INTERNATIONAL MONETARY FUND

IMF Country Report No. 19/164

IRELAND

June 2019

2019 ARTICLE IV CONSULTATION—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR IRELAND

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2019 Article IV consultation with Ireland, the following documents have been released and are included in this package:

- A **Press Release** summarizing the views of the Executive Board as expressed during its June 14, 2019 consideration of the staff report that concluded the Article IV consultation with Ireland.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on June 14, 2019, following discussions that ended on May 10, 2019 with the officials of Ireland on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on May 30, 2019.
- An **Informational Annex** prepared by the IMF staff.
- A **Statement by the Executive Director** for Ireland.

The document listed below have been or will be separately released.

Selected Issues

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

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INTERNATIONAL MONETARY FUND — COMMUNICATIONS DEPARTMENT

Press Release No. 19/221
FOR IMMEDIATE RELEASE
June 17, 2019

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Executive Board Concludes 2019 Article IV Consultation with Ireland

On June 14, 2019, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[1] with Ireland.

The strong growth of the Irish economy continued as multinational sector-led net exports boosted real GDP growth in 2018 to 6.8 percent, while (modified) domestic demand expanded by 3.3 percent. Solid job creation pushed the unemployment rate below 6 percent, with strengthening net inward migration. Inflation has been gradually rising on the back of sustained demand pressures and dissipating effects of past sterling depreciation. Public finances improved further, supported by strong output growth and abundant unforeseen corporate income tax proceeds. Public debt declined by almost 4 percentage points to below 65 percent of GDP (105 percent of GNI*). The current account surplus widened moderately to 9.1 percent of GDP, mainly reflecting activities of multinationals.

The downsized banking sector is well capitalized and liquid, but profitability is under pressure and credit to the economy has only recently begun to expand. While still high, nonperforming loans have declined. At the same time, investment funds and other financial intermediaries continue to grow rapidly, lifting the overall size of Ireland's financial sector above its pre-crisis level. Household balance sheets have improved on the back of strong income growth. Housing prices continued to grow, but at a slower pace amid signs that the supply of housing has begun to respond to rising demand.

The outlook is broadly positive, provided Brexit proceeds in an orderly manner. Growth is projected to slow to about 4 percent in 2019 as one-off factors driving MNEs' net exports dissipate, and to gradually converge to its potential rate of close to 3 percent over the medium term, thereby closing the positive output gap. Further employment growth will tap foreign labor inflows, reduce unemployment to about 5 percent, and support earnings and private

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

(continued…)

consumption. Headline inflation is expected to reach 2 percent over the medium term. Public finances are estimated to improve further. The external current account surplus is projected to subside to below 5 percent of GDP over the medium term.

Executive Board Assessment[2]

Executive Directors agreed with the thrust of the staff appraisal. They welcomed Ireland's strong, broad-based growth, bringing unemployment down to historical lows and strengthening public and private balance sheets. Directors noted that while the outlook remains favorable, there are challenges from domestic capacity constraints and external downside risks, notably a no-deal Brexit, escalation of global protectionism, and adapting to ongoing international tax changes. Against this background, Directors encouraged the authorities to strengthen fiscal buffers, address key structural bottlenecks to growth, and continue preparing for Brexit.

Noting the advanced cyclical position and external risks to the outlook, Directors encouraged the authorities to accelerate fiscal consolidation to alleviate demand pressures and build buffers. They saw merit in saving additional corporate tax revenue, broadening the tax base to reduce dependency on uncertain revenues, reforming personal income taxation to make it more efficient, and enforcing spending limits. They underscored the importance of ensuring value-for-money in public infrastructure investments. Directors supported establishing the Rainy-Day Fund as a fiscal tool for unforeseen events and welcomed the authorities' commitment to using all proceeds from financial sector divestments to reduce public debt. They encouraged the authorities to continue implementing the international tax reform agenda, develop an ambitious strategy to achieve Ireland's climate change commitments, and strengthen the long-term financial soundness of the Social Insurance Fund.

Directors acknowledged that Ireland is uniquely vulnerable to a no-deal Brexit. They concurred that, if this risk were to materialize, the government should let automatic fiscal stabilizers operate freely and provide targeted support to hard-hit sectors. A fiscal stimulus may be called for, depending on the severity of the downturn in the broader economy. In case of a sharp credit contraction, Directors considered that the countercyclical capital buffer could be released.

Directors welcomed the progress in balance sheets repair of the domestic banks but stressed that continued efforts to improve asset quality remain a priority. To help reach the targets for NPL reduction, they supported measures to accelerate legal processes, encourage creditor-borrower engagement, and enhance supervisory efforts. Directors welcomed the proactive use of macroprudential policy tools and endorsed the expansion of the toolkit with a systemic risk

[2] At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

buffer and debt-based measures. They also encouraged further strengthening the AML/CFT framework.

Directors noted the authorities' efforts in data collection on the large and fast-growing nonbank sector. They encouraged the authorities to further improve data collection, closely monitor risk build-up, and develop system-wide stress testing. In view of the sector's global reach, Directors emphasized the need for continued engagement in international cooperation. Close cooperation with the EU and the U.K. should continue to avoid cliff-edge risks related to Brexit.

Directors underscored the importance of addressing key structural bottlenecks to growth. They welcomed the progress in the provision of social housing and encouraged the authorities to continue their efforts to boost housing supply, including through further rationalizing building regulations. Directors recognized the need to boost productivity in domestic firms, also by direct funding of innovation, employee training programs, and infrastructure investments. They supported the authorities' measures to increase female employment, notably through the affordable child care program, and encouraged further aligning educational paths with business demand for high-skilled jobs.

Ireland: Selected Economic Indicators, 2016–24

Populations (2018, millions): 4.8 — Per capita income (euros): 37,545
Quota (as of Apr. 30, 2018, millions of SDRs): 3,449.9 — At-risk-of -poverty rate [1/]: 16.6

	2016	2017	2018	2019	2020	2021	2022	2023	2024
			Projections						
	(annual percentage change, constant prices, unless otherwise indicated)								
Output/Demand									
Real GDP	4.9	7.2	6.8	4.1	3.4	3.1	2.9	2.7	2.7
Domestic demand	22.7	-13.0	4.4	3.8	3.3	3.0	2.8	2.7	2.7
Public consumption	3.5	3.9	6.4	3.0	1.7	2.5	2.9	2.1	2.3
Private consumption	3.7	1.9	3.0	2.5	2.5	2.4	2.4	2.3	2.3
Gross fixed capital formation	53.2	-30.2	7.8	5.9	5.2	4.1	3.5	3.5	3.5
Exports of goods and services	4.4	7.7	8.9	4.6	4.4	4.3	4.2	4.1	4.1
Imports of goods and services	18.5	-9.3	7.2	4.5	4.6	4.6	4.6	4.6	4.6
Potential growth	3.5	8.5	6.0	4.3	3.7	3.5	3.2	3.0	2.8
Output gap	1.9	0.7	1.5	1.3	1.1	0.7	0.5	0.2	0.0
Contribution to growth									
Domestic demand	16.0	-10.7	2.8	2.6	2.3	2.1	2.0	1.9	1.9
Consumption	1.7	1.1	1.7	1.1	1.0	1.0	1.1	1.0	1.0
Gross fixed capital formation	12.6	-10.7	1.8	1.5	1.3	1.0	0.9	0.9	0.9
Inventories	1.7	-1.1	-0.6	0.0	0.0	0.0	0.0	0.0	0.0
Net exports	-12.1	18.9	4.4	1.5	1.1	1.0	0.9	0.8	0.8
Residual	1.0	-1.0	-0.4	0.0	0.0	0.0	0.0	0.0	0.0
Prices									
Inflation (HICP)	-0.2	0.3	0.7	1.2	1.5	1.7	1.9	2.0	2.0
GDP deflator	-0.8	0.4	1.4	1.2	1.4	1.8	2.0	2.0	2.0
Terms-of-trade (goods and services)	-0.4	-1.8	-0.8	-1.0	-0.1	0.2	0.4	0.3	0.2
Employment and wages									
Employment (ILO definition)	3.6	2.9	2.9	1.9	1.4	1.1	1.0	1.0	1.0
Unemployment rate (percent)	8.4	6.7	5.8	5.4	5.0	5.0	4.9	4.9	4.9
Average nominal wage	1.1	2.3	3.6	2.7	2.6	2.6	2.6	2.6	2.6
	(percent of GDP)								
Public Finance, General Government									
Revenue	27.0	26.1	25.8	25.9	25.5	25.3	24.7	24.6	24.5
Expenditure	27.6	26.3	25.8	26.0	25.3	25.0	24.2	24.0	23.8
Overall balance	-0.7	-0.3	0.0	0.0	0.2	0.3	0.5	0.7	0.7
Primary balance	1.6	1.7	1.7	1.5	1.5	1.5	1.6	1.8	1.8
Structural balance (percent of potential GDP)	-1.5	-0.4	-0.5	-0.4	-0.2	0.1	0.3	0.6	0.7
General government gross debt	73.5	68.6	64.8	62.3	58.8	57.0	54.0	51.1	48.0
General government net debt	64.8	59.8	55.8	53.1	51.5	49.5	46.7	44.1	41.2
Balance of payments									
Trade balance (goods)	38.9	36.7	34.5	32.8	32.0	31.7	31.5	31.4	31.4
Current account balance	-4.2	8.5	9.1	7.9	6.9	6.3	5.8	5.2	4.6
Gross external debt (excl. IFC)	294.4	255.0	221.3	209.7	200.3	191.5	183.3	176.3	169.8
Saving and investment balance									
Gross national savings	33.7	33.2	35.0	35.6	35.2	34.9	34.6	34.3	33.9
Private sector	32.4	31.7	33.3	34.0	33.5	33.1	32.7	32.3	31.9
Public sector	1.3	1.5	1.7	1.6	1.7	1.8	1.8	2.0	2.0
Gross capital formation	37.9	24.8	25.1	26.5	26.9	27.1	27.2	27.4	27.5
	(percent)								
Monetary and financial indicators [2/]									
Bank credit to private sector (growth rate)	-7.6	-3.2	-3.4	...	...	...	...	...	...
Deposit rates	0.7	0.4	0.3	...	...	...	...	...	...
Government 10-year bond yield	0.7	0.8	1.1	...	...	...	...	...	...
Memorandum items:									
Nominal GDP (€ billions)	272.9	293.7	318.3	335.4	351.8	369.4	387.7	405.9	425.0
Modified total domestic demand (percent)	8.4	1.4	3.3	3.6	3.2	3.1	3.0	2.7	2.7
Potential real GNI* growth (percent)	2.4	2.1	1.9	...	...	...	...	...	...
Population growth (percent)	1.2	1.1	1.2	1.3	1.0	1.0	1.0	1.0	1.0

Sources: CSO; DoF; Eurostat; and IMF staff.

[1/] Share of population with an equivalised disposable income (including social transfers) below the threshold of 60 percent of the national median equivalised disposable income after social transfers. Data is as of 2016.

[2/] Latest observation is November 2018.

INTERNATIONAL MONETARY FUND

IRELAND

STAFF REPORT FOR THE 2019 ARTICLE IV CONSULTATION

May 30, 2019

KEY ISSUES

Context. The Irish economy continues to expand strongly, benefitting from higher net exports by multinational enterprises and robust domestic demand. Accelerating wage growth reflects tight labor market conditions and inflation has started to pick up. Crisis legacies have diminished but some vulnerabilities persist.

Outlook and risks. The outlook remains broadly positive, provided Brexit proceeds in an orderly manner. However, the economy operates near full capacity and an accelerating cyclical momentum could re-ignite a boom-bust dynamic. A no-deal Brexit represents the key downside risk, while escalation in global protectionism and sudden changes in corporate tax planning of multinational enterprises in Ireland could adversely affect the economy and public finances.

Challenges and policy priorities. Major challenges are to lessen capacity constraints and steer the economy through the fallout of Brexit, also by reducing fiscal vulnerabilities and addressing structural bottlenecks. Particularly:

- ***Fiscal***. Accelerate fiscal consolidation to alleviate demand pressures, reduce dependency on uncertain revenues, and build buffers against risks. Reform the income tax system to make it more efficient while broadening the tax base, enforce spending limits, and enhance efficiency of public investment. Continue active engagement in implementing the international corporate tax reform agenda and develop a strategy to achieve Ireland's climate targets. Strengthen the long-term financial soundness of the Social Insurance Fund.
- ***Financial***. Step up efforts to reduce nonperforming loans to the target level. Complement macroprudential toolkit with debt-based instruments and a systemic risk buffer. Monitor closely potential risks in and spillovers from the growing non-bank sector. Continue to ensure high-quality authorization of Brexit-related relocations.
- ***Structural***. Improve infrastructure quality, with emphasis on investment outcomes, and expand the housing supply. Continue to align education and training programs to labor demand in sectors with high-skills, high-pay jobs. Tackle the gender pay gap and ensure equal job opportunities for women.

Approved By
Enrica Detragiache (EUR) and Vikram Haksar (SPR)

Discussions were held in Dublin during April 30–May 10, 2019. The mission comprised E. De Vrijer (head), A. Jewell, J. Podpiera, and A. Shabunina (all EUR). A. McKiernan and P. Mooney (OED) participated in the discussions. The team was supported from headquarters by M. Maneely, A. Musayev, G. Ordonez-Baric, and N. Romanova (EUR). The mission met with the Minister for Finance and Public Expenditure & Reform P. Donohoe, Governor P. Lane, other officials, parliamentarians and private sector representatives, and held a teleconference with ECB's SSM staff.

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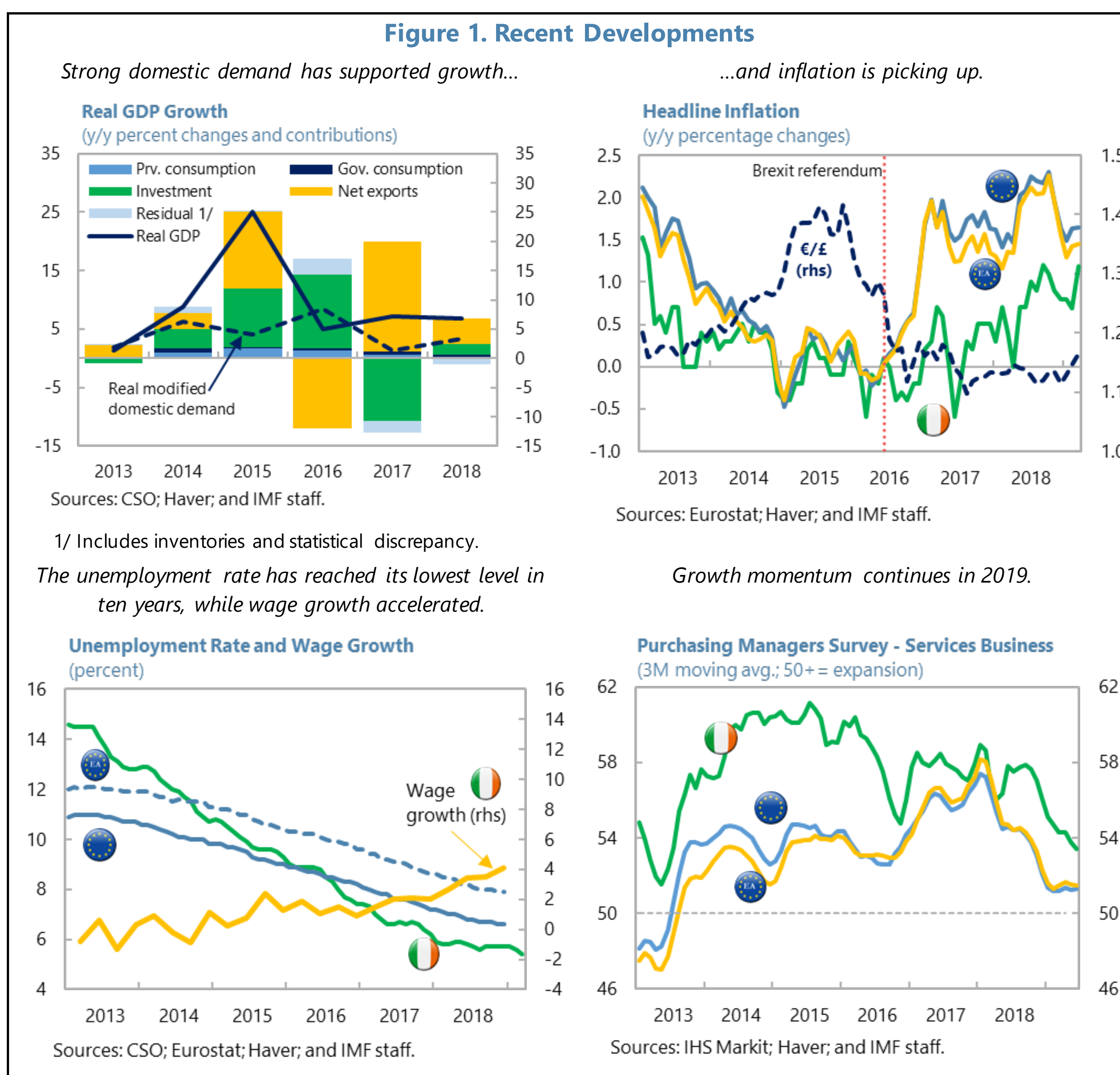
CONTEXT: A BROAD-BASED EXPANSION

1. Strong growth continues, underpinned by robust external and domestic demand. Multinational sector-led net exports boosted real GDP growth in 2018 to 6.8 percent, while real modified domestic demand expanded by 3.3 percent. Private consumption benefitted from continued employment gains, accelerating pay increases, and tax cuts. Investment in equipment and construction has accelerated, while declines in intangibles and aircraft weakened headline investment. Continued job creation pushed the unemployment rate below 6 percent in April 2019, with strengthening net inward migration. Inflation has been gradually rising on the back of sustained demand pressures and dissipating effects of past sterling depreciation. High frequency indicators point to continued growth momentum in 2019.



2. The strong expansion has advanced the cyclical position. Relying on GNI*, which better measures the underlying economy than GDP, the output gap is estimated to be positive and close to 2 percent of potential GNI* in 2018. While unemployment has approached historical lows, capacity is being stretched through employment gains from net immigration, accounting for more than half of population growth in 2018. This also adds to demand for housing, pushing up housing prices. Core inflation has picked up, to one percent at end-2018, and became the major driver of headline inflation in the first quarter of this year.

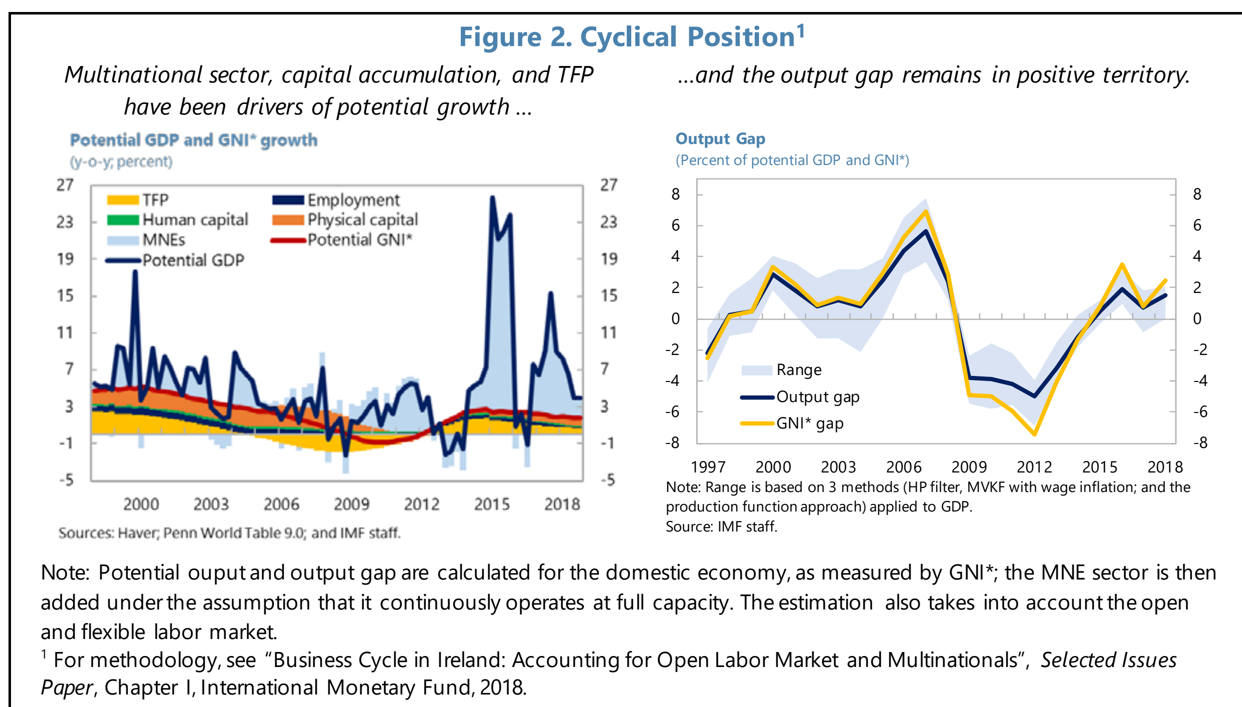


Figure 2. Cyclical Position[1]

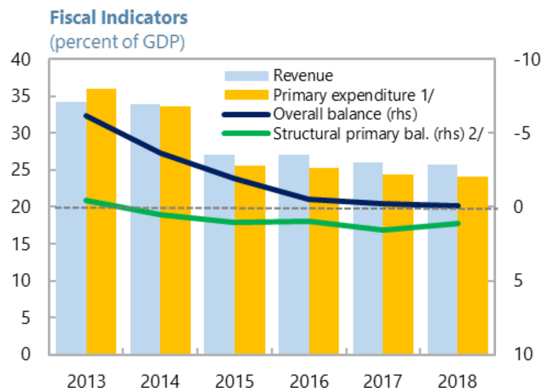
Note: Potential ouput and output gap are calculated for the domestic economy, as measured by GNI*; the MNE sector is then added under the assumption that it continuously operates at full capacity. The estimation also takes into account the open and flexible labor market.

[1] For methodology, see "Business Cycle in Ireland: Accounting for Open Labor Market and Multinationals", *Selected Issues Paper*, Chapter I, International Monetary Fund, 2018.

3. Public finances improved further, thanks to strong output growth and better-than-expected revenues, but the fiscal effort has weakened. The budget closed in balance in 2018, 0.2 percentage points of GDP better than expected. Abundant unforeseen corporate income tax (CIT) proceeds more than offset additional expenditure growth of 3 percent, compared to Budget 2018, especially in healthcare and capital expenditures. However, the structural deficit has remained unchanged from the previous year, reflecting government's risk management approach with respect to the need to alleviate demand pressures and to prepare for downside risks. Public debt declined by almost 4 percentage points to below 65 percent of GDP (105 percent of GNI*). Market conditions remain favorable with low spreads, reflecting Ireland's A sovereign rating with all major rating agencies and the ECB's quantitative easing. In the first quarter of 2019, Exchequer returns have been broadly in line with budget projections.

Figure 3. Fiscal Developments

Fiscal consolidation endures but at a slower pace.

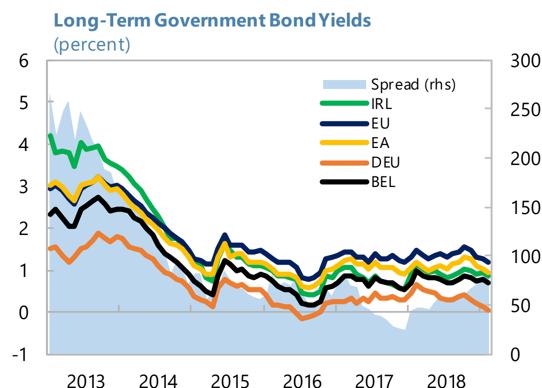


Sources: Eurostat and IMF staff.

1/ Excluding bank support.

2/ percent of potential output

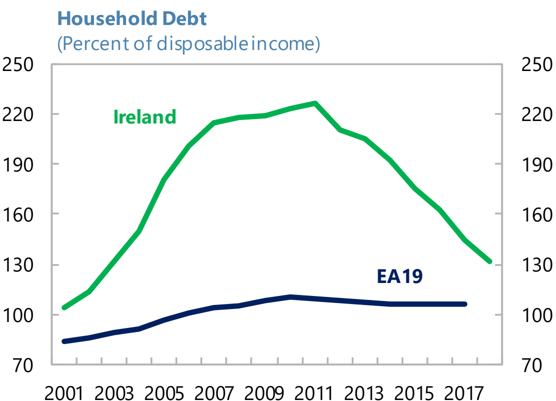
Favorable market conditions persist.



Sources: ECB; Haver; and IMF staff.

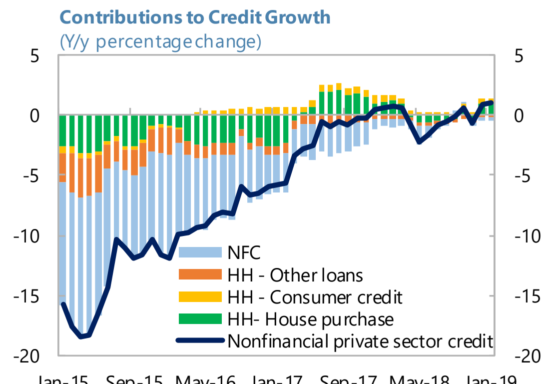
Figure 4. Credit Developments

Household balance sheets are strengthening...



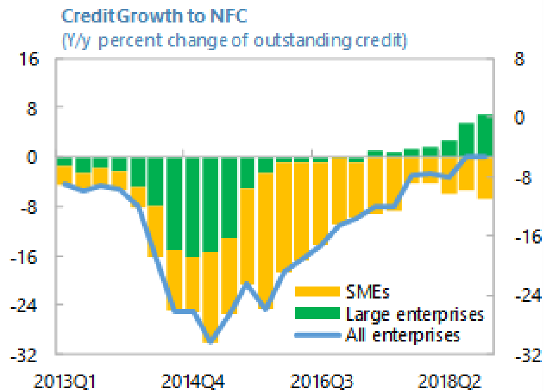
Sources: CSO and Eurostat.

...and supporting a recovery in credit growth.



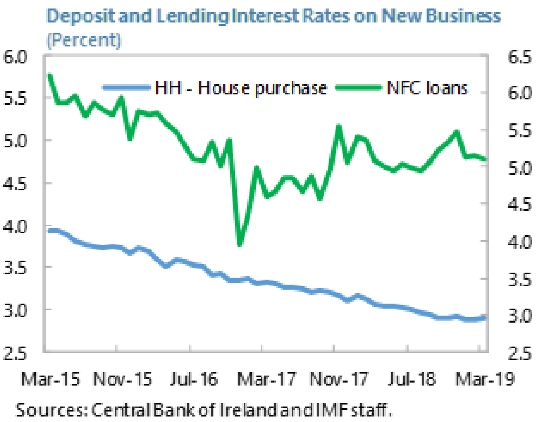
Source: Central Bank of Ireland.

Credit to large enterprises is picking up while SMEs continue to deleverage.



Source: Central Bank of Ireland.

Interest rates on business loans have risen.

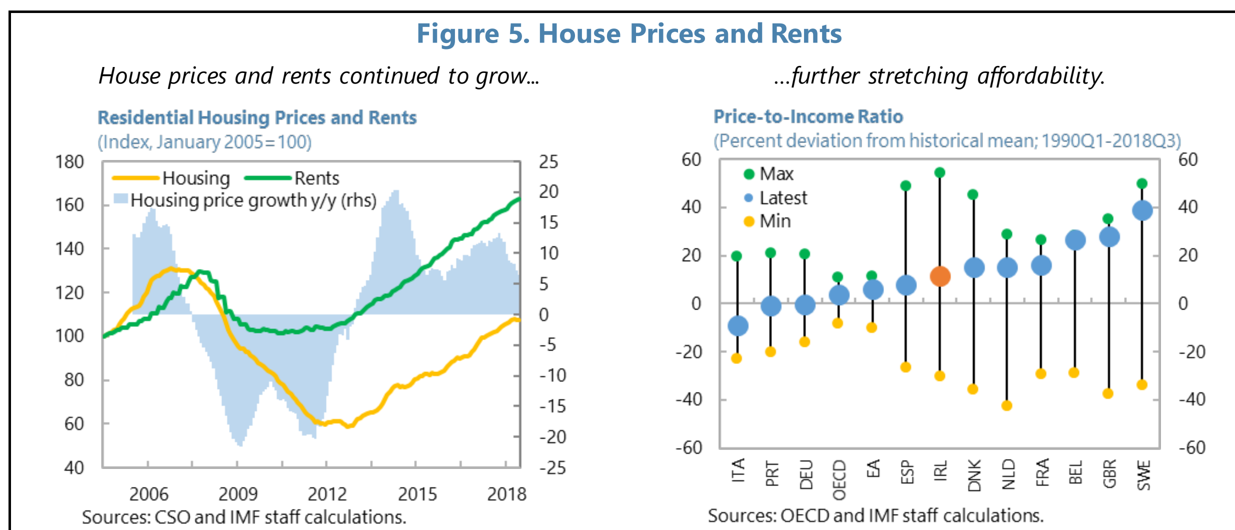


Sources: Central Bank of Ireland and IMF staff.

