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COMMISSION OPINION

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GENERAL CONSIDERATIONS

1. Regulation (EU) No 473/2013 sets out provisions for enhanced monitoring of budgetary policies in the euro area for ensuring that national budgets are consistent with the economic policy guidance issued in the context of the Stability and Growth Pact and the European Semester for economic policy coordination.

2. Article 6 of Regulation (EU) No 473/2013 requires Member States to submit annually to the Commission and to the Eurogroup a Draft Budgetary Plan presenting by 15 October the main aspects of the budgetary situation of the general government and its subsectors for the forthcoming year.

CONSIDERATIONS CONCERNING IRELAND

3. On the basis of the Draft Budgetary Plan for 2016 submitted on 15 October 2015 by Ireland, the Commission has adopted the following opinion in accordance with Article 7 of Regulation (EU) No 473/2013.

4. Ireland is currently subject to the corrective arm of the Stability and Growth Pact. The Council opened the Excessive Deficit Procedure for Ireland in April 2009. On 7 December 2010, the Council adopted revised recommendations to Ireland. The country is recommended to correct the excessive deficit by 2015.

5. The Irish economy is experiencing a much stronger-than-expected economic rebound. Real GDP grew by 5.2% in 2014, up from 1.4% in 2013. In the first half of 2015 real GDP growth accelerated to 7% in annual terms. Additional government expenditure in 2015, which the Irish government announced in October, adds to the exceptionally strong growth momentum. Subject to future revisions of the generally volatile Irish national accounts, the growth performance in the first half of 2015 sets the ground for annual average real GDP growth of at least 6% in 2015 and still strong, but more moderate growth next year. Consumer price inflation is expected to be close to zero in 2015, on account of energy prices, but to recover in 2016, driven primarily by wage developments. The Draft Budgetary Plan presents a significantly revised macroeconomic scenario compared to the 2015 Stability Programme. Real GDP is expected to grow by 6.2% in 2015 and by 4.2% in 2016. The level of nominal GDP in 2015 and 2016 is now expected to be nearly 7% higher than in the 2015 Stability Programme. The Commission forecast for real GDP is very close to the one included in the macroeconomic scenario of the Draft Budgetary Plan. Given the still high levels of household indebtedness in Ireland, the Commission expects somewhat more moderate growth in private consumption. Overall, the macroeconomic scenario underlying the Draft Budgetary Plan is plausible.

6. Regulation (EU) No 473/2013 requires the Draft Budgetary Plan to be based on independently endorsed or produced macroeconomic forecasts. The macroeconomic forecasts underlying the 2016 Draft Budgetary Plan of Ireland have been endorsed by the Irish Fiscal Advisory Council (IFAC). The IFAC is a statutory body mandated to monitor public finances; its independence is formally guaranteed by law.

7. The Draft Budgetary Plan projects a general government deficit of 2.1% of GDP in 2015, down from 2.3% of GDP in the 2015 Stability Programme and well within the 3%-of-GDP reference value of the Treaty. On top of the expenditure increases and tax cuts already included in the 2015 budget, the new target incorporates additional government expenditure of around 0.7% of GDP announced in October. The slight improvement in the deficit target compared to the 2015 Stability Programme reflects considerably better-than-expected tax revenues, especially corporate income taxes, in the wake of the strong economic rebound. Thanks to the positive macroeconomic outlook, public finances are expected to improve further in 2016. The Draft Budgetary Plan forecasts the 2016 general government deficit at 1.2% of GDP, 0.5 of a percentage point below the target included in the 2015 Stability Programme.

   As a result of lower market rates and the early repayment of IMF loans, total interest payments by the general government have decreased over the last few years. Interest expenditure in Ireland equalled 4.1% of GDP in 2012. It peaked at 4.3% of GDP in 2013 and is expected to fall to 3.4% of GDP in 2015 and to decrease further next year, to 3.1% of GDP, based on the information provided in the Draft Budgetary Plan. This interest windfall does not seem to have contributed to the improvement of the structural budget balance in the period 2012-2016.

8. The Commission forecast projects a government deficit of 2.2% of GDP and 1.5% of GDP in 2015 and 2016 respectively. In 2016, the difference compared to the deficit target of the Draft Budgetary Plan is chiefly due to a more conservative assumption on relatively tax-rich private consumption and a somewhat more dynamic forecast of government expenditure motivated by recurring overspending especially towards year end, compared to government plans, in the past several years. Risks to the fiscal projections of the Commission mainly relate to the sustainability of the favourable macroeconomic outlook and the existing discretionary power to change domestic expenditure ceilings.

9. Ireland's general government debt-to-GDP ratio is expected to continue to fall after having peaked at 120% in 2013. The Draft Budgetary Plan projects gross government debt to fall below the level of GDP in 2015 and to reach 92.8% of GDP in 2016. The improvement compared to the projections of the 2015 Stability Programme results from the combined effect of much better-than-expected economic growth, lower interest expenditure and somewhat larger primary surpluses. The debt projections in the 2016 Draft Budgetary Plan are broadly in line with the Commission forecast.

