Budget 2022: A Macroeconomic Perspective

EVENT
ESRI Post-Budget Seminar

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Context

- Budget framed against a unique set of circumstances
- Pandemic necessitated significant Government expenditure
    - Supporting household incomes and firms
- Evident that the Irish economy has emerged in a robust manner
- Risk of overheating, yet unemployment is still at 10%
- Recent increases in spending reflect lack of spend during post-GFC recovery?
- Appropriate policy stance
- Difficult to assess!!

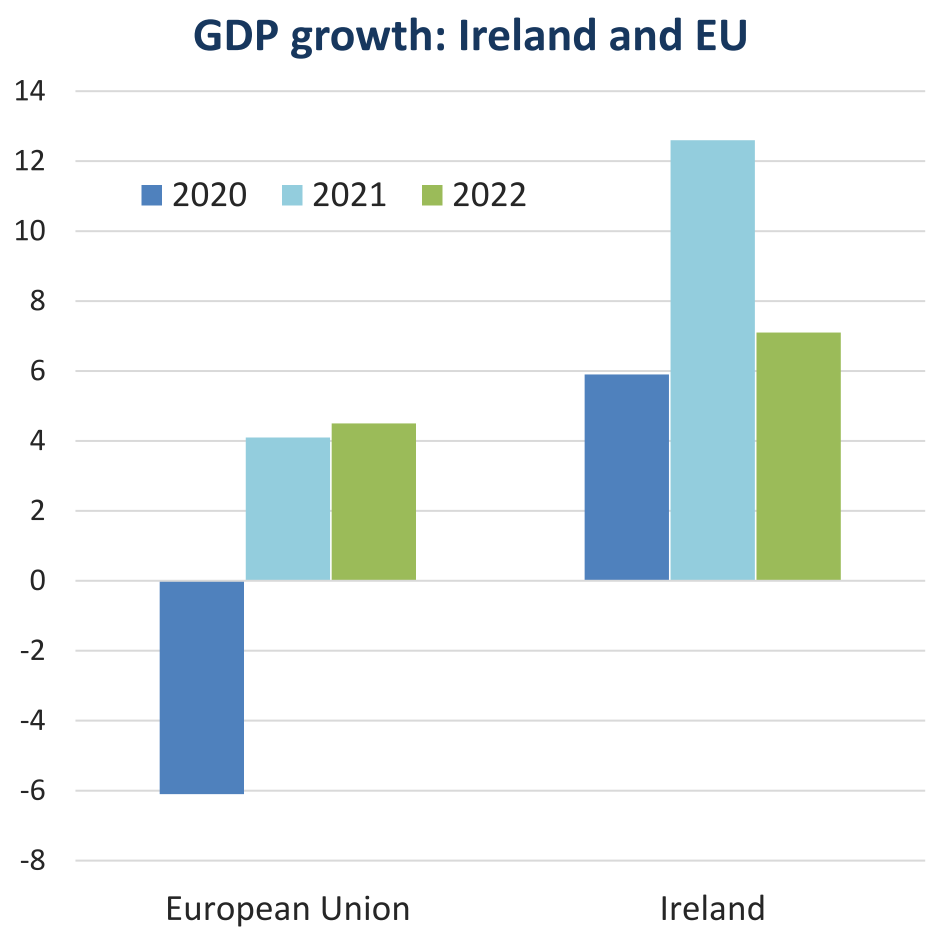
Overview

- Discuss the likely growth performance
- Look at implications for the fiscal accounts
- Overall budgetary stance
    - Recent & future expenditure levels
- Implications for future fiscal policy

Robust economic performance

- Ireland alone in the EU experienced economic growth in 2020 and
- We expect a strong recovery in 2021, with
    - **GDP** forecast to increase **12.6 per cent** in 2021 and **7.1 per cent** in 2022.
    - **Modified domestic demand** is set to grow over **7 per cent** in 2021.

- The robust performance and reduction in unemployment will ease the pressure on public finances.