4. Household balance sheets strengthened, and credit has started to increase. Private sector credit grew by 1 percent last year, largely due to increasing net lending to households, notably mortgages. Net lending to large non-financial corporations increased, while SMEs continued to deleverage. On the back of rising incomes, the household debt-to-disposable income ratio declined further to 126 percent. Nonetheless, Irish households remain among the most indebted in the EU. Banks have accelerated the repair of their balance sheets, but profitability remains at risk. Interest rates on new loans to non-financial corporations remain relatively high, reflecting crisis legacies and limited competition in the banking sector. However, credit demand of SMEs is low, and cost of credit is not reported as a major obstacle to new investment.

5. Housing prices continued to grow, largely reflecting supply shortfalls, but at a slower pace. Residential property prices increased by 6 percent in 2018, well above household income growth, and are now at their highest level since 2009. The pace of house price growth, however, moderated from 12 percent in 2017, amid signs that the supply of housing has begun to respond to rising demand. Price-to-rent and price-to-income ratios are above long-term averages, but not excessively so, while econometric models suggest that housing prices are close to, or somewhat above, fundamental values. Forward-looking indicators point to a continued expansion in housing supply, which could mitigate price pressures in coming years. Rental prices, meanwhile, increased for the eighth consecutive year and stand well above pre-crisis levels, reflecting supply shortages.

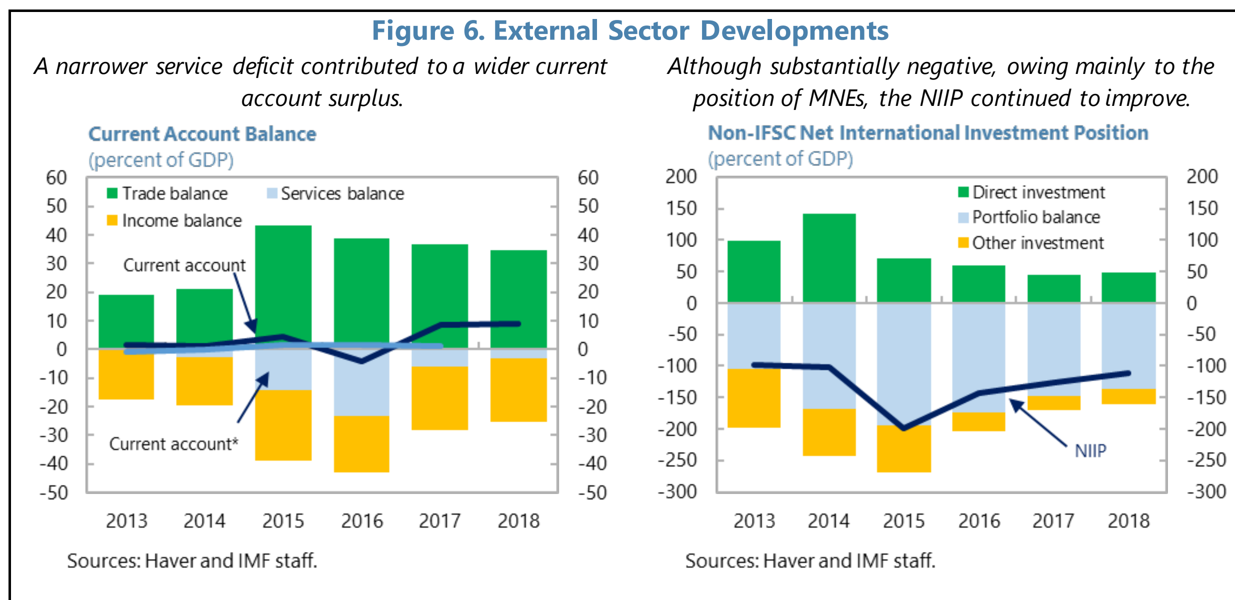
Figure 5. House Prices and Rents



6. Ireland's current account surplus is estimated to have widened moderately in 2018. Preliminary information indicates that the current account surplus increased from 8.5 percent of GDP in 2017 to 9.1 percent last year, mainly reflecting a smaller deficit in the services balance and boost in pharmaceutical exports. Ireland's current account balances in 2015–17 were revised significantly downward last year, after more information about the operations of multinational enterprises (MNEs) became available. Staff anticipates that the preliminary surplus recorded in 2018 will also be revised downward for similar reasons. Taking into account an estimated range of such an

adjustment, staff assesses Ireland's external position to be broadly consistent with medium-term fundamentals and desirable policy settings (Annex II). This assessment is subject to considerable uncertainty due to data volatility and the role of MNEs in affecting the headline current account balance. The real effective exchange rate appreciated modestly in 2018 and is deemed to be close to its equilibrium value. Ireland's net international investment position (NIIP), although substantially negative, continued to improve thanks to the growing foreign assets of the banking sector.

Figure 6. External Sector Developments



OUTLOOK AND RISKS

7. The outlook remains favorable. Based on the assumption of an orderly Brexit, growth is projected to slow to about 4 percent in 2019 as one-off factors driving MNEs' net exports dissipate, and to gradually converge over the medium term to its potential rate of close to 3 percent, thereby closing the positive output gap. Domestic demand is expected to be the main growth driver, while net exports, primarily through the multinational sector, will continue to contribute positively. Further employment growth will tap foreign labor inflows, reduce unemployment to about 5 percent, and support earnings and private consumption. With further wage increases, headline inflation is expected to reach 2 percent over the medium term. Exports and imports are assumed to grow in line with global trade patterns and domestic demand. Activities of multinationals are expected to boost their profitability further, thereby increasing income outflows and gradually reducing Ireland's current account surplus to 4.6 percent of GDP by 2024.

Macroeconomic Projections, 2017–24
(Percentage change, unless indicated otherwise)

	2017	2018	Projections 2019	2020	2021	2022	2023	2024
Real GDP	7.2	6.8	4.1	3.4	3.1	2.9	2.7	2.7
Final domestic demand	-12.2	5.5	3.8	3.4	3.0	2.9	2.7	2.7
Private consumption	1.9	3.0	2.5	2.5	2.4	2.4	2.3	2.3
Public consumption	3.9	6.4	3.0	1.7	2.5	2.9	2.1	2.3
Fixed investment	-30.2	7.8	5.9	5.2	4.1	3.5	3.5	3.5
Change in stocks (contribution to growth)	-1.1	-0.6	0.0	0.0	0.0	0.0	0.0	0.0
Net exports (contribution to growth)	18.9	4.4	1.5	1.1	1.0	0.9	0.8	0.8
Exports	7.7	8.9	4.6	4.4	4.3	4.2	4.1	4.1
Imports	-9.3	7.2	4.5	4.6	4.6	4.6	4.6	4.6
Current account (percent of GDP)	8.5	9.1	7.9	6.9	6.3	5.8	5.2	4.6
Unemployment rate (percent)	6.7	5.8	5.4	5.0	5.0	4.9	4.9	4.9
Output gap	0.7	1.5	1.3	1.1	0.7	0.5	0.2	0.0
Consumer prices (HICP)	0.3	0.7	1.2	1.5	1.7	1.9	2.0	2.0
Memorandum item:								
Real modified domestic demand	1.4	3.3	3.6	3.2	3.1	3.0	2.7	2.7
Real GNI* 1/	0.4	6.1	…	…	…	…	…	…

Note: 1/ Deflated with the deflator of modified domestic demand; 2018 is a projection.
Sources: CSO; Haver; and IMF staff projections.

8. However, the outlook is clouded by several risks:

- ***Boom-bust dynamic.*** The economy is operating near full capacity, with increasing signs of a tight labor market. With abundant CIT receipts, pressure on the minority government continues for tax cuts, wage hikes, and public investments. At this juncture, a further weakening of fiscal restraint could push the continued strong expansion towards a boom-bust dynamic.

- ***Brexit.*** Multifaceted linkages with the U.K. make Ireland uniquely vulnerable to Brexit. The form of Brexit will determine the size of the negative impact on Ireland. Annex III describes the likely impact of a no-deal Brexit. In this event, the government should allow automatic fiscal stabilizers to operate freely. In addition, staff would support targeted, temporary, and effective government assistance to help hard-hit industries adjust to the new circumstances. The government should also prepare to mount a broader fiscal stimulus and deploy the Rainy-Day Fund, depending on the severity of the downturn in the broader economy. Discretionary infrastructure investment projects ought to be well-prepared, in line with PIMA recommendations. The Central Bank of Ireland (CBI) should release the countercyclical capital buffer in the event of a sharp contraction in bank credit. Staff would not recommend adjusting macroprudential policies geared toward limiting excessive leverage in the housing market.

- ***International corporate tax reforms.*** While the effects of the recent U.S. CIT reform have been limited so far, significant changes in tax planning strategies of U.S. MNEs, which play an important role in the Irish economy and contribute significantly to CIT revenue, would reduce investment and tax revenues. In addition, full implementation of the G-20/OECD Base Erosion

and Profit Shifting (BEPS) initiative, including the EU Anti-Tax Avoidance Directives (ATAD), and unilateral introduction of digital taxes in more EU member countries may somewhat reduce corporate profits taxed in Ireland. Mitigation policies would include tax-base broadening in a growth-friendly manner.

- ***Escalation in protectionism***. Given its deep integration into global value chains and its highly concentrated industrial base, the Irish economy would be significantly hit by spillovers from escalated trade tensions (IMF, forthcoming 2019). In response to such tensions, the government should participate in a coordinated policy response at the European and global level; let automatic stabilizers operate freely; improve SME access to financing and ease impediments to productivity growth; and smooth out debt issuance by using cash buffers.

Authorities' Views

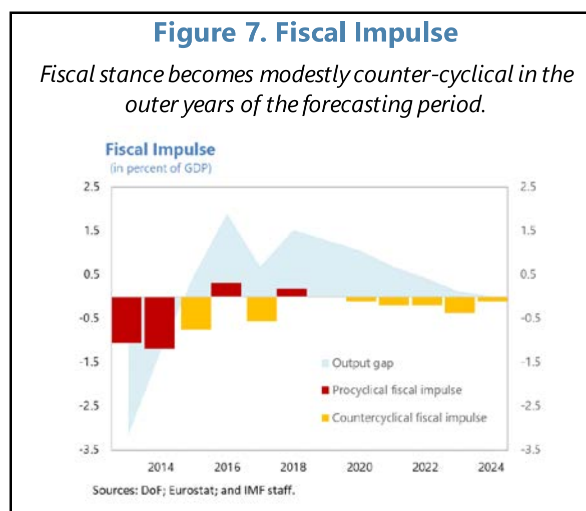
9. The authorities broadly agreed with staff's outlook and risk assessment. Like staff, they expect robust but moderating growth, driven by solid domestic demand and multinationals-led net exports, gravitating towards its potential rate over the medium term. Given the advanced cyclical position and pressing uncertainties around Brexit, the authorities acknowledged the need to build buffers, while continuing to prepare for disruptive effects of Brexit. In the event of a no-deal Brexit contingency, they considered that carefully targeted, temporary fiscal and other support would be warranted to protect jobs and assist businesses to develop viable medium-term adjustment plans. They are already working with SMEs on trade diversification and preparations for customs declarations. However, it would be difficult to ramp up capital expenditures, given capacity constraints. The authorities also acknowledged risks to growth and fiscal revenues from uncertainties around international trade and international corporate tax changes. To strengthen the capacity to respond to adverse shocks, they are establishing the Rainy-Day Fund this year.

FISCAL: ENSURING RESILIENCE

10. The government's budget position is solid, but underlying consolidation efforts remain on hold. Budget 2019 targets maintaining overall balance. Budgeted spending increases, including for wages and capital allocations, and some further reductions in personal income taxes, would be broadly offset by growing, but potentially uncertain CIT revenues and the VAT increase for the hospitality sector from 9 to 13.5 percent. The Medium-Term Objective for a structural deficit of 0.5 percent of GDP is expected to be achieved this year, while the government plans a structural surplus of 0.2 percent of GDP in

Figure 7. Fiscal Impulse

Fiscal stance becomes modestly counter-cyclical in the outer years of the forecasting period.



Sources: DoF; Eurostat; and IMF staff.

2021, after addressing major infrastructure needs (see Capital Plan). Budget 2019 also includes a €500 million annual contribution to the Rainy-Day Fund (RDF).[1] The government targets reducing public debt from currently almost 65 percent of GDP (105 percent of GNI*) to 45 percent (70 percent), by the next decade. It has committed to use any proceeds from disinvestments in the financial sector for debt reduction.

Fiscal Projections Comparison
(Percent of GDP)

			Projections 1/					
	2017	2018	2019	2020	2021	2022	2023	2024
Staff								
Growth	7.2	6.8	4.1	3.4	3.1	2.9	2.7	2.7
Output gap	0.7	1.5	1.3	1.1	0.7	0.5	0.2	0.0
Overall balance	-0.3	0.0	0.0	0.2	0.3	0.5	0.7	0.7
Structural balance 2/	-0.4	-0.5	-0.4	-0.2	0.1	0.3	0.6	0.7
Structural effort (pp)	1.0	0.0	0.0	0.3	0.3	0.2	0.3	0.1
Public debt 3/	68.6	64.8	62.3	58.8	57.0	54.0	51.1	48.0
Department of Finance								
Growth	7.2	7.5	4.2	3.6	2.5	2.6	2.7	...
Output gap	-1.0	1.6	1.3	0.6	0.4	0.2	0.0	...
Overall balance	-0.2	-0.1	0.0	0.3	0.4	1.1	1.4	...
Structural balance 2/	0.4	-1.0	-0.7	0.0	0.2	1.0	1.4	...
Structural effort (pp)	...	-1.4	0.3	0.7	0.2	0.8	0.4	...
Public debt 3/	68.4	64.0	61.4	56.5	55.3	53.1	51.1	...

Sources: Budget 2019; and IMF staff.
1/ Based on current policies.
2/ In percent of potential GDP.
3/ Taking into account the accumulation of the Rainy-Day Fund of €0.5 billion starting in 2019.

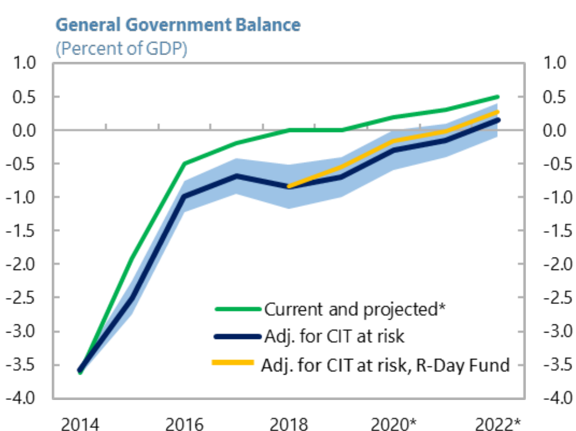
11. Under current policies, staff estimates the fiscal stance to be broadly neutral during 2019–20. Consolidation is expected to resume in the outer years of the forecast with the structural balance reaching a surplus of 0.7 percent of GDP by 2024. Staff's fiscal projections are somewhat less optimistic than those of the authorities, due to more conservative tax buoyancy and expenditure assumptions.

[1] The Strategic Investment Fund will contribute €1.5 billion to the RDF.

12. However, vulnerabilities are building mainly through increasing dependency on potentially fragile CIT revenue. CIT revenue now accounts for nearly a fifth of total tax revenues, up from 7 percent in 2014. Budget 2019 would show a deficit of 0.5 percent of GDP when adjusted for a part of CIT revenues that are estimated at risk (Box 1).[2] While only a small fraction of the additional CIT revenue is saved in the RDF, much of it has been allocated to permanent measures, such as funding healthcare budgetary over-runs and reducing the income tax and the Universal Social Charge (USC). Following repeated reductions in the USC, it now practically duplicates the income tax, with additional administrative costs and little tax broadening.[3] The share of healthcare in the budget has increased to 25 percent – the highest in the EU and 10 percent above the EU average.

Figure 8. Medium-Term Fiscal Consolidation Relies on CIT Revenues at Risk

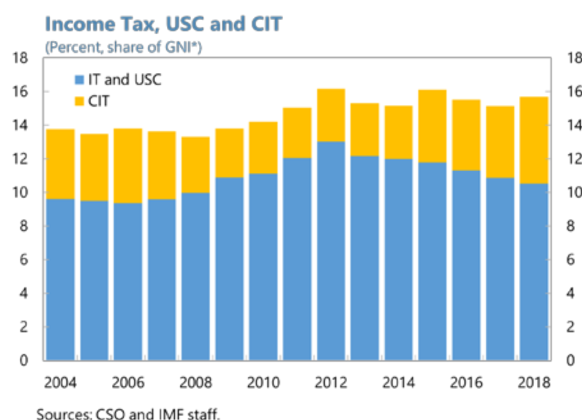
Fiscal consolidation efforts have weakened recently amid abundant unexpected CIT revenues.



Sources: Haver and IMF staff.

Figure 9. Income Taxes

CIT revenue has been also used to reduce personal income taxes.



Sources: CSO and IMF staff.

[2] See also "The Impact of International Tax Reforms on Ireland", *Selected Issues Paper*, Chapter II, International Monetary Fund, 2018.

[3] See "Personal Income Tax Reform: Past and Present", Selected Issues Paper, Chapter I., International Monetary Fund, 2019.

Box 1. CIT Revenue at Risk

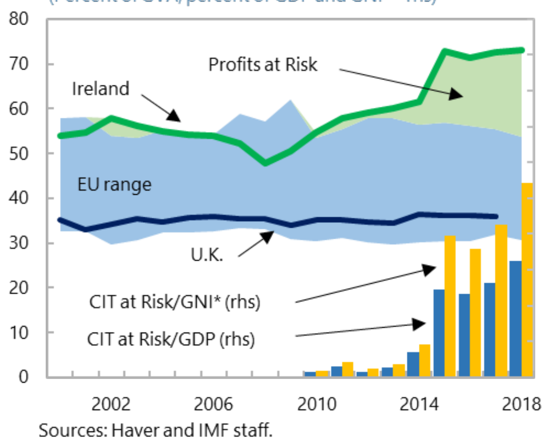
Ireland's CIT revenue has outpaced expectations for several years. While some increase in profits and taxes was brought by the recovering economy, a sizable part is attributable to the activities of MNEs and is inherently fragile due to high concentration and weak links to the domestic economy (contract manufacturing in particular). Two ways have been used to estimate a rough range of MNE profits and taxes at risk:

- *The relative share of gross profits in gross value added (GVA) of the non-financial sector (NFS)*, compared to peers. CIT revenue at risk is calculated by applying the effective CIT rate to the extra profits, derived as the difference between Ireland's share of gross profits in GVA of the NFS and the highest gross profits/GVA ratio of EU peers. This measure represents a lower bound since it does not include the financial sector and uses the highest ratio of EU peers.

- *The imputed underlying gross profits* (including the financial sector) based on their past growth. CIT revenue at risk is estimated by applying the effective CIT rate to the difference between actual and imputed profits. The imputed profits for 2015–18 are projected using the 2014 growth rate of profits, which is the year prior to the substantial structural changes stemming from MNE balance sheet restructuring, contract manufacturing, and IP investments.

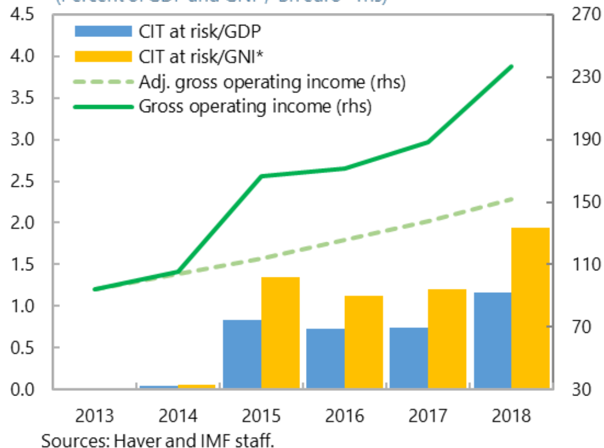
The resulting CIT revenue at risk ranged from 0.6 to 1 percent of GDP, or 1.1 to 1.8 percent of GNI* in 2018.

Profitability has increased to unprecedented levels…



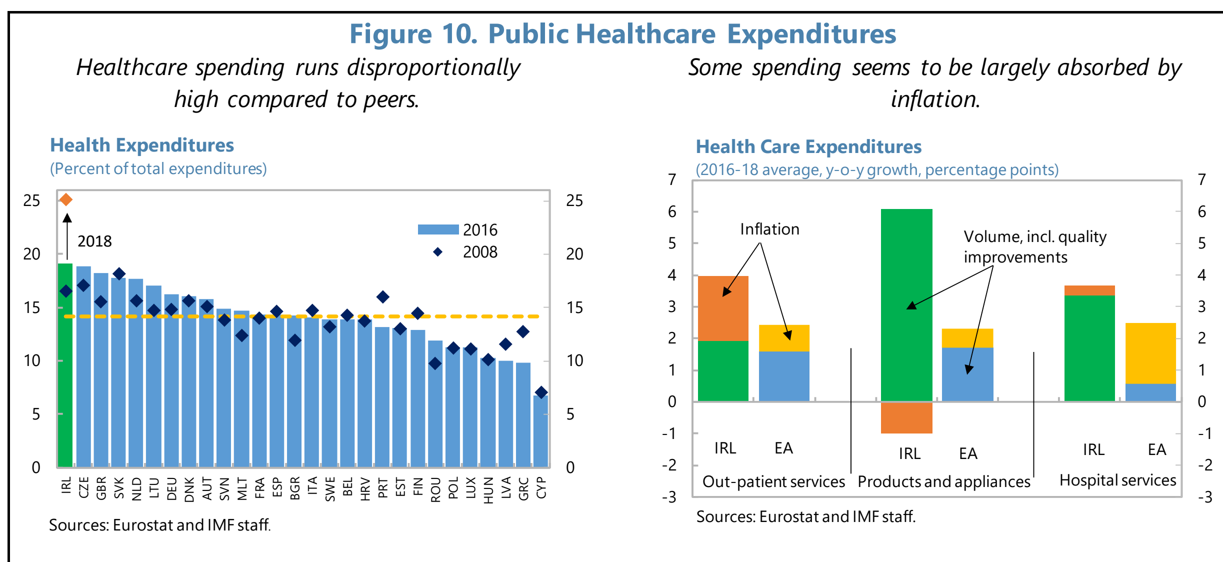
Sources: Haver and IMF staff.

… implying significant CIT revenue at risk.

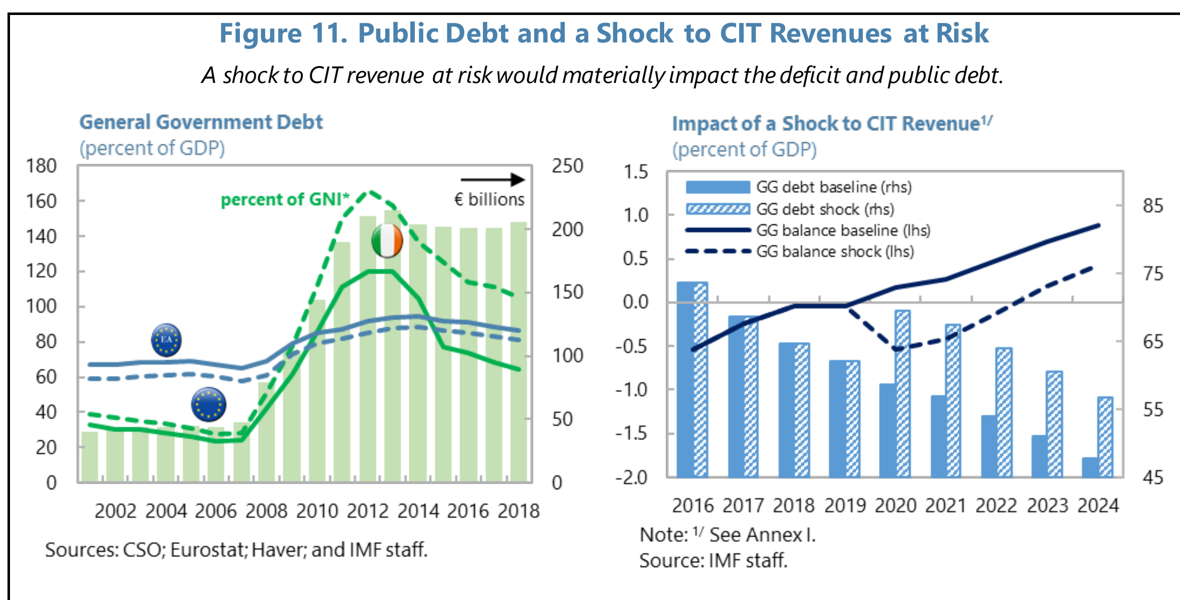


Sources: Haver and IMF staff.

Sources: Haver; DoF; and IMF staff.



13. The still high public debt represents a vulnerability to adverse shocks. Specifically, were part of the CIT revenue at risk to dry up, this could meaningfully increase the public debt, from already elevated levels, with possible adverse implications for government's borrowing and debt refinancing (Annex I).



14. Considering vulnerabilities and the advanced cyclical position of the economy, fiscal policy should resume consolidation efforts to rebuild buffers. Although Ireland has some fiscal space thanks to pre-financing, moderate gross financing needs, and long debt maturities, further consolidation is needed. This would reduce vulnerability to shocks by limiting the dependency on CIT revenue and allowing a faster debt reduction (or increasing savings in the RDF). The government should aim at an overall surplus of 0.2 percent of GDP in 2019, which could be achieved by strictly adhering to budgeted expenditures, a small structural effort, and saving any additional unforeseen CIT revenues (either in the RDF or to reduce public debt). In 2020, the government should target a

surplus of 0.5 percent of GDP. Over the medium term, the budget strategy should be consistent with reducing the public debt ratio to below 50 percent of GDP. This could be achieved by realigning moderate structural expenditure growth with broad and stable revenue raising measures:

- ***VAT preferential rates and exemptions could be further streamlined.*** The increase in the VAT rate for the hospitality sector in Budget 2019 is a welcome step, but there is scope to further streamline Ireland's five-rate VAT system. According to the authorities, narrowing the VAT rate structure could yield between 0.2–0.8 percent of GDP. Income distribution concerns could be mitigated by means-tested allowances for low-income households.

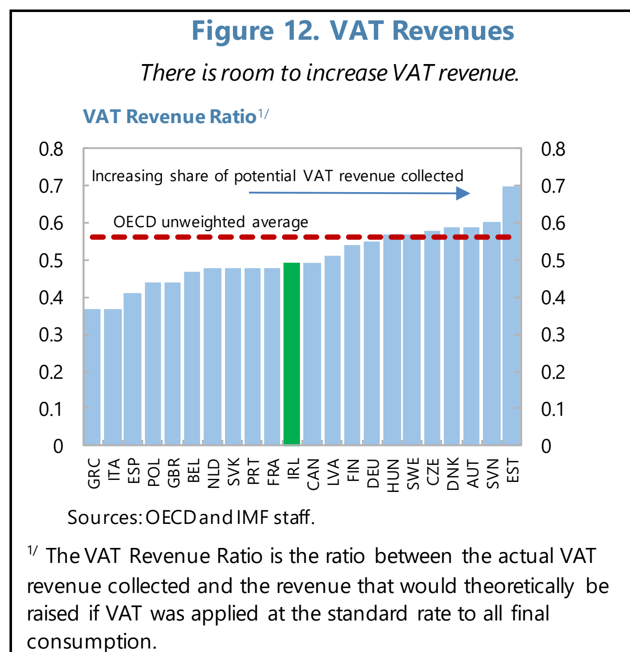


Figure 12. VAT Revenues

There is room to increase VAT revenue.

Sources: OECD and IMF staff.

1/ The VAT Revenue Ratio is the ratio between the actual VAT revenue collected and the revenue that would theoretically be raised if VAT was applied at the standard rate to all final consumption.

