Spring Economic Statement

Speech by the Minister for Finance

Mr. Michael Noonan T.D.

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Introduction

A Cheann Comhairle,

Since taking office in 2011, the Government has been determined to fulfil the mandate given to us by the Irish people. To repair the economy and public finances, to create jobs and to give hope and confidence to our citizens of a better future. The scale of the economic crisis that we have gone through has been unprecedented in Ireland's history. We have essentially lost a decade in terms of economic growth and job creation. Difficult decisions have been taken and huge sacrifices have been made by the Irish people. But this has not been in vain.

A Cheann Comhairle, the Spring Economic Statement published today confirms that the path that has been taken was the right one. As we now plan for the remainder of this decade, our Citizens have every reason to be confident and hopeful about their future. A future of steady, stable economic growth and a future with more people working in secure and sustainable jobs than ever before in the history of the State. A future of stable public finances that will deliver money in people's pockets, higher quality public services and strategic investment in essential infrastructure throughout the Country.

But I want to stress, A Cheann Comhairle, such a bright future is not guaranteed and is contingent on a continuation of the policies and reforms introduced and being followed by this Government. There are external risks, no doubt, but the choices taken within this House matter. A return to the "if I have it, I'll spend it" ways of the past or indeed the "even if I don't have it, I'll spend it" policy stance taken by the opposition over the past four years, is by far the biggest risk.

Any rowing back on the reform measures through, for example, narrowing the tax base, increasing taxes on work and on businesses, halting labour force activation measures, or reducing Ireland's competitiveness, will cost jobs, reduce growth rates and tax receipts and reduce the living standards of the Irish people.

Protecting and securing these hard won gains

Protecting and securing the hard won gains of the last four years and building on them for the future is the priority.

The facts clearly show that the policies of this Government have worked and will continue to work in the years ahead.

- The economy is growing at the fastest rate in Europe - by 4.8 per cent in 2014 and my Department is forecasting growth of 4 per cent this year. Steady, stable economic growth of 3¼ per cent on average is forecast for the remainder of the decade

- The recovery is jobs rich with 95,000 jobs added from the low point in 2012.

- My Department is forecasting that we will pass the two million people in employment mark next year, replace all of the jobs lost during the downturn by 2018 and, in total, between 2015 and 2020, add 200,000 new jobs.

- Net outward migration is expected to cease next year with a return to inward migration from 2017 onwards. The young people who have left are coming back and will continue to do so.

- The public finances are under control with the deficit falling below 3per cent this year and debt levels are set to move down towards the European average in the next few years.

- As a result we will be in a position to implement another expansionary Budget this year and every year out to 2020, if this is deemed prudent and appropriate. We will meet our medium term objective of a balanced budget in structural terms over the forecast horizon.

The Spring Economic Statement being published today sets out the policies to build upon the recovery and deliver these objectives over the remainder of this decade through a continuation of prudent, medium-term focussed budgetary and economic policies that will secure sustainable increases in jobs and in living standards. The April 2015 Update of the Stability Programme is also being published today and will be submitted to the European Commission later this week in line with our requirements under the European Semester.

The Spring Economic Statement is part of a much broader reform of the Budgetary framework. The next in this new framework is the National Economic Dialogue which will take place in in July.

This will widening consultation on the Budget with key stakeholders, while fully respecting the role of the Government and the Oireachtas to make policy. The National Economic Dialogue is about ensuring we have an informed and mature discussion regarding both the short- and medium-term priorities. Full details on these reforms and other reforms are included in section 5.3 of the Spring Economic Statement

Economic developments and outlook

Turning to the economic situation, I am greatly encouraged by the dataflow over the past year or so, which clearly shows that the recovery is gaining momentum and, importantly, is becoming more broadly-based. This is just the start of the recovery and the figures tally with what I see on the ground: more people are working; people have more income in their pockets; people are more confident about the future; businesses are being created and are expanding.

Following GDP growth of nearly 5 per cent last year, as I said my Department is projecting GDP growth of 4 per cent this year, with positive contributions from both exports and domestic demand. Over the remainder of the decade my Department estimates that the economy has the capacity to expand by around 3¼ per cent per annum.

Economic recovery is yielding benefits in the labour market. The figures show that 95,000 net new jobs have been created since the low-point of the crisis, and the latest data show job creation in 11 of the 14 sectors of the economy reported by the Central Statistics Office. The Action Plan for Jobs has played a key role in bringing together all Government Departments and the target of one hundred thousand additional jobs by 2016, will be met this year. Unemployment has fallen by 5 percentage points since its peak and we will continue to work to reduce it further.

