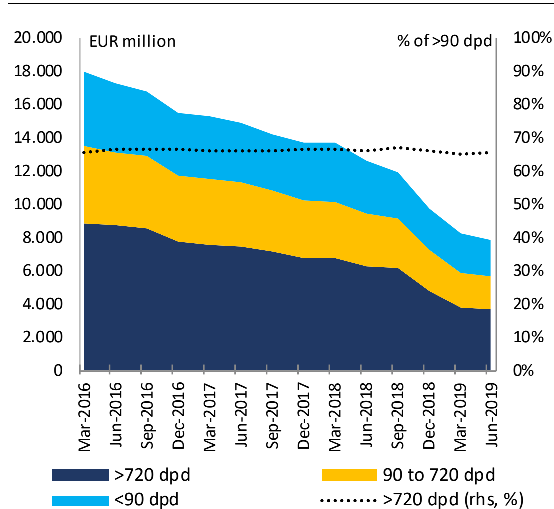
Long-term mortgage arrears in the banking sector account for a significant proportion of the NPLs. Recent NPL sales and securitisations have focussed on long-term arrears (loans that are more than 720 days past-due). These loans represent two-thirds of all loans that are more than 90 days past-due, and they are likely to be the most challenging to be resolved, in spite of the existence of public programmes such as the Mortgage-to-Rent scheme ([25]). At the end of the second quarter of 2019, almost 19 000 mortgage accounts held by banks, with an outstanding balance of EUR 3.7 bn, were in long term arrears. More than 70% of this balance relates to primary dwelling homes, with the rest related to buy-to-let properties. Meanwhile, repossession activity remains relatively limited, inter alia due to reputational risks for banks when exercising collateral enforcement options, and lengthy recovery proceedings and a limited use of contractual write-offs.

([23]) The European Systemic Risk Board (ESRB) has identified vulnerabilities in the housing sector, notably related to high household debt and strong price increases. However, it considers that the mortgage measures put in place by the Central Bank effectively mitigate those risks. See ESRB, Vulnerabilities in the residential real estate sectors of the EEA countries, 23 September 2019.

([24]) Based on financial reporting (FINREP) data published by the ECB. Narrowing the sample to the five Irish retail banks yields somewhat higher NPL-ratios, but the underlying trends and developments remain unaffected.

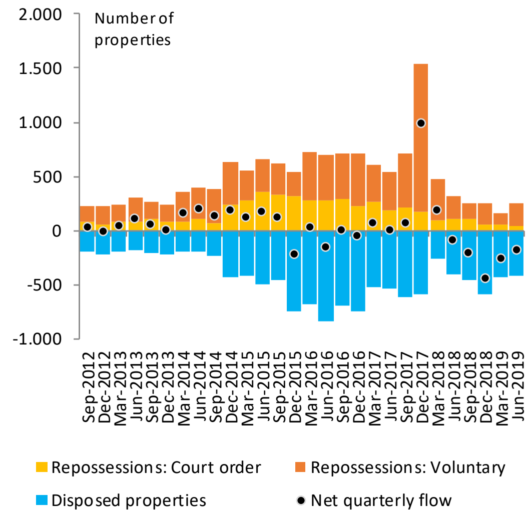
([25]) Scheme that supports mortgage holders in arrears. Under this scheme, a homeowner's property is bought by an approved housing body and rented out to the original mortgage holder, who remains in it as a social tenant. The scheme was revised over the course of 2017 with a range of amendments to eligibility criteria and administration in view of making it more flexible and accessible to borrowers.

Graph 2.4: Residential mortgage arrears in the banking sector



The graph distinguishes between all loans held by banks in terms of days past-due ('dpd').
Source: CBI

Graph 2.5: Residential mortgage repossessions



Figures include activity by banks, credit servicers, and retail credit firms. Disposed properties are those that were sold, which no longer remain on the balance sheets of the financial institution that held the assets.
Source: CBI

NPL sales by banks imply that mortgages in arrears are increasingly held by non-bank entities. At the end of the second quarter of 2019, non-bank entities held 42% of all mortgage accounts in arrears, representing 50% of the outstanding balance (based on CBI mortgage arrears data). This compares to 20% and 24%, respectively, in the second quarter of 2016. The presence of non-bank entities is particularly strong in the long-term arrears over 720 days, where they held 54% of accounts, representing 60% of the outstanding balance.

