

Committee on Budgetary Oversight
Opening Statement
by Minister McGrath

12th July 2023

Introduction

Thank you for the opportunity to attend the Committee today, alongside my colleague Minister Donohoe, to discuss the Summer Economic Statement, which sets out the fiscal parameters for Budget 2024.

Economic & Fiscal Context

I will begin by briefly outlining the economic and fiscal context for the Budget.

Our economy has weathered a series of unprecedented challenges remarkably well. The level of Modified Domestic Demand (MDD) is well above its pre-pandemic peak with little, if any, evidence of any ‘scarring’ to the economy from these shocks.

The underlying strength of the Irish economy is particularly evident in the labour market: there are now more people at work in our country than ever before, with the unemployment rate at its lowest level in modern history.

Inflation is on a clear downward trajectory and the ongoing easing in energy prices will help support growth through the remainder of the year.

On the international front, the economic outlook remains uncertain and weak.

According to the OECD, in its summer economic assessment, global GDP growth in 2023 is expected to be 2.7 per cent. With the exception of the pandemic-hit year of 2020, this is the lowest annual growth rate since the global financial crisis and growth is expected to see a very modest improvement next year.

Much of the growth is disproportionate and is expected to come from China and emerging markets. Growth is, however, slowing in many of our key export markets, as the impact of significant monetary policy tightening in most regions weighs on demand.

The outlook amongst Ireland's main trading partners, for example is particularly weak, with growth of 0.9 per cent, 1.6 per cent and 0.3 per cent projected this year in the euro area, the US and the UK, respectively.

Irish exports will not be immune from weaker external demand, although headline exports may continue to benefit from the resilience of exports in some of the multinational-dominated sectors.

In addition, we cannot ignore the potential impacts of the war in Ukraine. The uncertain course of the war could very well lead to further disruptions in global energy and other commodity markets including food.

To summarise, on the domestic front, it is clear that the economy is now operating at full capacity, having rebounded strongly following a series of negative supply-side shocks.

However, internationally, the overall outlook remains muted, with downside risks to the fore, despite the fact that energy prices and inflation are on a downward trajectory.

I am of course acutely conscious that, despite our strong economic performance, there are still many challenges facing our economy and our society.

Core inflation has been more persistent than expected, reflecting continuing capacity constraints, lagged pass-through of energy prices and, also some evidence of growing profit margins.

The rise in interest rates, while necessary to curb inflation, has placed a greater burden on households and businesses. This also has implications for Government borrowing over the medium term.

We have demonstrated consistently that we will act when appropriate and as needed to maintain public services and protect incomes. Over the last two years, we have made available €12 billion in direct support to help to offset some of the impact of inflation.

However, it is important to emphasise Governments have a responsibility to strike a delicate balance between addressing the issues of today and ensuring that we are prepared for the challenges of the future.

At the headline level, our public finances are performing well. For the first half of the year, we are, broadly speaking, where we expected to be in respect of tax revenues. Significant budgetary surpluses are in prospect for the next several years.

However, beneath the surface there are real vulnerabilities. I – and Minister Donohoe – have said many times that the exceptionally high growth in corporation tax we have seen over the last several years is not sustainable.

These receipts are welcome, but will not last forever. Estimates by my Department suggest that half the entire corporate tax yield this year is windfall in nature.

That is why it is so important that Government follows a fiscal strategy that strikes the right balance that allows for continued investment in our public services and infrastructure but also maintains our public finances on a positive trajectory.

Budgetary strategy

I believe the strategy which Government set out in the Summer Economic Statement last week achieves this.

Budget 2024 will comprise a total package of €6.4 billion, consisting of slightly above €1.1 billion in taxation measures and new core expenditure of just over €5.2 billion.

This brings core spending growth in Budget 2024 to 6.1 per cent. I recognise that this is above the original 5 per cent target that was set out in Government's medium-term strategy two years ago.

However, as the Committee will appreciate, that strategy was framed in a radically different context.

A realistic fiscal strategy must take into account the prevailing economic environment. Adjusting the fiscal parameters for Budget 2024 makes sense in a context where, even though inflation is easing, prices remain elevated.

It gives us the additional flexibility that we need to maintain the real value of public services, invest in the productive capacity of our economy, and to adjust tax credits and bands so that workers do not face a higher tax burden just because their wages have risen.

The strategy set out in the Summer Economic Statement also represents an important step forward in how we approach the issue of windfall corporation tax receipts. Across the period 2024-2026, €2.25 billion of this windfall will be deployed to support additional infrastructure projects.

This form of capital investment will be contingent on ‘windfall’ receipts remaining at elevated levels and it is intended that investment will be used for projects that can actually be delivered within the time period. Minister Donohoe will provide more details in his opening remarks.

We are all very much aware of the risks of using temporary windfalls to fund permanent spending. We are not going to make that mistake. Instead, we are recognising that these revenues are temporary.

We will take advantage of some of this windfall to build improvements to our economy that will continue to pay dividends long after these transient receipts have fallen away.

We are also setting aside some of the windfall to build up our fiscal buffers and ensure we can face future shocks from a position of strength. €6 billion in windfall receipts have already been transferred to the National Reserve Fund over the last 12 months.

Furthermore, work is currently well underway on proposals for a new, longer-term, savings fund that will allow us to invest excess tax receipts to prepare for the challenges on the horizon, including the long-term structural pressures from an ageing population and the digital and climate transitions.

Parallel to that, we are working on proposals for an additional public investment fund to be utilised during an economic downturn. In the past during challenging economic times, we have had to cut back on capital investment which has had a negative impact on employment.

It is intended that this fund would help maintain capital investment during an economic downturn thus supporting jobs at a critical time and ensuring that major infrastructure projects are delivered.

I intend to bring proposals in this regard to Cabinet over the coming weeks.

Conclusion

The strategy announced in the Summer Economic Statement is a roadmap for building on the progress that we have made. It ensures that we have the flexibility to respond as needed to the challenges of today and those we face in the future.

We have come a long way over the last few years, but there are more challenges that must be addressed. The Summer Economic Statement provides a roadmap for how we will do so.

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