A continuation of the current strategy will see two million people at work by the end of 2016. The employment lost during the downturn will be recovered by 2018 and there will be more people working in Ireland by 2020 than ever before.

Rebuilding the economy sector by sector

Stable public finances are essential for economic growth and the first task of the Government was to stabilise the deficit and put it on a downward trajectory. However, the annual Budget is not simply an exercise to meet a deficit target. The design of a Budget is part of a much broader strategy to manage the economy for growth and job creation. In each of the Budgets introduced since 2011 re-building the economy sector-by-sector has been a key feature. So unlike in the past, we in the future will not be reliant on one particular sector – the construction sector – for jobs and growth, and the transactional taxes that flow from this. We must never again repeat the boom and bust economic model. Over the remainder of this decade we expect all sectors of the economy to contribute to growth and employment.

In some areas – such as tourism and agri-food – the approach has been about building on our comparative advantage and exploiting new external market opportunities. The reduction of the VAT to 9% in the tourism and hospitality sector, the abolition of air travel tax and the tax changes to support farmers gearing up for the ending of the milk quota, have all proven very successful. In other areas – particularly construction – the focus has been on repairing a sector that was hugely affected by the crisis. The Government has presented plans to continue the sector by sector approach to growing the economy.

Let me give a few examples of the level of ambition embodied in these strategies:

- Our tourism strategy “People, Place and Policy – Growing Tourism to 2025” aims to increase revenue from overseas visitors by €1.5 billion to €5 billion and to increase employment in the sector by one-fifth to 250,000 by 2025

- IDA’s “Winning Foreign Direct Investment 2015 – 2019” aims to win 900 new investments for Ireland over the period to 2019, creating 80,000 new jobs and 35,000 net jobs. It also sets an objective of winning €3 billion in new research and development investment projects.

- Enterprise Ireland’s “Driving Enterprise Delivering Jobs” strategy to 2016 sets out a range of actions and initiatives that will create over 40,000 new jobs in Irish companies, increasing Irish exports by €5 billion to €22 billion by 2016 and beyond that to €27 billion by 2020.

- The International Financial Services (IFS) Sector 2015 – 2020 targets 10,000 new jobs in the IFS sector by 2020

- Construction 2020 sets out the Government’s strategy for a renewed construction sector which can meet the medium-term demand for about 25,000 new dwellings a year over the next 15 years as well as the other infrastructure needs of the economy.

- The Government is driving a very ambitious and successful growth agenda for the agri-food sector under Food Harvest 2020. The strategy's target amount for all primary output of €5,977m was virtually achieved by 2014, while a 42 per cent increase in exports and a 40per cent increase in value added by 2020 remain on course.

- The rapid development of new payments technologies is fundamentally changing the landscape and throwing up new opportunities and challenges. The advent of SEPA has created a single, integrated payments market in Europe for the first time that can be developed further. Ireland is already an attractive destination for international payment firms but the Government wants to maximise our potential in this sector of the economy and has tasked Enterprise Ireland, in the IFS2020 Strategy, with establishing a payments forum to review the positioning, opportunities and dependencies of the sector.

- Irish Water has set out an ambitious strategy to invest €5.5bn between 2014 and 2021. The increased investment over the period ahead will be vital in ensuring communities can access reliable, high quality drinking water and sewerage services, and our economy can continue to facilitate and attract water-intensive industries – ICT, pharma-chem and agri-food – which, combined, currently provide well over 200,000 jobs. The investment is also required to prevent the massive wastage of water through leaks and to ensure a reliable safe water supply for all our citizens.

The role of the Financial System

This broad based economic strategy is supported by a domestically re-focused banking and financial system, beginning to lend into a much broader range of sectors.

Banking supervision has been improved with a strengthening of the powers of the Central Bank, while at a European level the move towards a Banking Union is continuing. All of these will help prevent excessive credit growth to one sector of the economy in the future. It will also ensure that our SME's and households have access to multiple sources of low cost credit; an essential ingredient for growth.

Addressing personal indebtedness is essential as our economy returns to strength. A mortgage is the single biggest debt most people will ever take on. The number of households unable to meet their monthly mortgage repayments increased with the decline in the economy, as incomes fell and unemployment increased. Supporting homeowners in arrears has been a priority for this Government and a broad strategy has been introduced to keep as many families in their home as possible. This strategy has assisted borrowers and lenders reaching agreement to restructure about 115,000 mortgage accounts.

As the economy continues to improve and incomes rise, the number of arrears cases is falling. However, there are over 37,000 mortgage accounts, representing about 30,000 homeowners, in long term arrears of over two years. The Government is actively considering a range of options to strengthen the mortgage arrears framework in order to ensure that families in long term arrears can find a solution. For the majority of these families the best route to a sustainable and binding solution is through engagement with their bank. Many others will find solutions through the options offered by the Insolvency Service of Ireland.

