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The Government's *Mid-Year Expenditure Report 2019*: A PBO Analysis

PBO Publication 41 of 2019

Key Messages:

- While the Mid-Year Expenditure Report (MYER) focusses on inputs (monies) and not outputs (services provided etc.), it does then discuss outcomes (at a high level). While outcomes are only discussed briefly, it would be better practice to discuss all three in tandem in accordance with the principles of the Programme Logic Model.[1]
- MYER 2019 is different to previous years as there are two scenarios presented in advance of Budget 2020: 'Scenario A' - an orderly Brexit at the end of 2020 and 'Scenario B' - a disorderly Brexit at the end of October this year. However, a significant level of detail is given *only* in respect of Scenario A, and the starting point for Scenario B builds upon the fiscal position (including pre-committed expenditure) in A.
- A budgetary package of €2.8 billion, based on a headline surplus of 0.4% of GDP for 2020 (Scenario A), is set out in the MYER 2019. Of this amount, €1.9 billion has been pre-committed to expenditure increases while €0.2 billion is to be set aside for a capital reserve. Of the remaining €0.7 billion, €0.3 billion has at this point been included in the 2020 voted current expenditure ceiling.
- Gross voted current expenditure for the first half of the year amounts to 48.8% of the overall gross current expenditure allocation for 2019 while gross voted capital expenditure amounts to 31.6%.
- Between 2019 and 2022, the gross voted current expenditure *ceiling* is set to rise by €4.4 billion or 7.4%. However, based on the policy stance set out in the Summer Economic Statement (SES), current expenditure (including yet to be allocated resources) are projected to increase in that period by an additional €1 billion leading to a 9.3% increase.
- The non-allocation of the projected additional current expenditure of €1 billion is intended, by Government, to address the risk that "expenditure ceilings become floors for budgetary discussions". This appears to acknowledge that the Ministerial Ceilings act as a baseline for budgetary negotiations. The non-allocation of pre-committed expenditure as a measure for controlling expenditure implies that the Ministerial Ceilings are treated not as the projected maximum for expenditure but as the minimum above which incremental adjustments are made. The PBO (and IFAC) have raised concerns that the Expenditure Ceilings are not acting as an effective expenditure control, an issue that this treatment of the Ministerial Ceilings may contribute to.
- Included in capital expenditure increases is a €200 million reserve in 2020 to meet any costs arising from the National Broadband Plan (NBP) and National Children's Hospital (NCH), and €200 million allocated towards the NBP in 2021 and 2022. A capital reserve was previously recommended by the PBO.
- If current expenditure pressures result in Supplementary Estimates in November 2019, this may restrict potential for increased allocations to Vote Groups in 2020. Particular reference is made in the MYER to the fact that only 2% of the additional €0.9 billion allocated to day to day Health expenditure this year has been profiled for expenditure in Q4 2019.
- The MYER also references the Spending Review 2019, although there is no direct link between the two and the Spending Review papers have not been published yet.

Introduction

The Mid-Year Expenditure Report (MYER) provides the pre - Budget baseline for examination of budgetary priorities. It should also identify any areas where significant expenditure pressures or risks are developing.

The opening pre-Budget position for 2020 set out in the MYER is consistent with the budgetary parameters in both the Stability Programme Update (SPU) and the Summer Economic Statement (SES). This year's SES outlines two scenarios for Budget 2020: 'Scenario A' - an orderly Brexit at the end of 2020 and 'Scenario B' - a disorderly Brexit at the end of October this year. The Government will decide in September which is the more likely scenario. The level of detail provided for Scenario B is very limited.

1 See PBO Note 25 of 2018, Performance Information and the Revised Estimates for Public Services.

The MYER 2019 is structured as follows:

Chapter	Issues addressed
One	• Sets out the pre - budget expenditure position; • Gives an update on in-year expenditure at the midpoint of the year; and • Provides multi-annual ceilings for expenditure.
Two	• Examines the trends that are driving the overall volume of public expenditure. • Sets out the 'Medium Term Expenditure Policy'.
Three	• Discusses the objectives, emerging themes and outcomes of the Spending Review 2017 - 2019.

