

# PRE-BUDGET OUTLOOK

## OCTOBER 2006

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## Preface

*This report was prepared by the Department of Finance based on data available at end September, 2006. The report covers the period 2006 - 2008 and updates the economic and fiscal projections presented in the Budget Booklet published on Budget day last December.*

*The expenditure figures in this report are based on those presented in the Budget Booklet 2006 adjusted for decisions taken to the end of September. They provide for the estimated cost in 2007 and 2008 of maintaining existing levels of public service and include provision to cover specific commitments under the national agreement "Towards 2016". Tax projections have been updated to take account of performance to the end of September 2006 and revisions to the economic projections since Budget 2006. An unallocated provision is also included in the budgetary arithmetic for 2007 and 2008.*

*Section 1 briefly summarises the outlook for the Irish economy and budget for 2006 - 2008 and the risks attaching to this outlook. Section 2 reviews economic performance in 2006 and Section 3 assesses the outlook for 2007 and 2008. Section 4 updates the budgetary arithmetic for 2006 to 2008*

*The **Pre-Budget Outlook** replaces the Economic Review and Outlook as part of the reform of the budgetary process announced by the Minister in last December's Budget.*

*The projections in this Outlook are made on a pre-2007 published Estimates and a pre-2007 Budget basis. **Final policy decisions in the Estimates and Budget on spending and taxation will affect these projections so that the post-Budget position to be presented on Budget day will inevitably differ from those in the Pre-Budget Outlook.***

*Department of Finance*

*19 October 2006*

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## **Section 1 – Summary Outlook and Commentary**

### **1.1 Economic Outlook**

The outlook for the Irish economy over the period 2006 – 2008 is broadly positive. The external environment looks reasonably favourable, with most international economic organisations projecting continued growth in the world economy. However, notwithstanding some easing in recent months, the relatively high level of oil prices, as well as rising interest rates, could ultimately slow the pace of growth in many of our trading partners as well as in Ireland. Further growth in the Irish economy is forecast, reflecting the strength of domestic demand and a broadly positive external environment. Against this background, growth in both GDP and GNP terms is expected to average 5% per annum over the period.

### **1.2 Budgetary Stance**

Based on the parameters set out in the Preface, the projected budgetary position over the period 2006 - 2008 is for a General Government budget surplus of 1.0% of GDP in 2006 followed by surpluses of 0.4% in 2007 and 0.2% in 2008. The debt-to-GDP ratio will be maintained at the second lowest in the euro area – around 25½% for the forecast period – in line with the Government's long-term priorities. The market value of the assets of the National Pensions Reserve Fund is estimated to be not less than 9.5% of GDP at the end of 2006.

**Table 1 – Projected General Government Balance and Debt Ratio**

<b>% of GDP</b>	<b>Budget 2006</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>
General Government Balance	-0.6	1.0	0.4	0.2
Debt Ratio (year end)	28	25½	25½	25½

Source: Department of Finance

### **1.3 Commentary**

The Irish economy continues to perform reasonably well, with GDP growth of 5¼% currently expected for 2006. The labour market remains buoyant, with further strong employment growth expected. Unemployment this year is likely to remain amongst the lowest in the EU. However, inflation began to pick up during 2006 but should fall back as 2007 progresses. The public finances remain in good health, showing a projected General Government surplus of 1% of GDP and a debt-to-GDP ratio of 25½% in 2006.

The central projections for the period 2006 – 2008 are:

- Both GDP and GNP are forecast to expand by 5% per annum over the period;
- Employment growth is forecast to average 3% per annum, with unemployment remaining relatively low over the forecast horizon;
- HICP inflation is forecast to average 2½% over the period;
- General Government finances are forecast to be in surplus by 1% of GDP in 2006 and 0.3% on average in 2007 and 2008;
- General Government Debt should decline, on this basis, from 27.4% of GDP in 2005 to 25½% of GDP in 2008.

While the outlook is broadly positive it is not without risks. The main external and domestic risks, such as possible adverse developments in the US economy, commodity prices, housing and competitiveness, are discussed in Section 3.

Ireland's medium term economic prospects depend on improving competitiveness and maintaining fiscal sustainability. Continued wage moderation and labour market flexibility are essential to support competitiveness. The implementation of "*Towards 2016*" and the adherence to the earnings changes agreed therein will be critical to future success.