- ***The USC could be replaced by a reformed income tax.*** In the current setting, the USC largely duplicates the Income Tax (IT) but adds administrative costs. The USC could be discontinued, while its yield could be achieved through a reformed IT with somewhat higher rates, broader base, and more tax bands to reduce disincentives to work, while preserving the current income redistribution.

- ***The implementation of the local property tax*** could be improved by adhering to the three-year valuation assessment frequency and capping the rate of annual tax base increases to smooth tax payments, while preserving the tax rate.

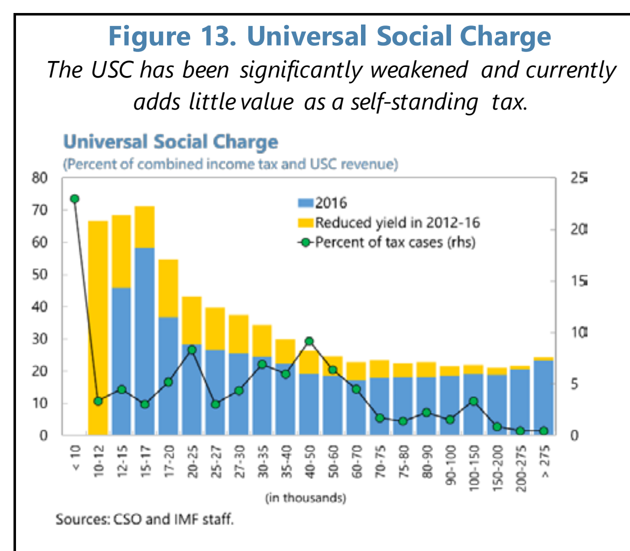


Figure 13. Universal Social Charge

The USC has been significantly weakened and currently adds little value as a self-standing tax.

Sources: CSO and IMF staff.

15. Expenditure growth should be moderated, and spending efficiency improved. While several spending reviews have been helpful in re-allocating resources within current expenditures, deeper analyses in specific areas, such as healthcare, are needed to avoid soft budget constraints. The introduction of the Investment Projects and Programmes Tracker is welcome as it enhances transparency and monitoring of expenditures under the significantly enlarged capital budget (see National Development Plan 2018–2027), but further improvements in planning, selecting, costing (including PPPs), and ex-post assessing of projects are needed to close Ireland's efficiency gap (IMF PIMA).

16. Ireland should continue its proactive approach to engage on and implement the international corporate tax reform agenda. Ireland has been compliant in implementing the G20/OCED BEPS actions and other international standards in tax transparency and exchange of information. The government is committed to continue implementing agreed reforms, as set out in Ireland's Corporation Tax Roadmap, including the EU Anti-Tax Avoidance Directives (ATADs). Ireland should also engage in ongoing multilateral efforts to address digitalization and tax avoidance. The impact on the economy of such measures would be mitigated by the country's various other competitive advantages, such as its welcoming business environment and qualified labor force.

17. The long-term financial soundness of the Social Insurance Fund (SIF) needs to be strengthened to avoid future shortfalls. Population aging is expected to increase pensions and other social expenditures in the coming years. According to projections by KPMG, the SIF faces significant deficits starting in 2030 of about 1 percent of GDP, increasing to 3 percent by 2055. Measures should be developed, including a review of social security contributions and benefits, to safeguard the SIF's long-run viability. The planned increases in the state pension age are steps in the right direction.

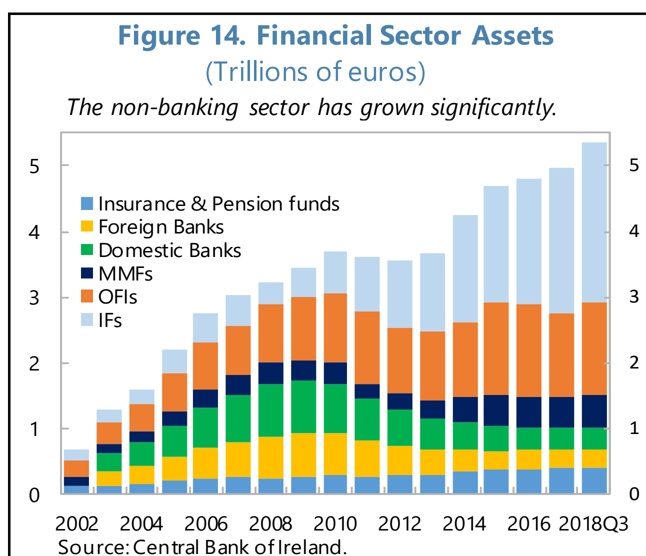
18. Ireland should step up policy efforts to achieve its climate targets. Ireland is the only EU country with rising greenhouse gas emissions, on average by 2 percent per year during 2015-17, bringing it further away from its Paris Climate Agreement commitments. Partial measures are in place, including electric car incentives and a surcharge for diesel passenger car registrations. A comprehensive and appropriately ambitious strategy should be developed and implemented to transform the carbon-based economic model, particularly through decarbonizing agriculture, housing, and transport, and phasing out peat and coal heating. Such a strategy should include increasing the carbon tax.

Authorities' Views

19. The government affirmed its commitment to further strengthening public finances. The authorities noted intensifying spending pressures related to the election cycle, challenges in public investment, and risks of repeated healthcare spending overruns. They agreed with staff that fiscal policy should focus on building buffers to enlarge the fiscal space needed to withstand potential adverse shocks. In this context, the government intends to save additional CIT revenue, enhance spending controls and increase the efficiency of public investment. It acknowledged the need to review the current VAT and income taxation frameworks and was preparing the ground for updating property taxation by next year. The government also reaffirmed its commitment to use future proceeds from disinvestments in the banking sector and National Asset Management Agency profits to reduce public debt. The government emphasized its continued constructive engagement with the international corporate tax reform agenda. It recognized the need to strengthen the long-term financial soundness of the SIF and is pursuing a review of social contributions to that end. The government is also working on an upgraded comprehensive climate strategy, aimed at fulfilling Ireland's 2030 carbon emission targets. The authorities noted that Ireland is making significant progress on renewable energy.

FINANCIAL SECTOR: STAYING SAFE AND SOUND

20. The size of Ireland's financial sector has surpassed its pre-crisis level as bank deleveraging was more than offset by the expansion of the non-bank sector. Total financial sector assets in 2018:Q3 were 1.6 times higher than in 2009. While domestic and foreign banks' balance sheets have shrunk by 60 percent, investment funds (IFs) assets grew fivefold, reaching €2.4 trillion. Money market funds (MMFs) and Other financial intermediaries (OFIs) grew by 58 and 43 percent, respectively. IFs, MMFs, and OFIs account for 80 percent of total financial sector assets.



21. Domestic banks are well capitalized and liquid. Their capital ratios have somewhat declined in 2018 but remain among the highest in Europe. The common equity Tier 1 ratio for the three largest domestic banks, at 17.8 percent, is well above regulatory requirements and EU peer average. Irish banks also fared well in the EU-wide banking stress tests published in November 2018. Under a severe adverse shock their capital ratios would remain above the regulatory minimum despite being among the most affected, second after U.K. banks.[4] A comparison of the stress scenario assumptions[5] to the no-deal Brexit scenario as modelled by the CBI, suggests that banks would be resilient in case of a disorderly Brexit. The Irish banking system's liquidity coverage ratio continues to be in line with international peers, and well above minimum requirements.

Irish Banks: Key Financial Indicators of Selected Banks[1/]

(Percent)

	2013	2014	2015	2016	2017	2018
Credit growth	-7.0	-5.4	-5.3	-9.4	-3.9	-3.4
to Irish residents	-9.2	-3.6	-1.1	-7.5	-2.1	1.2
Return on assets	-0.8	0.5	0.7	0.8	0.8	0.8
Pre-provision profits 2/	0.4	0.4	0.7	0.8	0.8	0.7
Net interest margin	1.2	1.3	1.8	2.0	2.2	2.1
Cost-to-income ratio	72.8	64.1	63.2	60.2	68.1	70.8
NPL ratio	27.1	23.2	16.1	12.9	10.7	8.1
Coverage ratio	51.4	51.7	51.6	50.3	45.6	37.7
CT1 ratio	13.3	15.5	14.9	16.8	18.4	17.8
Net loan to deposit	110.7	108.2	105.9	102.4	94.9	93.8

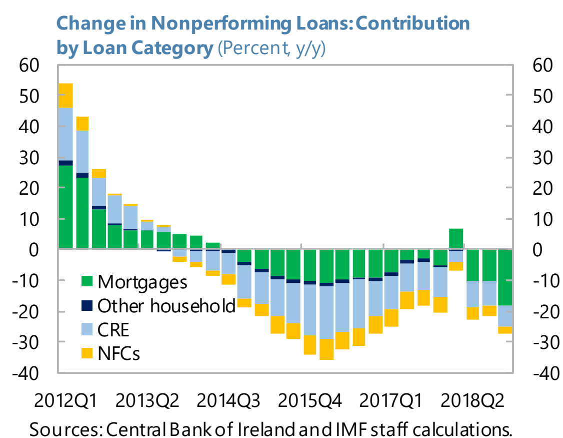
Sources: CBI and IMF staff.
1/ Indicators cover the three main domestic banks: Allied Irish Banks, Bank of Ireland, and Permanent TSB. Figures are based on Q4 data, unless otherwise
2/ Excluding nonrecurrent items, as a share of average total assets.

[4] The fully loaded Common Equity Tier 1 ratio for the two largest banks under the adverse scenario was projected at 10.5 percent in 2020, above the EU average of 10 percent.

[5] The adverse macroeconomic scenario for Ireland assumed worse than the EU-average GDP and unemployment shocks, but a milder property price shock.

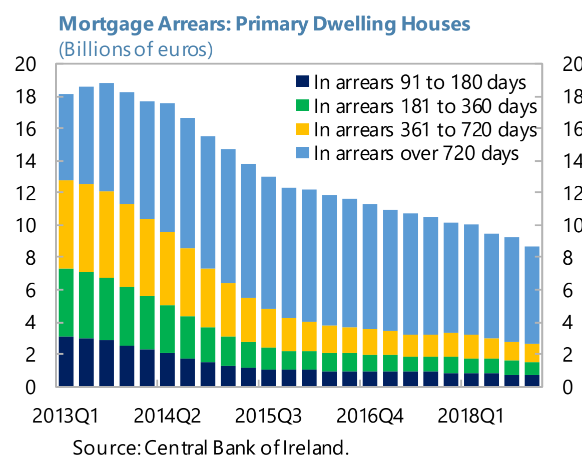
Figure 15. Banking Developments

Non-performing loans have declined across all segments....



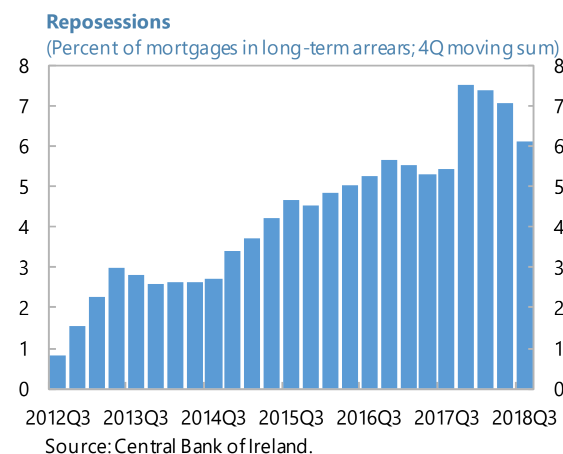
Sources: Central Bank of Ireland and IMF staff calculations.

...but the absolute level remains high and the share of mortgages with long-term arrears is increasing.



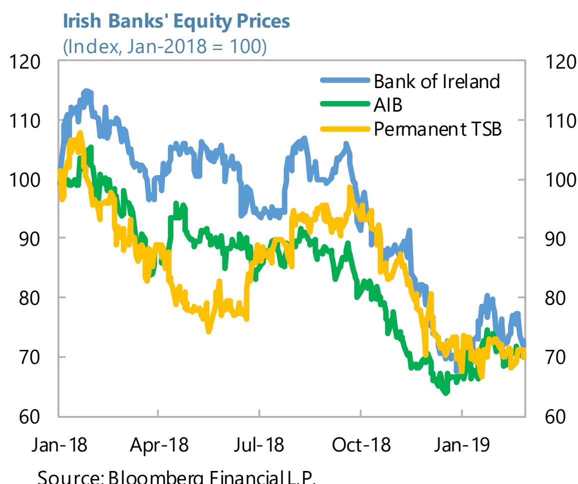
Source: Central Bank of Ireland.

The repossession rate has declined in recent quarters.



Source: Central Bank of Ireland.

Adverse global developments, Brexit risks, and weak profits have negatively affected banks' market valuation.



Source: Bloomberg Financial L.P.

22. **However, the high stock of non-performing loans and other crisis legacies continue to weigh on banks' profitability.** Domestic banks' profits have declined last year on lower interest rate margins. Moreover, average margins of Irish banks continue to be weighed down by the high level of nonperforming loans (NPL), a sizable portfolio of low-rate tracker mortgages, regulatory requirements to build up loss-absorbing liabilities, and elevated operational costs.[6] Bank loan portfolios remain heavily concentrated in property-related lending (above 70 percent of total loans) and the potential for market growth appears limited. In addition to continuing their balance sheet

[6] The examination of cases where banks mishandled tracker mortgages by unduly denying borrowers tracker products or charging them wrong rates is expected to be completed in the first half of 2019. At end February 2019, total compensation amounted to €0.67 billion covering 40 thousand customers.

repair, banks should step up efforts to improve cost efficiency, upgrade IT systems, and diversify their lending.

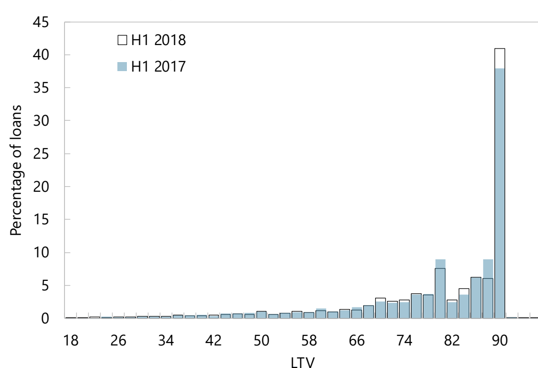
23. Efforts to improve banks' asset quality need to continue, building on recent progress. The NPL ratio for the three largest domestic banks declined to 8.1 percent in 2018 from 10.7 percent at end-2017, helped by portfolio sales, improved economic conditions, and stepped-up resolution activities. Non-performing loans have declined across all market segments with the largest absolute decline in mortgages on primary residences. However, the share of mortgages with long-term arrears remains high and the repossession rate is low by international standards. Provisioning for impaired loans decreased and is well below the EU average. Continued loan-restructuring efforts, accompanied by strengthened borrower-creditor engagement, accelerated legal proceedings, and enhanced supervisory efforts are needed to reduce the NPL ratio to the 5 percent target by 2020.

24. Macroprudential policy settings appear appropriate, but the toolkit should be expanded. Last November's review of mortgages kept the prudential settings unchanged, with the current LTVs and LTIs limits, aimed at preventing excessive household leverage, becoming more binding. Given that there are no signs of deterioration in lending standards, the current macroprudential stance appears appropriate. In view of the subdued credit growth, immediate financial stability risks are limited. Going forward, staff encourages the authorities to introduce debt-based measures (DTI and DSTI), that better capture household repayment capacity. The countercyclical capital buffer increase to 1 percent, announced last year, will come into effect in July and constitutes an appropriate policy buffer in view of the advanced business cycle and risks to the outlook. Given Ireland's openness and proneness to volatility and external shocks, expanding the toolkit with a systemic risk capital buffer is important to bolster system resilience.

Figure 16. Macroprudential Measures Effect

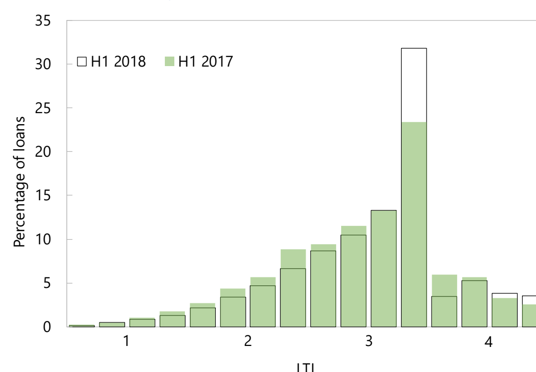
LTV limit of 90 percent becomes more binding for first time buyers in 2018.

First Time Buyers LTV 2017 vs 2018



Share of FTB with LTI at the limit of 3.5 increased significantly.

First Time Buyers LTI 2017 vs 2018

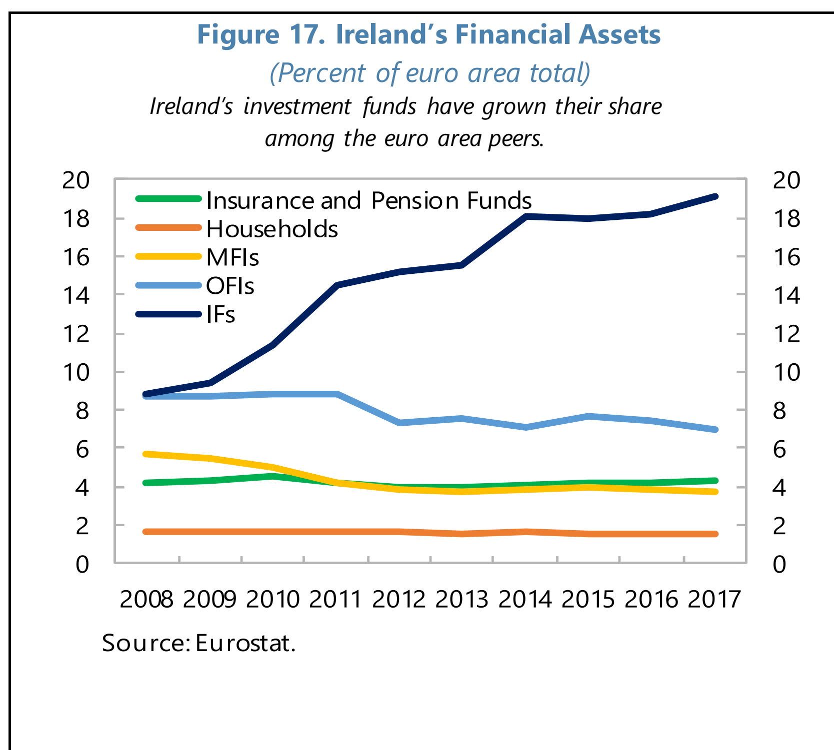


Source: CBI.

25. The non-bank financial sector is large and growing fast. Total assets of IFs and OFIs amounted to €3.9 trillion in 2018:Q3 (12 times annual GDP), up from €1.4 trillion at end-2009. Growing non-bank financial intermediation is an EU-wide and global phenomenon, with growing interconnectedness of banks and non-bank financial intermediaries, including close ownership links. Since the crisis, Irish investment funds have doubled their share in the euro area's investment funds sector to almost 20 percent. In comparison, the share of Irish households' financial assets remained flat at 1.6 percent of euro area household assets. This points towards strong financial linkages between the Irish funds' industry and the rest of the world.

Figure 17. Ireland's Financial Assets

(Percent of euro area total)



Source: Eurostat.

26. Most exposures of the investment funds and OFI sector are to non-residents, but domestic links are non-trivial and growing. Flow of funds data confirm that most of Irish funds' and OFIs' exposures are to foreign investors. However, links with some domestic sectors are also significant. Insurance companies and pension funds have invested 9 and 8 percent of their respective assets in funds and vehicles. Non-financial corporations hold about 4 percent of their assets in OFIs, while domestic banks invested about 14 percent of their assets into IFs and OFIs and receive 11 percent of their funding from the industry. OFIs hold more than a quarter of households' liabilities (e.g., securitized mortgages and NPL portfolios).[7] Therefore, a large shock to the non-bank financial sector could have a non-trivial adverse impact on the Irish economy. Additionally, Ireland can become a conduit of global financial shocks and ultimately won't be immune from it either.

[7] This largely reflects the creation of securitization SPEs by banks.

Irish Financial Accounts: Whom-to-Whom Table

(Percent of GDP, 2018 Q3)

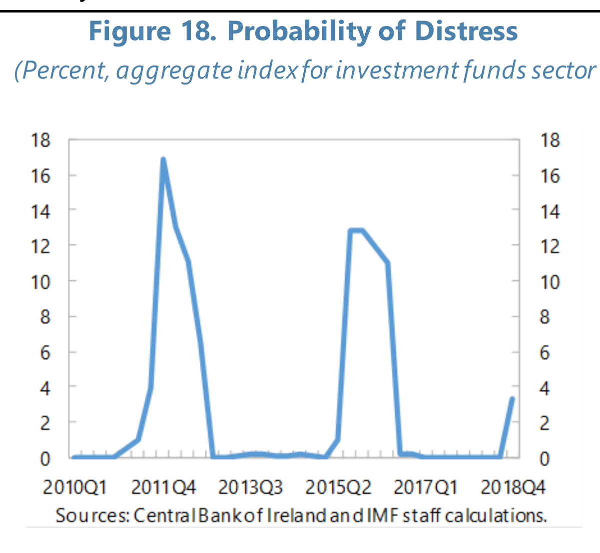
Unit: Per cent of GDP		Liabilities												
		CBI	DMFIs	FMFIs	MMFs	NMIFs	OFIs	ICs	PFs	GOV	NFCs	HHs	ROW	Total
Assets	CBI	-	1	0	-	-	1	-	-	16	-	-	14	32
	DMFIs	3	17	3	1	1	13	0	0	3	12	29	22	103
	FMFIs	4	-	1	-	0	1	0	0	-	1	1	59	68
	MMFs	-	-	0	0	0	1	-	-	-	0	-	154	155
	NMIFs	-	3	2	7	38	24	0	-	0	4	0	690	768
	OFIs	-	9	1	-	12	33	2	-	3	25	13	322	418
	ICs	-	1	0	0	4	4	1	0	1	2	1	78	91
	PFs	-	1	0	0	1	3	-	-	0	3	-	33	40
	GOV	11	1	1	0	0	4	0	-	3	5	1	7	34
	NFCs	1	15	1	1	3	15	1	-	2	84	1	399	523
	HHs	-	31	4	0.1	0.3	0.4	18	40	11	6	-	6	117
	ROW	6	27	43	146	704	314	73	-	49	547	1	1	1,911
	Total	26	106	57	155	764	411	95	40	87	688	47	1,784	4,262

CBI – Central Bank of Ireland; DMFIs – Domestic Monetary Financial Institutions; FMFIs – Foreign Monetary Financial Institutions; MMFs – Money Market Funds; NMIF – Non-Money market Investment Funds; OFIs – Other Financial Institutions; IC – Insurance Companies; PFs – Pension Funds; GOV – Government; NFCs – Non-financial Corporates; HHs – Households; ROW – Rest of the World.

27. **The overall financial stress level in the investment funds sector remains low, but vulnerabilities are emerging.**[8] The aggregate probability of distress index[9] shows that the financial stress level in the Irish funds industry is significantly lower than it was during the European sovereign debt crisis or the normalization of U.S. monetary policy in 2016. There was a moderate increase in 2018:Q4, largely reflecting the pullback in global equity markets. At the same time, liquidity transformation has increased somewhat across all fund types, especially in real estate and bond funds. Bond funds and real estate funds have also increased maturity transformation (e.g., for bond funds only 11 percent of their short-term liabilities are covered by short-term assets). Bond funds account for 30 percent of total funds' assets. Real estate funds are small but growing fast, have strong links to the domestic economy, and are highly leveraged.

Figure 18. Probability of Distress

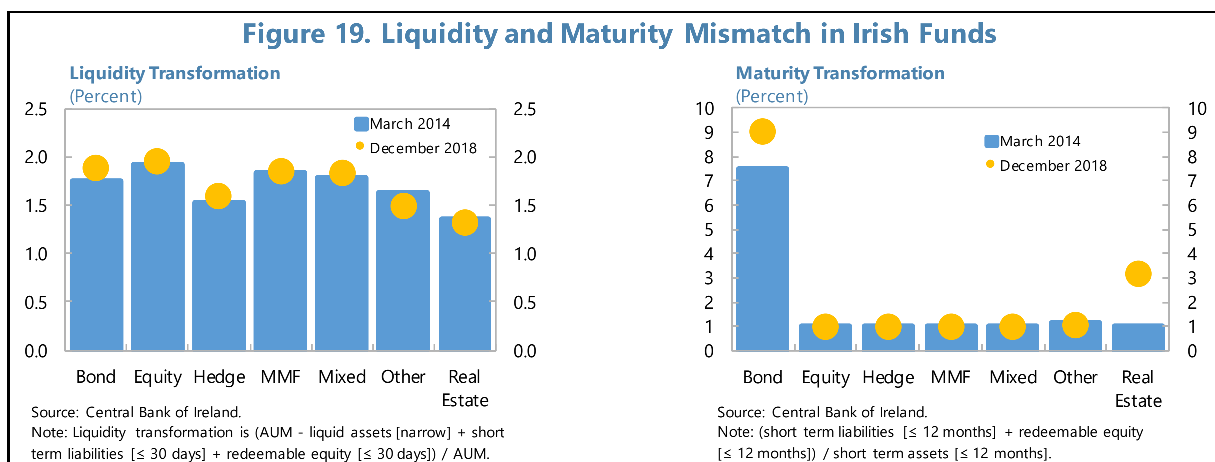
(Percent, aggregate index for investment funds sector



Sources: Central Bank of Ireland and IMF staff calculations.

[8] See "Non-bank Financial Sector in Ireland: Linkages and Risks", Selected Issues Paper, Chapter II., International Monetary Fund, 2019.

[9] Estimated following the methodology described in "A Comprehensive Multi-Sector Tool for Analysis of Systemic Risk and Interconnected".



28. The authorities should further improve data collection, closely monitor risk build-up, initiate system-wide stress-testing, and continue intensive international cooperation. The CBI and the Central Statistics Office (CSO) have continued to develop deeper insights into the funds and vehicles sector and expanded data collection[10]. Going forward, the authorities should enhance surveillance of the sector, including by closely monitoring liquidity and maturity mismatches and excessive leverage; provide guidance to the industry on liquidity stress-testing and the use of liquidity management tools; build the capacity that would allow for system-wide stress testing; and contribute to the development of standardized cross-border data-sharing arrangements through international fora.

29. Financial sector preparations for Brexit appear broadly adequate to mitigate major disruptions. The CBI continues to closely monitor Brexit contingency planning of Irish financial firms. According to the latest report by the Task Force on Brexit, the majority of Irish banks, insurers and brokers provided their assessment and contingency plans, which the CBI deemed to be adequate in most cases. The CBI cooperates closely with the EU and U.K. institutions to ensure business continuity and avoid cliff-edge risks in the financial sector.[11] Given continued uncertainty, it is essential that banks and other financial institutions remain conservative in their internal stress tests and risk assessments. It is also important to analyse the potential impact of Brexit-related financial market shocks, including on the nonbank financial sector. More than one hundred U.K.-based firms have been seeking authorization from the CBI to relocate some of their activities to Ireland to continue business in the EU after Brexit.[12] Staff encourages the CBI to continue to devote adequate resources to guarantee a high-quality authorization process.

30. The authorities should continue to strengthen Ireland's AML/CFT regime and ensure the integrity of its globally interconnected economy. Since the last FATF assessment, legislative steps aimed at transposing the 4th Anti-Money Laundering Directive have been taken, including to

[10] E.g., "New Data Collection on Special Purpose Vehicles in Ireland: Initial Findings and Measuring Shadow Banking"; "Shining a light on special purpose entities in Ireland"; and "Liquidity Analysis of Bond Funds and MMFs".

[11] Recent measures include agreement on central clearing of derivatives, central depository services, and OTC derivative contract renovation.

[12] Thus far, Dublin is the main destination of Brexit-related relocations followed by Frankfurt and Luxembourg.

establish the legal basis for a central registry of beneficial ownerships and enhance due diligence requirements for politically exposed persons. The authorities should continue their AML/CFT efforts, notably with respect to the effective implementation of existing requirements relating to customer due diligence; politically exposed persons; transparency of beneficial ownership; and suspicious transaction reporting by banks, the real estate sector, lawyers, and trust and company service providers. In view of the rapidly growing financial sector and Brexit-related relocations, it is crucial to have an appropriate framework in place to mitigate any new risks.

