Capital Spending Main Focus of Budget 2019

One of the main annual events in the political calendar occurs today, when the Minister for Finance presents his budget for the coming year to the Dáil. This may not have the same drama as the budgets delivered earlier in the decade, but it will still be closely followed.

The Irish economy has performed very strongly in recent years, helping to boost tax receipts. Corporation tax receipts have risen particularly strongly. Meanwhile, debt interest costs have fallen quite sharply, aided by the ECB's quantitative easing and negative interest rate policies. As a result, the budget deficit declined at a much quicker than expected pace for much of this decade.

However, the pace of deficit reduction has slowed considerably in the past couple of years as public spending has picked up. The Government is forecasting that the deficit in 2018 will equate to 0.1% of GDP compared to 0.3% last year and 0.5% in 2016. The deficit was as high as 8% of GDP as recently as 2012.

In absolute terms, the general government deficit is forecast at €0.2bn for this year, down from €1bn in 2017 and €1.4bn in 2016. It stood at a very high €14bn in 2012, so remarkable progress was made in reducing the budget deficit between 2012 and 2016.

The ESRI has called for a 'holding budget' in 2019, i.e. a neutral budget, with spending rising broadly in line with tax revenues. Others have argued for a tightening of fiscal policy, but the ESRI believes that a 'holding budget' is the most appropriate approach given the need to tackle large infrastructure deficits in areas like housing, as well as the mounting external risks faced by the economy, in particular Brexit.

The expectation is that today's budget will be broadly in line with the advice of the ESRI. The Pre-Budget White Paper published at the weekend shows that net voted government spending will rise by €2.4bn next year, with tax receipts increasing by €2.3bn. The expenditure rise includes an increase of almost €1.5bn in net voted capital spending, most notably on housing.

The White Paper projections do not take into account the changes that the Minister will announce in his budget speech today, but these will not have a major impact on overall public finances. The Government is projecting that it will have a balanced budget in 2019 and the public finances will move into surplus in 2020.

The economic projections underpinning the 2019 budget look reasonable and our best judgement is that the outturn next year will be close enough to target. GDP is projected by the Dept. of Finance to grow by 4.1% next year, broadly in line with most other forecasts.

Notably, the Minister is not going to use all the fiscal space available to him in today's budget, declining the option of announcing even bigger spending increases and tax cuts. This would seem appropriate given the still high very level of public debt, strength of economic activity and doubts about the sustainability of the marked jump in corporation tax receipts in recent years.

However, it does mean that there will be little enough in the way of tax relief in the budget, especially for the so-called squeezed middle-income earners. This will essentially be a tax and spend budget.

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