## **Section 2 – Economic Performance 2005 - 2006**

### **2.1 The Economy in 2005**

National income and expenditure data show that GDP and GNP rose by 5.5% and 5.3%, respectively, in 2005, slightly higher than assumed on Budget day. However, some features of this performance should be highlighted. The first relates to the composition of growth, which was entirely driven by domestic demand, with net exports exerting a drag on growth. While some of this reflects sector-specific issues, it also reflects the general deterioration in cost competitiveness in recent years. Secondly, with employment rising by 4.7% last year, the output figures suggest a fairly modest rate of labour productivity growth. This is partly explained by the sectoral composition of output growth – labour intensive sectors such as construction and services were the main driving forces behind growth in 2005.

### **2.2 The Economy in 2006**

Available data point to a continuation of strong economic growth in 2006. On Budget day, GDP growth of 4.8% (GNP of 4.6%) was projected, with domestic demand once again being the main driving force behind growth. Available data are broadly consistent with this overall picture. However, reflecting somewhat stronger data for some components of demand, the forecasts for both GDP and GNP have been revised upwards.

#### **Domestic Demand**

After slowing noticeably over the period 2002-2004, personal consumption growth picked up in 2005 and this trend appears to have continued in 2006. Quarterly national accounts data show that the volume of personal consumption in the first half of 2006 was 6.5% higher than in the same period of last year. This reflects further strong disposable income growth, which, in turn, is due to the continued expansion in employment and increases in per capita earnings. Over the second half of the year, the maturing of the SSIA scheme is expected to provide a further impetus to consumption, although the main impact is likely to be in 2007 (see Appendix 1). For 2006 as a whole, personal consumption is expected to increase by 6½% compared to 5.8% projected at Budget time.

Investment spending rose by 2.9% year-on-year in the first half of the year. Building and construction spending rose by an estimated 7.1%, supported by a further increase in residential construction. Indeed, the generally held assumption of a small decline in new housing output this year may not now be justified, with indicators pointing to another year of record new housing output. If this proves to be the case, 2006 will be the thirteenth successive year in which positive growth has been recorded. Purchases of machinery and equipment declined by an estimated 10.5% year-on-year in the first half of this year, although growth rates in this component can be volatile, as they are sometimes influenced by aircraft purchases. Reflecting the upward revision to the new residential construction forecast, total investment growth is now forecast to be 6¾% this year.

### **Public net current expenditure**

In the first half of 2006, net current expenditure by central and local government on goods and services was 4.2% higher in volume terms than in the same period of 2005. For 2006 as a whole, an increase of 3½% is expected, in line with Budget day projections.

### **Exports of Goods and Services**

The volume of exports rose at an annual rate of 6.0% in the first half of 2006. Strong services sector exports was the main factor underpinning this growth, with balance of payments data indicating that the value of services exports was 18.9% higher in the first half of this year. In contrast, merchandise exports have recorded a somewhat weaker performance in the year to date, with an annual average volume growth rate of just 1.5% in the first half. Taking these data into account, as well as competitiveness trends and demand developments in our major trading partners, the volume of exports of goods and services is now forecast to rise by 4¾% this year.

### **Final Demand and Imports**

In the first half of 2006 imports of goods and services rose at an annual rate of 7.2% in real terms. Balance of payments data show that the value of services imports rose by 15.3% in the first half of the year. At the same time, the volume of merchandise imports rose at an annual average rate of 6.9% in the first half of the year, partly reflecting strong

demand for consumer goods. For the year as a whole, final demand is projected to rise by around 5½% in 2006 in volume terms, with imports projected to rise by 6%.

### **Balance of Payments**

The current account of the balance of payments deteriorated in 2005, with a deficit of €4.2 billion (3.1% of GNP) compared with a deficit of 0.7% of GNP in 2004. The relatively large deficit last year reflects both a decline in the merchandise trade surplus and a widening of the invisibles deficit. The widening of the current account deficit indicates growing imbalances in the economy with competitiveness pressures resulting in a weaker export performance.

With domestic demand likely to be the main driving force behind growth, a further deterioration in the current account is likely this year. Available data are consistent with this analysis, with a deficit of €3.8 billion recorded in the first half of 2006. For the year as a whole, a current account deficit of 4% of GNP is currently projected.