The Pre-Budget Position

The fiscal strategy for Budget 2020 was set out in SES 2019 and considered two budgetary scenarios with regard to the UK's exit from the European Union. The first, 'Scenario A' involves an orderly exit at end of 2020, while 'Scenario B' involves a disorderly exit at the end of October 2019.

A headline surplus of 0.4% of GDP (unchanged from the SPU) is forecast for 2020 in Scenario A. Based on SES fiscal projections, a budgetary package of €2.8 billion can be accommodated in this scenario in Budget 2020. Within this €2.8 billion, €1.9 billion has been pre - committed to expenditure increases in the following areas:

- €0.7 billion increase in capital expenditure;
- €0.3 billion carryover costs associated with Budget 2019 measures;
- €0.4 billion in public sector pay (PSSA) increases; and
- €0.5 billion for demographic costs.

For 2020, the total figure allocated in the Ministerial Vote Group ceilings for demographics across Health, Social Protection and Education is €451 million. This figure may be updated if the relevant Spending Review 2019 paper is updated and published. As the PBO pointed out in Publication 1 of 2019 (p.34) focussing on these three areas excludes a range of other areas which are likely subject to expenditure change as a result of demographics.

A further €0.2 billion has been allocated to a capital expenditure reserve to accommodate spending requirements relating to the National Children's Hospital (NCH) and National Broadband Plan (NBP) as proposed in the SES. This was recommended by the PBO in Publication 10 of 2019 (see 'Key Messages') and is a welcome development. This leaves €0.7 billion for further allocation in Budget 2020 - the SES sets out €0.3 billion of that amount for current expenditure; however a decision on the final split between taxation/expenditure will be taken as part of the Budget/Estimates 2020 process.

With regard to Scenario B, the budgetary strategy for 2020 would be anchored to the budgetary parameters as in Scenario A. That is, all of the pre-committed expenditure set out in Scenario A will still be provided for as the starting point for Scenario B, but would also involve:

- Allowing the automatic stabilisers provide counter - cyclical support;
- Temporary, targeted funding for the sectors most affected, particularly in the areas of Agriculture and Enterprise. Scenario B would also necessitate increased spending in the area of Social Protection.

Depending on the scale of the economic shock arising from a disorderly Brexit, a headline deficit of approx. 0.5% to 1.5% of GDP is projected for 2020.

The MYER sets out ceilings for voted expenditure for 2020-2022. Between 2019 and 2022 the gross voted ceiling is projected to increase by €6.1 billion; from €66.6 billion to €72.7 billion (see Table 1 below). This is made up of €4.4 billion in current expenditure and €1.6 billion in capital[2]. These ceilings and how they break down between Vote Groups are set out in Tables 1.3 (Current) and 1.4 (Capital) of the MYER 2019. However, changes in the Vote Group ceilings are limited to increases in respect of demographics for the three largest Vote Groups of EASP, Health and Education. Changes in the total ceilings as a result of the PSSA, carryover of Budget 2019 measures and resources to be allocated (indicative, and at a global level) are also detailed.

Table 1: Multiannual Expenditure Ceilings 2019-2022 (€ Billions)

	2019	2020	2021	2022
Current	59.3	60.7	62.2	63.7
Capital	7.3	8.1	8.7	8.9
Total	66.6	68.8	70.8	72.7

Source: Budget 2019 and MYER 2019 (Tables 1.3 and 1.4)

2 Breakdown of current and capital affected by 'rounding'.

Impact of Increased Expenditure Growth in the Summer Economic Statement

A distinction is made in the MYER between the expenditure ceilings for Voted expenditure at the time of the SPU (as set out in table 1) and the increased annual growth in overall Voted expenditure post 2020 presented in the SES. While the medium term current expenditure ceilings included in the SPU have an annual growth rate of 2.5% per annum, the SES has a growth rate of 3.25% in this regard. Using SES growth rates, overall Voted expenditure is expected to increase by €7.3 billion, from €66.6bn in 2019 to €73.9bn in 2022 (see Table 2 below). **€5.5 billion of this will be in current expenditure** while €1.8 billion would be made up of capital expenditure.

