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**Meeting with the**

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# Speaking Note

**[Check against delivery]**

Thank you very much. It is an honour to have been invited again to appear before this committee.

As you know, a week ago, the Commission presented the so-called Spring Package. This continues the 2018 cycle of coordination of economic policies across the European Union, the European Semester. The package also includes the assessments of the National Reform Programs and the 2018 Stability and Convergence Programmes, which were submitted by the Member States one month ago.

Let me recall that the European Semester starts in the autumn of the year before with the adoption by the Commission of the Annual Growth Survey, the Alert Mechanism Report and the recommendations for the euro area.

The **Annual Growth Survey** sets the priorities for the year ahead at the European level. This year, the Commission calls on the Member States to continue the efforts along the virtuous triangle of economic policy: boosting investment, pursuing structural reforms and ensuring

responsible fiscal policies. It has placed as well an emphasis on the European Pillar of Social Rights.

The **Alert Mechanism Report** is an integral tool, which aims to address imbalances that hinder the smooth functioning of Member States' economies and to prompt the right policy responses (Macroeconomic Imbalances Procedure). The report identifies the Member States for which an in-depth review of possible imbalances is warranted. Ireland was included in this group of countries.

The autumn package also includes the recommendation on the economic policy of the euro area, of which all Member States whose currency is the euro are meant to ensure full and timely implementation.

This is followed by the **Country Reports**, which were published in March and provided the assessment of the economic and social situation in Member States, including progress made in implementing past Country-Specific Recommendations. The Country Reports also include the in-depth review for the concerned countries.

On the basis of the in-depth review published in the Irish Country Report, the Commission found that Ireland is still experiencing macroeconomic imbalances, characterised by large stocks of external, private and public debt, high non-performing loans and rising property prices.

The Country Reports together with the National Reform Programmes and the Stability (or Convergence) Programmes are the basis for the Commission's proposal for the **Country-Specific Recommendations** put forward last week.

The recommendations adopted by the Commission last week are framed in a context of the fastest growth pace of the European economy in a decade, with record employment, recovering investment and improved public finances. However, new risks are emerging such as volatility in global financial markets and trade protectionism. For that reason, it is important that we use without delay the current favourable conditions to make Europe's economies and societies stronger and more resilient.

The Commission has adopted three recommendations for Ireland covering, first, budgetary policy and fiscal structural issues, including

taxation and sustainability of public finances, second, infrastructure and skills, and, finally, measures aiming at fostering productivity growth and at reducing the stock of non-performing loans.

The first recommendation addresses compliance with EU fiscal rules. It reflects the projections of the Commission 2018 spring forecast and the assessment of the Stability Programme.

Ireland is currently in the preventive arm of the Stability and Growth Pact. Based on the Commission 2018 spring forecast, there is a risk of some deviation from the recommended fiscal adjustment in 2018 and over 2017 and 2018 taken together.

In 2019, the structural balance is forecast to reach a deficit of 0.4% of GDP, thus achieving the medium-term budgetary objective of a deficit of 0.5% of GDP. For this to happen, growth of government expenditure should remain below 5.3% in 2019.

Ireland is expected to comply with these provisions. Ireland is also expected to comply with the debt rule.

However, the steady fall in the debt-to-GDP since its peak has also been the result of strong nominal GDP growth, including the mechanical denominator effect of the exceptionally large surge in 2015 GDP. Given this, Ireland's current cyclical conditions and the heightened external risks, the use of any **windfall gains** to further reduce the general government debt ratio would be prudent.

I have learnt that the recent plans for a Rainy Day Fund would set aside EUR 8 billion over the medium-term. I believe that this is an important development, as an appropriately designed fund could provide a fiscal buffer during a future economic downturn.

Moving to the composition of public finances and, in particular, taxation, corporate taxes as a proportion of total taxes continued to rise. Such taxes are highly concentrated among a few large multinational enterprises and prone to volatility. Some recent tax measures have focused on cuts and reliefs and seem to have further increased reliance on highly pro-cyclical sources of revenue. The Commission considers

that broadening the tax base could help improve revenue stability in the face of economic fluctuations. Moreover, there exists further potential to improve the way Ireland's tax system can support environmental objectives.

Long-term fiscal sustainability risks related to the cost of ageing also remain. Ireland has introduced some significant measures to increase the efficiency of public healthcare spending, such as a cost-saving agreement with the pharmaceutical industry, a financial management system and activity-based funding. Some measures have also been taken to improve the availability of primary health care. It has also introduced a wide range of reforms to contain public pension expenditure. Nevertheless, according to the most recent long-term assessment approved by the Ageing Working Group of the Economic Policy Committee, the cost of ageing represents a medium fiscal sustainability risk for Ireland over the long-term.

On this basis, there is a need to increase the cost-effectiveness of the healthcare system and to pursue the envisaged pension reforms.

Moving now to the real economy and to the second recommendation, the Commission found in the Country Report that barriers to inclusive growth remain in the form of skills mismatches, skills shortages and the insufficient access to affordable, quality childcare.

Although unemployment fell to 6.7 % in 2017, certain groups are still largely detached from the labour market and socially excluded.

In addition, years of reduced government investment are taking their toll on the availability of housing and appropriate clean energy, transport and water infrastructures.

In housing markets, persistent supply shortages, coupled with increasing demand, continue to fuel property price increases.

The Commission concludes that addressing emerging infrastructure bottlenecks is essential for sustainable and balanced growth in the future.

The Commission therefore recommends Ireland to improve the skills of the adult population and to timely and effectively implement the relevant

parts of the National Development Plan, including on infrastructure and childcare.

Finally, the Commission finds that the productivity of domestic companies is lower, and growing at a slower pace, in comparison with the multinationals operating in Ireland.

Given the current favourable economic conditions but also keeping in mind the existing risks and uncertainties, the Commission, in the third recommendation, recommends to stimulate research and innovation with a view to enhance the resilience of the domestic sectors.

Although Ireland continued to make progress in reducing non-performing loans, their ratio to total gross loans remains among the highest in the EU. Particularly worrying are long-term mortgage arrears, which are those in arrears for over two years. They represent 60% of the total mortgages in arrears in 2017. Reducing the long-term arrears could improve the resilience of the Irish banking sector and also help address the problem of debt overhang, which reduces the incentives for small and medium–sized enterprises to put credit in more productive uses.

On this basis, and as part of the same third recommendation, the Commission recommends promoting a faster and durable reduction of long-term mortgage arrears.

In sum, the Commission proposes a comprehensive package to underpin the sustainability of public finances, foster productivity and enhance the resilience of Ireland to external shocks, to which Ireland, as any other small open economy, is highly exposed.

This goes very much along the lines of the strategy of the Irish authorities to build resilience in the face of global challenges and the recommendations of the National Competitiveness Council.