### **Employment and Earnings**

Total employment rose by 89,000 (4.6%) year-on-year in the first half of 2006, and by the second quarter the level of employment exceeded 2 million for the first time in the history of the State. As has been the case in recent years, employment increases in the construction and services sectors were particularly strong, with annual increases of 8.6% and 5.9%, respectively, in the first half of the year. The labour force expanded at an annual rate of 95,000 (4.7%), mainly reflecting higher female participation rates and continued net inward migration. Indeed, non-Irish nationals now account for around 10% of the labour force. The average unemployment rate was 4.3% in the first half of this year.

Available data point to a continuation of favourable labour market trends over the second half of the year, so that for 2006 as a whole, total employment is forecast to rise by 84,000 (4¼%). With the labour force forecast to rise by 4¼%, the unemployment rate is expected to average 4¼% this year, broadly unchanged from last year's rate.

Sectoral data are consistent with a slight moderation in the rate of wage inflation this year. In the construction sector, where the strongest increases have been recorded in

recent years, hourly earnings rose by 2.5% year-on-year in the first half of the year. In the industrial sector, hourly earnings rose at an annual rate of 3.7% in the first quarter. In the business and distribution services sector, weekly earnings rose by 5.4% year-on-year in the first quarter; in the financial sector the equivalent rate of increase was 4.2%, while in the public sector, weekly earnings rose by 5.6%. Taking these data into account, together with indications of a further increase in labour supply due to immigration, non-agricultural earnings per capita are forecast to rise by 4¾% this year.

### **Gross Domestic Product and Gross National Product**

In overall terms, GDP is projected to rise by 5¼% in 2006. In the first half of the year, GNP growth averaged 8%, significantly higher than the GDP growth rate. However, GNP figures are particularly volatile on a quarterly basis, as they are affected by both profit outflows and inflows. Allowing for this volatility, the growth rate of GNP is now likely to be higher than GDP, although the gap is not expected to be as large as indicated by the data for the first half of the year. In overall terms, therefore, GNP growth of 5¾% is now expected.

### **Inflation**

After averaging 2.5% in 2005, the annual rate of inflation, as measured by the Consumer Price Index (CPI), has picked up this year. The acceleration in the rate of increase is mainly attributable to the impact of higher mortgage interest repayments which, in turn, reflects increases in wholesale rates. In addition, a higher level of oil prices has had an adverse impact on the rate of inflation. With CPI inflation averaging 3.8% in the first eight months of the year, it is now possible that inflation will average 4% for the year as a whole.

In terms of euro area comparisons, the appropriate measure of inflation is the Harmonised Index of Consumer Prices (HICP), which differs from the CPI in terms of coverage. The most notable difference relates to the exclusion of mortgage interest repayments from the HICP. As a result, the increase in the HICP this year has been lower than that of the CPI, with HICP inflation averaging 2.8% in the first eight months of the year. However, Irish HICP inflation has been around ½ percentage points higher than the euro area equivalent over the period, mainly reflecting higher services sector inflation in Ireland. For the year as a whole, HICP inflation is forecast to average 3% in 2006.

**Table 2 – Economic Indicators 2006: Budget Forecast and Current Forecast**

% change (unless otherwise indicated)	2006 Forecast (December 2005)	2006 Forecast (October 2006)
GNP	4.6	5¼
GDP	4.8	5¼
<b>Components of real GDP</b>		
Private consumption expenditure	5.8	6½
Public consumption expenditure	3.5	3½
Gross domestic fixed capital formation	4.7	6¾
Exports of goods and services	4.0	4¾
Imports of goods and services	4.5	6
<b>Price Developments</b>		
Harmonised Index of Consumer Prices	2.0	3
<i>Consumer Price Index</i>	2.7	4
<b>Employment</b>		
Unemployment rate (%labour force)	4.3	4¼
Employment growth ('000)	60	84
Employment growth	3.1	4¼

Source: Department of Finance.

## **Section 3 - Economic Outlook 2007 - 2008**

### **3.1 Overview**

The external environment facing the Irish economy looks reasonably sound, with most international economic organisations projecting continued growth in the world economy. However, notwithstanding some easing in recent months, oil prices remain relatively high and the possibility of further increases cannot be ruled out. At the same time, rising interest rates could ultimately slow the pace of growth in many of our trading partners. In addition, there are growing concerns regarding the short-term outlook for the US economy, partly related to developments in the US housing market.