The number of repossessions remains low. Despite concerns in recent years over increasing collateral enforcement activity by NPL acquirers, the overall number of repossessions that were initiated each quarter has been declining since early 2018 while an increasing share of all repossessions is voluntary (Graph 2.5). Moreover, although they hold more than a quarter of the total stock of mortgage arrears, the number of repossessed properties held by credit acquirers represent only 12% of the total. While some of these developments may be linked to the introduction of the Mortgage-to-Rent scheme, current figures provide no evidence that repossession activity is speeding up or that credit acquirers are more likely to engage in repossessions.

While NPL reduction contributes to balance sheet repair, banks' aggregate provisioning for NPLs appears low. The average coverage ratio for the Irish banking sector was 27.4% in June 2019, down from 32.1% a year ago. This ratio is lower than the EU average of 46.2%. While both the trend and current level of the average coverage ratio for the Irish banking sector is largely explained by the predominance of non-performing mortgage loans, there appears to be significant variability between different banks. Moreover, the coverage ratios of non-mortgage exposures, including most notably commercial real estate and other corporate sectors, appear lower than the EU averages ([26]).

Ireland's large and growing non-bank financial sector deserves continuous monitoring. In the EU, a sound regulatory framework for investment funds was put in place after the crisis and supervisory tools are available to deal with particular stress episodes. However, investment

([26]) According to a recent report by EBA, the average coverage ratios for the CRE, SME, and large corporate sectors were 37.2%, 49.8%, and 67.6% as of June 2019. In comparison, figures reported by the Central Bank of Ireland show that the average coverage ratio for Irish banks' non-performing CRE and corporate exposures (comprising mostly of SME loans) were 29.5% and 42.5%, respectively. For more, see EBA (2019), *EBA Report on NPLs: Progress Made and Challenges Ahead.*

funds with strong liquidity mismatches or high leverage are vulnerable to shocks, which may have adverse repercussions for financial stability, both at national and international level. Although the funds industry has relatively modest direct links with the local economy, its sheer size (the net asset value of Irish resident investment funds, including money market funds, stood at EUR 2.9 trillion at the end of the third quarter of 2019, making Ireland the second largest investment fund domicile in the EU after Luxembourg) and growing interconnectedness within the financial system exposes Ireland to global shocks.

A significant proportion of the gross premium incomes of Irish insurers are based on UK businesses. Although the authorities have enacted temporary regimes to address these challenges, it remains to be seen how Brexit will impact insurers' business models in the long term. The Irish insurers are also highly exposed to the UK market through their investment portfolios. This exposes them to exchange rate and market risk in case of market valuation fluctuations, although the predominance of unit linked business and the matching of assets and liabilities (by currency and duration) mitigates the impact of such fluctuations on firms.

3. POLICY ISSUES

3.1. PUBLIC FINANCES

While the overall fiscal outlook is positive, prudence on the expenditure side is warranted. In recent years, there has been a tendency for spending to accelerate towards the end of the year, which put Ireland at risk of not complying with EU fiscal rules. Budget 2020 prudently already incorporates some expected overruns in 2019, in particular related to health care expenditure ([27]). It also includes additional funds for the Christmas bonus. Furthermore, the Irish Fiscal Advisory Council highlighted that some other areas are facing expenditure slippages, including the local government and housing bodies ([28]). Enhancing current expenditure planning and control, and ensuring its growth is sustainable remains highly important to increase the resilience of public finances. To this end, the extent to which the spending review process could improve budget planning and administration remains unclear. In 2020, the Department of Public Expenditure and Reform plans to examine the degree to which the process has achieved its objectives and ways to improve it.

