Opening Statement – Oireachtas Committee on Budgetary Oversight

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Introduction

Let me begin by thanking the Chair for the invitation to the ESRI to appear before the Committee. I am Dr. Conor O'Toole, and I am joined by my colleagues Dr. Karina Doorley and Dr. Paul Egan. We are grateful for the opportunity to appear before the Committee today to provide our views on Budget 2026.

Macroeconomic Context

Let us first provide our latest macroeconomic assessment. Consumer expenditure and tax receipts have continued to grow in 2025. Employment growth has also continued, although the pace of increases in 2025 and 2026 are likely to be slower than in recent years. The unemployment rate remains low despite recent indications of a slight increase. In this context, the domestic economy can be characterised as operating at or close to capacity. We expect the economy to continue to grow robustly next year, but there are some tentative signs of a modest slowdown in the labour market.

As a result, our contention is that the macroeconomy does not need strong government support. Focused and targeted expenditure should be the priority, particularly aimed towards removing bottlenecks in infrastructure.

Macroeconomic impact of Budget 2026

Budget 2026 deployed a budgetary package of approximately €9.4bn across taxation and spending measures. The majority of the package was on spending (at €8.1bn). While an emphasis on investment is welcome, our concerns can be separated into two strands.

First, the fiscal stance at present - how much money the government puts into the economy in spending relative to how much it takes out in taxation - is arguably too loose. A counter-cyclical fiscal policy would consist of running a larger government surplus (lower deficit) to reduce demand pressures towards the peak of the economic cycle. Ireland's fiscal policy in recent years has done the opposite with very strong spending increases. The implications of this can be damaging in the long-term; for example, if capacity constraints or cost inflation prevent the full delivery of the National Development Plan. Recent evidence of an acceleration in wage growth in the construction sector is concerning in this regard.

Second, the windfall nature of a large proportion of Ireland's corporate tax receipts means that they could vanish quickly. In 2026, corporation taxes are predicted to account for over 30 per cent of all revenues and the windfall element specifically to account for over 17 per cent of all taxation. Based on the innate vulnerability of windfall revenues and the need to pursue counter-cyclical policy, we would urge the Government to move towards a windfall-adjusted surplus. At present, budgeted figures suggest that the windfall-adjusted deficit will continue to increase. From a macro-fiscal perspective, we are moving in the wrong direction.

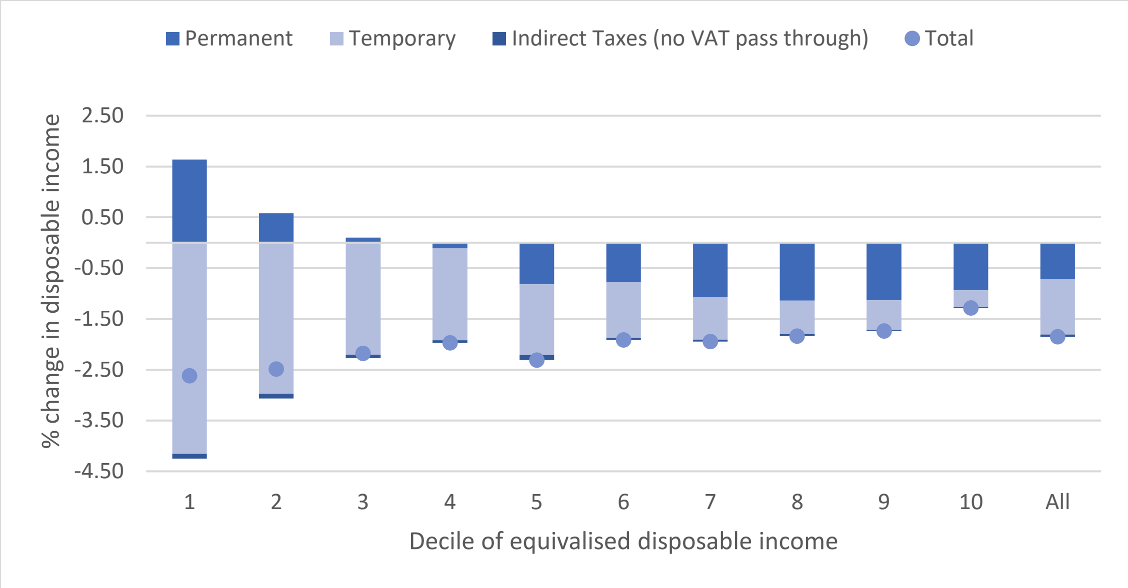
Distributional impact of Budget 2026

Every year, the ESRI carries out a distributional impact assessment of the Budget using SWITCH, the ESRI's tax-benefit model. This work is possible thanks to core funding provided to the ESRI by the Department of Public Expenditure, NDP Delivery and Reform and funding for the SWITCH work program provided by the Departments of Health, Finance, Social Protection and Children, Equality, Disability, Integration and Youth.

We compare the effect of the budgetary reforms to a scenario in which policy reform keeps the distribution of income constant. In practice, this implies comparing changes in the parameters of the tax and welfare system to an 'indexed' baseline, in which these parameters change in line with forecast income growth.

At the household level, measures announced as part of Budget 2026 will result in small income losses next year — averaging 2% of household disposable income — compared to a budget indexed to forecast income growth.

Figure 1 The effect of Budget 2026 on the Distribution of income compared to an income-indexed 2025 policy



Source: Authors' calculations using SWITCH run on 2022 Survey of Income and Living Conditions data, uprated to 2026 income levels.

Notes: Deciles are based on equivalised household income, using CSO national equivalence scales.

Temporary cost-of-living policies, which have been a feature of the last number of budgets, have now been withdrawn. While inevitable, this withdrawal will result in a reduction in households' standard of living, with low-income households losing significantly more as a proportion of their disposable income compared to high income households. The withdrawal of temporary measures results in losses of 4.1% of disposable income for the lowest income households compared to losses of 0.3% for higher income households.

For high-income families, these losses will be exacerbated by the freeze to tax bands and credits, which amount to an effective tax rise if wages grow at their forecasted rate of 3.7% in 2026. For low-income families, the withdrawal of one-off measures will be partly cushioned by the welfare package, which is mostly above forecast inflation and wage growth. The extension of the VAT cut to electricity and gas and the introduction of a cut to VAT on hospitality and hairdressing may result in small income gains, which are larger for high income households, if they are passed on to consumers.

The budgetary measures targeted at children, such as increases to the Child Support Payment and the Working Families Payment, are well-targeted. However, their effect on child at-risk-of-poverty rates will be small as they are accompanied by the withdrawal of many temporary measures. We estimate that these measures will lift around 2,000 children out of income poverty, compared to a budget pegged to income growth. However, many more targeted measures will be necessary to achieve the government target for child consistent poverty of 3% or below.

Concluding remarks

Budget 2026 comes at a time of continued robust growth in the Irish domestic economy. The labour market is operating at close to capacity and infrastructure and housing bottlenecks are a major threat to our competitiveness. However, it is also an epoch of rising global uncertainties and potential geopolitical fragmentation which may impact historical trading relationships. Evidence of a modest slowdown in the labour market is building which may hint at lower near term growth rates. At such a juncture, prudent fiscal policy would ensure sufficient build up of buffers to be used counter-cyclically in any downturn. The funnelling of windfall taxes into saving funds as well as into long term capital investments should ensure resources are available to support the economy when needed while adding to the productive capacity of the economy.