The Government intends making an announcement on this issue in the coming weeks. A particular focus will be on enhancing the role of the Insolvency Service and the range of solutions that become available through an insolvency arrangement.

Access to credit for households is as important as access to credit to businesses. The mortgage interest's rates being charged by Banks in Ireland have not been reduced in line with the rate reductions by the ECB. I recently discussed this issue with the Central Bank Governor and he updated me on the ongoing work that the Central Bank is carrying out on this issue. The Central Bank will report back to me in the coming weeks and I intend, during the month of May, to initiate discussions with the 6 main lenders in Irish Banking on the issue and look forward to hearing their plans for reducing interest rates.

Budgetary strategy and the fiscal rules

Sustainable public finances are a pre-requisite for improvements in living standards. This Government is committed to prudent management of the public finances in the years ahead and there will be no return to the boom and bust model of the past. This commitment is supported by the fiscal rules that are applicable to Ireland and indeed all other Member States of the European Union. The fiscal rules are designed to support economic growth.

Over the last number of years the need to bring the deficit below 3 per cent of GDP has been the anchor for our fiscal policy. This was a hugely important commitment and each year we set a target to reduce the deficit on a phased basis. Each year we overachieved on our fiscal target, sending a strong message to the public, to SME's, to the FDI sector and to investors at home and abroad that Ireland was regaining control of our public finances. This, in turn, led to increased confidence, increased investment, lower interest rates and borrowing costs; supporting growth and job creation throughout the country.

Over the period 2011 – 2015 the deficit was reduced from €15 billion to €4.5 billion. However, we were in a position to achieve these targets with less tax increases and expenditure cuts than originally envisaged and bring an end to the era of austerity budgets much earlier than originally planned.

My Department is now forecasting a deficit of 2.3 per cent of GDP in 2015. There are obviously risks to this forecast and it is essential that discipline is maintained in the management of the public finances. With the deficit falling below 3%, from next year onwards a different set of rules apply and we will be required to make progress towards a balanced budget in structural terms. This will be the new anchor for budgetary policy and it is designed to ensure that budgetary policy supports economic growth. Put simply it is designed to ensure that the days of "if I have it, I'll spend it" are over and this new approach will protect the Irish people from the boom and bust policies of the past. If these rules had been in place, and properly applied and adhered to in the early 2000's, Ireland would have been far better positioned to weather the global financial crisis.

As the House will be aware, the rules can throw-up anomalies from time-to-time, I recently raised this issue with my European colleagues. What I was concerned about was to ensure a credible application of the rules.

I am pleased to inform the House that the European Commission has accepted that I have a strong point and has agreed to a change in the application of the rules. As a result, the Government will be in a position to introduce our second expansionary Budget in October. Fiscal space of the order of €1.2 billion and up to €1.5 billion will be available for tax reductions and investment in public services. The final scale of the space will become clearer closer to the Budget.

The partners in Government have also agreed that the agreed space will be split 50:50 between tax cuts and expenditure increases and the actual measures will be announced in Budget 2016.

Current indications are that a similar amount of space will be available in later years, while at the same time ensuring the achievement of a balanced budget before the end of the decade.

Reducing the burden of debt

We must continue to reduce the national debt. The budgetary strategy we are pursuing will ensure that our debt levels continue to fall and we are well positioned to withstanding any shocks that may occur in Ireland, in Europe or in the global economy

Reducing the debt remains a key priority and the Government has been working hard to reduce the burden of this debt. We have succeeded in:

- Reducing the interest rate on the European loans provided under the programme;
- Securing agreement to extend the maturity of the European loans;
- Replacing the promissory notes with very long-dated government bonds;
- Replacing just over €18 billion of IMF loans with cheaper market-based funding.

The national debt peaked in 2013 and is on a firm downward path, and is expected to drop below 100 per cent of GDP and move towards the EU average in the years ahead.

Our net debt, taking account of cash the NTMA is holding and other assets is of course much lower.

The cost of servicing the debt has also reduced. Interest rates on 10-year Irish Government paper are below 1 per cent, the lowest ever and Irish government debt is now classified as investment grade by all of the main credit rating agencies.

So we are now in a much better position. Going forward, the fiscal rules require an annual reduction in the debt ratio by $1/20^{th}$ of the difference between the actual level and the 60 per cent of GDP threshold. Contrary to what some of the opposition have stated, this will not require further consolidation by way of tax increases and expenditure cuts. This is because with a growing economy the debt-to-GDP-ratio will fall once we run prudent fiscal policies – in other words growth will do the heaving lifting. This is another reason why stable, steady economic growth combined with prudent budgetary policy is the way forward.