Authorities' Views

31. Notwithstanding recent progress, the authorities emphasized the need to further strengthen financial sector resilience. They noted the progress in banks' balance sheet repair and the successful issuance of MREL. The authorities agreed that progress needs to be maintained in NPL reduction. They expect banks to use the full toolkit to reduce NPLs, including restructuring and sale of loan portfolios, while ensuring full compliance with statutory consumer protections. Going forward, they acknowledged the need to continue strengthening banks' business models. They viewed the current macroprudential policy settings as vital to limit financial stability risks, including in the housing market, and will consider enhancing the CBI's macroprudential toolkit by completing the capital buffer framework with and a systemic risk buffer. The national authorities emphasized their commitment to improving data collection and deepening understanding of the stability risks in the large and growing non-bank financial sector, including through expanding stress testing. On Brexit contingency planning, the authorities emphasized their continued and intense engagement while assessing financial sector preparations as already broadly adequate to mitigate major disruptions. The national authorities also emphasized their determination to maintain an appropriate anti-money laundering framework to mitigate any new risks that may arise.

ADDRESSING KEY BOTTLENECKS TO GROWTH

32. To support high sustainable growth and enhance resilience to shocks, continuous efforts are needed to address Ireland's three main structural gaps:

- ***Housing gap.*** Structural measures aimed at expanding housing supply are essential to ease price pressures in Ireland's dynamic economy with a growing population (Box 2). It is important to ensure proper zoning and planning to support building houses in areas where demand is strong, and to streamline administrative requirements. Measures to improve the access to financing of distressed but viable construction firms could also help. In addition, it is important to ensure that tax measures to counter land hoarding in urban growth areas are effective. Measures to improve housing affordability need to be targeted to low-income households and the homeless to avoid exacerbating housing price pressures.

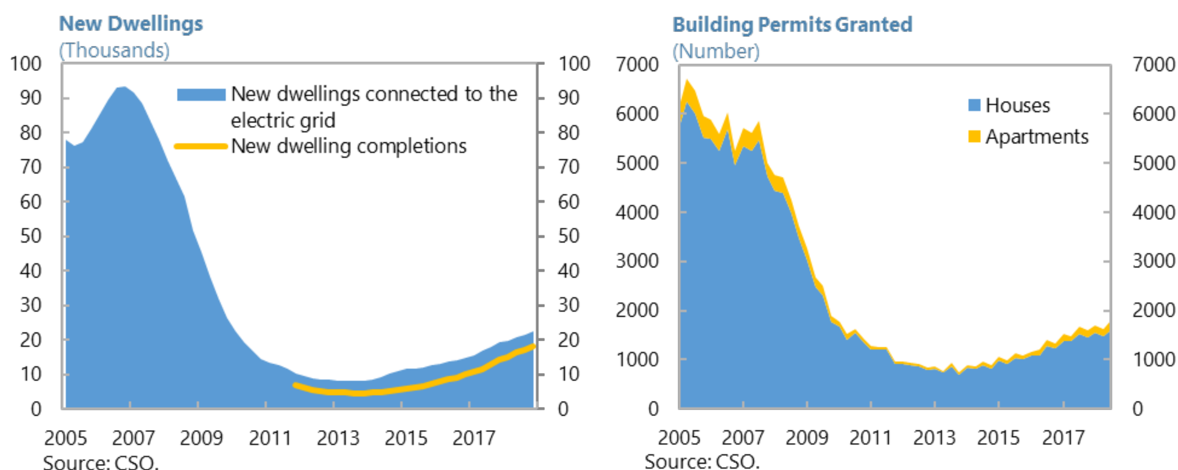
- ***Productivity and skills gaps.*** Aggregate productivity in Ireland is high and its growth is faster than in most European countries. The highly-productive and profitable MNE sector is a major contributor. SMEs' productivity is below that of MNEs' but higher than average SME productivity in other European countries. However, a sectoral breakdown reveals that average productivity of

Box 2. Expanding the Supply of Housing

Unlike during the pre-crisis period, rising housing prices have not been fueled by excessive credit but rather by a lagging supply response to rising demand. Robust job creation, rising wages, low interest rates, and population growth have all contributed to a strong recovery in housing demand since 2013. The supply of housing, however, has not kept pace. The main factors that have prevented a faster expansion in housing supply are constraining regulations, weaknesses in the zoning and planning process, financial difficulties of construction firms, skills shortages in the construction sector, and land hoarding.

The government has taken several measures to increase housing supply, develop the rental market, and improve affordability.[1] *The Rebuilding Ireland Action Plan for Housing and Homelessness*, announced in July 2016, seeks to double the annual level of residential construction to 25,000 homes by 2020, deliver an additional 50,000 social housing units in the period to 2021, and meet the housing needs of an additional 87,000 households through housing assistance schemes. *Home Building Finance Ireland*, a newly established state lender for financially constrained developers, aims to deliver up to 7,500 new homes over the next five years, financed by a €750 million investment from the Ireland Strategic Investment Fund. Other initiatives include an infrastructure fund designed to provide local public infrastructure to facilitate housing development, and a new fast-track planning process for large-scale housing developments.

There are indications that the housing supply will continue to expand. The number of new dwellings connected to the electric grid increased by 17 percent in 2018—the fifth consecutive year of growth, albeit from a low base—while new dwelling completions have also grown rapidly. Forward-looking indicators point to further growth. Building permits granted for the construction of houses and apartments increased by 8.5 percent year-on-year in 2018:Q3, and employment continues to increase in the construction sector.

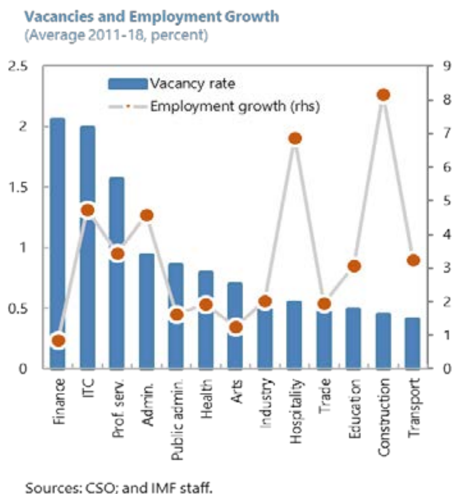


[1] See the 2018 Article IV Consultation Staff Report, IMF Country Report No. 18/194.

firms in transportation, accommodation, food services, and agriculture has declined over the last decade. These are also the sectors that will be most exposed to a Brexit shock. Policies should be aimed at improving enabling environments in these sectors, including through direct funding of R&D, training of employees, and quality infrastructure investment. Finance, professional services, and ICT sectors experience persistent difficulties in hiring qualified candidates. These skills mismatch could be addressed by tailoring education profiles to these sectors.

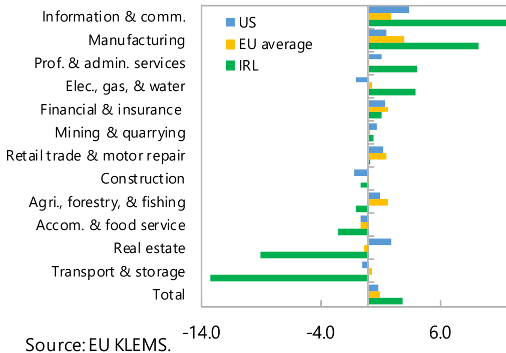
Figure 20. Productivity and Skills

Higher qualification jobs seem to be hard to fill …



and productivity is lagging in several sectors.

Labor Productivity Growth, 2005-2015
(Y/y percent change, average annual growth in GVA per employee)

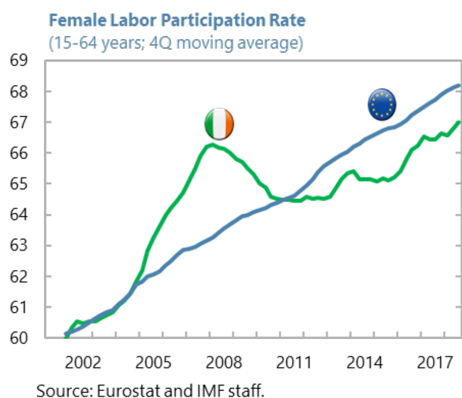


Source: EU KLEMS.

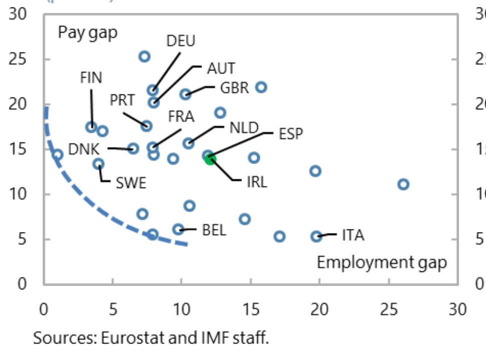
- ***Gender gap.*** Female labor force participation, albeit increasing, continues to lag the EU average. Closing the employment gap would result in boosting potential GNI* by up to 10 percentage points. The high child care cost is a major limitation for greater female labor force participation, especially for low-income families (ESRI report). In this respect, the launch of the Affordable Childcare Scheme in 2019 is welcome. Further policies should aim at removing the large gender employment and pay gaps, also by promoting equal opportunities, flexible work schedules, income tax individualization, and gender pay transparency at company level, and fostering women's entrepreneurship.

Figure 21. Gender Gap

Female labor participation rate lags the EU average, while the pay gap remains substantial.



Gender Employment and Pay Gap[1/]
(percent)



Sources: Eurostat and IMF staff.

[1/] The employment gap measures the difference between the employment rates of men and women aged 20 to 64. The unadjusted gender pay gap measures the difference between average gross hourly earnings of male paid employees and of female paid employees as a percentage of average gross hourly earnings of male paid employees.

Authorities' Views

33. The authorities showed strong resolve to tackle the challenging structural agenda. They noted that implementation of the *Rebuilding Ireland Action Plan* is on track to meet its home-building targets, and that loan applications with *Home Building Finance Ireland* have been in line with expectations. While enhanced supply has contributed to house price moderation, they acknowledged that the housing supply needs to expand further and that affordability remains an issue. At the same time, they stressed that social housing has increased substantially and that further efforts are underway, while the number of homeless people has stabilized. They considered that the vacant site levy has been effective at stimulating development at the local level even though more information is needed to identify vacant sites in urban growth areas. The authorities noted that they have expanded training programs, including free of charge for skilled women out of the labor force, and will soon roll out the *Affordable Childcare Scheme* to help increase female labor force participation. They are progressing towards Technology Skills 2022 targets to increase the number of much-needed ICT graduates. The authorities also flagged that they have bolstered R&D spending in recent years but noted that constraints on economies of scale and absorptive capacity of SMEs hamper greater efficiency gains.

STAFF APPRAISAL

34. The Irish economy has become one of the most dynamic in Europe but faces several external risks. Economic growth is strong and broad-based, unemployment is nearing historical lows, and public finances have improved. The baseline outlook is favorable but the country is uniquely vulnerable to Brexit. Also, an escalation in global protectionism and changes in international corporate taxation could have negative spillovers. Ireland's external position is broadly in line with its medium-term fundamentals and desirable policy settings but important measurement issues regarding activities of multinationals continue to complicate the overall assessment.

35. Policymakers should manage these risks by focusing on building buffers and strengthening resilience of the economy, both to alleviate demand pressures and prepare for the possibility of a major external shock.

36. Fiscal policy should be tightened to alleviate demand pressures and build buffers against potential shocks. Barring a no-deal disorderly Brexit, staff recommends pursuing small budget surpluses in 2019–20, including by avoiding further spending overruns and saving any corporate tax windfalls, and to aim at reducing the public debt ratio below 50 percent over the medium term. To reduce the dependency on fragile corporate taxes, the VAT should be further streamlined, income taxation reformed, and property taxes gradually increased. Moderating expenditure growth while increasing its efficiency, notably in healthcare and public investment, is equally important. Any proceeds from government disinvestments in the financial sector should be used for public debt reduction.

37. A disorderly no-deal Brexit would have significant and immediate adverse consequences for the Irish economy and reduce long-run output. If this risk materializes, the government should allow automatic fiscal stabilizers to operate freely and provide targeted, temporary, and effective support to hard-hit sectors. It should also prepare for a fiscal stimulus, depending on the severity of the downturn in the broader economy. In the event of a sharp contraction in bank credit, the central bank should release the countercyclical capital buffer.

38. Ireland should continue its proactive approach to the international corporate tax reform agenda. The government's commitment to implement agreed reforms to reduce profit shifting is welcome. Staff encourages the authorities to continue to constructively engage in ongoing multilateral efforts to address digitalization and tax avoidance.

39. It is important to tackle long-term challenges related to population ageing and climate change. To safeguard the SIF's long-term viability and avoid future pressure on the government budget, a review of social security contributions and benefits is needed. Ireland should also step up policy efforts to achieve its climate targets. There is an urgent need to develop and implement a comprehensive and appropriately ambitious strategy to transform the carbon-based economic model.

40. Efforts to safeguard financial sector stability should continue. Domestic banks have improved their resilience, but profitability remains vulnerable. Banks should further reduce nonperforming loans, including through loan-restructuring and portfolio sales, improve their cost-efficiency, and diversify lending. Although financial stability risks in the non-bank financial sector are currently limited, its rapid growth calls for improving data collection, closely monitoring the build-up of risks, developing system-wide stress testing, and continuing intensive international cooperation between supervisors. Financial sector preparations for Brexit appear broadly adequate, but close cooperation with the EU and U.K. should continue to ensure business continuity and avoid cliff-edge risks. It is also crucial to maintain a high-quality authorization process for U.K.-based financial firms seeking to relocate some of their activities to Ireland.

41. Macroprudential policies appear to be appropriately calibrated, but the toolkit should be enhanced. To better capture household repayment capacity of mortgages, the authorities should complement the existing limits on loan-to-value and loan-to-income ratios with debt-based measures. Given the openness of the economy and its vulnerability to external shocks, expanding the toolkit with a systemic risk capital buffer would bolster system resilience.

42. Further steps are needed to strengthen Ireland's anti-money laundering regime and ensure the integrity of its globally interconnected economy. The progress in transposing the 4th EU Anti-Money Laundering Directive into national legislation is welcome. The authorities should continue their efforts to ensure effective implementation of preventive measures by banks and key gatekeepers to the financial system, and strengthen transparency of beneficial ownership.

43. Addressing bottlenecks to growth remains important. Further efforts are needed to address the housing shortage, including by improving spatial planning, rationalizing building regulations, and effectively countering land hoarding in urban growth areas. The ongoing expansion of social housing is welcome. To boost productivity of domestic firms, the government should improve the enabling environment in lagging sectors, including through direct funding of research and development, training of workers, and quality infrastructure investment. Better aligning education outcomes with business needs and increasing female employment are also important.

44. Staff proposes that the next Article IV consultation with Ireland take place on the standard 12-month cycle.

Table 1. Selected Economic Indicators, 2016–24

Populations (2018, millions):	4.8	Per capita income (euros):	37,545
Quota (as of Apr. 30, 2018, millions of SDRs):	3,449.9	At-risk-of -poverty rate 1/:	16.6

				Projections					
	2016	2017	2018	2019	2020	2021	2022	2023	2024
	(annual percentage change, constant prices, unless otherwise indicated)								
Output/Demand									
Real GDP	4.9	7.2	6.8	4.1	3.4	3.1	2.9	2.7	2.7
Domestic demand	22.7	-13.0	4.4	3.8	3.3	3.0	2.8	2.7	2.7
Public consumption	3.5	3.9	6.4	3.0	1.7	2.5	2.9	2.1	2.3
Private consumption	3.7	1.9	3.0	2.5	2.5	2.4	2.4	2.3	2.3
Gross fixed capital formation	53.2	-30.2	7.8	5.9	5.2	4.1	3.5	3.5	3.5
Exports of goods and services	4.4	7.7	8.9	4.6	4.4	4.3	4.2	4.1	4.1
Imports of goods and services	18.5	-9.3	7.2	4.5	4.6	4.6	4.6	4.6	4.6
Potential growth	3.5	8.5	6.0	4.3	3.7	3.5	3.2	3.0	2.8
Output gap	1.9	0.7	1.5	1.3	1.1	0.7	0.5	0.2	0.0
Contribution to growth									
Domestic demand	16.0	-10.7	2.8	2.6	2.3	2.1	2.0	1.9	1.9
Consumption	1.7	1.1	1.7	1.1	1.0	1.0	1.1	1.0	1.0
Gross fixed capital formation	12.6	-10.7	1.8	1.5	1.3	1.0	0.9	0.9	0.9
Inventories	1.7	-1.1	-0.6	0.0	0.0	0.0	0.0	0.0	0.0
Net exports	-12.1	18.9	4.4	1.5	1.1	1.0	0.9	0.8	0.8
Residual	1.0	-1.0	-0.4	0.0	0.0	0.0	0.0	0.0	0.0
Prices									
Inflation (HICP)	-0.2	0.3	0.7	1.2	1.5	1.7	1.9	2.0	2.0
GDP deflator	-0.8	0.4	1.4	1.2	1.4	1.8	2.0	2.0	2.0
Terms-of-trade (goods and services)	-0.4	-1.8	-0.8	-1.0	-0.1	0.2	0.4	0.3	0.2
Employment and wages									
Employment (ILO definition)	3.6	2.9	2.9	1.9	1.4	1.1	1.0	1.0	1.0
Unemployment rate (percent)	8.4	6.7	5.8	5.4	5.0	5.0	4.9	4.9	4.9
Average nominal wage	1.1	2.3	3.6	2.7	2.6	2.6	2.6	2.6	2.6
	(percent of GDP)								
Public Finance, General Government									
Revenue	27.0	26.1	25.8	25.9	25.5	25.3	24.7	24.6	24.5
Expenditure	27.6	26.3	25.8	26.0	25.3	25.0	24.2	24.0	23.8
Overall balance	-0.7	-0.3	0.0	0.0	0.2	0.3	0.5	0.7	0.7
Primary balance	1.6	1.7	1.7	1.5	1.5	1.5	1.6	1.8	1.8
Structural balance (percent of potential GDP)	-1.5	-0.4	-0.5	-0.4	-0.2	0.1	0.3	0.6	0.7
General government gross debt	73.5	68.6	64.8	62.3	58.8	57.0	54.0	51.1	48.0
General government net debt	64.8	59.8	55.8	53.1	51.5	49.5	46.7	44.1	41.2
Balance of payments									
Trade balance (goods)	38.9	36.7	34.5	32.8	32.0	31.7	31.5	31.4	31.4
Current account balance	-4.2	8.5	9.1	7.9	6.9	6.3	5.8	5.2	4.6
Gross external debt (excl. IFC)	294.4	255.0	221.3	209.7	200.3	191.5	183.3	176.3	169.8
Saving and investment balance									
Gross national savings	33.7	33.2	35.0	35.6	35.2	34.9	34.6	34.3	33.9
Private sector	32.4	31.7	33.3	34.0	33.5	33.1	32.7	32.3	31.9
Public sector	1.3	1.5	1.7	1.6	1.7	1.8	1.8	2.0	2.0
Gross capital formation	37.9	24.8	25.1	26.5	26.9	27.1	27.2	27.4	27.5
	(percent)								
Monetary and financial indicators 2/									
Bank credit to private sector (growth rate)	-7.6	-3.2	-3.4	...	...	...	...	...	...
Deposit rates	0.7	0.4	0.3	...	...	...	...	...	...
Government 10-year bond yield	0.7	0.8	1.1	...	...	...	...	...	...
Memorandum items:									
Nominal GDP (€ billions)	272.9	293.7	318.3	335.4	351.8	369.4	387.7	405.9	425.0
Modified total domestic demand (percent)	8.4	1.4	3.3	3.6	3.2	3.1	3.0	2.7	2.7
Potential real GNI* growth (percent)	2.4	2.1	1.9	...	...	...	...	...	...
Population growth (percent)	1.2	1.1	1.2	1.3	1.0	1.0	1.0	1.0	1.0

Sources: CSO; DoF; Eurostat; and IMF staff.

1/ Share of population with an equivalised disposable income (including social transfers) below the threshold of 60 percent of the national median equivalised disposable income after social transfers. Data is as of 2016.

2/ Latest observation is November 2018.

Table 2. Statement of Operations of the General Government, 2016–24
(Percent of GDP, unless otherwise indicated)

			Projections 1/						
	2016	2017	2018	2019	2020	2021	2022	2023	2024
Revenue	**27.0**	**26.1**	**25.8**	**25.9**	**25.5**	**25.3**	**24.7**	**24.6**	**24.5**
Taxes	19.4	19.0	19.0	19.2	19.1	19.1	18.6	18.7	18.6
Personal income tax	7.5	7.3	7.0	7.1	7.0	7.0	6.9	6.9	6.9
Corporate income tax	2.7	2.8	3.4	3.3	3.2	3.0	2.9	2.9	2.8
VAT	4.7	4.5	4.5	4.6	4.7	4.8	4.7	4.7	4.7
Excises	1.6	1.5	1.5	1.5	1.5	1.5	1.5	1.5	1.5
Other taxes	2.9	2.9	2.7	2.7	2.7	2.7	2.6	2.7	2.7
Social contributions	4.4	4.3	4.2	4.4	4.5	4.4	4.4	4.4	4.5
Other revenue	3.1	2.7	2.5	2.3	2.0	1.8	1.7	1.6	1.5
Expenditure	**27.6**	**26.3**	**25.8**	**26.0**	**25.3**	**25.0**	**24.2**	**24.0**	**23.8**
Expense	25.7	24.6	23.8	23.7	23.1	22.8	22.0	21.7	21.6
Compensation of employees	7.1	7.0	7.0	6.9	7.0	7.0	6.9	6.9	6.9
Use of goods and services	3.5	3.4	3.4	3.8	3.8	3.7	3.7	3.7	3.7
Interest	2.3	2.0	1.6	1.5	1.3	1.2	1.1	1.1	1.1
Subsidies	0.6	0.6	0.5	0.5	0.5	0.5	0.5	0.5	0.5
Social benefits	10.5	9.9	9.4	9.0	8.7	8.4	8.0	7.8	7.8
Other expense	1.7	1.6	1.8	1.9	1.8	2.0	1.9	1.8	1.8
Net acquisition of nonfinancial assets	1.9	1.8	2.0	2.2	2.2	2.2	2.2	2.2	2.2
Net lending(+)/borrowing(-) (overall balance)	**-0.7**	**-0.3**	**0.0**	**0.0**	**0.2**	**0.3**	**0.5**	**0.7**	**0.7**
Net financial transactions	-0.8	-0.4	-0.2	-0.1	0.2	0.2	0.4	0.6	1.0
Net acquisition of financial assets	-1.7	-0.6	0.5	-0.4	-1.4	0.3	0.1	0.1	0.1
Net incurrence of liabilities	-0.8	-0.2	0.7	-0.3	-1.7	0.1	-0.3	-0.5	-0.8
Memorandum items:									
One-off measures	0.1	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Structural balance	-1.4	-0.4	-0.5	-0.4	-0.2	0.1	0.3	0.6	0.7
Structural primary balance	0.8	1.5	1.2	1.1	1.2	1.3	1.4	1.8	1.8
Gross public debt 2/	73.5	68.6	64.8	62.3	58.8	57.0	54.0	51.1	48.0
in percent of GNI*	114.2	111.1	105.5	97.6	90.8	87.5	82.6	78.0	73.1
in percent of revenue	272.9	263.1	251.4	240.1	230.6	225.1	218.6	207.3	195.4
Net public debt 3/	64.8	59.8	55.8	53.1	51.5	49.5	46.7	44.1	41.2
Interest (in percent of revenue)	8.4	7.6	6.4	5.9	5.2	4.7	4.5	4.5	4.3
Currency and deposits 4/	5.4	5.8	6.7	6.3	4.9	5.3	5.2	5.1	5.0
GDP at current market prices (in billions of euros)	272.9	293.7	318.3	335.4	351.8	369.4	387.7	405.9	425.0

Sources: DoF; Eurostat; and IMF staff.

1/ Starting in 2019, staff assumes that the resources available for additional spending but not allocated by the Budget 2018 are distributed mainly among compensation of employees, use of goods and services, and net acquisition of nonfinancial assets.

2/ Includes the accumulation of a Rainy Day Fund of €0.5 billion starting in 2019.

3/ Gross debt minus financial assets corresponding to debt instruments (currency and deposits, debt securities, and loans).

4/ Includes the Rainy Day Fund.

Table 3. Summary of Balance of Payments, 2016–24

	2016	2017	2018	2019	2020	2021	2022	2023	2024
				Projections					
	(percent of GDP)								
Balance of Payments									
Current account balance	-4.2	8.5	9.1	7.9	6.9	6.3	5.8	5.2	4.6
Balance of goods and services	15.5	30.4	31.2	30.4	29.8	29.6	29.6	29.4	29.2
Trade balance	38.9	36.7	34.5	32.8	32.0	31.7	31.5	31.4	31.4
Exports of goods	70.8	65.7	65.4	65.8	64.7	64.3	64.1	64.0	64.1
Imports of goods	31.9	29.0	31.0	33.0	32.7	32.6	32.6	32.6	32.8
Services balance	-23.4	-6.2	-3.2	-2.4	-2.2	-2.1	-2.0	-2.0	-2.1
Primary income balance	-18.3	-20.4	-20.5	-20.9	-21.3	-21.7	-22.1	-22.6	-23.0
Credit	25.8	26.6	26.0	26.0	26.0	26.0	26.0	26.0	26.0
Debit	44.1	47.0	46.6	47.0	47.4	47.8	48.2	48.6	49.0
Secondary income balance	-1.4	-1.6	-1.6	-1.6	-1.6	-1.6	-1.6	-1.6	-1.6
Capital account balance	-1.6	-9.6	-7.0	-3.8	-3.5	-3.3	-3.3	-3.3	-3.3
Financial account balance	-3.1	1.6	8.1	4.1	3.4	3.0	2.5	2.0	1.3
Direct investment	-3.1	-11.4	21.2	-3.8	-3.6	-3.4	-3.2	-3.1	-3.0
Portfolio investment	10.2	-18.8	-3.4	9.8	9.3	8.9	8.5	8.1	7.7
Other investment	-10.7	31.7	-9.9	-2.0	-2.4	-2.5	-2.7	-3.0	-3.4
Change in reserve assets	0.5	0.1	0.2	0.0	0.0	0.0	0.0	0.0	0.0
Net errors and omissions	2.7	2.7	6.0	0.0	0.0	0.0	0.0	0.0	0.0
Net International Investment Position									
Net investment position	-170.6	-149.3	-142.3	-131.0	-121.5	-112.8	-104.9	-98.2	-92.5
Net direct investment	5.5	-9.3	0.7	-3.1	-6.5	-9.6	-12.4	-14.9	-17.2
Net portfolio investment	-171.0	-145.2	-116.4	-100.7	-86.6	-73.6	-61.6	-50.8	-40.8
Net other investment	-6.4	4.0	-28.1	-28.6	-29.7	-30.8	-32.0	-33.6	-35.5
Reserve assets	1.2	1.3	1.4	1.4	1.3	1.2	1.2	1.1	1.1
External Debt									
Total external debt	818.4	725.8	732.7	695.0	662.9	632.1	603.1	577.2	552.7
Non-IFSC external debt	294.4	255.0	248.0	235.1	224.4	214.5	205.2	197.2	189.8
IFSC external debt	523.9	470.8	484.6	460.0	438.5	417.6	397.9	380.0	362.9
Short-term debt	145.6	147.3	168.5	159.9	152.5	145.4	138.7	132.8	127.1
Medium & long term debt	672.8	578.5	564.2	535.2	510.5	486.7	464.4	444.4	425.6
Memorandum item:									
Modified current account balance (CA*)	1.7	1.1	…	…	…	…	…	…	…

Sources: CBI; CSO; and IMF staff.