The sustainability of the current high level of corporate tax revenue is uncertain. In 2018, receipts from corporate taxes reached a record of 18.7% of total tax revenue. These proceeds remain heavily concentrated among a small group of companies, with the top ten firms accounting for 8.5% of the total tax revenue in 2018. Foreign multinational companies account for approximately 77% of total corporate tax receipts and 25% of all income tax receipts ([29]). The Parliamentary Budget Office (PBO) reckons that if a typical large multinational left Ireland, it would reduce revenue by approximately EUR 440 million (around 0.7% of total revenue) through, inter alia, corporation and income tax. The Department of Finance considers that a reversion of corporate tax receipts to 2014 levels, a fall in the share of corporate taxes to the long-run norm, or an increase in corporate tax revenue in line with GNI* could lead to a permanent budgetary gap of EUR 2 to 6 billion, depending on the scenario under consideration ([30]).

Broadening the tax base would strengthen public finances. The high concentration of corporate taxes, their volatility and potentially transient nature, along with their rising share in total tax proceeds underline the risks of relying excessively on these receipts for the financing of permanent current expenditure. Broadening the tax base would mitigate these risks.

Recent revenue measures are not contributing to broadening the tax base. The main revenue-raising measures in Budget 2020 include an increase in the carbon tax rate by EUR 6 to EUR 26 per tonne, an increase in the stamp duty on non-residential property from 6% to 7.5% and several anti-avoidance measures ([31]). However, these measures are not contributing to tax base broadening. Some measures included in Budget 2020 even broaden the scope for tax expenditure and narrow the tax base. These include increases in certain tax credits, an extension of the Help-to-Buy scheme and higher capital acquisition tax allowances. Furthermore, the re-valuation of the local property tax was deferred by one year, to November 2020. The Working Group responsible for examining options for amalgamating the Universal Social Charge and the Pay Related Social Insurance concluded that, while feasible, it was not possible to identify an appropriate approach. There are no further measures announced regarding the alignment of the diesel and petrol excise rate.

The financial sustainability of the Irish healthcare system is not ensured. Over the last years, overruns in the Department of Health led to expenditure increases for healthcare without significant improvements in performance. This contributed significantly to the limited compliance

([27]) Supplementary expenditure of around EUR 440 million is needed in 2019 to cover for recurring spending overruns in the health, education and justice departments.

([28]) The Irish Fiscal Advisory Council further points out that even though these areas are outside the government's direct control they still impact the economy and therefore should be included in the budget planning.

([29]) Parliamentary Budget Office (2019), Pre-Budget 2020 PBO Commentary, Publication 55 of 2019.

([30]) Department of Finance, Budget 2020 Addressing Fiscal Vulnerabilities, October 2019.

([31]) Along with changes in electricity and vehicle registration taxes. An increase in the excise on tobacco products was also announced, but ESRI expressed concerns regarding the revenue this measure can raise. https://www.esri.ie/news/extra-2020-spending-on-public-services-and-pay-funded-by-real-tax-increases.

with EU fiscal rules. In Budget 2020, the government incorporated supplementary spending for health of EUR 335 million for 2019 (around 0.1% of GDP). The health spending at the end of December 2019 was ahead of profile by EUR 383 million, slightly above expectations. Budget 2020 has not announced any further measures to address the cost-effectiveness of the healthcare system. The implementation of the *Sláintecare* reform, introduced in 2019, is endangered by the difficulties in improving budget management in the health system to avoid recurrent overspends.

Persistent fiscal vulnerabilities call for further strengthening the resilience of public finances. A balanced budget and a declining debt-to-GDP ratio, combined with favourable near-term growth prospects, put Ireland in a good position to further strengthen its public finances in the face of substantial downside risks (see section 2.2). There is a strong case for using any windfall revenue to build fiscal buffers, either by ramping up the Rainy Day Fund (RDF) or by reducing debt. At the end of October 2019, the RDF was established and EUR 1.5 billion (0.4% of GDP) were transferred to it from the Ireland Strategic Investment Fund. In accordance with the relevant legislation, a Parliament resolution was passed on 17 December 2019 not to pay the previously budgeted 2019 annual allocation to the RDF of EUR 500 million (approximately 0.2% of GDP).