Source: ESRI calculations and EU Commission

Drivers of Growth

- Key factors contributing to the economic recovery in Ireland:
  - Sustained economic likely to lead to a rebound in consumption.
  - **Unemployment rate** is expected to lower swiftly.
  - **Exports** and multinational activity continue to grow.
  - Underlying **investment** set to rebound as the economy recovers.

	2020	2021	2022
Private Consumer Expenditure	-10.4	7.5	8.0
Exports	9.5	14.3	9.0
Modified Domestic Demand	-4.2	7.2	7.1
Unemployment Rate	19.4	16.3	7.1

Public Finances: Strong performance in tax receipts…

- Overall taxation receipts increased substantially in 2021.
  - Tax receipts increased **16.6 per cent** between 2020 and 2021
  - All tax items have registered strong growth.
  - Expect overall growth in tax receipts to be **11.5 per cent** in 2021.

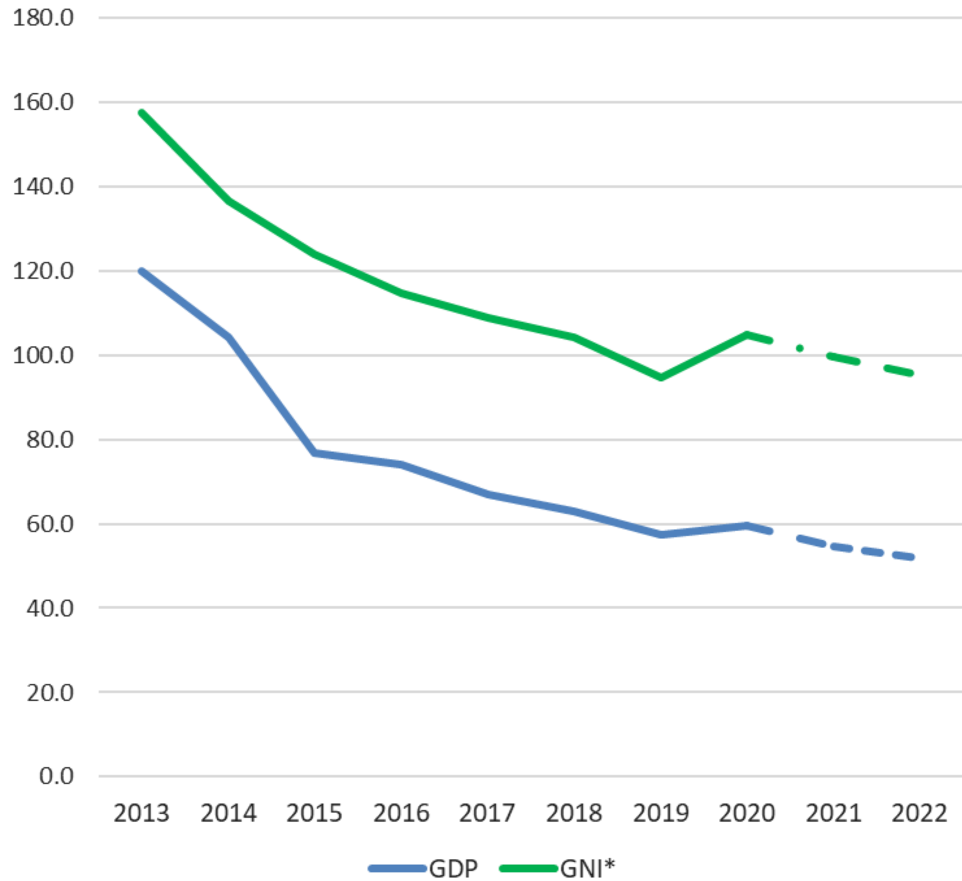
- Tax receipts have increased beyond their projected growth had the pandemic not occurred.
  - We estimate total tax receipts in 2020 had the pandemic not occurred.
  - Using this counterfactual figure, we find that tax receipts still registered an increase of **6.4 per cent** in 2021.
  - Increase not only due to a low base in 2020, but rather to strong overall activity in 2021.

...are driving improvements in the general government balance

- The pace of Ireland's recovery coupled with the boost in taxation receipts has led to improvements in the debt to GDP and debt to GNI* ratios.
- We anticipate further reductions in these ratios throughout 2022, signaling Ireland's improvements in the general government balance.