Table 2: Projected overall Voted Expenditure 2019-2021 (€ Billions)

	2019	2020	2021	2022
Current	59.3	60.7	62.7	64.8
Capital	7.3	8.3	8.9	9.1
Total	66.6	69.0	71.6	73.9

Source: Budget 2019 and MYER 2019

Most of this increase in capital expenditure was previously set out in the National Development Plan 2018-2027 (p.19).However, it also includes the €200 million reserve in capital expenditure in 2020 to meet any costs arising from the NBP and NCH, and €200 million allocated towards the NBP in 2021 and 2022.[3]

The unallocated monies projected to be spent between 2020 and 2024 are set out in Table 3.

Table 3: Additional unallocated expenditure 2020-2024 based on 3.25% growth (€ Billions)

	2020	2021	2022	*2023*	*2024*
Gross Voted Current	0	0.5	1	*1.5*	*2.1*
Gross Voted Capital	0.2	0.2	0.2	*0.3*	*0.3*
Total Gross Voted	0.2	0.7	1.2	*1.8*	*2.4*

Source: MYER 2019, Table 2.2

The strategy of leaving these monies unallocated is intended to address the risk that expenditure ceilings become floors for budgetary discussions.

3 The impact of the increased expenditure on the NBP was previously addressed by the PBO in Publication 30 of 2019.

The MYER states that:

> *"The rationale for this approach is clear, where the non-application of price increases (de-indexation) can be used as a mechanism to generate efficiency dividends and promote productivity where State bodies are effectively challenged to maintain the existing level of service with less resources. Adopting this approach addresses the risk that expenditure ceilings become floors for budgetary discussions and create increased expectations in relation to available expenditure increases, particularly so in an environment where in-year expenditure increases are provided."*[4]

The PBO and IFAC have both highlighted issues with regard to the aforementioned approach with IFAC stating that: *"Upward revisions to ceilings are frequent and the ceilings fail to function as an effective tool for controlling spending"*.[5] The PBO has also expressed the view that:

> *"Ministerial Expenditure Ceilings appear to be treated by key expenditure Departments (Health, Housing, Planning and Local Government, and Education and Skills) as the baseline for expenditure expectations, and are regularly exceeded by any unforeseen events, inefficiencies or overruns in cost."*[6]

With regard to the sustainability of increases in expenditure in recent years the MYER states:[7]

> *"….since the end of 2014 it has been possible to increase expenditure on public services and infrastructure. These increases have been managed in a sustainable manner with voted expenditure growing by €13 billion and Exchequer tax revenue and PRSI growth of €20 billion".*

However it is important to note the role played by Corporation tax receipts in Exchequer tax revenue. Net Receipts in Corporation Tax have more than doubled from €4.6bn in 2014 to €10.4bn in 2018.[8] The PBO has raised concerns regarding the profiling of corporation tax receipts and therefore the sustainability of expenditure based on these profiled receipts.[9]

4 MYER 2019. p. 25.
5 Irish Fiscal Advisory Council - Fiscal Assessment Report June 2019, p. 41
6 See PBO Publication 11 of 2019 - Multiannual Expenditure Ceilings p. 1.
7 MYER 2019 p.ii.
8 Office of the Revue Commissioners - Corporation Tax 2018 Payments and 2017 Returns.
9 See PBO Publication 39 of 2019 - An Overview of the Corporation Tax Base in Ireland and PBO Working Paper Series No. 1 of 2019 - Examining the Volatility of Ireland's Tax Base in the Paradigm of Modern Portfolio Theory.