The Department of Finance (DoF) proposed several measures to address fiscal vulnerabilities ([32])**.** These include reducing the exposure to corporate taxes by setting aside the windfall receipts in the RDF and broadening the tax base. Also, it proposed defining a tailor-made general government balance that excludes corporate tax windfalls and setting short- and medium-term debt targets as percentage of GNI*. The DoF also proposed to use alternative estimates of potential growth, which would better reflect the idiosyncrasies of the Irish economy, to identify the true underlying position of the economy and recalculate the structural fiscal balance and the maximum expenditure growth. These initiatives are welcome. Against this backdrop, the Minister for Finance has announced a new target for the debt-to-GNI* ratio of 60% ([33]), including an interim target of 85% by 2025. The Minister also announced a target for the budgetary surplus of 1% of GDP by 2022 (1.7% of GNI*). Both targets are contingent of continued economic growth ([34]).

3.2. FINANCIAL SECTOR POLICIES

As NPL sales pick up, there is increasing focus on the political and social dimensions of repossessions. A number of initiatives have been proposed or implemented over the past years 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. The Land and Conveyancing Law Reform Act, which entered into force in August 2019, sets out the considerations courts must take into account when a lender is seeking an order for the repossession of lands. Some initiatives, such as the so-called 'No Consent, No Sale' Bill, which was proposed in January 2019 by the opposition, could however have unintended consequences by unduly undermining creditors' rights.

The Mortgage-to-Rent scheme is attracting an increasing number of applications, but approvals remain lower than hoped. A number of mortgage associations have positioned themselves to offer the scheme to vulnerable households qualifying for social housing. The number of applications has increased since the introduction of the revised scheme at end-2017. However, approvals remain low and they dropped from 20% to around 15% in the year to September. The total number of approved applications since January 2018 is 278, which is much lower than the total number of expected applications since the revision of the scheme in late 2017. It remains to be seen if these challenges will be overcome by the recently renewed efforts by banks and the authorities.

([32]) Department of Finance, Budget 2020 Addressing Fiscal Vulnerabilities, October 2019.

([33]) This would represent around 37% of GDP, based on the 2018 GDP and GNI* values.

([34]) Under a no-deal Brexit scenario the debt target would be between 90% and 95% of GNI* by 2025. Also, the budget deficit is estimated to be around -0.6% of GDP in 2020 (in line with Budget 2020), and expected to return to balance by around 2023.

The CBI continues to make active use of its macro-prudential toolkit to ensure the financial system remains resilient. The CBI has implemented the CCyB at a rate of 1% in July 2019. Following its review during the fourth quarter of 2019, the CBI decided to maintain the rate at its current level. While the CBI observes a gradual build-up of cyclical risks emanating from both the domestic environment and global financial conditions, it sees no evidence for excessive credit growth. Separately, the announced transposition of the systemic risk buffer into domestic law will further expand the CBIs macro-prudential toolkit.

Following its annual review, the CBI kept the calibration of the mortgage measures unchanged. The mortgages measures, i.e. limits on loan-to-value (LTV) and loan-to-income (LTI) ratios ([35]), were introduced in 2015 and are reviewed by the CBI on an annual basis. The latest review in the fourth quarter of 2019 coincided with easing housing market activity, reflected in a slowdown both in price and credit growth. Overall, the CBI considers that the measures have met their objectives, namely to increase borrower and lender resilience, and to dampen the pro-cyclicality of credit and house prices. Against this background, the CBI decided to keep the calibration of the LTV and LTI limits and of the allowances unchanged for 2020. This conclusion is also supported by a recent assessment by the European Systemic Risk Board (ESRB) ([36]).

Continued uncertainty over the final Brexit outcome is a concern for the Irish insurance sector. The Irish and UK authorities have put in place 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. In addition, the Irish insurers and their UK-based parents are highly exposed to the UK market through their investment portfolios. This exposes them to significant exchange rate and market risk in case of market valuation fluctuations.