Table 4. Monetary Survey, 2013–2019

(Billions of Euros, unless otherwise specified, end of period)

	2013	2014	2015	2016	2017	2018	2019 1/
Aggregate balance sheet of domestic market credit institutions							
Assets	476.6	423.4	377.6	356.2	331.6	333.3	354.2
Claims on Central Bank of Ireland	2.0	3.3	5.5	10.4	9.9	8.2	7.6
Claims on Irish resident Other MFIs	48.6	47.3	46.1	41.5	38.4	34.0	33.5
Claims on Irish resident non MFIs	280.5	236.5	205.8	190.5	183.6	178.3	176.9
General government	20.5	20.1	18.4	17.3	15.9	16.2	17.6
Private sector	260.0	216.4	187.4	173.2	167.7	162.1	159.2
Households	107.7	96.9	92.0	88.2	89.8	91.3	89.7
Non-Financial Corporations	78.0	58.0	44.2	39.5	38.4	37.7	37.1
Non-Bank Financial Intermediaries	74.3	61.5	51.2	45.5	39.6	33.1	32.4
Claims on non-residents	105.5	94.0	83.5	72.6	63.9	72.9	93.6
Other assets	40.1	42.3	36.7	41.2	35.7	39.9	42.7
Liabilities	476.6	423.4	377.6	356.2	331.6	333.3	354.2
Liabilities to Eurosystem 2/	30.5	13.6	10.0	7.0	7.4	3.0	3.0
Liabilities to Irish resident Other MFIs	52.1	49.8	46.3	39.4	35.6	29.5	29.1
Deposits of Irish resident non MFIs	175.3	163.1	166.6	169.1	174.5	178.7	180.0
General government	13.7	8.6	4.2	3.7	3.0	3.0	2.5
Private sector	161.6	154.5	162.3	165.4	171.4	175.7	177.5
Households	91.1	91.4	94.7	97.1	99.1	103.8	105.8
Non-Financial Corporations	32.4	37.5	40.1	42.5	47.5	47.9	46.9
Non-Bank Financial Intermediaries	38.1	25.6	27.5	25.8	24.8	24.1	24.8
Deposits of non-residents	72.2	63.7	42.8	38.5	23.8	31.6	48.5
Debt securities	26.9	27.4	25.2	23.1	21.2	25.5	24.0
Capital and reserves	96.6	80.2	67.2	61.3	57.5	54.0	54.2
Other liabilities (incl. Central Bank of Ireland)	22.9	25.5	19.5	17.8	11.7	11.0	15.5

Table 4. Monetary Survey, 2013–19 (Concluded)
(Billions of Euros, unless otherwise specified, end of period)

	2013	2014	2015	2016	2017	2018	2019 1/
Money and credit 3/							
Net foreign assets	-12.3	20.7	43.3	41.0	48.9	53.0	...
Central Bank of Ireland 4/	-51.2	-17.1	2.5	5.9	13.9	24.1	...
Commercial banks	38.9	37.8	40.8	35.1	34.9	28.9	35.6
Net domestic assets	198.3	179.1	158.1	175.0	170.7	191.0	...
Public sector credit	20.7	20.8	19.4	18.3	16.9	17.3	18.8
Private sector credit	278.3	226.7	199.9	185.8	179.1	173.9	170.8
Other	-100.6	-68.4	-61.1	-29.1	-25.3	-0.2	...
Irish Resident Broad money (M3) 5/	186.0	199.8	201.5	216.0	219.6	243.9	228.9
Irish Resident Intermediate money (M2) 5/	182.7	171.8	184.0	191.7	200.9	211.1	215.8
Irish Resident Narrow money (M1)	113.4	115.9	132.9	146.5	158.7	171.6	174.7
			(Percent of GDP)				
Public sector credit 6/	45.3	40.5	27.4	23.5	20.5	20.0	...
Private sector credit 6/	573.5	435.5	278.9	235.9	216.2	199.5	...
			(Percentage change y/y)				
Broad money - Irish contribution to euro area M3 7/	10.7	-0.7	5.0	7.0	1.6	10.8	6.1
Irish Public sector credit 7/ 8/	-58.1	-3.0	-9.4	-5.2	-5.8	3.8	9.1
Irish Household and non-financial corporations credit 7/ 8/	-4.9	-4.1	-4.0	-1.7	0.1	1.9	2.5
Memorandum items: 9/							
Credit to deposits (in percent) 10/	160.9	140.0	115.4	104.7	97.8	92.3	89.7
Deposits from Irish Private Sector (y-o-y percent change)	8.9	-3.0	5.8	0.7	5.0	2.3	3.0
Wholesale funding (billions of euros)	135.8	126.9	105.4	92.9	73.3	79.0	92.4
Deposits from MFIs	109.0	99.5	80.2	69.8	52.1	53.5	68.4
Debt securities	26.9	27.4	25.2	23.1	21.2	25.5	24.0
Wholesale funding (y-o-y percent change) 11/	-12.3	-6.7	-17.9	-7.5	-19.8	12.6	30.8
Wholesale funding (percent of assets) 11/	28.5	30.0	27.9	26.1	22.1	23.7	26.1

Sources: CBI and IMF staff.
1/ As of March 2019.
2/ Relating to Eurosystem monetary policy operations.
3/ Including banks in the International Financial Service Center.
4/ Sourced from quarterly IIP statistics.
5/ Differs from the M3 (M2) Irish contribution to euro area as only liabilities vis-a-vis Irish residents are used.
6/ Refers to credit advanced by domestic market credit institutions.
7/ Includes IFSC.
8/ Growth rates adjusted for valuation, reclassification, derecognition/loan transfer to non-MFIs, and exchange rates.
9/ Excludes IFSC.
10/ Domestic market credit institutions' private sector credit to deposits.
11/ Includes resident and non-resident MFI deposits, and debt securities issued.

Table 5. Main Domestic Banks' Aggregated Summary Financial Statements, 2017Q4–2018Q4 [1/]

(Billions of Euros, unless otherwise indicated)

Balance Sheet	2017Q4	2018Q4	Y/Y change	
	€ bn.	€ bn.	€ bn.	%
Cash & due from Eurosystem	15.6	14.3	-1.3	-8.3
Net loans	154.9	155.4	0.5	0.3
Due from banks	3.9	1.7	-2.2	-56.2
Securities & derivatives	35.6	38.7	3.1	8.7
Other assets	9.1	10.8	1.7	19.3
Total assets	219.1	221.0	1.8	0.8
Total average assets (TAA)	188.5	187.5	-1.0	-0.6
Due to Eurosystem	6.3	2.6	-3.7	-58.3
Due to banks	6.4	4.6	-1.8	-27.8
Deposits	155.6	162.0	6.4	4.1
Debt & derivatives	20.9	21.6	0.7	3.4
Other liabilities	4.5	4.2	-0.3	-7.3
Total liabilities	193.7	195.0	1.3	0.7
Net equity	25.4	25.9	0.5	1.9
Total liabilities & equity	219.1	221.0	1.8	0.8

Profit and Loss Account	2017Q4		2018Q4	
	€ bn.	% of TAA	€ bn.	% of TAA
Interest income	6.0	3.2	5.6	3.0
Interest expense	-1.1	-0.6	-0.3	-0.2
Net interest margin	4.8	2.6	5.3	2.8
Net fee income	1.2	0.6	1.0	0.6
Net trading gains	0.2	0.1	0.0	0.0
Other nonrecurrent items	0.2	0.1	0.2	0.1
Gross operating income	6.3	3.4	6.5	3.5
Operating expenses	-4.3	-2.3	-4.1	-2.2
o/w: administration & other	-0.3	-0.2	-0.4	-0.2
o/w: staff	-4.0	-2.1	-3.8	-2.0
Preprovision profits (PPP)	2.0	1.1	2.4	1.3
Loan loss & NAMA provisions	0.0	0.0	0.1	0.1
Loss on derecognized assets	0.1	0.1	0.0	0.0
Net income before tax	2.2	1.2	2.5	1.4
Tax effects & other	4.0	2.1	3.6	1.9
Net income	6.2	3.3	6.2	3.3

Memorandum items:

	2017Q4	2018Q4	Y/Y change € bn.	Y/Y change %
Gross loans 2/	162.4	156.8	-5.6	-3.4
Loan loss provisions	7.9	4.8	-3.1	-39.4
Gross NPLs	17.4	12.7	-4.7	-26.9
Gross NPLs to gross loans (%)	10.7	8.1		-24.3
Provisions to gross NPLs (%)	45.6	37.7		-17.2
Net NPLs to net equity (%)	37.3	30.6		-17.9

	2017Q4 € bn.	2017Q4 % of TAA	2018Q4 € bn.	2018Q4 % of TAA
PPP net of other nonrecurrent items	1.9	1.0	1.6	0.8
Return on equity		24.5		23.8
Provisions to gross loans		1.1		0.9
Risk weighted assets (RWA)	107.3	56.9	111.3	59.4
Core tier 1 capital (CT1) and CT1 to RWA (%)	19.7	18.4	19.8	17.8
CT1 to total assets = leverage ratio (%)		9.0		9.0

Sources: CBI and IMF staff.

1/ Bank of Ireland, Allied Irish Banks, and Permanent tsb.

2/ Includes loans held for sale, classified on balance sheet as other assets.

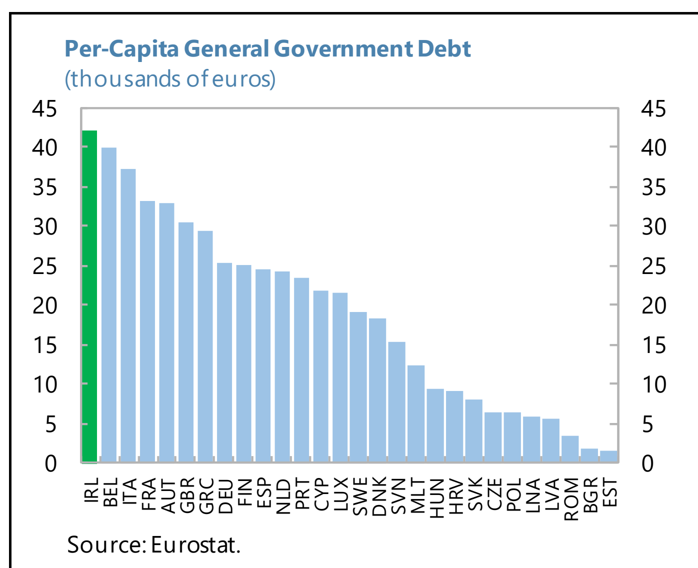
Annex I. Public Debt Sustainability Analysis (DSA)

A. Summary

1. Ireland's public debt sustainability continued to improve, mainly benefiting from strong real GDP growth and sustained budget primary surpluses. In addition, prolonging debt maturities while pre-financing for nearly a year ahead at currently low yields helped reduce borrowing requirements and costs in the short term. While CDS and bond spreads are expected to remain low due to ECB's QE policy, an increase in interest rates is estimated to have a negligible short-term impact on debt dynamics, as most public debt is at fixed rates and with medium-term maturity. It is expected that National Asset Management Agency's winding down in 2020 might generate a profit of €4 billion, which the government has earmarked for debt reduction. Further disposal of government's stakes in the banking system presents an upside risk.

2. However, the debt burden remains elevated and vulnerabilities persist.

- Alternative scaling metrics such as GNI*, which provides a more accurate measure of the size of the economy than nominal GDP, government revenue, or in per-capita terms show that Ireland's public debt burden remains high.

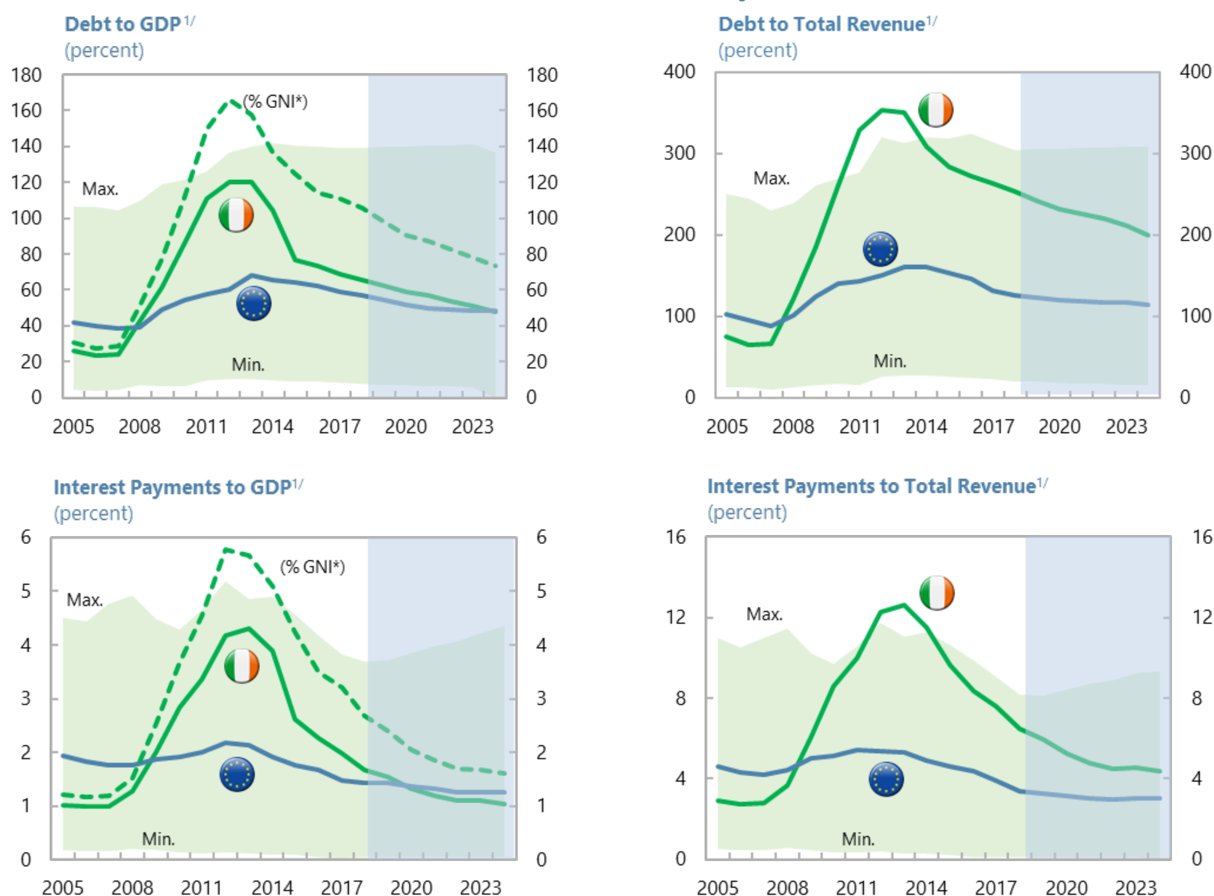


Source: Eurostat.

- Debt dynamics are vulnerable to macro-financial and contingent liability shocks. While debt metrics remain within the tolerance limits when expressed in terms of GDP, the heat map would turn mostly red, especially for the debt stock, when GNI* is used as yardstick.

- The relatively high share of debt held by non-residents poses potential vulnerabilities, but a sudden-stop scenario represents a tail risk since non-resident holders are mainly real-money investors with long-term investment horizon.

Public Debt and Interest Payments



Sources: CSO; Eurostat; Haver Analytics; WEO; and IMF staff.
1/ EU indicators were calculated excluding Greece and Ireland; the line indicates the unweighted median.

B. Baseline Scenario

3. Ireland's public debt burden is projected to decline steadily over the medium term. Solid fiscal performance, as incorporated in staff's forecast[1], and the positive real growth-interest rate differential would bring the gross public debt to 48 percent of GDP (41 percent of GDP in net terms) by 2024 from about 65 percent (55 percent in net terms) in 2018. However, conventional debt metrics overstate the improvement due to the well-known specifics of Ireland's headline GDP figures.

4. Expressed in terms of GNI* or general government revenue, the improvement path would be slower. These alternative metrics show that, although remaining on a downward path, the debt burden would continue to compare unfavorably with EU peers. However, privatization

[1] Over 2007–15, there is no evidence of systematic bias in the staff projections of the main macroeconomic and fiscal variables except during the crisis period and at the time of the large revision of national accounts in 2015.

proceeds and any potential funds related to a settlement of the EC ruling on Apple Inc., which have not been incorporated into current projections, may provide additional resources for debt reduction.

Main Working Assumptions

The following assumptions have been made to carry out the public DSA:

1. The DSA exercise has been carried out as if all the public debt was denominated in euros since the share of debt denominated in foreign currency (mainly, the U.K. bilateral loan granted during the crisis) is very small (about 2 percent of the outstanding stock) and fully hedged.
2. About 10 percent of Ireland's public debt is represented by the State Savings Scheme, including Post Office Savings bank deposits, that, although redeemable on demand, have been a stable source of medium-term funding, even during the crisis period. For the calculation of gross financing needs, it is assumed that 20 percent of the stock of these liabilities falls due each year of the projection period and is fully rolled-over with a medium-term maturity beyond the projection period. Similar assumptions were made for another small portion of Ireland's public debt (2 percent of the total), which is due to local authorities and other general government entities. As a result, both these components of the public debt are kept constant over the projection period at their (estimated) 2018 level.
3. In line with the prospective gradual normalization of ECB's monetary policy over the medium term, the 10-year bond spread between Ireland and Germany is projected to gradually widen to 125 basis points from the current 60 basis points. As a result, the real interest rate on new issuances becomes closer to real output growth, although the growth-interest rate differential remains positive.

5. Gross financing needs (GFNs) are estimated to remain modest. As result of the government's prudent fiscal stance and the relatively long maturity of the public debt, Ireland's GFNs are estimated to average about 4.5 percent of GDP (about 7 percent of GNI*) over the 2019–24 period. However, some 20 percent of the estimated GFNs (equivalent to about one percent of GDP) is represented by stable liabilities (see Box), which have historically been fully renewed, thus reducing the government's need to tap financial markets.

6. However, vulnerabilities persist. The Irish economy is highly integrated into the world economy and is concentrated in a small number of sectors. This leaves the economy, and hence the public finances, vulnerable to a broad range of common and idiosyncratic shocks. In addition, CIT proceeds, which account for nearly 20 percent of total revenue, are highly concentrated, with the top ten payers accounting for about 40 percent of the tax receipts. Furthermore, staff estimates that more than 50 percent of Ireland's total CIT revenue is paid by affiliates of U.S.-based MNEs. Therefore, the U.S. corporate tax reform might affect Ireland's public finances.[2]

[2] See "The Impact of International Tax Reforms on Ireland", *Selected Issues Paper*, Chapter II, International Monetary Fund, 2018.

C. Risk Assessment

7. In carrying out the stress scenarios, shocks were calibrated to consider Ireland-specific features. In particular:

- ***The growth shock*** is normally assumed to be one standard deviation of the historical growth rate calculated over a 10-year period (2009–18). However, since growth in 2015 was heavily distorted by corporate balance sheets relocation, the standard deviation has been calculated over 2008–2018, excluding 2015. The resulting growth shock of -4.7 percent is comparable to the 4½ percent average output decline during 2008-09.

- ***The primary balance shock*** is usually modeled as half of the historical standard deviation (2009–18) of the primary balance in percent of GDP. However, in the case of Ireland, the historical primary balance would include also the financial support granted to the banking sector during the crisis. The standard deviation was therefore recalculated excluding those expenditures to provide a more accurate picture of underlying developments. This, nonetheless, implies a significant worsening of the primary balance, which shifts from a surplus of 1.6 percent of GDP in 2019 to an average deficit of about 0.5 percent in 2020–21.

- ***The interest rate shock*** is by default equal to the difference between the average effective (real) interest rate on government debt in the projection period (2019–24) and the maximum value of that variable in the previous 10 years. Given the high interest rates on government debt during the financial crisis, this standard methodology would result in an interest rate shock of over 800 basis points (bp); more than ten times the current spread for Irish government bonds. The shock was therefore capped at 200bp, which would imply issuing government bonds at an interest rate almost three times the current one.

- ***A combined macro-fiscal shock*** estimates the impact of the above-described shocks together.

- ***A contingent financial liability shock (CFL)*** combines a growth shock, like the one described above, with a one-time increase in public expenditure equal to 10 percent of banks' assets. However, this is likely to be a tail risk as domestic banks have significantly strengthened their capital buffers.

- ***A customized shock*** was devised by assuming a permanent decline in CIT revenue by 20 percent, reflecting the volatility of MNEs' operations. This is equivalent to about two-thirds of the difference between actual and expected CIT revenue in 2015 (the year of the large revision of national accounts), about half of the CIT proceeds from the ten largest companies, and almost half of the estimated CIT losses, should the Irish affiliates of U.S.-based MNEs allocate their profits more in line with their activity in Ireland. In this scenario, lower MNEs' profits are accompanied by a severe one-time drop in headline GDP, calculated to be about 12 percent

based on the accounting relationship between GDP, profits, wages, and taxes.[3] Assuming the consequences for the underlying domestic economy are limited, non-CIT revenues are kept unchanged in nominal terms compared to the baseline. A similar assumption is made regarding public expenditure.

8. Based on traditional metrics, debt dynamics appears to be resilient to shocks, although vulnerable to macro-financial shocks. As shown in the heat map (Figure 5), all the debt metrics expressed in terms of GDP would remain within the risk assessment benchmarks, except for the CFL shock scenario.

- In the CFL shock scenarios, the debt-to-GDP ratio almost reaches the 85 percent threshold, with the GFNs briefly surpassing the 20 percent of GDP vulnerability mark. Although returning on a downward path, the debt-to-GDP ratio would remain close to 75 percent in 2024; more than 20 percentage points higher than in the baseline and about 10 percentage points above the starting point.

- In the growth-shock scenario as well as in the combined macro-financial and customized scenarios, the debt burden would return approximately to the level at the beginning of the scenario analysis (around 62 percent of GDP). In these circumstances, the government's goal of bringing the debt-to-GDP ratio below 60 percent in the early part of the next decade would require additional fiscal measures.

- The interest rate and primary balance shocks would have a modest impact on debt dynamics. In the former case, this is due to the relatively long maturity of Ireland's public debt and limited GFNs.[4] In the latter case, the impact would be even smaller if the increase in spending, which drives the primary balance shock, were to translate into higher growth.

- In all the scenarios, the GFN-to-GDP ratios remain well below the vulnerability threshold and decline over time.

9. When debt metrics are measured relative to GNI*, the vulnerabilities become more evident. In this case, the debt burden would fall below the 80 percent of GDP benchmark towards the end of the projection period only in the baseline scenario. However, the risks associated with the GFNs would remain relatively low, except in the CFL shock scenario, although in a few scenarios the GFN-to-GNI* ratio would be closer to the vulnerability thresholds.

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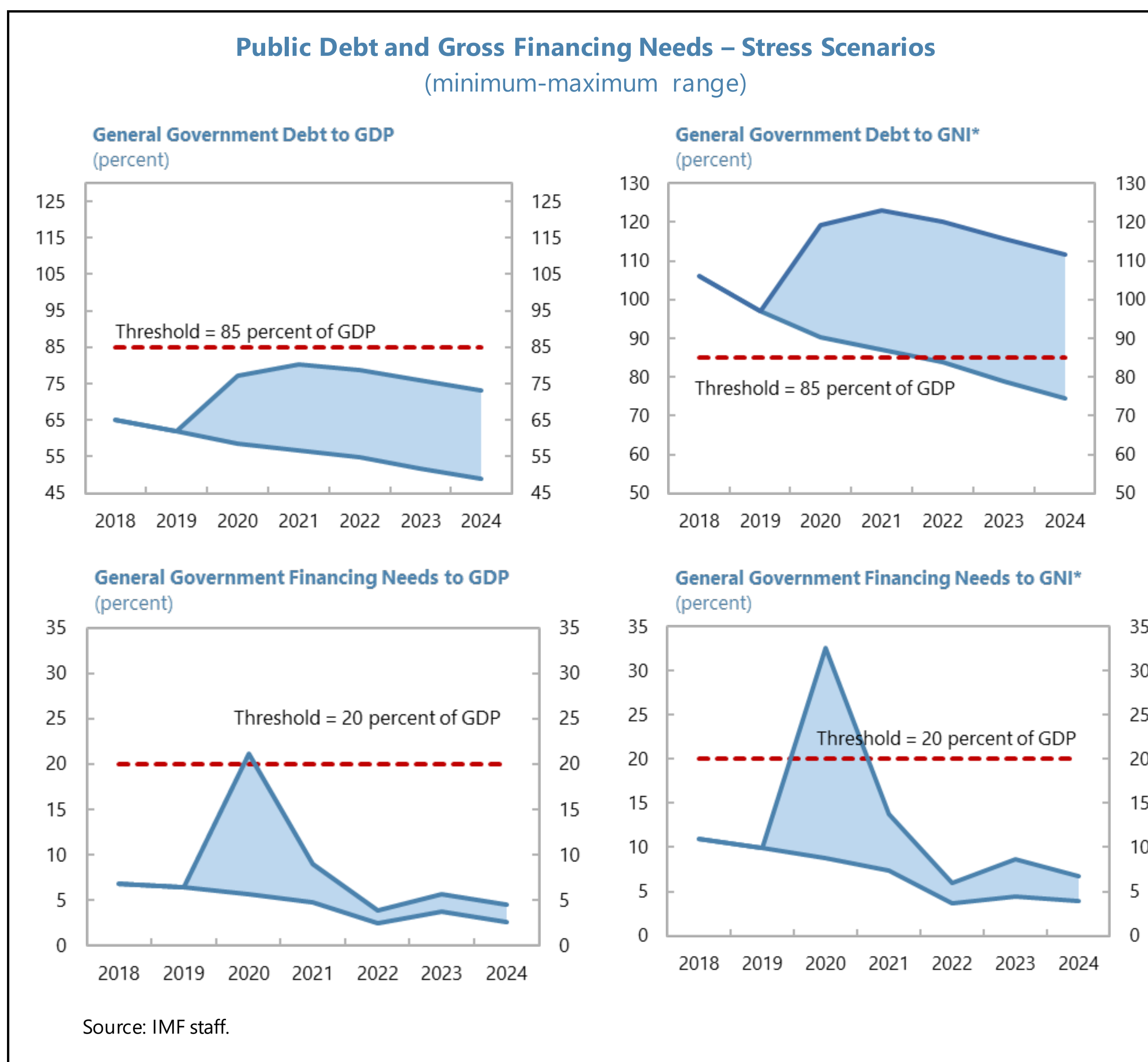
[3] It was assumed that $NGDP_t^{post-shock} = Profit_t^{post-shock} + Wage\ Bill_t^{post-shock} = \left(CIT_t^{post-shock}/\pi_t^{pre-shock}\right) + Wage\ Bill_t^{baseline}$; where $\pi_t^{pre-shock} = \frac{CIT_t^{pre-shock}}{Profit_t^{pre-shock}}$. Assuming the GDP deflator remains unaffected, the real GDP and hence growth were derived accordingly.

[4] The impact of an interest rate shock on Ireland's real output is rather small.



10. A few considerations mitigate the assessment of the risks associated with the large share of public debt held by non-residents and the substantial external financing requirements. Since non-resident holders are mainly real-money investors with long-term investment horizon, the likelihood of a sudden stop represents rather a tail risk. In addition, Exchequer's cash balances also provide a buffer to cover more than a year of GFNs.[5] The substantial external financing requirements mostly reflect intra-company and intra-group operations of large MNEs, which also hold large financial assets.

[5] As of end-January, total Exchequer cash balance amounted to nearly €25 billion, equivalent to about 14 months of the average GFNs in 2019–20.

Authorities' Views

11. The authorities broadly concurred with staff's analysis. They recognized the need to complement the traditional debt-to-GDP ratio with alternative measures since GDP has become distorted by activities of multinationals. They agreed that public debt is still high when using alternative measures, such as debt-to-GNI* or debt-to-revenue ratios, that better reflect the underlying economic activity. At the same time, they pointed to steps taken to mitigate risks. They have maintained a strong liquidity position, covered their refinancing needs for nearly a year ahead; locked in currently low fixed interest rates; extended the average debt maturity to 10 years; and diversified the investor base. They have also continued building buffers, including the Rainy-Day Fund, which importantly lowers the net debt burden. Finally, contingent liabilities have declined with improving financial soundness of the banking sector, while proceeds from the National Asset Management Agency, estimated at close to €4 billion over the next two years, will be used to reduce public debt.