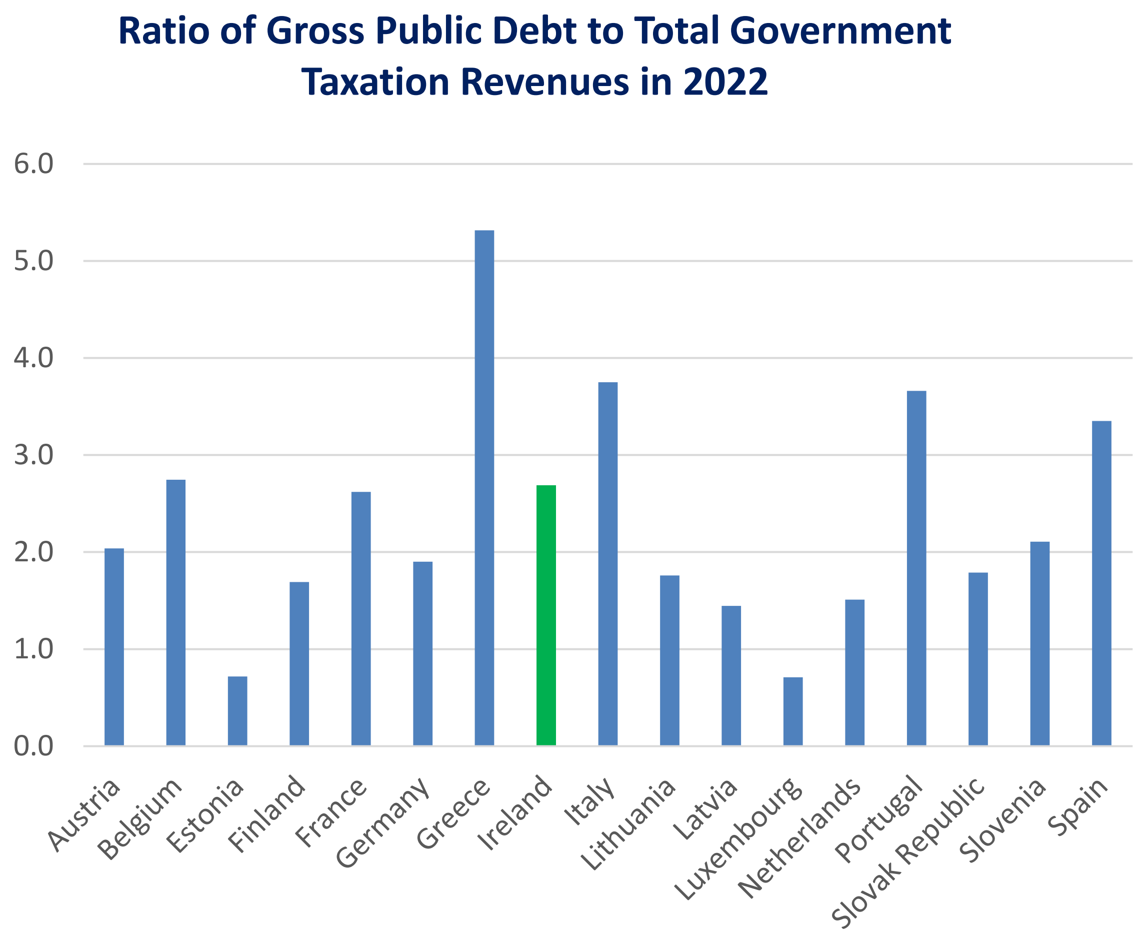
	2020	2021	2022
GGB	-€18.4bn	-€14.7bn	-€8.0bn
(% of GDP)	-4.9%	-3.4%	-1.7%