Authorities aim to introduce a number of initiatives to address several concerns regarding non-life insurance segments. In addition to concerns over anti-competitive practices, limited investigating capacity of the Irish police regarding fraudulent and false claims, inflation in personal liability awards, as well as high legal costs appear to be the main drivers behind increasing cost of insurance higher. In response to this, the authorities are implementing the recommendations of the Cost of Insurance Working Group - formed in 2016 - in motor insurance and employer/public liability insurance. The Judicial Council Act of July 2019 addresses a key issue, enabling the Judiciary to review and provide guidance on liability award levels. It is hoped that this exercise will result in a general reduction in award levels and more generally result in a more stable claims environment in which claims are settled outside of court, thus reducing legal costs and uncertainty. In addition, the Irish Competition and Consumer Protection Commission announced in August 2019 that it has initiated an investigation into anti-competitive practices in the insurance industry.

The rapid growth of non-bank financial intermediation in recent years requires a close assessment of the resilience of the various entities and activities engaged in it. The CBI has already been moving in this direction in a number of recent publications, and additional insights are expected going forward, for example in the context of the Financial Sector Assessment Programme that the International Monetary Fund will conduct in the course of 2020.

([35]) The mortgage measures provide for a set of upper limits on these two ratios, which differ depending on the type of borrowers and purpose (first-time vs subsequent buyer, buy-to-let). Lenders are allowed to exceed caps for a set proportion of mortgages. Some additional exemptions also apply.

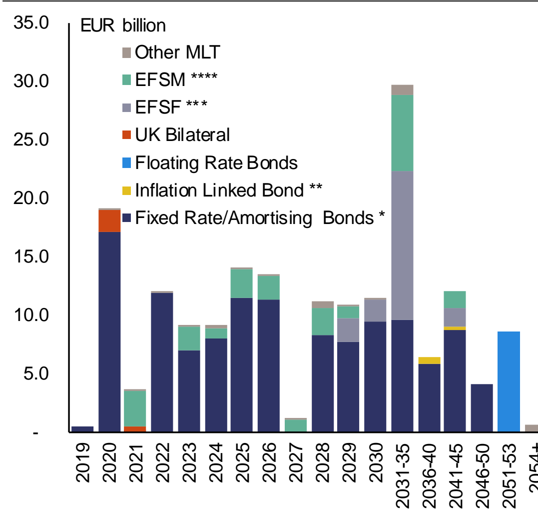
([36]) In September 2019, the ESRB concluded that the macro-prudential measures implemented by the CBI were fully appropriate and fully sufficient to address the identified financial vulnerabilities emanating from the residential real estate sector (ESRB, Vulnerabilities in the residential real estate sectors of the EEA countries, 23 September 2019).

4. SOVEREIGN FINANCING ISSUES

Sovereign financing remains comfortable. The sovereign had EUR 16.5 billion in cash at the end of 2019. The long-term debt due to mature in 2020 stands at EUR 19 billion (Graph 4.1). In 2019, the National Treasury Management Agency (NTMA) purchased a total of EUR 3.0 billion of the floating rate notes linked to the Irish Bank Resolution Corporation from the CBI and subsequently cancelled them. The outstanding balance remains at EUR 8.5 billion from an initial EUR 25.0 billion issued in 2013.

Government funding needs are expected to be lower in 2020. In 2019, the NTMA raised EUR 15.4 billion in cash proceeds from long-term bond funding, out of the targeted range of EUR 14 to 18 billion, including EUR 2 billion of green bonds. In 2020, NTMA targets to issue between EUR 10 to 14 billion of government bonds. The NTMA will use part of the opening cash balance of EUR 16.5 billion to meet 2020 redemptions.

Graph 4.1: Maturity profile of long-term marketable and official debt (end-November 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).
(2) Bilateral loans were provided from Sweden and Denmark, which were repaid in 2018, and from the United Kingdom.
* Includes NTMA Repo activity. Amortising bonds are adjusted by sink factor. ** Index inflation linked bonds adjusted for month-end value. *** EFSF loans reflect the maturity extensions agreed in June 2013. **** EFSM loans are also subject to extension, such that their original aggregated weighted average maturity will be a maximum of 19.5 years. 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 table and graph above reflect both original and revised maturity dates of individual EFSM loans.
Source: National Treasury Management Agency

Monetary policy developments play an important role for market conditions. ECB actions, in particular the non-standard asset purchase programmes, have compressed sovereign borrowing costs and, in turn, debt servicing costs. This appears to have also had an impact on the extension of the sovereign debt maturity profile ([37]). 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 0.003% in December. The spread against the German benchmark has trended upwards until September

([37]) 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.