Figure 1. Ireland: Public DSA – Baseline Scenario

(Percent of GDP, unless otherwise indicated)

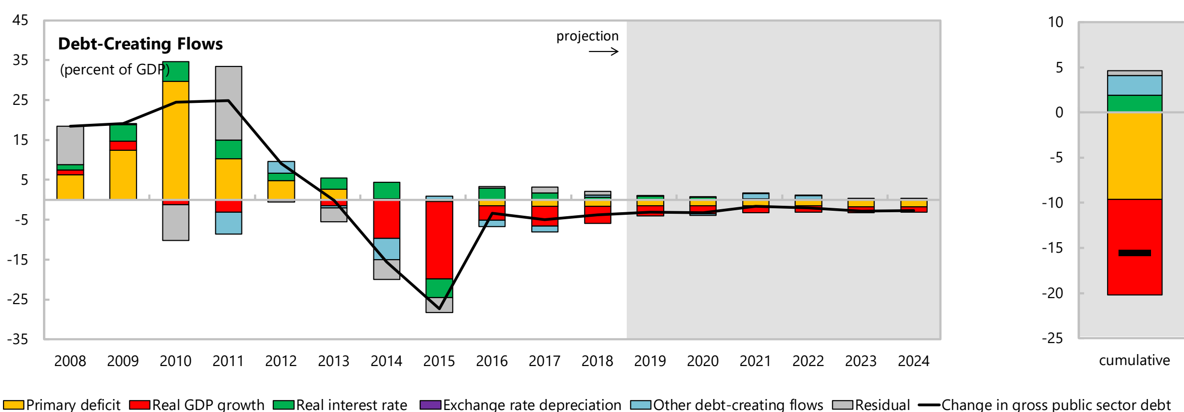
Debt, Economic and Market Indicators [1]

	Actual			Projections					
	2008-2016 [2]	2017	2018	2019	2020	2021	2022	2023	2024
Nominal gross public debt	88.4	68.6	64.8	61.7	58.5	56.8	54.9	52.0	49.2
Public gross financing needs	14.8	9.4	6.7	6.4	5.8	5.5	2.5	3.8	2.8
Real GDP growth (in percent)	4.0	7.2	6.8	4.1	3.4	3.1	2.9	2.7	2.7
Inflation (GDP deflator, in percent)	0.0	0.4	1.4	1.2	1.4	1.8	2.0	2.0	2.0
Nominal GDP growth (in percent)	4.3	7.6	8.4	5.4	4.9	5.0	5.0	4.7	4.7
Effective interest rate (in percent) [4]	3.9	2.9	2.6	2.7	2.5	2.3	2.1	2.1	2.3

As of March 19, 2019		
Sovereign Spreads		
EMBIG (bp) 3/		59
5Y CDS (bp)		36
Ratings	Foreign	Local
Moody's	A2	A2
S&Ps	A+	A+
Fitch	A+	A+

Contribution to Changes in Public Debt

	Actual			Projections							
	2008-2016	2017	2018	2019	2020	2021	2022	2023	2024	cumulative	debt-stabilizing primary balance [9]
Change in gross public sector debt	5.5	-5.0	-3.8	-3.0	-3.3	-1.6	-2.0	-2.9	-2.7	-15.6	
Identified debt-creating flows	4.7	-6.4	-4.8	-3.1	-3.3	-1.7	-2.1	-3.0	-2.8	-16.1	
Primary deficit	7.1	-1.6	-1.6	-1.5	-1.5	-1.5	-1.6	-1.8	-1.8	-9.6	-1.1
Primary (noninterest) revenue and grants	31.8	26.0	25.7	25.9	25.5	25.3	24.7	24.6	24.5	150.6	
Primary (noninterest) expenditure	38.9	24.4	24.1	24.4	24.0	23.8	23.1	22.8	22.8	141.0	
Automatic debt dynamics [5]	-1.5	-3.2	-3.7	-1.7	-1.4	-1.5	-1.5	-1.4	-1.2	-8.7	
Interest rate/growth differential [6]	-1.5	-3.2	-3.7	-1.7	-1.4	-1.5	-1.5	-1.4	-1.2	-8.7	
Of which: real interest rate	2.5	1.7	0.7	0.9	0.6	0.2	0.0	0.1	0.2	1.9	
Of which: real GDP growth	-3.9	-4.9	-4.3	-2.5	-2.0	-1.7	-1.6	-1.4	-1.3	-10.6	
Exchange rate depreciation [7]	0.0	0.0	0.0	…	…	…	…	…	…	…	
Other identified debt-creating flows	-1.0	-1.5	0.5	0.0	-0.4	1.3	1.0	0.1	0.1	2.2	
Privatization/Drawdown of Deposits (+ reduces financing need) (ne	-1.0	-1.5	0.5	-0.4	-1.4	0.3	0.1	0.1	0.1	-1.2	
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Stock/flow adjustment	0.0	0.0	0.0	0.5	1.0	1.0	0.9	0.0	0.0	3.3	
Residual, including asset changes [8]	0.8	1.4	1.0	0.1	0.1	0.1	0.1	0.1	0.1	0.5	



Source: IMF staff.

1/ Public sector is defined as general government.

2/ Based on available data.

3/ Long-term bond spread over German bonds.

4/ Defined as interest payments divided by debt stock (excluding guarantees) at the end of previous year.

5/ Derived as [(r - π(1+g) - g + ae(1+r)]/(1+g+π+gπ)) times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

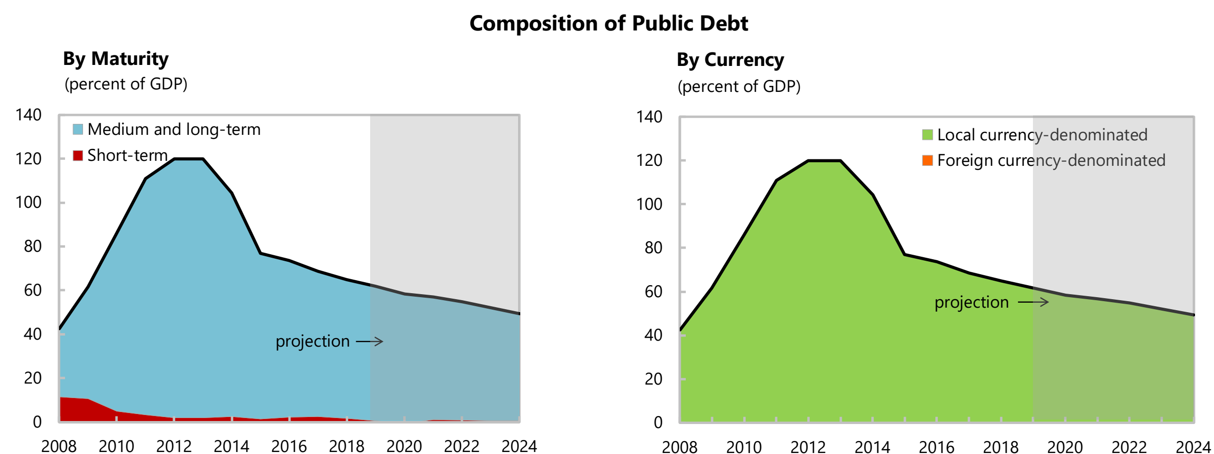
6/ The real interest rate contribution is derived from the numerator in footnote 5 as r - π (1+g) and the real growth contribution as -g.

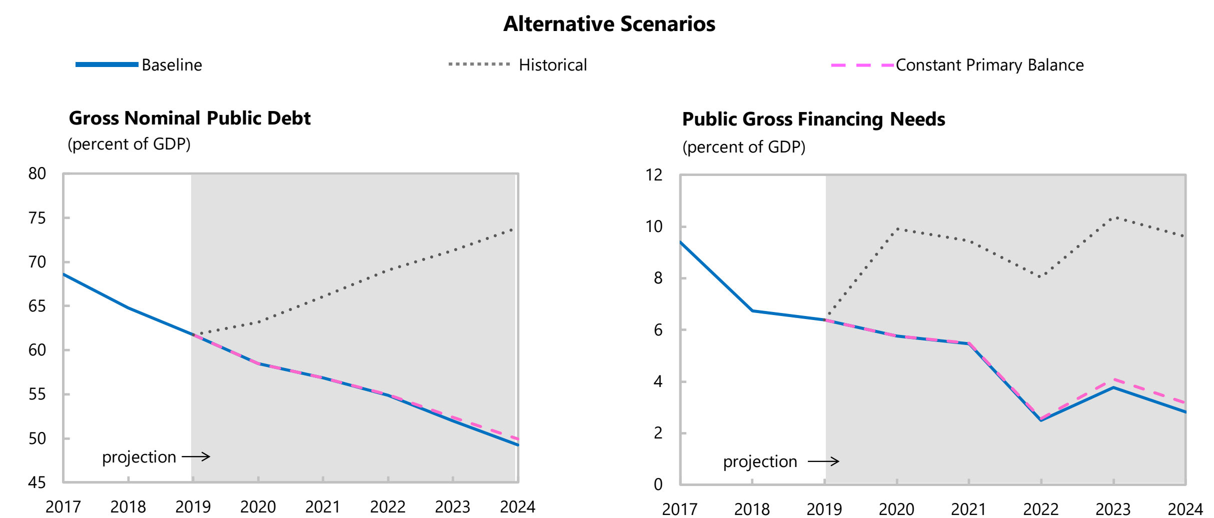
7/ The exchange rate contribution is derived from the numerator in footnote 5 as ae(1+r).

8/ Includes asset changes and interest revenues (if any). For projections, includes exchange rate changes during the projection period.

9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Figure 2. Ireland: Public DSA – Composition of Public Debt and Alternative Scenarios





Underlying Assumptions
(percent)

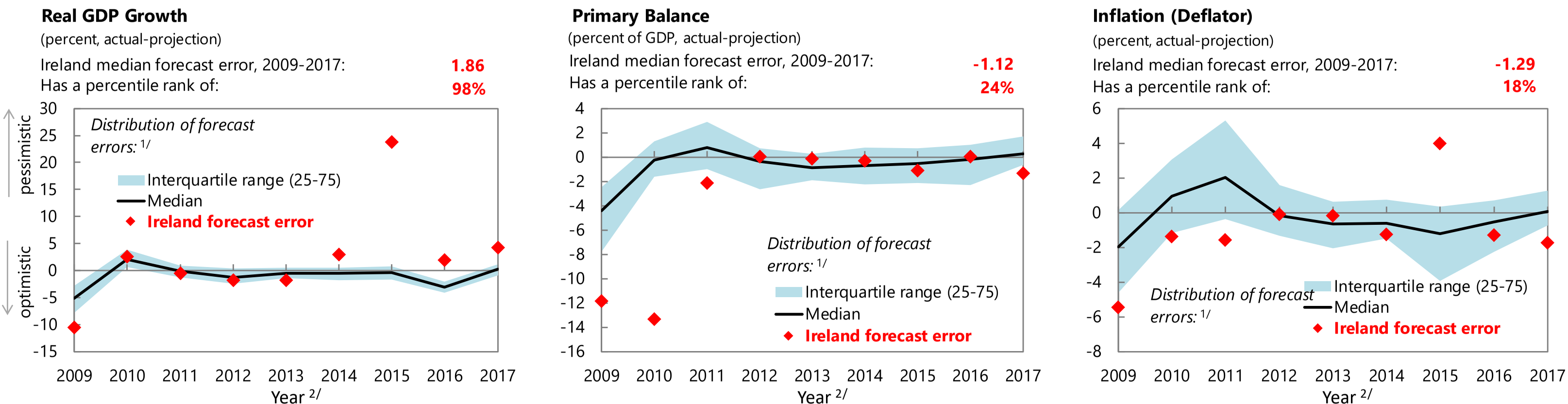
Baseline Scenario	2019	2020	2021	2022	2023	2024
Real GDP growth	4.1	3.4	3.1	2.9	2.7	2.7
Inflation	1.2	1.4	1.8	2.0	2.0	2.0
Primary Balance	1.5	1.5	1.5	1.6	1.8	1.8
Effective interest rate	2.7	2.5	2.3	2.1	2.1	2.3
Constant Primary Balance Scenario						
Real GDP growth	4.1	3.4	3.1	2.9	2.7	2.7
Inflation	1.2	1.4	1.8	2.0	2.0	2.0
Primary Balance	1.5	1.5	1.5	1.5	1.5	1.5
Effective interest rate	2.7	2.5	2.3	2.1	2.1	2.4

Historical Scenario	2019	2020	2021	2022	2023	2024
Real GDP growth	4.1	2.5	2.5	2.5	2.5	2.5
Inflation	1.2	1.4	1.8	2.0	2.0	2.0
Primary Balance	1.5	-2.6	-2.6	-2.6	-2.6	-2.6
Effective interest rate	2.7	2.5	2.6	3.0	3.3	3.8

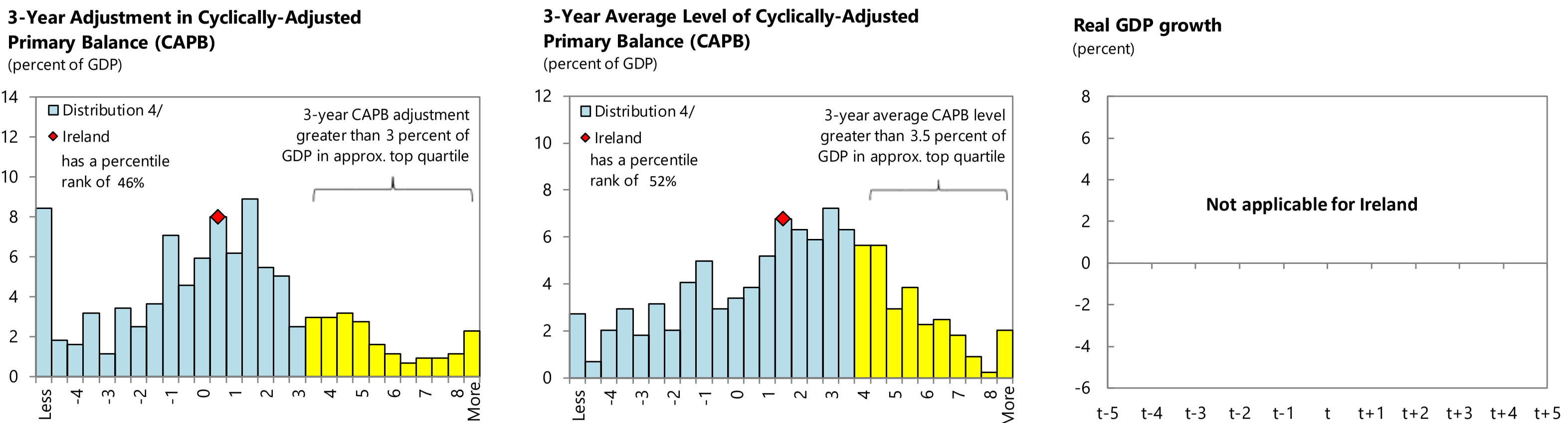
Source: IMF staff.

Figure 3. Ireland: Public DSA – Realism of Baseline Assumptions

Forecast Track Record, versus surveillance countries



Assessing the Realism of Projected Fiscal Adjustment



Boom-Bust Analysis 3/

Source : IMF Staff.

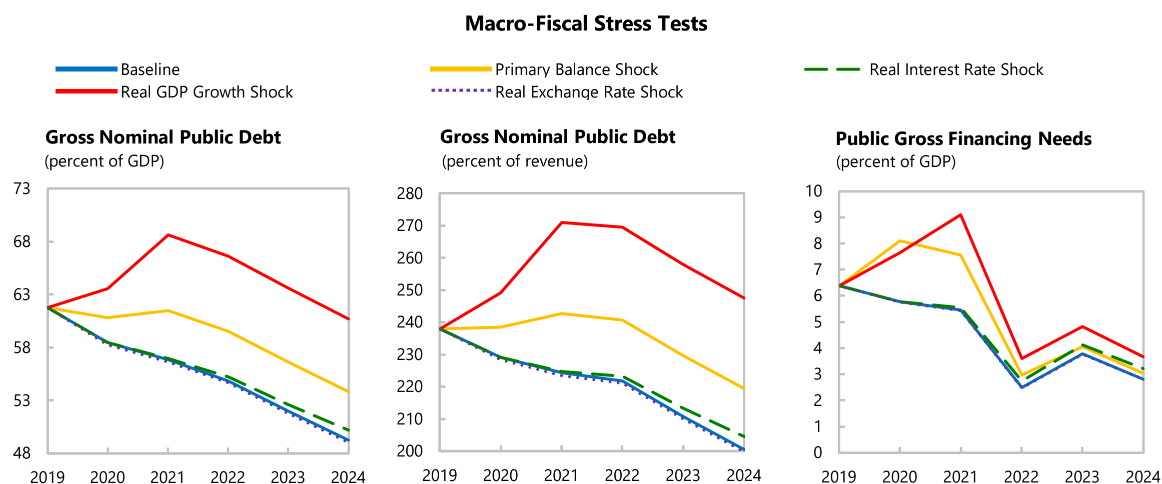
1/ Plotted distribution includes surveillance countries, percentile rank refers to all countries.

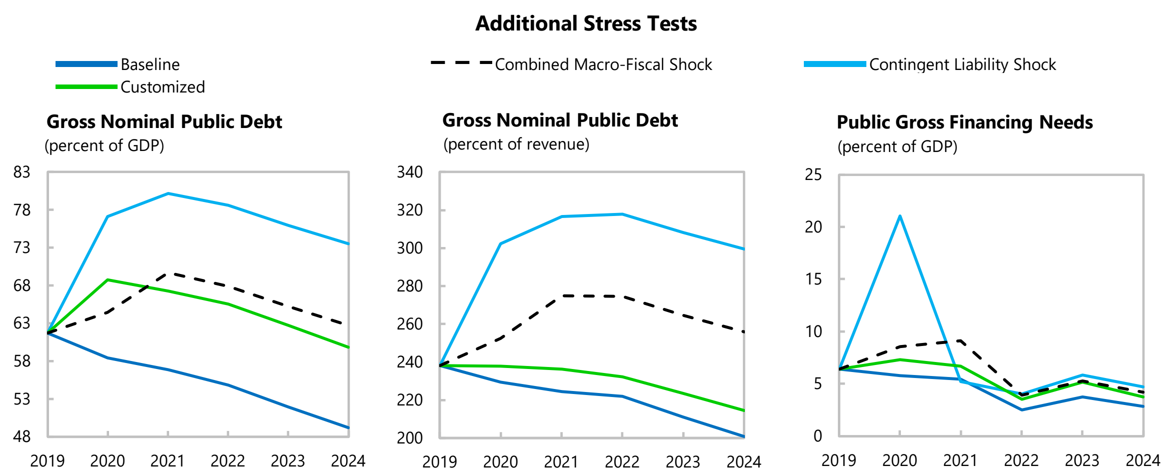
2/ Projections made in the spring WEO vintage of the preceding year.

3/ Ireland has had a positive output gap for 3 consecutive years, 2016-2018. For Ireland, t corresponds to 2019; for the distribution, t corresponds to the first year of the crisis.

4/ Data cover annual obervations from 1990 to 2011 for advanced and emerging economies with debt greater than 60 percent of GDP. Percent of sample on vertical axis.

Figure 4. Ireland: Public DSA – Stress Tests





Underlying Assumptions
(percent)

	2019	2020	2021	2022	2023	2024
Primary Balance Shock						
Real GDP growth	4.1	3.4	3.1	2.9	2.7	2.7
Inflation	1.2	1.4	1.8	2.0	2.0	2.0
Primary balance	1.5	-0.8	-0.8	1.6	1.8	1.8
Effective interest rate	2.7	2.5	2.3	2.3	2.3	2.5
Real Interest Rate Shock						
Real GDP growth	4.1	3.4	3.1	2.9	2.7	2.7
Inflation	1.2	1.4	1.8	2.0	2.0	2.0
Primary balance	1.5	1.5	1.5	1.6	1.8	1.8
Effective interest rate	2.7	2.5	2.5	2.6	2.7	3.0
Combined Shock						
Real GDP growth	4.1	-1.3	-1.6	2.9	2.7	2.7
Inflation	1.2	0.2	0.7	2.0	2.0	2.0
Primary balance	1.5	-0.8	-1.4	1.6	1.8	1.8
Effective interest rate	2.7	2.5	2.5	2.7	2.8	3.2
Customized						
Real GDP growth	4.1	-11.3	3.1	2.9	2.7	2.7
Inflation	1.2	1.4	1.8	2.0	2.0	2.0
Primary balance	1.5	1.1	1.4	1.3	1.5	1.8
Effective interest rate	2.7	2.5	2.3	2.2	2.2	2.4

	2019	2020	2021	2022	2023	2024
Real GDP Growth Shock						
Real GDP growth	4.1	-1.3	-1.6	2.9	2.7	2.7
Inflation	1.2	0.2	0.7	2.0	2.0	2.0
Primary balance	1.5	0.0	-1.4	1.6	1.8	1.8
Effective interest rate	2.7	2.5	2.3	2.3	2.3	2.5
Real Exchange Rate Shock						
Real GDP growth	4.1	3.4	3.1	2.9	2.7	2.7
Inflation	1.2	1.8	1.8	2.0	2.0	2.0
Primary balance	1.5	1.5	1.5	1.6	1.8	1.8
Effective interest rate	2.7	2.5	2.3	2.1	2.1	2.3
Contingent Liability Shock						
Real GDP growth	4.1	-1.3	-1.6	2.9	2.7	2.7
Inflation	1.2	0.2	0.7	2.0	2.0	2.0
Primary balance	1.5	-13.2	1.5	1.6	1.8	1.8
Effective interest rate	2.7	2.7	2.9	3.2	3.2	3.4

Source: IMF staff.

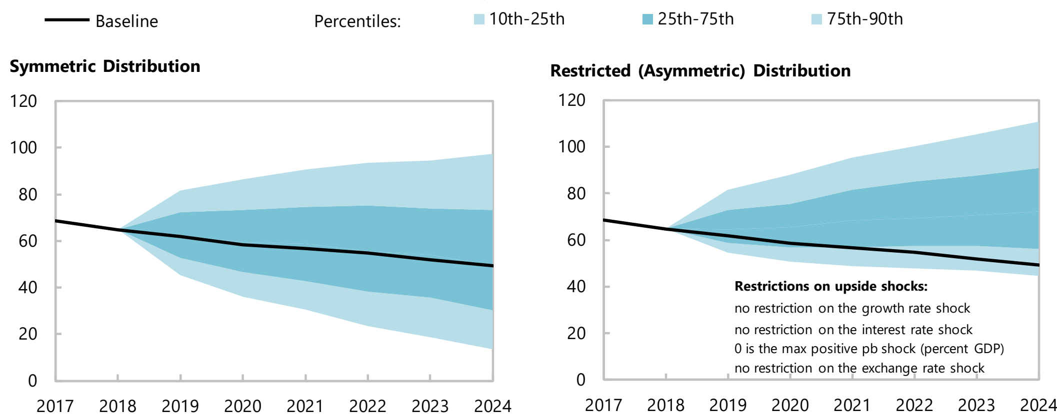
Figure 5. Ireland: Public DSA – Risk Assessment

Heat Map

Debt level [1/]	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability shock
Gross financing needs [2/]	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability Shock
Debt profile [3/]	Market Perception	External Financing Requirements	Change in the Share of Short-Term Debt	Public Debt Held by Non-Residents	Foreign Currency Debt

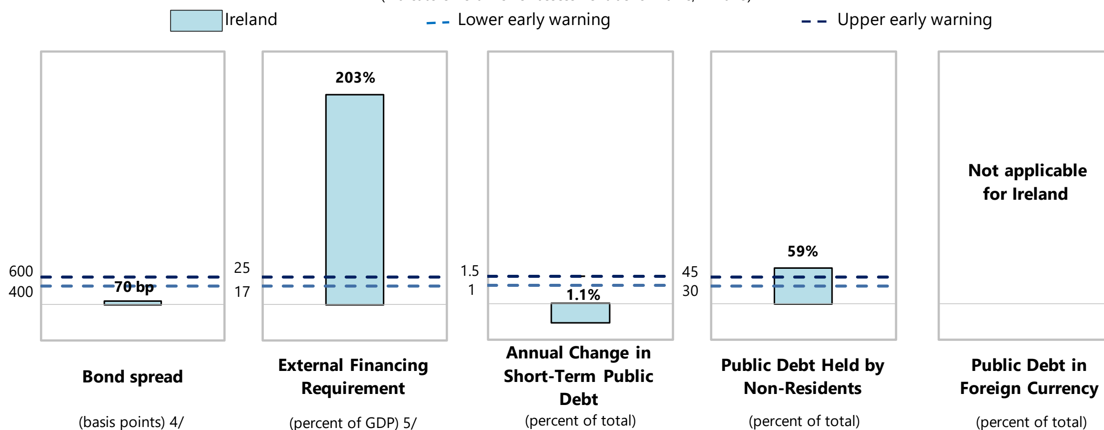
Evolution of Predictive Densities of Gross Nominal Public Debt

(percent of GDP)



Debt Profile Vulnerabilities

(indicators vis-à-vis risk assessment benchmarks, in 2018)



Source: IMF staff.

1/ The cell is highlighted in green if debt burden benchmark of 85% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

2/ The cell is highlighted in green if gross financing needs benchmark of 20% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

3/ The cell is highlighted in green if country value is less than the lower risk-assessment benchmark, red if country value exceeds the upper risk-assessment benchmark, yellow if country value is between the lower and upper risk-assessment benchmarks. If data are unavailable or indicator is not relevant, cell is white.

Lower and upper risk-assessment benchmarks are:

400 and 600 basis points for bond spreads; 17 and 25 percent of GDP for external financing requirement; 1 and 1.5 percent for change in the share of short-term debt; 30 and 45 percent for the public debt held by non-residents.

4/ Long-term bond spread over German bonds, an average over the last 3 months, 19-Dec-18 through 19-Mar-19.

5/ External financing requirement is defined as the sum of current account deficit, amortization of medium and long-term total external debt, and short-term total external debt at the end of previous period.

Annex II. External Stability Assessment

Ireland's large current account surplus widened somewhat further in 2018, driven by an improvement in the services balance. Staff nevertheless considers Ireland's external position to be broadly consistent with medium-term fundamentals and desirable policy settings—a conclusion that takes into account an expected downward revision of the current account surplus once more information about the operations of MNEs becomes available. Given the volatility of the data and the role of multinationals in affecting the current account balance, this assessment is subject to considerable uncertainty.

1. **Ireland's current account surplus widened modestly last year.** Preliminary data indicate that the surplus increased from 8.5 percent of GDP in 2017 to 9.1 percent of GDP in 2018. The improvement was driven by strong growth in exports of computer services, which helped to reduce the deficit in the services balance and a boost in pharmaceutical exports. The narrowing of the deficit in services was partially offset by a decline in the merchandise trade surplus. The primary and secondary income balances were roughly unchanged.

2. **Ireland's recent balance of payments (BOP) data have been subject to major revisions, complicating the analysis of its external position.** BOP data for 2015–17 underwent significant revisions last year, with the headline current account balance revised lower by between 4 and 7½ percentage points (Table 1). For the year 2016, the initially reported current account surplus of 3.3 percent of GDP was revised to a deficit of 4.2 percent. For all three years, the revisions to the current account were concentrated in the services balance (both service imports and exports) and, to a lesser degree, in the primary income balance (mainly direct investment income outflows). These revisions took place once more complete information about the activities of MNEs became available.

Table 1. Revisions to Ireland's Balance of Payments, 2015–17
(Percent of GDP)

	Initial			Revised			Change		
	2015	2016	2017	2015	2016	2017	2015	2016	2017
Current account balance	10.9	3.3	12.5	4.4	-4.2	8.5	-6.5	-7.5	-4.1
Balance of goods and services	33.2	22.0	32.2	28.9	15.5	30.4	-4.3	-6.5	-1.8
Trade balance	43.3	38.5	36.3	43.3	38.9	36.7	-0.1	0.4	0.4
Services balance	-10.2	-16.4	-4.1	-14.4	-23.4	-6.2	-4.2	-6.9	-2.1
Primary income balance	-20.9	-17.3	-18.2	-23.2	-18.3	-20.4	-2.2	-1.0	-2.2
Current transfers (net)	-1.3	-1.4	-1.4	-1.3	-1.4	-1.6	0.0	0.0	-0.1
Capital account balance	-0.5	-1.8	-9.1	-0.5	-1.6	-9.6	0.0	0.3	-0.5
Financial account balance	8.6	4.3	-0.3	2.4	-3.1	1.6	-6.2	-7.4	1.9
Direct investment	-16.4	4.9	-3.1	-17.0	-3.1	-11.4	-0.6	-8.0	-8.3
Portfolio investment	-44.6	12.4	-28.4	-33.7	10.2	-18.8	10.9	-2.3	9.6
Other investment	69.4	-13.5	31.1	52.9	-10.7	31.7	-16.5	2.9	0.6
Reserve assets	0.2	0.5	0.1	0.2	0.5	0.1	0.0	0.0	0.0
Net errors and omissions	-1.8	2.8	-3.7	-1.5	2.7	2.7	0.3	-0.1	6.4

3. For the purposes of this external stability assessment, staff adjusted the 2018 headline current account surplus downward, roughly in proportion to previous years' revisions.[1] To approximate the size of the expected revision, staff examined the historical relationship between the goods and services balance and the primary income balance. Between 2013–17, this ratio has been relatively stable, averaging 1.2 (post data revisions). Applying the same ratio to preliminary 2018 data, while holding the goods and services balance steady, leads to a 5½ percentage point downward revision to the primary income balance. This revision is consistent with expectations that robust pharmaceutical exports will contribute to high MNE profits that will ultimately be recorded as outflows in the primary income balance. The adjustment to the primary income balance results in a downward revision to the current account surplus from 9.1 percent to 3.4 percent, equivalent to €11 billion.[2]

4. Based on this adjustment, staff assesses Ireland's external position to be broadly consistent with medium-term fundamentals and desirable policy settings. The EBA model estimates that Ireland's cyclically adjusted current account norm was 2.9 percent of GDP in 2018, compared to a cyclically adjusted current account of 9.6 percent of GDP, implying a current account gap of 6.7 percent (Table 2). However, if one assumes a revision of the current account surplus to 3.4 percent of GDP, the gap is reduced to 1.0 percent. About a third of the 6.7 percent gap identified by the model is explained by policy variables—mainly credit and fiscal gaps—while the rest is attributed to unexplained residuals. The credit gap should be interpreted with caution given the impact of Ireland's mid-2000s credit bubble on statistical measures of credit trends. The fiscal gap points to policy distortions (overly loose fiscal policy) in the rest of the world.