2019 Expenditure Update

The MYER notes that gross voted current expenditure of €28,938 million for the first half of the year amounts to 48.8% of the overall gross current expenditure allocation. This compares to 48.3% at the same point in 2018. At end June 2019, 14 of the 17 Vote groups are broadly in line or below profile with regard to current expenditure.[10]

Gross voted capital expenditure of €2,318 million in the first half of the year amounts to 31.6% of the total gross voted capital allocation for 2019. This compares to 33.1% at the same time of the year in 2018. Of the 16 votes that have capital expenditure allocations, 14 are on or below profile at end June 2019.[11]

The MYER highlights day to day Health expenditure as a key driver in current expenditure and highlights the tendency for expenditure in Health to increase in the second half of the year, particularly in Q4. The MYER notes:

> *"In light of this trend, it is concerning that only 2 per cent of the additional €0.9 billion allocated to day to day health expenditure this year has been allocated to the final three months of 2019. Indeed, the Department are only projecting that Quarter 4 expenditure in 2019 will be €18 million higher than same quarter in 2018, an optimistic position given the trend in the year to date"* [12]

In addition, the PBO pointed out in Publication 34 of 2019 (Figure 3) that the published profile for the Health Vote anticipates that the relative growth in expenditure in 2019 versus 2018 will peak in May, decline for two months and the increase over last year will then remain close to average.

Public Expenditure Trends

The MYER identifies three key policy areas driving public expenditure:

1. Social Protection;
2. Health; and
3. Education.

Together, these three areas account for c. 80% of all Voted Expenditure.[13]

10 See PBO Quarterly Economic and Fiscal Commentary Q2 2019, p. 25 for a chart illustrating this.
11 See PBO Quarterly Economic and Fiscal Commentary Q2 2019, p. 27 for a chart illustrating this.
12 MYER 2019, p. 4.
13 MYER 2019, p.10.

Employment Affairs & Social Protection

As set out in PBO Publication 40 of 2019, Employment Affairs and Social Protection expenditure, which is funded through both the Vote and the Social Insurance Fund (SIF) was the largest area of expenditure (at 32%) in the 2018 Estimates for Public Services. Over the ten year period, 2008 -2018, Pension expenditure has increased by €1.9 billion or 33% while a significant increase of €697 million or almost 20% was seen in Illness, Disability and Carer programme expenditure.

The MYER highlights the primary factors driving changes in the composition of expenditure over the past decade, namely:

- Increasing number of pension recipients;[14]
- Falling number of those on the Live Register since 2012;[15] and
- Increases in social protection payment rates in recent years well above changes in the inflation rate as measured by the Consumer Price Index (CPI).

MYER 2019 does highlight that Ireland's social protection system is performing well in terms of redistributing income and reducing inequality by listing the following outcomes:

- In 2017 Ireland's Gini Coefficient[16] stood at 30.6, slightly better than the EU average of 30.7; and
- In 2017, Ireland's social transfer system reduced the 'at risk of poverty rate' from 43.8% to 15.7%.

With regard to future issues, the MYER highlights that demographic pressures will continue to increase recipient numbers and therefore costs, particularly with regard to the State pension. Previous analysis carried out by IGEES (2016)[17] estimated the average short term increase to the EASP budget at €253 million. Further analysis is expected in the Spending Review 2019.

Health

The MYER notes issues with assessing Health expenditure since 2009 due to the significant changes that have occurred over the period, e.g. the transfer of Children and Families expenditure to Children and Youth Affairs in

14 See PBO Publication 40 of 2019.
15 *Ibid.*
16 The Gini coefficient measures the degree of equality with 0 representing perfect equality and 100 representing total inequality.
17 *Budgetary Impact of Changing Demographics 2017 -2027.*

2014 and the disestablishment of the HSE vote in 2015. However after attempting to control for these changes as far as possible we see Voted expenditure for Health has increased substantially over the period, going from €14.8 billion in 2009 to €16.8 billion in 2018 with a further increase of c. €1.1 billion in the Voted Health allocation in 2019.

The MYER highlights the main factors as driving expenditure over the past 10 years as:

- Demographics – the overall population increased by 0.32 million or 7% between 2009 and 2018; and
- Reductions in staffing numbers and the use of the Financial Emergency Measures in the Public Interest (FEMPI) resulted in the HSE pay bill reducing by an estimated 11% between 2009 and 2013. Since 2014 HSE staffing numbers have increased by over 20,000 FTE (20%).