10. The Draft Budgetary Plan includes new measures of around 0.7% of GDP consisting of tax cuts and spending increases. On the tax side, measures mainly focus on reducing income taxes through cuts to the Universal Social Charge (USC). On the expenditure side, increases mainly target public sector pay and social protection. Government investment expenditure, which was significantly reduced during the post-2007 consolidation process, continues to be subdued. The level of gross voted capital expenditure projected for 2016 is 1.4% lower than the latest estimates for 2015.

11. For 2015, the Draft Budgetary Plan projects a headline deficit of 2.1% of GDP, well below the 3%-of-GDP reference value of the Treaty. Similarly, the Commission forecast expects Ireland to bring its headline deficit to 2.2% of GDP in 2015, the deadline for correcting the excessive deficit, and to keep the deficit below 3% of GDP in the subsequent two years. By contrast, using much higher-than-expected

government revenues in 2015 and 2016 to finance additional permanent expenditure, especially at a time when economic growth is exceptionally strong, is not in line with the Council recommendation under the Excessive Deficit Procedure (EDP) and the 2015 Country Specific Recommendation which require Ireland to use windfalls to accelerate deficit and debt reduction. According to the Commission 2015 autumn forecast, both the unadjusted and the adjusted improvement in the structural budget balance in 2011-2015, i.e. the EDP period, fall short of the recommended cumulative improvement of 9½% of GDP. Moreover, the estimated yield of the permanent consolidation measures is also below the recommended cumulative adjustment.

12. Once a sustainable correction of the excessive deficit is achieved, Ireland would have to comply with the requirements of the preventive arm of the Stability and Growth Pact and be subject to the transitional debt rule. The Draft Budgetary Plan does not include sufficient information to assess compliance with the transitional debt rule. Based on the Commission 2015 autumn forecast, Ireland is making sufficient progress towards complying with the debt rule in 2016.

13. The recalculated improvement of the structural balance in 2016 in the Draft Budgetary Plan exceeds the 0.6% of GDP required to ensure sufficient progress towards the medium-term budgetary objective (MTO), and net government expenditure growth is presented to be in line with the expenditure benchmark. Based on the Commission 2015 autumn forecast, the estimated improvement of the structural balance in 2016 also exceeds the required 0.6% of GDP. Conversely, the growth rate of government expenditure, net of discretionary revenue measures, is expected to exceed the expenditure benchmark by some 0.4% of GDP in 2016, mainly on account of stronger expenditure growth and one-off factors, pointing to a risk of some deviation. Therefore, an overall assessment is warranted. The difference between the two indicators chiefly stems from the fact that the annual potential GDP growth rate used to estimate the improvement of the structural balance in 2016 is significantly higher than the recently updated medium-term reference rate of potential growth underpinning the expenditure benchmark, which can be considered to provide a more stable and prudent estimate of the medium-term growth potential. In fact, owing to the very open nature of the Irish economy and frequent revisions of Irish national accounts, the estimates of annual potential GDP growth for individual years exhibit considerable, often pro-cyclical variations. In conclusion, the overall assessment of Ireland’s Draft Budgetary Plan points to a risk of some deviation in 2016 from the required adjustment towards the MTO.

14. Concerning the recommendations in the area of fiscal governance, the Draft Budgetary Plan confirms Ireland's commitment to a continued reduction in the structural deficit. At the same time, no changes have been made to ensure the binding nature of the government expenditure ceiling as evidenced by the sizeable upward revisions of government expenditure in 2015 and 2016 compared to earlier plans. Whereas measures implementing the international agreed efforts to reduce tax avoidance may contribute to broadening the tax base, tax cuts introduced in 2016 may eventually narrow it. Little progress has been made in enhancing the growth and environmental friendliness of the tax system.

15. Overall, the Commission is of the opinion that the Draft Budgetary Plan of Ireland, which is currently under the corrective arm and could become subject to the preventive arm from 2016 in case a timely and a sustainable correction of the excessive deficit is achieved, is broadly compliant with the provisions of the Stability and Growth Pact. In particular, according to the Commission forecast, there is a risk

of some deviation from the expenditure benchmark in 2016. Moreover, the Commission notes that the extra government spending announced for the last three months of 2015 comes at a time when the Irish economy is already growing at exceptionally strong rates. The Commission therefore recalls earlier guidance as provided in the Council Recommendation under the Excessive Deficit Procedure of 7 December 2010 and in the context of the European Semester to use windfalls to accelerate debt reduction and invites the authorities to take the necessary measures within the national budgetary process to ensure that the 2016 budget will be compliant with the SGP.

The Commission is also of the opinion that Ireland has made some progress with regard to the Country Specific Recommendations issued by the Council in the context of the 2015 European Semester relating to fiscal governance and invites the authorities to make further progress. A comprehensive assessment of progress made with the implementation of the CSRs will be made in the 2016 Country Reports and in the context of the Country Specific Recommendations adopted by the Commission in May.

Done at Brussels, 16.11.2015

For the Commission
Pierre MOSCOVICI
Member of the Commission

CERTIFIED COPY
For the Secretary-General,

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Director of the Registry
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