Debt to GDP and GNI* Ratios



An alternative measure of Ireland's debt position…

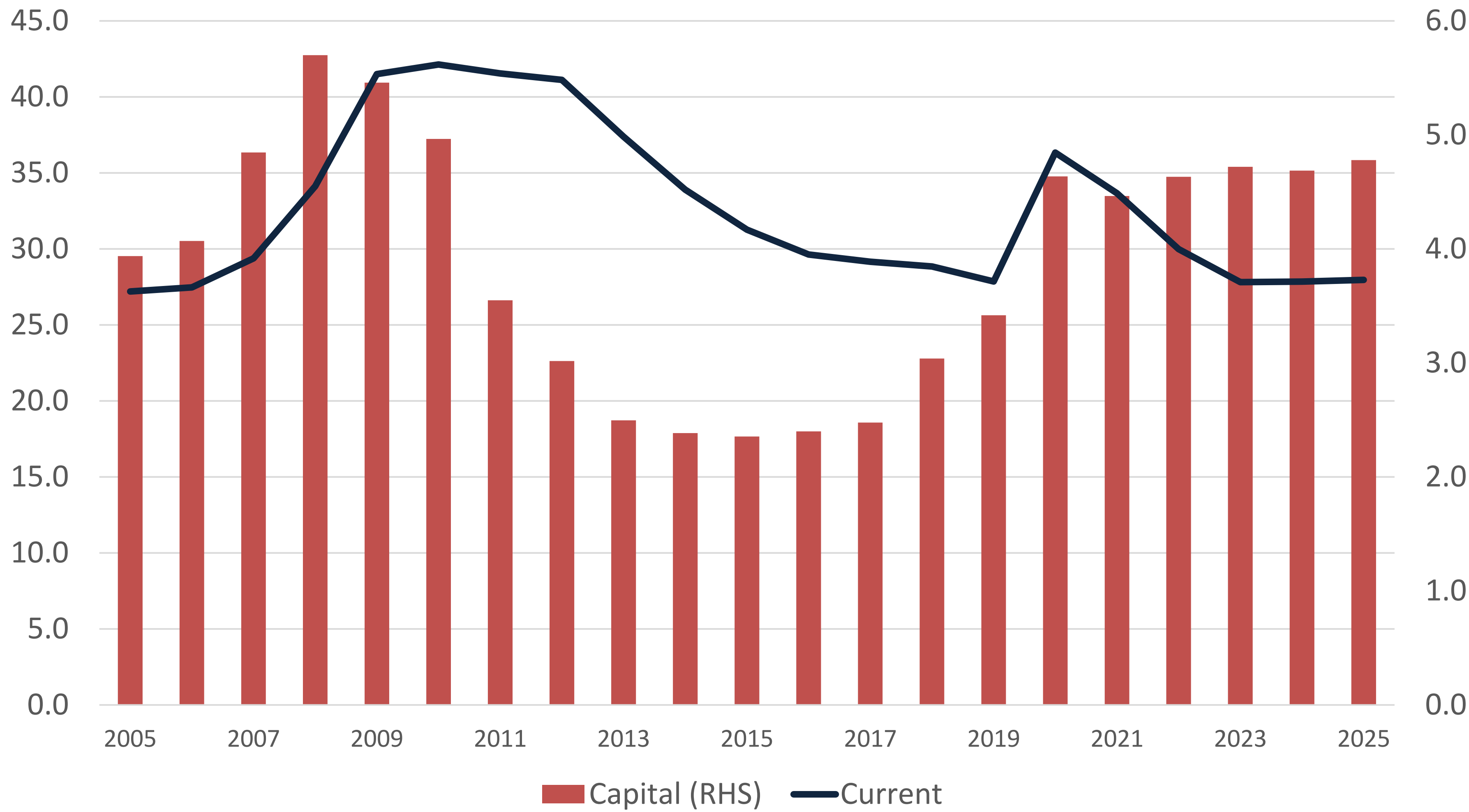
- Ratio of gross government debt to taxation revenue
- Measure of debt sustainability.
- In 2019 Irish ratio = 2.6,
- In 2011, ratio was 3.9.