2019, but from then to year-end declined to post-crisis lows of just over 30 basis points. Interest expenditure in Ireland is expected to have fallen from 1.6% of GDP in 2018 to 1.4% in 2019 and further decline to 1.1% in 2020. However, as a share of GNI*, interest expenditure still amounted to 2.6% in 2018 and an estimated 2.3% in 2019.

Risks for Ireland's capacity to service the EFSM and EFSF debt remain low. 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 and EUR 5 billion due in 2015 have already been extended ([38]). It is therefore not expected that Ireland will have to repay any of its EFSF and EFSM loans before 2027. 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	-0.6
Bond maturities (2)	8.9	13.1
UK bilateral loan (3)	0.0	1.6
Other bond flows (4)	6.8	5.5
Total requirement	**15.6**	**19.5**
Funding sources		
Government bonds (5)	17.5	15.3
Other (6)	2.8	5.4
Use of cash & other short-term investment balances (- represents an increase)	-4.8	-1.2
Total sources	**15.6**	**19.5**
Financial buffer (7)	**15.3**	**16.5**

2019 figures are provisional outturns, as of January 2020.
Rounding may affect totals.

(1) 2019 figure from Fiscal Monitor December 2019, published by Department of Finance, 3 January 2020.
(2) Includes Amortising Bonds.
(3) Includes the effect of currency hedging.
(4) Includes floating rate notes purchases
(5) 2019 includes inflation linked bonds.
(6) Includes net State Savings (Retail), net short-term paper funding and other medium/long-term funding.
(7) Exchequer cash and liquid assets. Excludes non-liquid Exchequer financial assets.