Further strong growth is forecast for the Irish economy, partly reflecting the expected impetus to domestic demand arising from the maturing of the SSIA scheme. Against this background, both GDP and GNP are forecast to grow by 5% next year before slowing to 4½% in 2008, as the impetus to demand from SSIA's begins to fade. There are, however, some risks – both external and domestic – to this relatively benign scenario which could potentially result in below trend growth. On the external side, the key identifiable risks relate to the possibility of a sharp dollar depreciation, given the magnitude of the US current account deficit<sup>1</sup>. In addition, the impact of volatile oil prices on both the global and Irish economies is a cause for concern. Finally, there remains the possibility of lower international economic growth.

On the domestic side, the economy may suffer a further deterioration in domestic competitiveness, through, for example, above normal inflation or low productivity growth. In addition, economic activity is heavily concentrated on one particular sector - construction. It accounts for 12.5% of employment in Ireland compared with 8% in the EU25<sup>2</sup>. As a result, the economy is exposed to adverse developments in this sector, such as rising interest rates. By reducing the demand for housing, higher interest rates could potentially result in lower housing output. The forecasts in this document take account of interest rate changes in the year to date, and assume that the average rate for next year is higher than that of this year.

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<sup>1</sup> The US current account deficit amounted to nearly 6½ per cent of US GDP last year.

<sup>2</sup> 2005 data.

## External Outlook

According to the IMF World Economic Outlook, the outlook for the international economy is positive. Nevertheless, significant downside risks remain which could dampen the rate of global expansion. The IMF forecasts for GDP growth in key economies are set out in the table below.

**Table 3 – GDP Growth in Ireland’s Main Trading Partners**

	2005	2006	2007
Euro area	1.3	2.4	2.0
Germany	0.9	2.0	1.3
France	1.2	2.4	2.3
Italy	0.0	1.5	1.3
UK	1.9	2.7	2.7
EU25	1.8	2.8	2.4
US	3.2	3.4	2.9
Japan	2.6	2.7	2.1

Source: IMF World Economic Outlook, September 2006.

## Domestic Demand

Domestic demand is likely to remain the major driving force behind growth over the forecast horizon. Personal consumption growth should remain robust, supported by strong earnings and employment growth. In addition, the maturing of the SSIA scheme will provide an impetus to personal consumption expenditure, particularly in 2007 when the bulk of the funds become available. In overall terms, growth in personal consumption of 7% is forecast for next year, with a deceleration to 5% projected for 2008 as the impact of the SSIA scheme on consumption begins to fade.

Net current expenditure by central and local government on goods and services is assumed to increase by an average of 3½% per annum over the period 2007 – 2008.

Investment growth over the period 2007 – 2008 is forecast to decelerate somewhat. This partly reflects the assumption that new residential construction will not contribute to growth to the same extent as in the recent past, partly reflecting higher interest rates feeding through to activity. The overall level of new housing output in 2007 is projected to be broadly in line with 2006. However, it is assumed that the maturing of the SSIA scheme will have a positive impact on this component through spending on home improvements. Investment growth in machinery and equipment is expected to average 6% per annum over the projection period, so that in overall terms, total investment is forecast to increase by 5½% in 2007 and by 4% in 2008.

### **Exports of Goods and Services**

Given the reasonably favourable economic environment in most of our major trading partners, exports of goods and services are forecast to rise by 4½% in both 2007 and 2008. Such a growth rate would be below that recorded in the 1990s, and this partly reflects the deterioration in our external competitiveness position in recent years.

### **Final Demand and Imports**

Final demand is forecast to increase by 5¼% in 2007 before slowing to 4½% in 2008, partly due to the unwinding of the SSIA impact on consumption. Imports of goods and services are forecast to expand by 6% next year, before slowing to 4¼% in 2008. The relatively high figure for 2007 reflects the assumption that a large portion of SSIA-related expenditure is on imported goods.

### **Employment and Earnings**

The outlook for the labour market remains reasonably favourable, although the rate of employment growth is expected to moderate from the current relatively high rates of increase. Total employment is forecast to rise by 3% in 2007 and 2% in 2008 with the services sector likely to be the main contributor to growth. The unemployment rate is expected to remain broadly stable over the forecast horizon. Growth in non-agricultural earnings per capita is likely to evolve in line with this year's rate of increase.

