## Meeting of the Budgetary Oversight Committee, 15th July 2021

## Opening Statement

## Minister for Finance, Paschal Donohoe

### Introduction

Chair, Members: let me thank the Committee for the invitation to appear here today to discuss the *Summer Economic Statement (SES)* which was published late yesterday evening. I am also happy to discuss 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.

### Summer Economic Statement (SES)

After a difficult – and unprecedented – sixteen months, we are beginning to see light at the end of the tunnel. The vaccination programme is well advanced with approximately half of the eligible population now fully-vaccinated. Restrictions are gradually easing and there are signs of recovery – albeit uneven – in the domestic economy.

Having said that, we cannot expect to return to the same world we occupied before. The pandemic has changed the way in which we work and the way in which we live, and there will be lasting implications that have still to become clear.

While our own vaccine programme is progressing well, we must also be cognisant that large parts of the global population – particularly in developing countries – will not be immunised for some time, leading to the possibility of the emergence of further strains of the virus.

This is the context in which the *Summer Economic Statement* – or SES – has been developed. The SES traditionally provides context for discussions of the various policy options and priorities in advance of the Budget, by setting out the available level of resources for the year ahead.

Taking account of the evolving situation since the publication of the Stability Programme Update in April, the SES incorporates an upward revision to the GDP projection for this year, which is now projected to grow by 8 ¾ per cent. Projected growth in modified domestic demand remains unchanged at 2 ½ per cent this year, and 7 ½ per cent next year, although the forecasts are, of course, contingent on the epidemiological situation.

Put simply, I expect the recovery to continue and to strengthen into next year. There are signs that households and firms have adapted to the changed landscape, with a move towards online transactions, and investment in remote working technologies. And as the public health containment measures ease, we can expect to see further recovery in the labour market.

It is an unfortunate reality, however, that some firms will not survive in the post-pandemic world. The Government will work towards assisting these firms in the transition to newer, more sustainable sectors. We will also facilitate workers in retraining and upskilling, assisting them in the transition from declining to expanding sectors.

## Fiscal response

The Government's approach since the outset of this pandemic has been to minimise the permanent fall-out through the provision of supports to both households and businesses.

To do this, budgetary policy took a counter-cyclical approach. However, counter-cyclical budgetary policy must work both ways to be effective. Therefore, as the private sector and the broader economy begins to recover, it will be necessary to roll back the temporary supports so as to prevent the economy overheating.

And those public supports have been substantial. Taking into account the measures announced in the *National Economic Recovery Plan,* approximately €48 billion has been made available from 2020 - 2022 in the form of direct expenditure, tax measures and 'below the line' supports.

Of the three main support schemes, over €8 billion has been paid to households through the *Pandemic Unemployment Payment,* over €6 and a half billion has been paid to employees through the *Employee Wage Subsidy Scheme* and its precursor, the *Temporary Wage Subsidy Scheme,* and approximately €650 million has been paid to businesses through the *Covid Restrictions Support Scheme.*

As I have stated on many occasions, allowing indebtedness to rise in order to absorb the shock and finance these supports has been the appropriate approach to take.

However, we also need to acknowledge that as the worst effects of the pandemic have passed and the economy begins its recovery, we cannot continue to finance large deficits. The current level of public spending is far in excess of what can be supported by the domestic tax base.

Our public debt ratio is now among the highest in the developed world, and is due to exceed a quarter of a trillion euro next year. Such a large debt burden increases our vulnerability and depresses the living standards of future generations.

## Fiscal policy going forward

Going forward, the Government's budgetary strategy will involve setting an expenditure ceiling of €88.2 billion for next year for core public expenditure. Additionally, we will also provide for a continuation of some temporary supports, amounting to some €6.8 billion. This will be consistent with a budgetary deficit of 6.2 per cent of modified gross national income.

The deficit projection is higher than that projected in April, at the time of the SPU. This is due to additional expenditure, which will allow for continued investment in housing and other critical infrastructure.

Expenditure ceilings are also being set for later years, so that the headline deficit will be around 2.8 per cent of modified gross national income – or 1.5 per cent of GDP – by the mid-part of the decade. Annual expenditure growth has been set at 5 per cent, broadly in line with the trend growth rate of the economy.

If the actual economic performance deviates from expectations, automatic stabilisers will be allowed to operate fully to keep expenditure fixed.

These projections cover the period 2021-2025; the production of this set of forecasts will, of course, require a set of conditioning assumptions *inter alia* regarding the epidemiology of this virus and its variants.

The Government's role will be to put the building blocks in place to allow workers and firms maximise the opportunities of the post-pandemic world, while stabilising the debt to income ratio.

## Future challenges

A key priority will also be reducing the deficit to low levels by the mid-part of the decade. Returning the public finances to a sustainable trajectory puts us in the best position to meet upcoming challenges. We have seen that entering the Covid-19 pandemic from a position of balanced budgets allowed us greater capacity to respond.

And while pandemics may be once-in-a-lifetime events, there are other longer-term challenges that we know will require some tough decisions in the months and years ahead.

A key priority for the Government is the need to finance the 'two transitions': the transition to carbon-neutrality and the transition to a digitised economy.

Ireland's population is ageing rapidly and the fiscal costs are substantial: age-related public expenditure will need to rise considerably simply to maintain service at existing levels.

While corporation tax has helped to 'plug the gap' in many areas of public policy in recent years, there is a very real possibility that this revenue stream will soon begin to decline. Further agreement is needed within the OECD framework. However, international corporate tax reform, when finalised, could reduce Ireland's relative advantage in this area. While the potential revenue loss depends on many factors, my Department's estimate is that corporation tax could be impacted by up to €2 billion annually over the short to medium term.

## Conclusion

In conclusion, I would think it fair to say that while we are facing into an improved and more hopeful period, there are still challenges remaining. We are certainly not out of the woods yet. Government policy will need to continue to adapt to the changing circumstances to sustainably build upon recovery and facilitate a transition to the post-pandemic economy that is as smooth as possible.

Finally, Chair, I would like to thank you once again for the invitation to appear in front of the committee. I look forward to your input and to having a positive exchange today.

**ENDS**