Table 2. External Sector Assessment, 2018
(Percent of GDP)

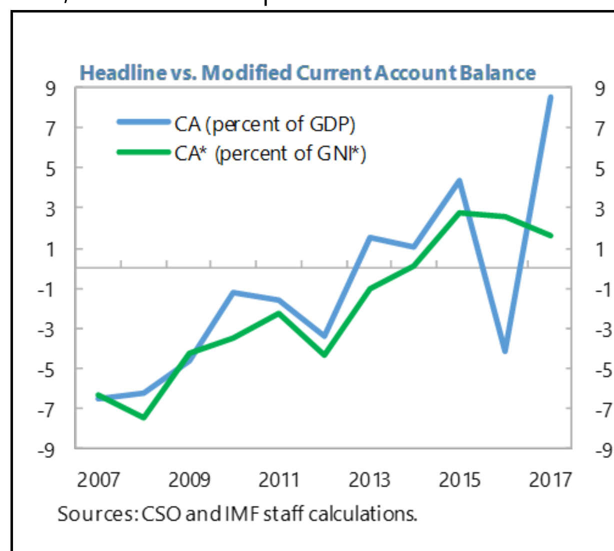
	Model results	Staff adjustment
Actual CA	9.1	**3.4**
Cyclical Contribution	-0.5	-0.5
Cyclically adjusted CA	9.6	**3.9**
Cyclically adjusted CA norm 1/	2.9	2.9
CA Gap	6.7	**1.0**
Policy gaps	2.2	2.2
Credit gap	1.9	1.9
Fiscal gap	0.4	0.4
Other gaps	-0.1	-0.1
Unexplained residual	4.5	-1.2
Total CA gap range 2/	[5.3%, 8,3%]	**[-0.5%, 2.5%]**

Sources: CSO and IMF staff calculations.
1/ Based on IMF EBA model results as of February 8, 2019.
2/ Total CA gap +/- 1.5 percent of GDP.

[1] The approach taken here, which anticipates revisions to the BOP data, differs from the approach adopted by staff in the 2018 Article IV consultation report, which was based on deriving a modified current account balance (CA*) excluding the activities of MNEs. Given the magnitude of the revisions to the BOP data for 2015–17, including the CA* balance, which came to light following the 2018 Article IV consultation, staff's view is that last year's approach is no longer the most appropriate.

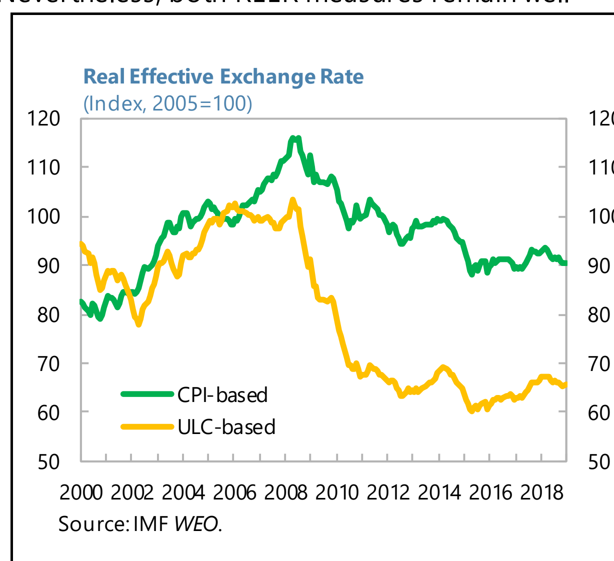
[2] Alternatively, holding the primary income balance steady while adjusting the goods and services balance to arrive at the 1.2 ratio leads to a downward revision of the current account surplus to 2.3 percent. Adopting this alternative methodology would not fundamentally alter the conclusion of this assessment. By comparison, the authorities' preliminary estimate of the 2018 current account surplus excluding the activities of multinationals (CA*) amounted to about €9 billion (see paragraph 5).

5. The assessment of Ireland's external position is clouded by the large-scale operations of multinationals, which have limited links to the domestic economy and distort the headline current account balance. To account for these effects, the authorities produce a modified current account balance (CA*), which can be compared to a modified version of gross national income (GNI*) to get a picture of Ireland's external position abstracting from the operations of multinationals. In 2017, CA* fell to 1.2 percent of GNI* from 2.6 percent in 2016 even as the headline current balance improved sharply, underscoring the challenges of interpreting Ireland's BOP.[3] The depreciation of foreign-owned domestic capital (related to net imports of intellectual property and imports of R&D services) accounts for much of the divergence between the headline current account balance and CA*.



Sources: CSO and IMF staff calculations.

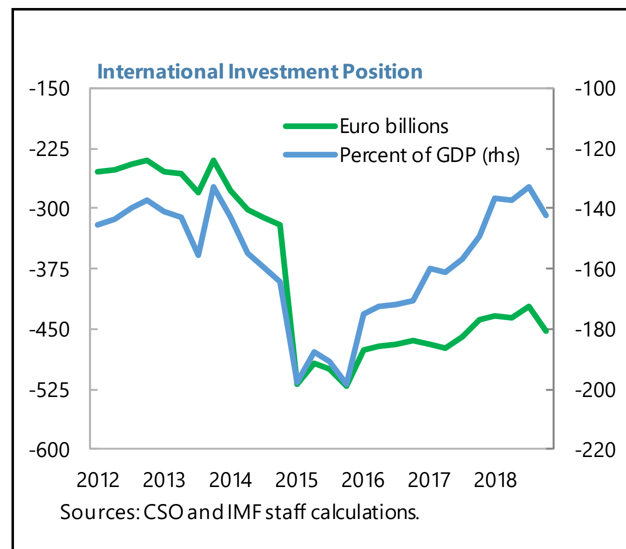
6. Ireland's REER appreciated modestly in 2018, both on a CPI and ULC basis. The CPI-based REER appreciated by 0.5 percent, while the ULC-based REER appreciated by 2.6 percent, continuing its modest upward trends since 2015. Nevertheless, both REER measures remain well below their long-term averages, reflecting competitiveness gains since the global financial crisis. The EBA REER Index approach points to an undervaluation of 9.8 percent, whereas the REER level approach yields an overvaluation of 15.6 percent. However, the explanatory power of policy variables is negligible in both cases, with the gaps almost entirely attributed to unexplained residuals in the models. Based on the staff-adjusted current account gap range of -0.5 percent to 2.5 percent of GDP, the REER is deemed to be close to its equilibrium value (ranging from an undervaluation of 2.7 percent to an overvaluation of 0.5 percent, using an elasticity of 0.92).



Source: IMF *WEO*.

[3] Preliminary estimates for 2018 suggest a CA* equal to about 4.6 percent of GNI*.

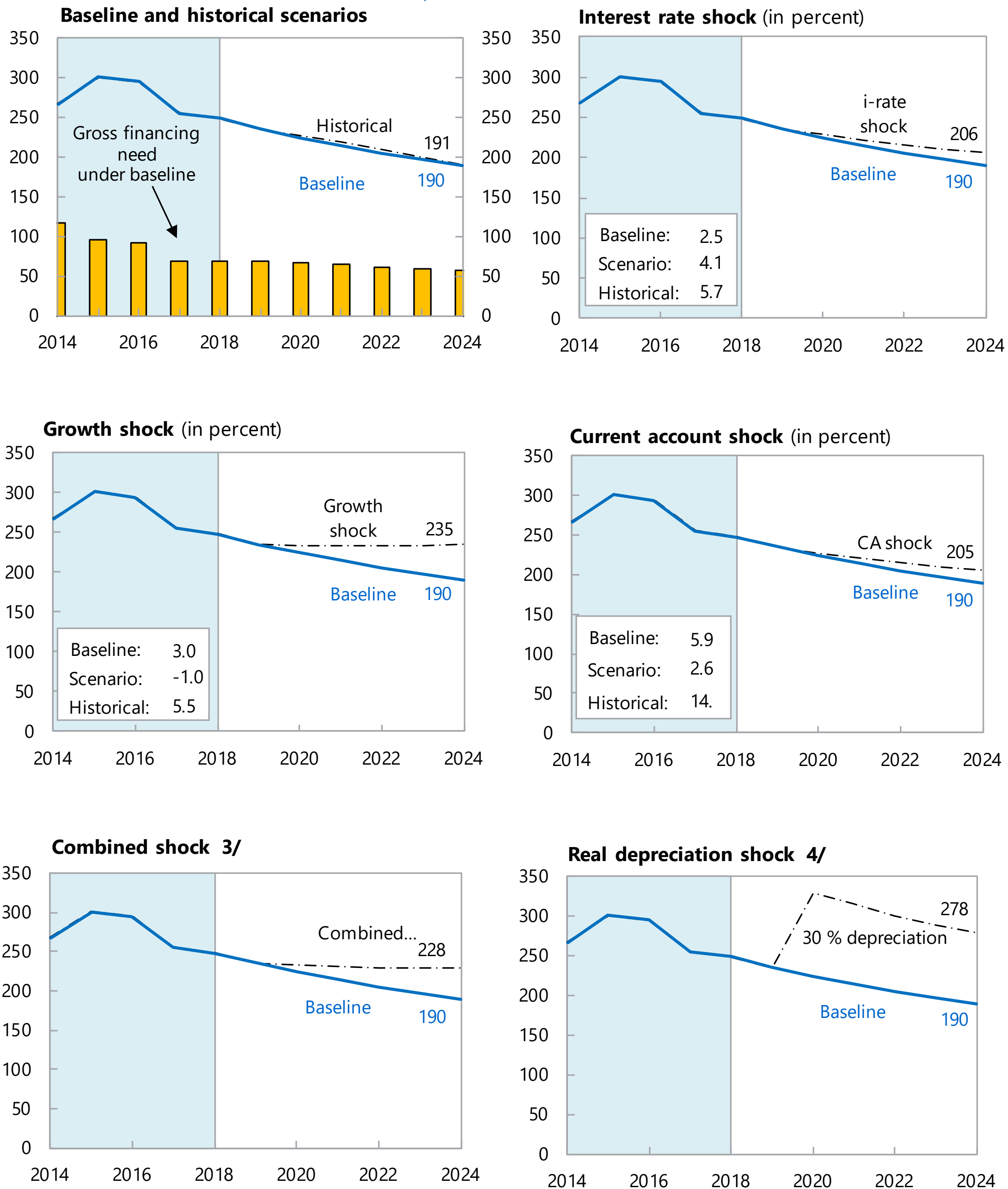
7. Ireland's net international investment position (NIIP), albeit deeply negative, continued to improve. At end-2018, the NIIP stood at an estimated -142 percent of GDP compared to nearly -200 percent of GDP in 2015. The improvement in the NIIP in recent years relates mainly to the growing foreign assets of the central bank and monetary financial institutions. The EBA's External Sustainability (ES) approach estimates that the current account norm sufficient to stabilize Ireland's net foreign assets (NFA) at a benchmark level of -91 percent of GDP is a deficit of 4.8 percent of GDP. This implies a gap of 8.2 percentage points relative to the revised current account surplus of 3.4 percent of GDP derived above. Assuming an elasticity of 0.92, the ES approach leads to an REER undervaluation of 9 percent. However, staff considers the ES approach less relevant for Ireland because of the country's role as a financial center and hub for MNEs.



Sources: CSO and IMF staff calculations.

	Ireland	Overall Assessment
Foreign asset and liability position and trajectory	**Background**. Ireland's net international investment position (NIIP), after declining to -199 percent of GDP in 2015 due to MNE-related restructuring operations, continued to improve in 2018, reaching -142 percent of GDP.[1] The NIIP excluding the International Financial Services Centers (IFSC) narrowed to -102.5 percent of GDP, while the IFSC NIIP worsened to -39.9 percent. Non-IFSC gross external debt was equal to 248 percent, down from a peak of 301 percent in 2015, and is projected to decline further over the medium term, reflecting current account surpluses, real GDP growth, and non-debt-creating capital inflows. **Assessment**. Ireland's NIIP reflects the activities of MNEs and market-based finance entities with few linkages to the Irish economy. Large gross IFSC positions do not affect domestic entities, and a large stock of IFSC intra-company and intra-group debt is regularly rolled over, mitigating risks. Stripping away the balance sheets of so-called "pass-through" entities (whose assets are located mainly outside Ireland and whose liabilities are mostly to foreign residents) results in an NIIP that is considerably less negative.[2]	**Overall assessment**: *Ireland's external position in 2018 was broadly consistent with medium-term fundamentals and desirable policy settings*. However, given the volatility of the data and the role of MNEs in distorting the current account balance, this assessment is subject to considerable uncertainty. Ireland's competitiveness has improved in recent years, as demonstrated by an increasing share of Irish exports in world exports. External balance sheets have strengthened, and FDI inflows continue to be strong, supported by a favorable business climate and robust economic growth. Productivity growth, however, varies sharply across sectors and is concentrated in large foreign-owned firms. **Potential policy responses**: To promote sustainable and inclusive growth, policies should focus on repairing banks' balance sheets, restoring fiscal buffers, broadening access to finance for indigenous SMEs, increasing public support for innovation, continuing targeted ALMPs, expanding technical and vocational training, and improving infrastructure (transportation and housing).
Current account	**Background**. The current account (CA) has averaged a surplus of 3½ percent of GDP since the 2013 recovery began, reflecting a large goods trade surplus. Ireland's share of world exports has been increasing, driven by exports of pharmaceutical products, business and financial services, and computer services. The CA surplus widened to 9.1 percent in 2018, as strong growth in exports of computer services helped to reduce the deficit in the services balance. The CA is projected to remain in surplus over the medium term but narrow somewhat. **Assessment**. CA surpluses for 2015–17 were subject to significant downward revisions last year, complicating the analysis of Ireland's external position. The 2018 cyclically-adjusted CA balance was 9.6 percent of GDP compared to the CA norm of 2.9, resulting in a CA gap of 6.7 percent of GDP. However, staff anticipates that the headline CA surplus will be revised downward once more complete information about the activities of MNEs becomes available. This expected revision would reduce the CA gap to 1.0 percent. The assessment of Ireland's external position is further complicated by the large-scale operations of MNEs, which have limited links to the domestic economy and distort the headline current account balance.	
Real exchange rate (REER)	**Background**. The ULC-based REER depreciated sharply following the global financial crisis, reflecting productivity gains and declining labor costs. Productivity growth, however, has been concentrated in large foreign-owned firms.[3] Since 2015, both the ULC-based and CPI-based REERs have appreciated modestly. In 2018, the CPI-based REER appreciated by 0.5 percent, while the ULC-based REER appreciated by 2.6 percent. **Assessment**. The EBA REER Index approach points to an undervaluation of 9.8 percent, whereas the REER level approach yields an overvaluation of 15.6 percent. However, the explanatory power of policy variables is negligible in both cases, with the gaps almost entirely attributed to unexplained residuals in the models. Based on the staff-adjusted current gap range of -0.5 percent to 2.5 percent of GDP, the REER is deemed to be close to its equilibrium value (ranging from an undervaluation of 2.7 percent to an overvaluation of 0.5 percent, using an elasticity of 0.92).	
Capital and financial accounts: flows and policy measures	**Background**. Ireland's capital and financial accounts are characterized by extreme volatility. In 2018, negative FDI inflows in Ireland increased sharply, driven by large repatriations of earnings by U.S. companies following changes to U.S. tax law. Consequently, net direct investment swung from -11.4 percent of GDP in 2017 to 21 percent in 2018. Other investments (on a net basis) moved in the opposite direction, turning sharply negative as liabilities spiked. The capital and financial accounts are heavily influenced by the operations of MNEs and have been subject to significant data revisions. **Assessment**. Inward FDI and foreign demand for Irish sovereign bonds have been supported by Ireland's strong economic performance and investor-friendly business climate, including a favorable tax environment.	
FX intervention and reserves	**Background**. The euro has the status of a global reserve currency. **Assessment**. Reserves held by the euro area are typically low relative to standard metrics. The currency is free floating.	
Technical Background Notes	1/ For more information about the impact of MNEs on Ireland's NIIP, see "The Role of Foreign-owned Multinational Enterprises in Ireland," IMF Country Report No. 17/172. 2/ See Galstyan, V., 2019, "Estimates of Foreign Assets and Liabilities for Ireland," Central Bank of Ireland and Trinity College Dublin. 3/ See "Firm-level Productivity and its Determinants: The Irish Case," IMF Country Report No. 16/257.	

Figure 1. Ireland: External Debt Sustainability; Bound Tests 1/ 2/
(Non-IFSC external debt in percent of GDP, unless otherwise indicated)



Source: IMF staff.
1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.
3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.
4/ One-time real depreciation of 30 percent occurs in 2019.

Table 3. Ireland: Non-IFSC External Debt Sustainability Framework, 2014–24

(Percent of GDP, unless otherwise indicated)

	Actual					Projections						
	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	Debt-stabilizing non-interest current account 6/
Baseline: External debt	267.2	300.9	294.4	255.0	248.0	**235.1**	**224.4**	**214.5**	**205.2**	**197.2**	**189.8**	**-6.1**
Change in external debt	-8.8	33.7	-6.4	-39.4	-7.0	-13.0	-10.6	-10.0	-9.2	-8.0	-7.3	
Identified external debt-creating flows (4+8+9)	-12.6	-25.0	-7.2	-46.1	-23.2	-13.9	-10.9	-9.3	-8.3	-7.2	-6.5	
Current account deficit, excluding interest payments	-13.1	-29.5	-4.8	-14.6	-11.2	-8.5	-6.3	-5.9	-5.8	-5.7	-5.6	
Deficit in balance of goods and services	-11.4	-23.4	-9.8	-25.0	-23.6	-22.7	-22.0	-21.8	-21.8	-21.6	-21.4	
Exports	95.0	109.1	106.9	106.8	105.8	106.1	105.1	104.7	104.5	104.5	104.6	
Imports	83.6	85.6	97.1	81.7	82.2	83.5	83.0	82.9	82.7	82.9	83.2	
Net non-debt creating capital inflows (negative)	5.8	-0.8	-3.8	-14.4	10.6	-1.9	-1.8	-1.7	-1.6	-1.6	-1.5	
Automatic debt dynamics 1/	-5.3	5.3	1.4	-17.1	-22.6	-3.5	-2.8	-1.7	-0.9	0.1	0.5	
Contribution from nominal interest rate	16.6	34.4	12.5	9.2	7.5	6.6	4.8	4.9	5.0	5.3	5.6	
Contribution from real GDP growth	-22.2	-59.6	-14.3	-19.3	-15.4	-10.1	-7.6	-6.6	-5.9	-5.3	-5.0	
Contribution from price and exchange rate changes 2/	0.4	30.5	3.2	-7.0	-14.7	...	...	...	...	...	...	
Residual, incl. change in gross foreign assets (2-3) 3/	3.8	58.7	0.8	6.7	16.3	1.0	0.3	-0.7	-0.9	-0.8	-0.8	
External debt-to-exports ratio (in percent)	281.3	275.8	275.4	238.9	234.4	221.5	213.6	204.8	196.4	188.7	181.4	
Gross external financing need (in billions of US dollars) 4/	229.5	248.8	249.8	204.0	216.9	230.8	233.6	235.4	237.0	239.3	242.2	
in percent of GDP	117.7	94.9	91.5	69.5	68.2	68.8	66.4	63.7	61.1	58.9	57.0	
Scenario with key variables at their historical averages 5/						**235.1**	**226.7**	**218.3**	**209.5**	**200.1**	**190.9**	**0.4**
Key Macroeconomic Assumptions Underlying Baseline												
Real GDP growth (in percent)	8.8	25.0	4.9	7.2	6.8	4.1	3.4	3.1	2.9	2.7	2.7	
GDP deflator in US dollars (change in percent)	-0.2	-10.2	-1.1	2.4	6.1	-3.5	2.1	2.7	2.8	2.6	2.8	
Nominal external interest rate (in percent)	6.5	14.5	4.3	3.4	3.4	2.7	2.2	2.3	2.5	2.7	3.0	
Growth of exports (US dollar terms, in percent)	15.6	54.3	2.0	7.5	7.4	5.6	3.9	4.6	4.7	4.8	4.8	
Growth of imports (US dollar terms, in percent)	18.9	37.6	18.0	-9.4	9.1	6.9	4.4	4.8	4.7	5.0	5.1	
Current account balance, excluding interest payments	13.1	29.5	4.8	14.6	11.2	8.5	6.3	5.9	5.8	5.7	5.6	
Net non-debt creating capital inflows	-5.8	0.8	3.8	14.4	-10.6	1.9	1.8	1.7	1.6	1.6	1.5	

Source: IMF staff.

1/ Derived as [r - g - r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock, with r = nominal effective interest rate on external debt; r = change in domestic GDP deflator in US dollar terms, g = real GDP growth rate, e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.

2/ The contribution from price and exchange rate changes is [-r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock. r increases with an appreciating domestic currency (e > 0) and rising inflation (based on GDP deflator).

3/ For projection, line includes the impact of price and exchange rate changes.

4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

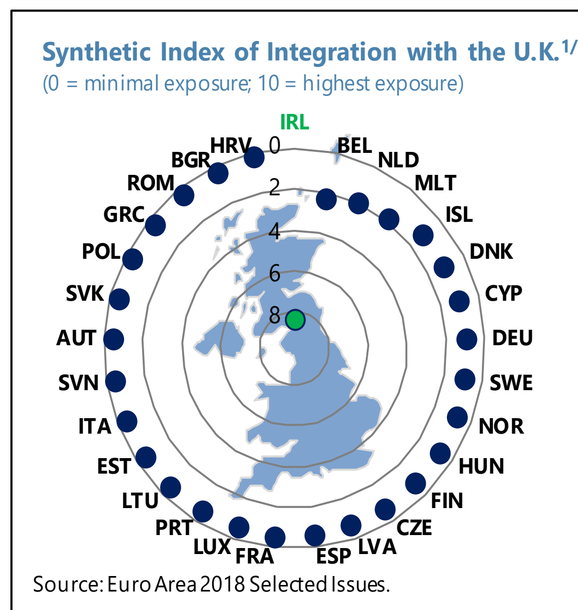
5/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

6/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

Annex III. How Would a No-Deal Brexit Affect Ireland's Economy?

1. Ireland is the EU country most exposed to a no-deal Brexit. Its close economic ties with the U.K. make it highly vulnerable to a disorderly Brexit scenario where all existing cooperation agreements between the EU and the U.K. cease to apply. Ireland's economic integration with the U.K. can be measured in different ways:

- **Trade linkages.** The U.K. is Ireland's second largest export destination and its largest import partner, accounting for nearly a fifth of all Irish trade in goods. Regarding trade in services, the U.K. is Ireland's largest export market and third-largest importer. Compared to other EU countries, only Luxembourg trades more with the U.K. as a percent of GDP. Ireland's exports of value-added to the U.K. as a percent of GDP surpass all other EU countries.
- **Financial linkages.** Ireland's two-way FDI stock with the U.K. (both inward and outward FDI) is the second largest in the EU relative to GDP. Two-way portfolio investments between Ireland and the U.K. are equal to over 200 percent of Ireland's GDP—by far the largest ratio in the EU and around ten times the EU average. The U.K. is the second largest market for Irish banks, accounting for a quarter of their credit exposure. Also, a quarter of the total assets of Irish investment funds and special purpose entities is invested in the U.K., while U.K, ultimate investors hold 12 percent of the total claims on Irish funds.[1]
- **Migration.** Ireland is host to a sizable British diaspora, equal to around 6 percent of Ireland's total population—the largest share in the EU for which data is available. Nearly half of these migrants are high-skilled. Conversely, Ireland has sent a larger percentage of its citizens to the U.K. than any other EU country.



Synthetic Index of Integration with the U.K.[1/]
(0 = minimal exposure; 10 = highest exposure)

Source: Euro Area 2018 Selected Issues.

2. Ireland stands out in a measure of economic integration with the U.K. Chen et al. (2018) constructed a synthetic index, measuring a country's economic integration with the U.K.[2] The index combines several indicators of integration (trade in domestic value-added, participation in supply chains, openness in service trade, cross-border banking position, and migration) and is rescaled so that a country's exposure ranges from 0 (minimal exposure) to 10 (highest exposure). Within the EU, Ireland's economy is by far the most integrated with the U.K. Moreover, the degree of integration has increased over time.

[1] See IMF Coordinated Portfolio Investment Survey, Table 8.

[2] See Chen, J. and others, 2018, "The Long-term Impact of Brexit on the EU," IMF Country Report No. 18/224.

3. A no-deal Brexit would affect Ireland through multiple channels:[3]

- **Trade.** A disorderly Brexit would reduce demand for Irish exports due to slower growth in the U.K., high tariff and non-tariff barriers, and exchange rate effects. The Bank of England estimates that, in a worst-case scenario, U.K. growth could fall by 8 percent in the first year and sterling would depreciate by 25 percent.[4] Such an outcome would have severe negative consequences for Irish exporters. Irish firms also depend heavily on imports of intermediate goods from the U.K. [5] In addition, the U.K. land bridge is used extensively to transport goods between Ireland and the continent. A disorderly Brexit that occurred before new border infrastructure and customs procedures were in place could disrupt supply chains and lead to delays at the border, potentially resulting in higher costs for Irish consumers. Border delays would have an especially adverse impact on agricultural products and pharmaceuticals.

- **Consumer spending and investment.** A disorderly Brexit would heighten economic uncertainty and dampen business and consumer confidence, causing firms to delay or cancel investment plans and consumers to cut spending. These effects would combine to reduce economic output.

- **Financial sector.** A disorderly Brexit would likely lead to financial market volatility, with possible spillover effects to other markets. A weaker sterling, while helping the U.K.'s economy adjust, would have negative implications for Irish competitiveness. Tighter financial market conditions would imply higher borrowing costs for firms and households, dampening economic activity. Irish banks could come under pressure from their exposures to the U.K. and to weakened domestic SMEs. Some real estate investment funds, especially those with higher leverage, could face funding pressures. A no-deal Brexit also poses risks to the continuity of financial services, though most of these risks have been mitigated by proactive policy actions. Most importantly, the U.K. and European regulators have signed an agreement that would allow continued delegation of asset management services as well as selling of fund shares in the event of a no-deal Brexit.

4. The impact of a no-deal Brexit on Ireland's economy would likely be severe. Various studies suggest that a disorderly Brexit would have a significant negative impact on the Irish economy in the short run and reduce output in the long run. Chen et al. (2018) estimated that higher tariffs and non-tariff barriers alone would cause Ireland's output to fall by nearly 4 percent in the long run—much more than in other EU countries. The Central Bank of Ireland estimated that a no-deal Brexit would reduce Irish growth by up to 4 percentage points in the first full year and lower output by 6 percent in the long run. Other studies put long-term output losses at between 2 and 7 percent.[6] Given the unprecedented nature of Brexit, these estimates are subject to significant

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[3] See Central Bank of Ireland, 2019, Quarterly Bulletin QB1 – 2019

[4] See Bank of England, 2018, "EU Withdrawal Scenarios and Monetary and Financial Stability."

[5] For Irish-owned firms, more than half of total imports from the UK are intermediate inputs. See Lawless, M., 2018, "Intermediate Goods Inputs and UK Content of Irish Goods Exports."

[6] See Bisciari, P., "A Survey of the Long-term Impact of Brexit on the UK and on the EU27 Economies," National Bank of Belgium Working Paper 366.

uncertainty. The short-term effects of a no deal depend crucially on the extent the U.K. and EU authorities enforce third-country rules. A no-deal Brexit could also take different forms—for example, with or without an extension of Article 50 to allow time to prepare, and with or without policy cooperation between the EU and U.K. to minimize disruptions.

