

Meeting of the Budgetary Oversight Committee, 11th March 2021

Opening Statement by John McCarthy, Chief Economist of the Department of Finance

Introduction

Chair, Members: let me thank the Committee for the invitation to attend (virtually) today in order to discuss the forthcoming *Stability Programme, April 2021 Update*. I am also happy to discuss – in general terms – the current economic and fiscal situation, and I look forward to hearing the Committee’s views regarding some of the key macro-economic and fiscal issues on the medium-term horizon.

April 2021 Update of the *Stability Programme*

Turning firstly to the *Stability Programme*: work is progressing on compiling the macro-economic and fiscal projections which are central to the document.

Compiling a set of macroeconomic projections in the current environment is, as you will appreciate, a challenging exercise and requires a set of conditioning assumptions *inter alia* regarding the epidemiology of this virus and its variants. It goes almost without saying, therefore, that the level of uncertainty regarding the short-term outlook is very high. Moreover, as the pandemic and the response to it constitute both a demand- and a supply-side shock, there remains uncertainty regarding the medium-term trajectory for the economy also.

Notwithstanding this uncertainty, there is merit, I believe, in producing and publishing a medium-term baseline projection against which we in the Department, on behalf of Government, can monitor and assess emerging

economic and fiscal developments in the coming quarters, and advise accordingly.

As is the norm, and in order to fulfil our legal requirement, we will begin the forecast endorsement exercise with the *Irish Fiscal Advisory Council* in the coming weeks. This is a very rigorous process and one which, in my view, enhances the public good dimension of the Department's biannual forecasts.

The aim is to publish this year's draft *Stability Programme* by mid-April, present it to the Oireachtas, and to transmit the final document to the Commission and Council by the end of that month.

Current economic and fiscal developments

Turning now to emerging economic developments, Members will be familiar with CSO data published last week which show that domestic economic activity contracted in the final quarter of last year. This mainly reflects the more stringent containment measures re-introduced during that quarter in order to suppress transmission of the virus.

Higher frequency data suggest a further contraction in activity in the current quarter. That said, available evidence suggests that households and firms have partly adapted, and this greater resilience suggests that the fall in domestic economic activity may not be as severe as in the first infection wave.

Vaccine development and roll-out signal that an inflection point is, hopefully, within sight. Our anticipation is that economic activity should gradually pick up over the second quarter, and accelerate thereafter, as restrictions are eased.

This trajectory is, of course, contingent upon the assumption that, firstly, the pace of vaccine roll-out ramps-up in the months ahead and, secondly, that vaccine-resistant variants of the virus do not emerge.

The fall-out in the labour market has been severe, though measurement challenges complicate the assessment. While the figure has ebbed and flowed in line with restrictions, the latest data show that, at the end of last year, the level of employment was around 390,000 below its pre-pandemic peak; the unemployment rate was 20 per cent at end-year, an exceptionally high rate. Beyond the short-term, a key risk is that shifting behavioural habits, as well as changes in production patterns that have accelerated on foot of the pandemic, leave lasting scars in the labour market.

The fiscal landscape has been transformed by the pandemic. A general government deficit of nearly €20 billion was recorded last year, around 5½ per cent of national income. This reflects the impact of discretionary policies designed to limit the impact of the pandemic on households and firms, as well as the full operation of the automatic stabilisers.

Rising public indebtedness has been an important shock absorber: at the end of last year, the debt-income ratio reached an estimated 108 per cent and a further increase in the ratio is projected for this year.

The Department will update the projections for the key fiscal variables in the *Stability Programme*.

Conclusion

In conclusion, Chair, thank you once again for the invitation. As I mentioned at the outset, I can discuss the emerging trends in general terms; quantifying these trends remains internal work-in-progress but these will, of course, be published in the *Stability Programme*.

ENDS