The MYER notes that with regard to outcomes that, *"the increased investment in Health over the past decades has been associated with improving Health outcomes in the population"*.[18] Irish life expectancy at birth had increased by over 4.5 years to 80.8 years between 1999-2010. In 2016 this had increased by another year to 81.8.

With regard to future issues in Health Expenditure, MYER 2019 highlights that:

- IGEES (2016) analysis indicates demographic pressures will result in additional costs of €130 million annually between 2017-2020;[19]
- While the impact of new high-tech drugs will have a positive impact in enhancing the wellbeing of individuals with specific illnesses, the associated higher costs will bring a significant challenge with regard to the overall budget impact; and
- Continued economic growth will likely put upward pressure on certain costs, however, declining medical card coverage associated with improvements in the labour market as well as pharmaceutical savings arising from the 2016 agreement with the IPHA may provide downward expenditure pressures.

18 MYER 2019, p.19.
19 *Budgetary Impact of Changing Demographics 2017 -2027.*

Education

Expenditure in Education and Skills (both Exchequer and the NTF) will be €10.8 billion in 2019 - its highest level to date. Expenditure in this area followed the same pattern as overall expenditure, falling by an average of 2% per annum from 2009 -2013, with an average annual growth rate of 3.5% from 2014 -2019. Pay is the single largest component of expenditure in this area, going from €5.1 billion in 2014 to just over €6.1 billion in 2018.

The MYER notes that a range of factors have contributed to driving the trend in education expenditure in the past 10 years and highlights:

- Considerable increases in student numbers from 2008-2018 of 77,000 (16%) in the primary sector, 53,000 (16%) in post-primary and 54,300 (30%) in third level;
- From 2008-2018, staffing in the primary education sector has increased by 21% and by 16% in second level. However, Exchequer funded third level staffing decreased by 10%; and
- Expenditure on special education needs has increased by almost 50% from 2011 to 2018 and now represents nearly 20% of the Department's gross current allocation in 2019. Various drivers have contributed to this increase in expenditure including an increasing proportion of children qualifying for SNA and special educational needs support as well as the underlying age in the school age population.

The MYER states that with regard to outcomes, investment in education *"…has played a pivotal role in improving outcomes and attainment"*[20]. These include:

- Between 2010-2018 the rate of students completing post primary education has increased from 87.7% to 91.6% with a more pronounced increase in DEIS schools, going from 73.2% to 85%;
- The rate of students taking higher level mathematics in the Junior Cert has increased from 45% to 56.7% from 2010 - 2019, while for the Leaving Cert the rate increased to 30.9% from 16% over the same period; and
- The rate of those in the labour force with a third level qualification increased from 39% in 2010, to 44% in 2018.

20 MYER 2019, p.23.

With regard to future issues in Education Expenditure, MYER 2019 highlights that while demographic pressures at primary level are expected to peak in 2018, this will then shift pressure to post primary and then on to third level as these students move through the education system.

Future Expenditure Policy

The expenditure strategy set out in the MYER promotes the adoption of an annual growth in expenditure below the projected growth rate in the economy as measured by GNI*. The use of GNI* is favoured as it better tracks Revenue growth than GDP. Based on the economic growth assumptions used in the SPU, the expenditure position set out in 'Scenario A' of the SES would result in an annual increase in expenditure of 3.5% out to 2024, below the 4% annual GNI* growth forecasted in the same period. The MYER states that:

> *This approach allows for increased investment in public infrastructure as outlined in Project Ireland 2040 and continued investment in public services. The focus of current expenditure will be to continue to ensure that demographic pressures in the key areas of Health, Social Protection and Health are met, with targeted measures to enhance the delivery of public services supported".*[21]

Spending Review 2018

Chapter three discusses the objectives, emerging themes and outcomes of the Spending Review 2017 - 2019. There appears to be no direct link between the two and the Spending Review findings are not discussed as they are, as of now, not published.

21 MYER 2019, p.26.

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