5. The Irish government has taken steps to prepare the country for a disorderly Brexit. The Central Bank of Ireland established a Brexit Task Force in 2016 to assess the risks arising from different Brexit scenarios. The government recently published a set of emergency laws that will be enacted if the U.K. leaves the EU without a deal, including a measure that would allow the government to assist stricken businesses. The European Commission has indicated that certain state aid regulations may be relaxed, paving the way for such government support without prior Commission approval. Other measures are aimed at maintaining financial markets settlements, insurance contracts, and electricity supplies. The government has also created online tools to help businesses and households prepare. A key risk, however, is that many firms will choose not to incur the cost of preparing for a scenario that may never materialize.

Annex IV. Risk Assessment Matrix[1]

Source of Risk and Likelihood (G-RAM)	Impact if Realized	Policy Recommendations Mitigation/Response
Medium ***Short- to medium-term*** **Rising protectionism and retreat from multilateralism:** In the near term, escalating and sustained trade actions threaten the global trade system, regional integration, as well as global and regional collaboration. Additional barriers and the threat of new actions reduce growth both directly and through adverse confidence effects (increasing financial market volatility). In the medium term, geopolitical competition and fraying consensus about the benefits of globalization lead to economic fragmentation and undermine the global rules-based order, with adverse effects on growth and stability.	**High** Ireland is highly integrated into global value chains and its production base is concentrated in a small number of sectors. This leaves the Irish economy and public finances vulnerable to a broad range of common and idiosyncratic shocks. Depending on the nature of the shock, the role of MNEs could mitigate or exacerbate the impact on the economy. While U.S.-China trade tensions have not yet affected Ireland, intensification of protectionism could have a major impact.	Participate in coordinated policy response at the European and global level. In the short run, let automatic stabilizers work. Smooth out debt issuance through use of cash buffers. Strengthening growth potential through reforms, improving SME access to financing, and easing impediments to productivity growth. Accelerate NPL reduction and strengthen banks' resiliency to negative shocks.
Medium/Low ***Short-term*** **Sharp tightening of global financial conditions:** causes higher debt service and refinancing risks; stress on leveraged firms, households, and vulnerable sovereigns; capital account pressures; and a broad-based downturn. The tightening could be a result of: • ***Market expectation of tighter U.S. monetary policy*** triggered by strong wage growth and higher-than-expected inflation. • ***Sustained rise in risk premium*** in reaction to concerns about debt levels in some euro area countries; a disorderly Brexit; or idiosyncratic policy missteps in large emerging markets.	**Medium** Ireland's public debt dynamics is resilient to interest rate shocks, given its relatively long maturity and limited gross financing needs over the medium-term. However, households and SMEs remain overleveraged and a sharp increase in interest rates might worsen their debt service burden. Sensitivities related to the Irish border question due to Brexit also present special challenges.	Smooth out debt issuance through use of cash buffers. Strengthen supervision to ensure banks can withstand negative shocks and accelerate banks' balance sheet repair. Continue to improve NPLs resolution framework.
Medium ***Short- to medium-term*** **Large swings in energy prices:** Risks to prices are broadly balanced, reflecting offsetting—but large and uncertain—supply and demand shocks. In the near term, uncertainty surrounding the shocks translates to elevated price volatility, complicating economic management and adversely affecting investment in the energy sector. As shocks materialize, they may cause large and persistent price swings. While, on aggregate, higher oil prices would harm global growth, they would benefit oil exporters.	**Medium/Low** Ireland is particularly affected by swings to energy prices due to its large openness. Negative terms of trade shocks would translate into weaker export growth, employment, and fiscal revenues.	Reduce vulnerabilities in public finances and financial sector; and strengthen potential growth through above described reforms.

[1]The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly. "Short term" and "medium term" are meant to indicate that the risk could materialize within 1 year and 3 years, respectively.

Source of Risk and Likelihood (G-RAM)	Impact if Realized	Policy Recommendations Mitigation/Response
High/**Medium** ***Short- to medium-term*** **Weaker-than-expected global growth:** The global growth slowdown could be synchronized as weakening outlooks in the U.S., Europe and China feed off each other and impact on earnings, asset prices and credit performance. • ***U.S.:*** Confidence wanes against a backdrop of a long expansion with stretched asset valuations, rising leverage, and unwinding of the fiscal stimulus, leading to abrupt closure of the output gap rather than a smooth landing. • ***Europe:*** In the near term, weak foreign demand makes euro area businesses delay investment, while faltering confidence reduces private consumption. Adverse financial market reaction to debt sustainability concerns further dampens growth. A disorderly Brexit could cause market disruption with negative spillovers. In the medium term, disregard for the common fiscal rules and rising sovereign yields for high-debt countries test the euro area policy framework, with adverse impact on confidence and growth. • ***China:*** In the short term, intensification of trade tensions and/or a housing market downturn prompt a slowdown, which is not fully offset by policy easing. Deleveraging is delayed and financial stresses, including capital outflow and exchange rate pressures, emerge. In the medium term, insufficient progress in deleveraging and rebalancing reduces growth and raises the probability of a larger disruptive adjustment. There would be negative spillovers on the global economy through trade volumes, commodity prices, and financial markets.	**High**/**Medium** Weaker-than-expected growth in key export markets (U.S., Europe) would significantly affect the Irish economy through the trade channel, thereby undermining domestic confidence, investment, and FDI inflows. In particular: Lower U.S. growth and increased uncertainty would create negative global spillovers, with adverse effects on consumer and investor confidence, and sovereign spreads. In addition, the recent U.S. CIT reform might lead to a reduction of U.S. MNE FDI flows to Ireland, with potentially adverse effects on employment, fiscal revenues, and the external position. Ireland's significant trade, financial and labor market links with the U.K. makes it vulnerable to a possible slowdown in the British economy, a sustained fall in the £/€ rate or an increase in trade barriers. Irish banks would be adversely affected given their direct and indirect exposures, aggravating the burden of impaired assets. A weakened external demand of the euro area may affect Ireland indirectly through a contract manufacturing slowdown.	In the short run, allow automatic stabilizers to work. In the medium term, fiscal policy, within the current envelope, should support growth, by accenting growth-friendly taxes and spending. Expenditure savings could be redirected to pro-growth initiatives. Strengthen growth potential through reforms, as noted above. Continue close monitoring of Brexit related risks and update contingency plans. Facilitate SMEs' trade diversification. On the banking side, continue close supervision and accelerate balance-sheet repair. Ensure that banks would be able to withstand negative shocks. Central bank should stand ready to provide liquidity support to banks if needed. ECB policy actions under its euro area-wide mandate would contribute to reviving growth and could also aid competitiveness.
High ***Short- to medium-term*** **Intensification of security risks** in parts of Africa, Asia, Europe, Latin America, and/or the Middle East cause regional socio-economic and political disruptions, with potential global spillovers.	**Medium**/**Low** Global spillovers from regional disruptions may affect Ireland through trade and financial channels.	Smooth out debt issuance through use of cash buffers. Make use of growth-friendly spending and tax policies and potential-growth-enhancing reforms, as described above.
Medium ***Short- to medium-term*** **Cyber-attacks** on critical global financial, transport or communication infrastructure and broader private and public institutions trigger systemic financial instability or widespread disruptions in socio-economic activities.	**Medium**/**Low** Such attacks, local or global, could produce temporary negative effects on growth and financial conditions.	Smooth out debt issuance through use of cash buffers. Central bank should stand ready to provide liquidity support to banks if needed.

Source of Risk and Likelihood	Impact if Realized	Policy Recommendations Mitigation/Response
Medium *Short- to medium-term* **Changes in corporate taxation in the U.S. and the EU:** The changes in the U.S. corporate tax regime and the EU anti-tax avoidance agenda could make Ireland a less attractive location for future FDIs and adversely affect government revenues.	Medium The high concentration of its industrial base makes the Irish economy vulnerable to sectoral and firm-specific shocks. The impact of changes in operations by multinational corporates (MNEs) on gross value added and employment may vary depending on the nature of their links with the Irish economy. Budget repercussions might be substantial as 40 percent of corporate tax (equivalent to about 7 percent of total revenues) is paid by 10 MNEs.	Facilitate diversification through structural reforms to strengthen productivity and competitiveness; invest in education and training to create necessary skills; maintain a flexible and competitive labor market. Ensure sound public finances and durable debt reduction to rebuild fiscal buffers. Broaden the tax base in growth-friendly manner.
Medium *Short- to medium-term* **Budgetary pressures amid challenging political context:** The minority government is facing increasing public expectations of spending increases and tax cuts during the current economic recovery.	Medium These factors complicate domestic policy-making. While the government is committed to prudent policies, public pressure is strengthening to slow fiscal consolidation, while increasing dependency on uncertain corporate tax revenues. This increases the economy's vulnerabilities to adverse shocks.	Ensure sound public finances and a durable debt reduction to rebuild fiscal buffers and avoid procyclicality. Prioritize growth-friendly fiscal measures, including tax-base broadening. Enhance communication strategy regarding policy and reform plans.
Low *Medium-term* **A sharp correction in housing prices:** Continued strong pressures in the housing market together with a limited supply response could develop into large imbalances, potentially leading to a sharp drop in house prices, especially if other adverse shocks were to materialize.	Medium Domestic banks and households are exposed to property market shocks. A sharp future housing price correction could weaken bank and household balance sheets, with adverse effects on financial stability and growth.	Monitor risks and review macro-prudential limits periodically. Continue to expand housing supply in a sustainable manner and ensure that measures to improve housing affordability are well-targeted.

Annex V. Progress Against IMF Recommendations

Several policy recommendations in the 2018 Article IV consultation have been taken on board.

Key recommendations	Implemented policies
Take advantage of the strong cyclical momentum to accelerate fiscal consolidation and build buffers against risks. Broaden the tax base, maintain moderate spending growth, and avoid the use of temporary revenue gains to fund permanent measures.	Public debt ratio has declined further, thanks to continued strong nominal GDP growth, while the headline deficit has been improving on the back of stronger-than-expected CIT revenues. However, abundant but uncertain CIT revenues have been used to some extent to fund current spending and further reductions in personal income taxes.
Continue active engagement in implementing the international tax reform agenda. Strengthen the financial soundness of the Social Insurance Fund.	The government issued a Roadmap for implementation of all commitments from international tax agenda.
Further rationalize building regulations to encourage housing supply, while ensuring that measures to improve housing affordability are well targeted.	The parliament established an agency, Home Building Finance Ireland (HBFI), that will lend for residential developments across Ireland to contribute to economic and social development and enhance competitiveness of the economy.
Macroprudential policy should continue to be deployed proactively and retain prudent lending policies.	According to the central bank's review in November 2018, macroprudential measures are having an effect as LTVs and LTIs have become more binding. This assures prudent lending standards in the mortgage segment.
Strengthen private sector balance sheets through a sustained reduction in nonperforming loans, including through enhancing supervisory efforts and accelerating legal proceedings.	The NPL ratio of the three largest Irish banks has declined somewhat further, thanks to portfolio sales but further efforts are needed to reach the goalpost of 5 percent by 2020.
Improve infrastructure quality, based on prioritization to achieve value-for-money, and encourage domestic firms' innovation, including through greater direct public support.	Budget 2019 allocated a significant increase in capital expenditures, as envisaged in the National Development Plan.
Continue to align educational paths and training programs to labor market needs. Address gender employment and pay gaps.	The Affordable Childcare Scheme to be launched in 2019 should help reduce high costs of childcare and lead to an increase in female labor force participation.

INTERNATIONAL MONETARY FUND

IRELAND

May 30, 2019

STAFF REPORT FOR THE 2019 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

Prepared By | European Department

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FUND RELATIONS

(As of April 30, 2019)

Membership Status: Joined August 8, 1957; Article VIII

General Resources Account:	**SDR Million**	**Percent of Quota**
Quota	3,449.90	100.00
Fund holdings of currency	2,643.16	76.62
Reserve position in Fund	806.78	23.39

SDR Department:	**SDR Million**	**Percent of Allocation**
Net cumulative allocation	775.42	100.00
Holdings	658.63	84.94

Outstanding Purchases and Loans: None

Financial Arrangements:

Type	**Approval Date**	**Expiration Date**	**Amount Approved (SDR million)**	**Amount Drawn (SDR million)**
EFF	12/16/10	12/15/13	19,465.80	19,465.80

Projected Payments to the Fund

(SDR million; based on existing use of resources and present holdings of SDRs, as of April 30, 2019):

	2019	2020	2021	2022	2023
Principal					
Charges/Interest	0.99	1.34	1.34	1.34	1.34
Total	0.99	1.34	1.34	1.34	1.34

Exchange Rate Arrangement and Exchange Restrictions:

Ireland's currency is the euro, which floats freely and independently against other currencies. Ireland has accepted the obligations of Article VIII, Sections 2, 3, and 4, and maintains an exchange system free of restrictions on payments and transfers for current international transactions, and has not notified the Fund of any restrictions under Decision No. 144 (52/51).

Article IV Consultation:

The last Article IV consultation was concluded on June 22, 2018. The associated Executive Board assessment is available at https://www.imf.org/en/News/Articles/2018/06/28/pr18264-imf-executive-board-concludes-2018-article-iv-consultation-with-ireland and the staff report (IMF Country Report No. 18/194) at https://www.imf.org/en/Publications/CR/Issues/2018/06/28/Ireland-2018-Article-IV-Consultation-Press-Release-Staff-Report-and-Statement-by-the-46026. Ireland is on the standard 12-month consultation cycle.

Financial Sector Assessment Program (FSAP) Participation and ROSC:

The Financial System Stability Assessment (FSSA) for the last mandatory FSA was discussed by the Board on July 27, 2016. The FSSA and accompanying Reports on the Observation of Standards and Codes (ROSCs) are available at http://www.imf.org/en/Publications/CR/Issues/2016/12/31/Ireland-Financial-System-Stability-Assessment-44142.

STATISTICAL ISSUES

I. Assessment of Data Adequacy for Surveillance
General: Data provision is broadly adequate for surveillance.
National accounts and real sector data: Quarterly national accounts are currently published within three months of its reference period. Other real sector data are relatively timely, with industrial production and retail sales data published within six weeks and employment data within 3 months of the reference period, but some non-SDDS series are published one and a half years later (e.g., household disposable income). Employment and unit labor costs, and national income and expenditure data are usually available with a three-month lag.
Wages and earnings statistics: The quarterly Earnings, Hours and Employment Costs Survey has replaced the four-yearly Labor Cost Survey, and also replaces all other existing short-term earnings surveys. The results are comparable across sectors and include more detail on components of earnings and labor costs than was available before. However, data are only available with more than a six-month lag.
Government finance statistics: The authorities publish Exchequer returns and indicative estimates of the general government balance on a monthly basis. The definitive general government balance is reported quarterly and annually. Ireland reports these data to STA through a conversion of the datasets reported to Eurostat under the "ESA Transmission Programme". Annual and quarterly fiscal data in the *GFSM 2014* framework are reported through the Eurostat convergence project with the IMF.
Monetary and financial statistics: The ECB reporting framework is used for monetary statistics and data are reported to the IMF through a "gateway" arrangement with the ECB. The arrangement provides an efficient transmission of monetary statistics for central bank and other depository corporations to the IMF and for publication in the IMF's *International Financial Statistics (IFS)*. Data are published in *IFS* with a lag of about a month. Ireland reports some data and indicators of the Financial Access Survey (FAS), including the two indicators adopted by the UN to monitor Target 8.10 of the Sustainable Development Goals (SDGs).
Financial sector surveillance: Ireland reports 11 of the 12 core and 9 encouraged FSIs for deposit takers, one FSI for other financial corporations, and 3 FSIs for real estate markets with quarterly frequency on a regular basis for posting on the IMF's FSI website.
External sector statistics: Quarterly balance of payments and international investment position (IIP) data are compiled by the Central Statistics Office. The authorities implemented the sixth edition of the *Balance of Payments and International Investment Position Manual (BPM6)*. The most recent balance of payments and IIP data reported to STA and disseminated in the *IFS* are for Q4/2018. Ireland reports data for the Coordinated Portfolio Investment Survey (CPIS), the

Coordinated Direct Investment Survey (CDIS), and the Data Template on International Reserves and Foreign Currency Liquidity.	
II. Data Standards and Quality	
Ireland is subject to the statistical requirements and timeliness and reporting standards of Eurostat and the European Central Bank (ECB). Ireland subscribes to the Fund's Special Data Dissemination Standard and uses SDDS flexibility options on the timeliness of wages and earnings, and central government debt data.	No data ROSC is available.

Ireland: Table of Common Indicators Required for Surveillance

(as of May 22, 2019)

	Date of Latest Observation	Date Received	Frequency of Data[7]	Frequency of Reporting[7]	Frequency of Publication[7]
Exchange Rates	May 22, 2019	5/22/2019	D	D	D
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	April 2019	5/20/2019	M	M	M
Reserve/Base Money	April 2019	4/30/2019	M	M	M
Broad Money	April 2019	4/30/2019	M	M	M
Central Bank Balance Sheet	March 2019	5/3/2019	M	M	M
Consolidated Balance Sheet of the Banking System	March 2019	4/30/2019	M	M	M
Interest Rates[2]	March 2019	5/10/2019	M	M	M
Consumer Price Index	April 2019	5/9/2019	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	2018:Q4	4/15/2019	Q	A	A
Revenue, Expenditure, Balance and Composition of Financing[3]– Central Government	April 2019	4/15/2019	M	M	M
Stocks of Central Government and Central Government-Guaranteed Debt[5]	2018:Q4	4/15/2019	Q	Q	Q
External Current Account Balance	2018:Q4	3/14/2019	Q	Q	Q
Exports and Imports of Goods and Services	2018:Q4	3/14/2019	Q	Q	Q
GDP/GNP	2018:Q4	3/14/2019	Q	Q	Q
Gross External Debt	2018:Q4	3/14/2019	Q	Q	Q
International Investment Position[6]	2018:Q4	3/14/2019	Q	Q	Q

[1] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[2] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[3] Foreign, domestic bank, and domestic nonbank financing.
[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
[5] Including currency and maturity composition.
[6] Includes external gross financial asset and liability positions vis-à-vis nonresidents.
[7] Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Annually (A); Not Available (NA).

Statement by Ms. McKiernan, Alternate Executive Director for Ireland and Mr. Mooney, Advisor
June 14, 2019

Context

We thank staff for their continuing positive engagement with our authorities and their insightful Report and Selected Issues Papers. The Irish economy is at an unusual conjuncture - faced with significant risks from Brexit and global trade developments on the one hand, and potential excess expansion on the other. The authorities acknowledge the challenges in the coming years but, importantly, these are being met from a strong position. GDP increased by 6.7 percent last year and modified (final) domestic demand (MDD) – a more accurate measure of underlying economic activity in Ireland – increased by 4.5 percent. On the domestic front, a combination of strong growth in disposable income, improving consumer confidence and modest inflation underpinned personal consumer spending growth of 3 percent in 2018. The headline export performance recorded growth of almost 9 percent in the same period. This healthy growth is paying dividends in the labor market, where the number employed last year reached the highest level in history.

The current administration - a minority government in a multi-party coalition – has been in place since 2016, extending its coalition agreement to unite behind the national Brexit strategy and contingency plans. After a decade-long fiscal adjustment path, it faces numerous competing pent-up spending pressures, including public sector wage increases and current and capital spending demands. Nevertheless, the authorities are committed to implementing prudent budgetary policy and rebuilding buffers, to be in a position to provide support in the event of a downturn and / or "No-Deal Brexit."

Brexit: Economic Impact & Preparedness

Ireland will be uniquely affected by Brexit, regardless of the ultimate arrangement. Reports commissioned by the authorities provide extensive analysis of the macroeconomic and trade impacts for Ireland. Compared to the UK remaining in the EU, GDP in Ireland is estimated to be c.2.6 percent lower after ten years in a "Deal" scenario, and 5 percent lower in a "Disorderly No-Deal" scenario.[1]

Whole-of-Government preparations have been taking place since before the Brexit referendum for many possible outcomes. These have developed into the Government's

[1] In the Deal scenario, the UK makes an orderly agreed exit from the EU. This involves a transition period covering the years 2019 and 2020, and a free trade agreement between the UK and the EU27 thereafter. In the Disorderly No-Deal scenario, the UK exits the EU without a deal and there is an additional disruption to trade in the short run.

Contingency Action Plan[2]- primarily for a "no-deal" scenario - which includes a planned fiscal response and the preparation of Brexit related legislation[3] to support the economy, enterprise and jobs, particularly in key economic sectors such as agriculture, food and transport. Several credit schemes aimed at the most vulnerable parts of the SME sector include a €300m Future Growth loan scheme to support long-term capital investment. In addition, the authorities have undertaken extensive financial sector contingency planning and collaborated with the EU and UK authorities as appropriate.

Fiscal Policy

The authorities are committed to careful management of the public finances, while also providing for spending plans that enhance the productive capacity of the economy into the future. While compliance with EU fiscal rules has provided an anchor, the authorities have gone beyond those requirements to generate some additional fiscal space. The 2019 Stability Program Update projects a small surplus this year, followed by a larger surplus in 2020 in the baseline case. Transfers amounting to €500m each year from 2019-2023 are committed to the "Rainy Day Fund," subject to the enactment of the necessary legislation this year. Nevertheless, the authorities acknowledge staff's advice on the need to tackle spending overruns in the health sector.

While the debt-to-GDP ratio is projected at 61.1 percent in 2019 - close to the EU fiscal rule threshold of 60 percent - other metrics such as the ratio of debt-to GNI*[4] show that, while declining, public indebtedness remains quite high. The government's fiscal strategy will further reduce public debt, via projected surpluses, receipts from the disposal of State ownership of banking assets, and the winding down of the National Asset Management Agency (NAMA). The latter is expected to generate a €4 billion surplus to the State in 2020-21.

The authorities welcome the results in the Selected Issues Paper on *Personal Income Tax Reform: Past and Present*. In particular they welcome the recognition of the overall high progressivity of Ireland's current PIT system, which is recognised internationally as having played an important role in income redistribution and alleviation of poverty (combined with Ireland's welfare benefits system), and which underpinned Ireland's inclusive framework in the years of fiscal retrenchment in response to the financial crisis. The authorities also consider that the main conclusion of the paper - suggesting further reform of the income tax system - is helpful, albeit merits further detailed

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[2] https://www.dfa.ie/media/dfa/eu/brexit/brexitcontingency/No-Deal-Brexit-Contingency-Action-Plan-December-18.pdf

[3] The Withdrawal of the United Kingdom from the European Union (Consequential Provisions) Act, which was signed into law by the President on 17 March 2019.

[4] GNI* excludes the profits of re-domiciled companies, the depreciation of intellectual property and aircraft leasing companies.

consideration. However, the authorities are less aligned with staff on the link drawn between the increase in CIT revenues and the funding of the reductions in personal income taxes.

The authorities continue to support and work towards an international, multilateral, cohesive and agreed approach to the international corporate tax environment. As a country with a small open economy, having a stable and consensus-based international tax framework is very important for Ireland, as it provides the necessary stability and certainty for investment decisions to be made. Ireland has been a strong proponent and implementor of BEPS and has taken significant steps to address aggressive tax planning, including amending tax residency rules, enhancing tax transparency and mandatory disclosure of tax planning arrangements by advisors. Indeed, Ireland achieved the highest standard for transparency under the BEPS framework.

Financial Sector

Brexit-related applications and plans for authorization are significantly impacting the Irish financial sector landscape. The Central Bank of Ireland has implemented a vigorous authorization process, in collaboration with EU authorities, where applicable, and is committed to upholding the highest standards of regulation and supervision to protect financial stability, consumers and investors. While the final relocation of financial services to Ireland post-Brexit will not be in place for some time, the expectation is that Ireland will become the fourth largest financial services centre in Europe, although the number of systemically-important institutions will not markedly change.

The financial position of the Irish banks continued to improve, and the two main banks recorded profits for the fifth consecutive year. In addition, net loan books expanded for the first time since the financial crisis.

Progress on NPL reduction continued, following vigorous policy and structural actions over a number of years. The average NPL ratio of domestic banks fell from 13.8 percent to 8.5 percent in the year to December 2018, 88 percent below their 2013 peak. Mortgage NPLs (70 percent of all NPLs) fell 39 percent in the Irish banks year on year, aided by loan sales as well as work through measures. The authorities are aware that ongoing work is required to continue these reductions, while also noting that the oldest NPL segments are dominated by restructured loans not currently in arrears and with a larger share of collateralization than EU norms.

The Macroprudential Policies, introduced in 2014, represented a key structural improvement in the Irish policy framework. The mortgage lending limits are reviewed annually to ensure they continue to achieve the objective of protecting the economy from unsustainable credit growth; the 2018 review concluded that the rules, as calibrated, remain unchanged, while becoming more binding as property values rise.

The CBI has set the countercyclical capital buffer (CCyB) at 1 percent effective from 1 July 2019 and has requested powers to introduce a systemic risk buffer.

Authorities welcome the Selected Issues Paper on the non-bank financial sector in Ireland. The Central Bank of Ireland has carried out extensive analysis to profile the many types of entity, business modes and activities of this sector, and the authorities welcome the Fund's focus on this area. In particular, they appreciate staff's focus on the non-bank activity and its potential interlinkages to the real economy (including non-bank investment in property and related assets), while agreeing with the conclusion that the employment and value-added linkages to the domestic economy remain weak.

AML/CFT

The Financial Action Task Force (FATF) mutual evaluation report of Ireland in September 2017 acknowledged the strength of Ireland's AML/CFT systems, the measures taken nationally on AML/CFT risks and the cooperation mechanisms developed thereon, while also making recommendations about the areas for further improvement. As part of the regular follow-up reporting, the authorities have submitted evidence for upgrades to compliance ratings on 13 of 40 FATF recommendations, based on the actions taken since 2017, which will be considered by FATF in October 2019. Accordingly, the authorities concur with the staff recommendation to continue to strengthen the AML/CFT regime and have many such measures underway. The 4th Directive has already been transposed into law while the 5th AMLD is largely transposed[5] and the beneficial ownership of trusts provisions are on schedule to be transposed before their deadline. A central register of beneficial ownership for corporates - required under 5AMLD - is expected to go live shortly, well ahead of the January 2020 deadline, as is work on establishing a central mechanism for the retrieval of information on the beneficial ownership of bank accounts and safety deposit boxes.

Housing

Sustained macroeconomic and demographic growth, strong employment and incomes growth, combined with structural factors limiting housing supply led to significant house price recovery since the trough in prices in early 2013. Given the criticality of a supply-side response to the housing market, a comprehensive 5-pillar government housing supply strategy has been underway for several years, facilitating an annual average supply increase of over 30 percent in 2014 – 2018. In the private sector, reforms such as fast-track planning, new building guidelines and the creation of Home Building Finance Ireland (HBFI) are facilitating further investment, as noted by staff in Box 2 of the Report.

[5] The Criminal Justice (Money Laundering and Terrorist Financing) (Amendment) Bill 2019

The increase in supply is integrated into improved spatial planning under the National Planning Framework (NPF), which guides strategic planning and development in Ireland over the next 20 years. The authorities are cognizant that further work is required in this area and are committed to ensuring that housing supply continues to meet the demands of the Irish population.

Labor Force Participation & Female Representation

With the unemployment rate now at historical lows, employment demand is met by sustained immigration. Ireland is one of the most positively disposed countries in Europe towards immigration, with authorities viewing it as enhancing the productive capacity of the economy and fostering multiculturalism.

To foster enhanced female labor force participation, the recently introduced National Childcare Scheme is designed to address the impediment of high childcare costs to female workers. It establishes an equitable and progressive system of universal and income-related subsidies for children up to the age of 15, alongside supports for lifelong learning.

Climate Change

As noted by staff, Ireland is the only EU country with generally rising greenhouse gas emissions. In recognition of the need to step up action, and to ensure the delivery of Ireland's 2030 targets, the government agreed in November 2018 to prepare a *new all-of-Government Climate Plan*. The Plan will build upon the existing National Mitigation Plan and aims to develop new initiatives across all sectors that contribute to reducing greenhouse gas emissions. The Irish government is committed to carbon pricing as a core element of its policy measures to reduce greenhouse gas emissions and signaled its intention, in the 2019 Budget Statement, to put in place a long-term plan (to 2030) for carbon tax increases, in line with recommendations of Ireland's independent Climate Change Advisory Council and the special Oireachtas (Parliamentary) Committee on Climate Action. In May 2019, the government declared climate as a national emergency, to highlight its commitment to fiscal and other policies to address climate risks.

Conclusion

While the Irish economy continues to grow, the authorities are cognizant of the need to address the vulnerability to significant external risks of Brexit and global trade, on the one hand, and to protect the hard-won fiscal and structural reforms, on the other. Difficult trade-offs lie ahead. The authorities appreciate the useful policy advice contained in the Report as they navigate these choices.