### **Gross Domestic Product and Gross National Product**

In overall terms, therefore, both GDP and GNP are forecast to increase by 5% next year, with slightly lower growth of 4½% expected in 2008. These forecasts are based on the assumption of no significant shocks affecting the economy over this period.

### **Inflation**

HICP inflation is forecast to be 2¾% in 2007 and 2% in 2008. These projections assume that oil prices stabilise at close to current levels, and hence do not impact on the annual rate of increase to the same extent as in the recent past. These forecasts also assume that SSIA-related expenditure has a limited effect on consumer prices, which in turn reflects the assumption that expenditure is concentrated on 'large' items (such as cars, foreign holidays, etc) most of which are imported (see Appendix 1).

**Table 4 – Macroeconomic Developments and Prospects**

% change (unless otherwise indicated)	2005	2006	2007	2008
GNP growth at constant market prices	5.3	5¼	5	4½
GNP at current market prices (€m)	135,914	148,875	161,425	174,250
GDP growth at constant market prices	5.5	5¼	5	4½
GDP at current market prices (€m)	161,163	175,625	189,650	204,475
<b>Components of real GDP</b>				
Private consumption expenditure	6.6	6½	7	5
Public consumption expenditure	4.6	3½	3½	3½
Gross domestic fixed capital formation	12.8	6¾	5½	4
Exports of goods and services	3.9	4¾	4½	4½
Imports of goods and services	6.5	6	6	4¼
<b>Price Developments</b>				
HICP	2.2	3	2¾	2
CPI	2.5	4	3¾	2¼
<b>Employment</b>				
Unemployment (% of labour force)	4.3	4¼	4¼	4½
Employment	4.7	4¼	3	2
Labour productivity (GDP / person employed)	0.8	1	2	2½

## **Section 4 – General Budgetary Position**

### **4.1 Summary**

The current outlook is for a General Government budget surplus of 1.0% of GDP in 2006 followed by surpluses of 0.4% in 2007 and 0.2% in 2008 on the basis of the parameters set out in the preface.

The debt/GDP ratio is projected to be around 25½% over the forecast period, less than half the present EU 25 average debt level, and the second lowest in the euro area.

### **4.2 General Government Balances**

The projected outlook for 2006 - 2008 takes account of updated assessments of the tax and expenditure projections in the Budget Booklet published last December. The tax projections have been updated to take account of performances under the main tax heads to the end of September 2006 and revisions to the economic projections since Budget 2006. The expenditure figures are based on the Budget 2006 estimated cost of maintaining existing levels of public service, updated to cover specific commitments under the national agreement "Towards 2016" and specific expenditure decisions to the end of September 2006. In addition, the figures include an unallocated provision for 2007 and 2008.

#### **2006 General Government Balance**

On this basis a surplus of 1.0% of GDP on the General Government Balance is currently projected for 2006, compared with the Budget Day forecast deficit of -0.6% of GDP.

The bulk of this improvement can be explained by the following factors:

- An improvement in tax receipts of €2,200 million or 1.3% of GDP, due mainly to a surplus in stamp duty and capital taxes;
- An improvement in the net surplus of the Social Security sector of €140 million or 0.1% of GDP;
- Tax accrual of 0.1% of GDP.

The performance of tax revenues in 2006 broadly reflects developments in the economy. It is projected that the four main tax heads – VAT, Income Tax, Corporation Tax and

Excise Duty – which together accounted for almost 88% of targeted tax revenues in Budget 2006 will be just over 2% above the Budget day target. As regards Stamp Duty and Capital Gains Tax, the very substantial projected surplus of €1.25 billion reflects the fact that contrary to the generally held assumption that 2006 would see some easing in the housing market and the construction sector generally, this sector of the economy has continued to perform particularly strongly.

The strong performance of Stamp Duty is evident in receipts from both residential and commercial property. It is currently expected that receipts from commercial property transactions will account for close to 45% of all Stamp Duty receipts in 2006, with receipts from residential property accounting for around 38%. It is estimated that first-time buyers will contribute €70 million or 2% of the total Stamp Duty yield this year.

The gross debt will fall to 25½% of GDP. It is estimated that the amount of accumulated funds in the National Pensions Reserve Fund will be not less than 9.5% of GDP at end-2006 giving a net debt of some 16% of GDP.