Source: OECD, Eurostat, and author's calculations

Recent and Future Expenditure Levels

Recent and future expected expenditure levels
As a % of GNI*



Two particular risks

- **Inflationary pressures**
  - Global trends are large contributors
  - 2021 has seen
    - substantial changes in the energy market and
    - disruptions in international supply chains.
- We forecast:
  - Inflation to reach 2.3 per cent in 2021 and
  - 2.5 per cent in 2022
- **Corporation taxes**
  - Implications of recent changes?
  - Conservative outlook for receipts?
- Long-term impact on receipts & investment?

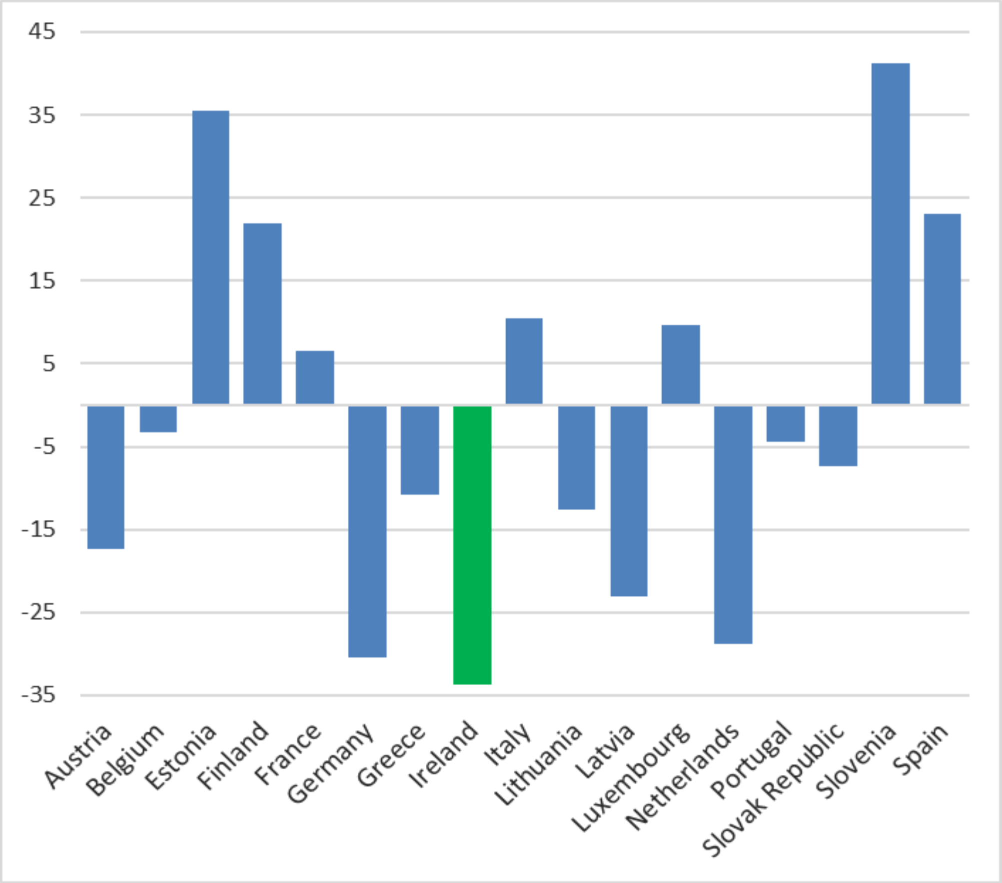
Post-COVID fiscal policy

- **Fiscal challenges** such as housing, climate change, and healthcare must be addressed in the medium-term.
- Future investment that addresses these challenges may stem from a mixture of increased tax revenues and maintaining a small, sustainable deficit.
    - Capital investment must prioritise projects which **increase the productive capacity** of the domestic economy.
- Restraint on current expenditure
- Risk of **overheating** in the domestic economy:
    - Policies that contributed to an erosion of the tax base in the past (ie benchmarking, cuts in taxation) must be avoided.
    - **Restraint** vis-à-vis current expenditure will be required given the increased capital expenditure.