Source: NTMA

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

ANNEX 1
Debt sustainability analysis

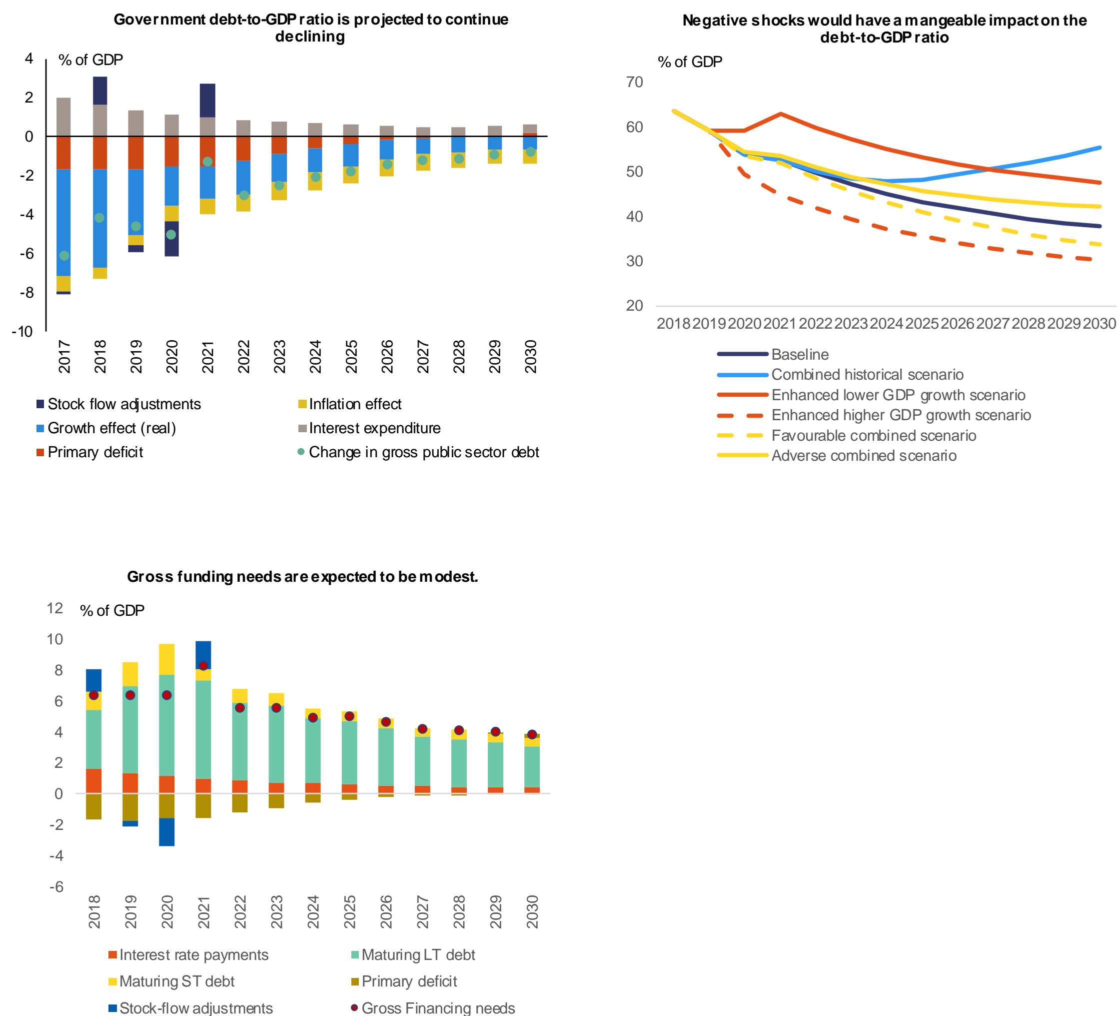
The public debt-to-GDP ratio is projected to continue declining. Based on the Commission 2019 autumn forecast and the no-policy-change assumption beyond the forecast horizon, the debt-to-GDP ratio is projected to decrease to 37.6% in 2030, well below the 60% Treaty reference value. The sale of government 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 4% by 2030, well below the 6% estimated for 2020 ([39]).

Debt sustainability risks are anticipated in the medium term. In principle, Ireland faces low fiscal sustainability risks in the medium term, as measured by both the debt sustainability analysis and the S1 indicator ([40]). This reflects a relatively strong initial budgetary position and a debt ratio already below 60% of GDP in 2019. When debt metrics are measured relative to gross national income (GNI), which can be considered a more accurate measure of repayment capacity for Ireland, medium-term vulnerabilities appear to be higher than suggested by the standard GDP metric ([41]). However, the Irish GNI is also inflated by the activities of multinationals. Therefore, the figures based on GNI still underestimate vulnerabilities in an Irish context. Analysis by the Irish Department of Finance, which uses GNI* as a reference, points to high risks to debt sustainability in the medium term ([42]).

([39]) European Commission - Directorate General for Economic and Financial Affairs, Fiscal Sustainability Report model, based on the European Commission 2019 autumn forecast.
([40]) The medium-term sustainability indicator S1 shows the additional adjustment required, in terms of improvement in the government structural primary balance over five years to reach a 60% public debt-to-GDP ratio by 2034, including financing for future additional expenditure arising from population ageing.
([41]) European Commission (2020), Debt Sustainability Monitor 2019, Chapter 6, January 2020.
([42]) Department of Finance (2019), Annual Report on Public Debt in Ireland 2019, August 2019.