### **Outlook for 2007 and 2008**

These projections do not take account of developments in the pre-Budget Estimates (to be published mid-November) or on Budget day itself (early December) but the forward projections provide for an unallocated provision for each of the years 2007 and 2008. Taking account of these factors a General Government surplus of 0.4% of GDP would be in prospect for 2007, followed by an estimated surplus of 0.2% in 2008. Ireland is expected to continue to have the second lowest debt to GDP ratio in the euro area with a ratio of around 25½% for the forecast period. These projections are based on the growth forecasts in Section 3. In the event that growth was, for example, 1% lower than forecast this would lead to a deterioration in the General Government Balance of about ½% of GDP. However, changes to the composition of growth can impact significantly on that general rule.

The data in Table 5 below update the budgetary projections in General Government terms and Table 6 updates Table 1 of the Budget 2006 – Statistics and Tables (see page D5 of the Budget Booklet). These projections will be subject to further revision as more data become available, especially in relation to revenue where November in

particular has a high tax yield (for Corporation Tax, CGT and self-employed income tax). In addition, the tax forecast for 2007 takes into account the loss to Corporation Tax of the cash flow benefit arising from the introduction of a current year payment system for Corporation Tax introduced on a phased basis between 2002 and 2006. This cash flow loss in 2007 will, however, be offset by the ending of the SSIA scheme.

In order to address acute infrastructural needs and provide a basis for growth in the medium-term, Ireland's investment in infrastructure is currently running well ahead of the EU average. Public investment, including PPP capital funded by annual payments from the Exchequer, will average about 5.0% of GNP over the period 2006-2010. This takes account of the impact of the "Transport 21" Programme. If public investment in Ireland were at the EU average level, the General Government Balance position would improve by about 1.5% of GDP.

At least 1% of GNP will continue to be set aside annually in the National Pensions Reserve Fund for the pre-funding of part of future pension liabilities, building up assets to help address costs associated with ageing in future decades. This pre-funding does not affect the General Government Balance, but does add to the General Government Debt.

**Table 5 – General Government Budgetary Developments and Prospects**

	2005 €m	2005 % of GDP	2006 (P) % of GDP	2007(P) % of GDP	2008(P) % of GDP
<b>Government surplus (+) / deficit (-) by sub-sector</b>					
General government (GGB)	1,745	1.1	1.0	0.4	0.2
Central government	966	0.6	0.8	0.4	0.2
Local government	185	0.1	-0.1	-0.1	-0.1
Social security funds	594	0.4	0.3	0.1	0.1

Source: Department of Finance. Figures may be affected by rounding.

(P): Projected

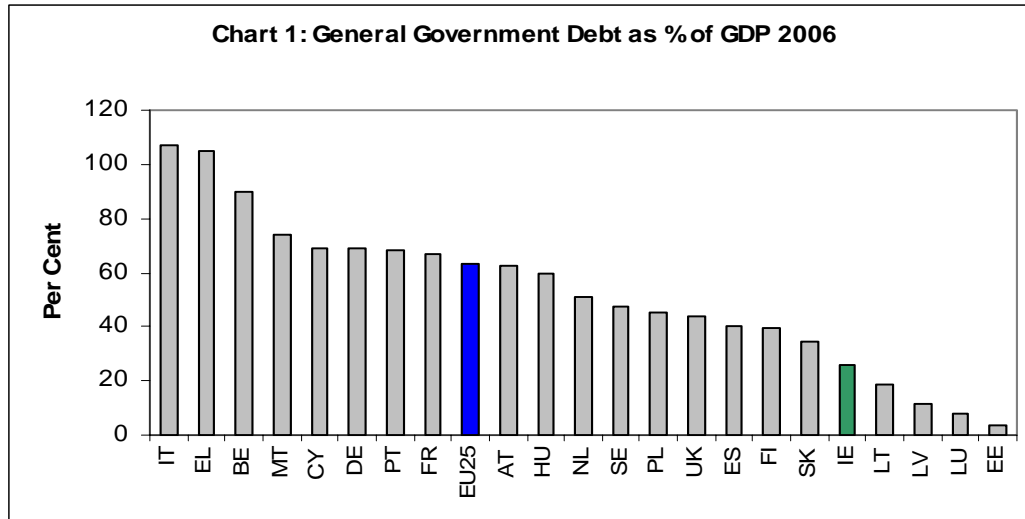
**Table 6 - Summary of Projected Current and Capital Budgets 2006 - 2008**