...illustrates improvements in the debt position over time

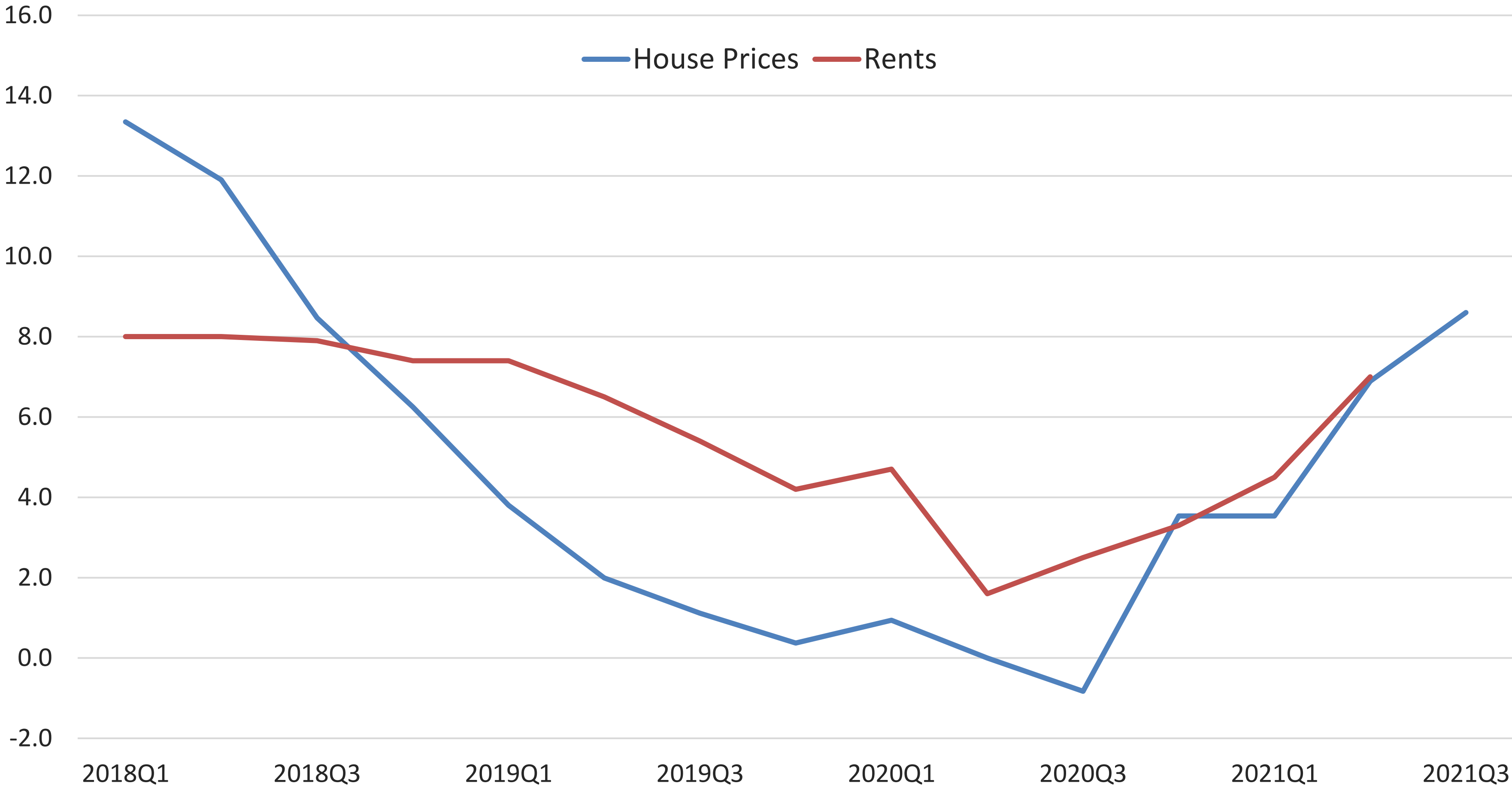
- Over the past 10 years Ireland has registered the largest decline in the debt ratio and is anticipated to continue to perform well.
- By 2022, Irish debt levels are set to be just above the EU average.
- The improvements in Ireland's debt position suggest that sustainable borrowing may be feasible over the medium-term in order to address pressing post-Covid challenges.

