Continuing Large Budget Surpluses

In recent years, the Irish public finances have been faced with the need to provide for short-term but often substantial government expenditure policy responses to a number of external shocks, including Brexit, COVID-19 and both the Ukrainian humanitarian and Cost of Living crises. The framework adopted by the Department of Finance (DoF) has been to separate out the use of temporary 'non-core' measures to meet these short-term additional resource requirements, from the ongoing day-to-day 'core' expenditure of government departments.

While these non-core measures relate to temporary challenges, their duration can last a number of years. The good news is that this non-core expenditure is declining, from €16.5bn back in 2020 to €7.2bn this year, and a projected €5.4bn in 2024, with further falls on the cards thereafter. The principal unknown factor in relation to the future path of non-core spending is the duration of the €2.5bn required each year for expenditure on the Ukrainian humanitarian crisis.

As the Irish Fiscal Advisory Council notes, there is an argument that non-core expenditure that appears to becoming longer lasting should be treated as core spending. The classification is important in terms of the projected future path of the public finances. In this regard, the budget surplus target for next year of €8.4bn is broadly unchanged from €8.8bn in 2023 and €8.5bn in 2022. However, the surplus is projected to rise to over €14bn in 2025 and 2026, largely on the basis of non-core spending falling to very low levels. As the DoF acknowledges, there is inherent uncertainty in this regard, especially in relation to the future spending requirements on refugees.

Furthermore, core/non-core spending classifications can lead to confusion around budgetary policy. The headlines following Budget 2024 proclaimed a €14bn package. However, of the €14bn, some €7.5bn related to the continuation of existing non-core spending programmes over the remainder of 2023 and in 2024, including humanitarian assistance, cost of living measures and COVID. In fact, the actual increase in gross voted government spending next year is €3.4bn. or 3.7%, with tax cuts costing €1.1bn. It is certainly true that core spending will increase by €5.3bn or 6.1% in 2024, but non-core expenditure is projected to fall sharply, in particular due to much lower spending on COVID and cost of living measures next year.

Overall, the budget surplus should rise somewhat from current levels post 2024, but maybe not to the extent shown in the DoF projections, unless corporate tax receipts resume their strong upward trend. There is scope for higher receipts, with the hike from 12.5% to 15% in the rate of corporate tax paid by larger companies coming into effect from next year. However, this could be offset by other factors,

such as lower levels of profitability. Indeed, the DoF is of the view that a large portion of corporate tax receipts could be windfall or temporary in nature and thus, may fall significantly in the coming years.

Hence, it is appropriate that Ireland is running large budget surpluses and that the government is establishing two Sovereign investment funds to house these surpluses. The funds are to be used to help finance spending pressures that will arise in the future from the ageing population, climate change, cyclical and other factors, in a welcome shift to greater long-term planning on the public finances.

Oliver Mangan
Chief Economist
AIB

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AIB Customer Treasury Services
DUBLIN / CORK
aib.ie/fxcentre

Customer Treasury Services NI
BELFAST
aibni.co.uk/fxcentre

Customer Treasury Services GB
LONDON
aibgb.co.uk/fxcentre

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