	2006 Budget Estimate	2006 Estimated Outturn	2007 Projection	2008 Projection
<u>Current Budget</u>				
	€m	€m	€m	€m
<u>Current Expenditure</u>				
	43,812	43,876	46,172	47,894
	4,339	4,339	4,673	4,871
	48,151	48,215	50,845	52,764
<i>less</i>	10,328	10,415	10,434	10,686
Net Current Expenditure	37,824	37,800	40,410	42,078
<u>Current Receipts</u>				
	41,650	43,850	47,400	50,700
	570	570	562	595
Total Current Receipts	42,220	44,420	47,962	51,295
Current Budget Balance	4,397	6,620	7,551	9,216
<u>Capital Budget</u>				
<u>Capital Expenditure</u>				
	6,741	6,767	7,407	7,879
	1,049	831	931	919
	1,447	1,447	1,614	1,742
<i>less</i>	94	124	87	87
Net Capital Expenditure	9,143	8,921	9,865	10,454
Capital Resources	1,819	1,675	1,412	1,473
Capital Budget Balance	-7,324	-7,246	-8,454	-8,980
Unallocated Provision			1,500	3,000
<u>Exchequer Balance</u>	-2,927	-626	-2,403	-2,764
<u>General Government Balance</u>	-952	1,800	720	500
<u>General Government Balance as a % of GDP</u>	-0.6%	1.0%	0.4%	0.2%
<i>GDP Value (ESA 95 basis)</i>	172,550	175,625	189,650	204,475
<i>GNP Value (ESA 95 basis)</i>	144,650	148,875	161,425	174,250

Source: Department of Finance. Note that figures may not add due to rounding.

### 4.3 Debt Level and Developments

As indicated by Chart 1 below, Ireland has one of the lowest debt/GDP ratios in the EU25. Over the Programme period, the gross debt level is expected to decline to around 25½% of GDP.



Source: European Commission Spring Forecasts 2006; Irish data: Department of Finance (estimates)

When account is taken of the build-up of assets in the National Pensions Reserve Fund, the debt-to-GDP ratio, net of those assets, is estimated to be some 16% of GDP at end-June 2006.

**Table 7 – General Government Debt Developments**

% of GDP	2005	2006	2007	2008
<b>Gross debt</b>	27.4	25½	25½	25½
<b>Change in gross debt ratio</b>	-0.9	-2	-	-

Source: Department of Finance

## Appendix 1: Special Saving Incentive Accounts

The Special Saving Incentive Accounts (SSIAs) mature over the period May 2006 to April 2007, with around two-thirds maturing next year. Almost 1.1 million accounts were opened with an estimated accumulated value in the region of €15 billion.

The maturing of the SSIA scheme has implications for the economy over the period 2006 – 2008, affecting key economic variables such as household consumption, investment and imports.

The actual economic impact depends on how the savings are used. Economic theory suggests that consumption decisions are made on the basis of households' perceptions of their permanent income rather than transitory or temporary changes in income. In these circumstances, it is reasonable to assume that while some increase in consumption is likely, a large portion of the accumulated funds will remain in the savings pool. In terms of the international experience, there are few, if any, very similar schemes to the SSIA scheme. However, the international experience that does exist suggests that the marginal propensity to consume from windfall gains is fairly low<sup>3</sup>, which would tend to support the conclusions of economic analysis.

The CSO included a series of questions on SSIAs as part of a special module attached to the final quarter of 2005 Quarterly National Household Survey. This provided some useful additional insights into the prospective impact of SSIA maturity on the economy. From the responses of those who had at least some idea as to their likely intentions, the results suggest that 31% of funds are likely to be spent on consumer items (cars, foreign holidays, home improvement); 12% of funds will be used to finance other (i.e. unspecified) expenditure; 46% of funds will be diverted into alternative savings products (i.e. pension funds, investments, other savings); and 10% of funds will be used to run down debt.

The survey reflects an individual's intentions at a point in time and these intentions can change, especially if economic circumstances change. Nevertheless, it can be tentatively concluded that over half of the accumulated funds are likely to remain in the savings pool and will not impact on economic activity in any significant way, while something of the order of one-third would be consumed on 'large' consumer items, many of which are imported.

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<sup>3</sup> See, for instance, OECD Economic Survey of Ireland, March 2006.