Change (%) in the Ratio of Gross Public Debt to Total Government Taxation Revenues (2011-2019)



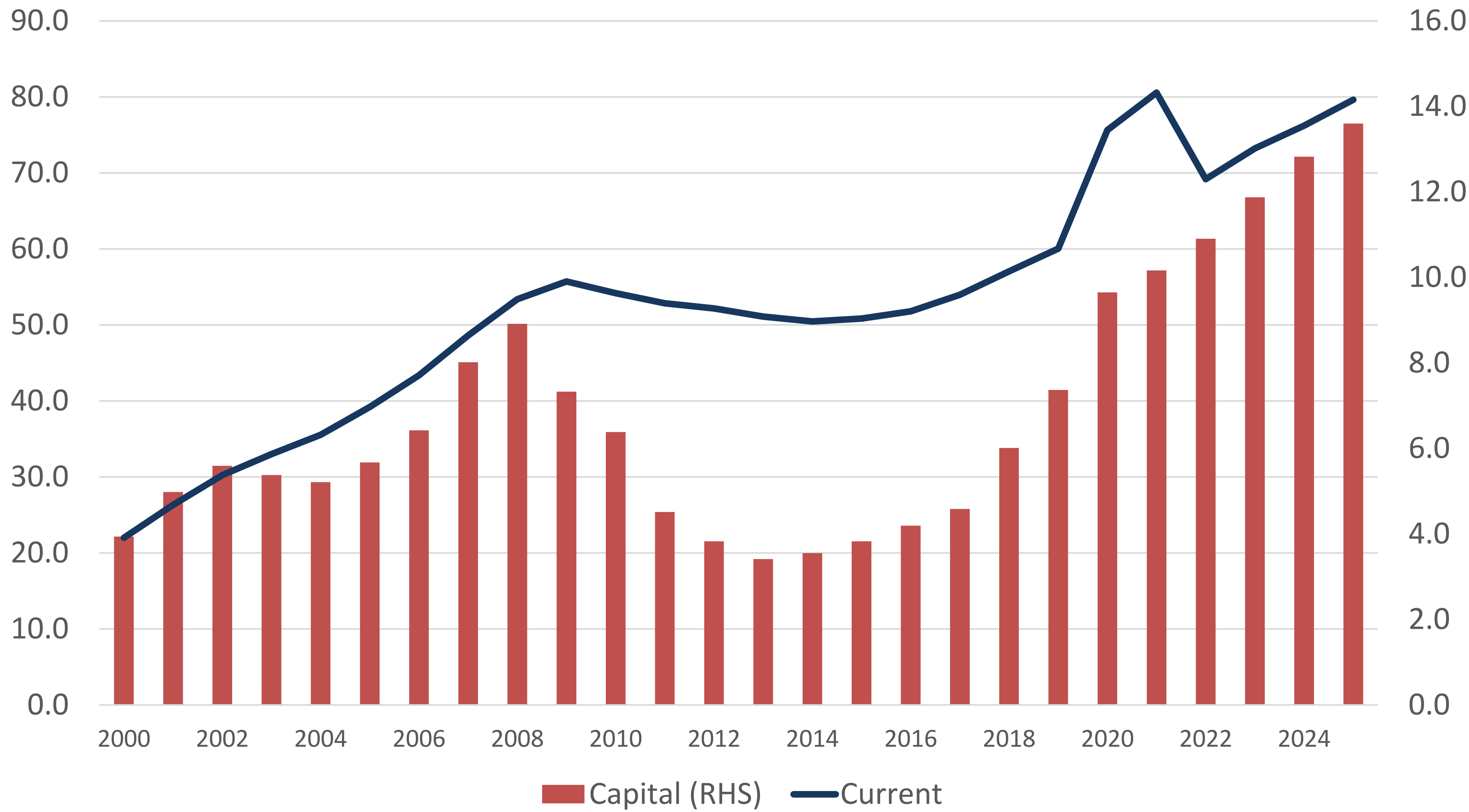
Source: OECD, Eurostat, and author's calculations.

Recent annual house price and rental inflation (%)



Recent and future expected expenditure levels (€bn)

Gross Voted



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Thank You