The value of our investment in AIB, Bank of Ireland and Permanent TSB continues to rise. It is not the State's intention to remain a holder of its banking investments in the long term. The exit strategy is about recovery of the full cost of the taxpayer's investment in these institutions and using the proceeds to further reduce the debt. The sale of 25% of PTSB that concluded yesterday, further improves the position and I am now confident that all the taxpayers money invested in AIB, BOI and PTSB will be fully recovered.

Risks of abandoning Budget discipline

The forecasts for future Budgets are contingent on continued sensible economic and budgetary policies being pursued. Prudent policies support growth, support job creation and generate the taxes and the fiscal space for further investment in the economy. The scale of the fiscal space available in later years will be determined by the growth and if the wrong policies are pursued, the economy will not grow and the fiscal space will not materialise. Equally important to the size and scale of Budget plans is the type of measure introduced. As I have stated lower taxes on income will support more jobs and higher taxes will cost tens of thousands of jobs. This is an economic fact.

In the early 2000's, our taxation system became over reliant on transaction and property based taxes. The revenues from the property boom were used to fund a narrowing tax base to an unsustainable level and to fund day-to-day current expenditure. The use of tax expenditures in the early 2000's not only served to hollow out the tax base but led to an overheating of the economy. When the property bubble burst, the Revenues dried up and the consequences have been 8 years of tax increases and expenditure cuts. The response of the Government of the day in the first instance was to load new and additional taxes on work through the introduction of the income levy and the Universal Social Charge.

We must never allow this to happen again and the base broadening measures that have taken place have moved the tax base to a much more stable and growth friendly footing; reducing the reliance on transaction based taxes. The curtailment of tax expenditures, the introduction of the property tax and introduction of alternative funding mechanism for vital public services such as Irish Water are all essential elements for stable public finances. The alternative policy choice in nearly all of these cases is to increase taxes on work, an alternative that can significantly impact on economic growth and jobs.

That is why in my first three Budgets I did not increase income tax or USC charges and at the first available opportunity in Budget 2015, I used available resource to reduce income tax and USC. Not only does this put more money into people's pockets but it boosts confidence and economic activity across the Country.

The Department of Finance estimates, based on the ESRI macroeconomic model, that continuation of the programme of reducing tax in incomes introduced in 2015 for 2016, 2017 and 2018 would increase employment by approximately 1 per cent, the equivalent of 20,000 jobs, by 2020 relative to baseline forecasts. On the other hand, the same research shows that increases in taxes on work would not only result in the loss of the additional jobs but would actually reduce growth and cost jobs over the next five years. In fact the principal domestic risk to Ireland's continued economic growth is the tax and spend policies of the Opposition.

Unfortunately the policies proposed by the opposition will do exactly this. They will increases taxes, increase expenditure, increase debt, lower growth rates, reduce tax buoyancy and cost jobs. The policies of the opposition will again cause the economy to spiral downwards.

This Government has a different policy perspective. The strong exchequer performance coupled with very positive high frequency data on the economy confirm the appropriateness, from an economic perspective, of the decision to reduce income tax and USC for every worker in the country. Putting more money into people pockets has boosted consumer confidence and demand in the domestic economy. It will also encourage young Irish people who are working overseas in good jobs to return home, confident that they will be able to find well paid jobs in Ireland. The Government will continue to follow this policy in the next Budget and in future Budgets if the Government is re-elected.

The 12.5% corporation tax rate will stay. This is a red line for the Government. We will continue to enhance Ireland's attractiveness for Research and Development by introducing a Knowledge Development Box in the next finance bill. We have no reluctance to continue, in parallel with our European Colleagues, in reforming corporation tax but we will not, as many in the opposition advocate, increase the 12.5% rate.

Conclusion

A growing economy is not an end in itself – it is the means by which we will improve living standards, create employment and deliver better public services to the Irish people.

Economic recovery provides us with the platform upon which to build for a future of economic growth, job creation and increased living standards.

A Cheann Comhairle, we must never again repeat the mistakes that left Ireland on the verge of bankruptcy in 2010 and resulted in a lost decade and such hardship in the lives of so many people.

This Government's strategy of steady, stable economic growth will benefit all of our citizens. It will provide the resources for investment in our public services. It will fund the building of new schools, health centres and essential infrastructure. It will deliver secure jobs to more people than ever before in the history of the State, it will put more money in people's pockets and give people security around their income and their pensions. It will entice our emigrants to return home and they in turn will help to build strong communities throughout the Country.