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



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

ANNEX 2
Supplementary tables

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

	2018	2019	2020	2021
		% of GDP		
Indirect taxes	7.9	7.8	7.8	7.7
Direct taxes	10.7	10.7	10.7	10.7
Social contributions	4.2	4.2	4.2	4.2
Sales	1.8	1.7	1.6	1.6
Other current revenue	0.6	0.6	0.6	0.6
Capital taxes	0.2	0.1	0.1	0.1
Total current revenue	**25.2**	**25.1**	**25.0**	**24.8**
Capital transfers received	0.2	0.1	0.1	0.1
Total revenue	**25.4**	**25.3**	**25.2**	**25.0**
Compensation of employees	6.9	6.9	6.8	6.7
Intermediate consumption	3.4	3.7	3.8	3.8
Social transfers in kind via market producers	2.1	2.0	1.9	1.8
Social transfers other than in kind	7.2	6.9	6.8	6.7
Interest paid	1.6	1.4	1.1	1.0
Subsidies	0.6	0.5	0.5	0.5
Other current expenditure	1.1	1.1	1.1	1.1
Total current expenditure	**22.9**	**22.3**	**22.0**	**21.6**
Gross fixed capital formation	2.0	2.3	2.4	2.4
Other capital expenditure	0.5	0.5	0.5	0.5
Total expenditure	**25.3**	**25.0**	**24.9**	**24.4**
General government balance	**0.1**	**0.2**	**0.3**	**0.6**
General government balance net of one-offs	**0.1**	**0.2**	**0.3**	**0.6**
		EUR billion		
Indirect taxes	25.5	26.9	28.3	29.2
Direct taxes	34.6	36.8	38.9	40.8
Social contributions	13.5	14.5	15.1	15.8
Sales	5.9	5.9	5.9	5.9
Other current revenue	1.9	2.1	2.1	2.1
Capital taxes	0.5	0.5	0.5	0.5
Total current revenue	**81.8**	**86.7**	**90.8**	**94.3**
Capital transfers received	0.5	0.5	0.5	0.6
Total revenue	**82.3**	**87.2**	**91.3**	**94.9**
Compensation of employees	22.2	23.8	24.7	25.5
Intermediate consumption	11.0	12.7	13.7	14.4
Social transfers in kind via market producers	6.7	6.8	6.8	6.9
Social transfers other than in kind	23.4	23.7	24.6	25.3
Interest paid	5.2	4.7	4.1	3.7
Subsidies	1.9	1.6	2.0	2.0
Other current expenditure	3.7	3.7	4.0	4.0
Total current expenditure	**74.1**	**76.9**	**79.8**	**82.0**
Gross fixed capital formation	6.3	7.8	8.6	8.9
Other capital expenditure	1.7	1.7	1.8	1.7
Total expenditure	**82.1**	**86.4**	**90.2**	**92.6**
General government balance	**0.2**	**0.8**	**1.1**	**2.2**
General government balance net of one-offs	**0.4**	**0.8**	**1.1**	**2.2**

Source: Eurostat and European Commission autumn forecast 2019

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

	2018	2019	2020	2021
Government balance (% of GDP)	**0.1**	**0.2**	**0.3**	**0.6**
Government gross debt (% of GDP)	63.5	59.0	53.9	52.6
	levels, EUR billion			
Government balance	**0.2**	**0.8**	**1.1**	**2.2**
Gross debt	205.9	203.4	195.4	199.8
Change in gross debt	4.5	-2.5	-8.1	4.4
Nominal GDP	324.0	345.0	362.4	379.8
Real GDP	281.7	297.6	308.1	318.1
Real GDP growth (% change)	**8.2**	**5.6**	**3.5**	**3.2**
Change in gross debt (% of GDP)	-4.2	-4.6	-5.1	-1.3
Stock-flow adjustments (% of GDP)	1.5	-0.5	-1.9	1.7
	% of GDP			
Gross debt ratio	**63.5**	**59.0**	**53.9**	**52.6**
Change in gross debt ratio	-4.2	-4.6	-5.1	-1.3
	contribution to change in gross debt			
Primary balance	1.7	1.6	1.4	1.6
"Snow-ball" effect*	-4.0	-2.5	-1.7	-1.5
of which				
Interest expenditure	*1.6*	*1.4*	*1.1*	*1.0*
Real growth effect	-5.1	-3.4	-2.0	-1.7
Inflation effect	-0.6	-0.5	-0.9	-0.8
Stock-flow adjustments	**1.5**	**-0.5**	**-1.9**	**1.7**
Implicit interest rate	*2.6*	*2.3*	*2.0*	*1.9*

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 2019.
Source: Eurostat and European Commission autumn forecast 2019

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