



Think-tank for action on social change

TASC submission to the Committee on Budgetary Oversight

Budget 2021



Introduction

The spread of COVID-19 has affected every country and society around the world. The resulting and necessary restrictions on economic and social activity have constituted a major shock to the Irish economy. As the situation has evolved, budgetary priorities have naturally changed as well. This submission examines the financial sustainability of the current budgetary trajectory and highlights areas where additional funds could be allocated.

In particular, TASC wishes to highlight the following:

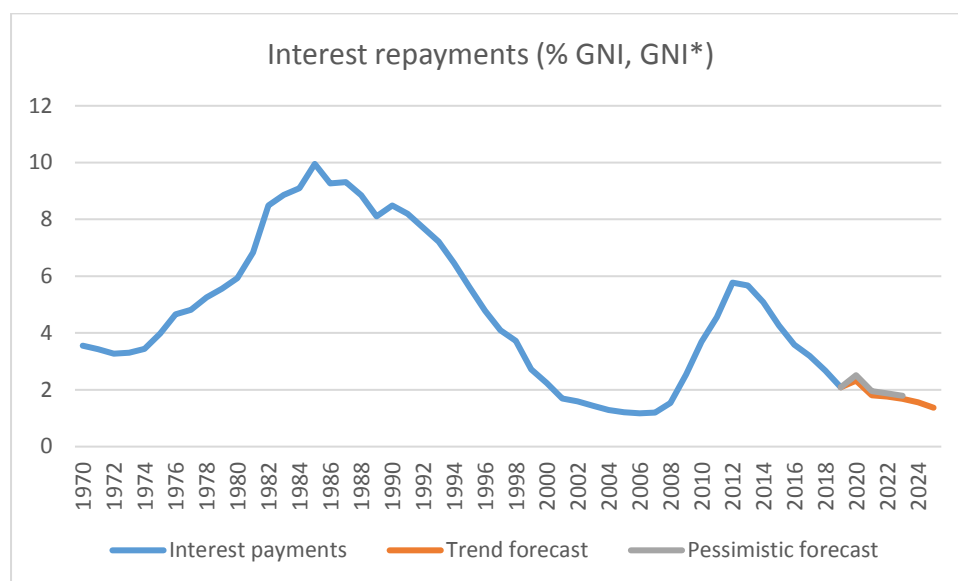
- The level of the deficit or level of indebtedness should not be the guiding metrics of financial sustainability
- Budgetary policy should focus on the debt-servicing burden, or interest payments relative to GNI*
- The financial outlook in the coming years is set to be benign, absent further shocks
- Inequality impact of COVID-19 is unclear, though inequality may increase due to high unemployment rates and weak recovery in particular sectors
- Investments in childcare and social welfare measures are essential to reducing inequality and poverty
- Advancing the implementation of Slaintecare is necessary both for providing greater economic security and to prepare for future public health crises; the trend toward privatisation of key care services should likewise be reconsidered
- The shortage of affordable housing means that greater public investment will be needed over the next decade
- The government needs to live up to its climate change obligations, though not through carbon taxes

Public financial sustainability in Ireland

On the face of it, the public finances appear to be vulnerable. The Irish Fiscal Advisory Council (IFAC) has projected a public deficit of between 13 and 17.4 percent of GNI*. At 85.8 percent of GNI*, government indebtedness was the fifth highest in the OECD (IFAC, 2020a: 24). The Department of Finance expects unemployment to be 15.9 percent for 2020 and 10.7 percent the following year. The latest projections for growth and unemployment for 2020 are, though, more optimistic than previous estimates. The most recent analysis forecasts a fall in GNI* of 5.6 percent for 2020 while growth of 1.8 percent is expected the following year. Just a few months ago, national income was expected to decline by double digit figures.

Clearly the economy will be in for a rough ride beyond 2020. The deficit, fall in tax receipts, and fall in national income raise legitimate questions about the sustainability of public finances. That said, the extent to which debt and deficits per se impose a burden on the Irish

economy is often overstated. Rather, it is servicing those debts through interest repayments that imposes costs, not the actual levels of indebtedness. This is because the state can actively manage debt through the debt management agency. For instance, when the principal of a loan comes due, it can simply be ‘rolled-over’, that is financed by new borrowings. The state can also retire old debt by issuing new debt at a lower interest rate if interest have fallen, as they have done. The state’s debt managers are also likely to avoid a large repayment of principal in a short timeframe, such as by investing in assets which come due at the same time as the debt repayment. As such, it is the interest payments on borrowings, not the level of indebtedness, which imposes a burden on the state.



Sources: CSO and IFAC (2020a; 2020c).

Notes: GNI used up to 1995, after which GNI* is used. Forecasts for GNI* are based on domestic demand forecast as per IFAC. Trend forecast is based on the mild scenario as set out in IFAC’s May statement and subsequently in its pre-budget statement. Pessimistic forecast is based on IFAC’s central scenario in its May statement, which subsequently turned out to overstate the damage done to demand, as discussed in IFAC’s more recent pre-budget statement. Forecasts for interest payments are based on IFAC pre-budget statement.

The figure above looks at interest payments on government debt in historical perspective. In 2019, the state paid over the equivalent of 2.1 percent of national income in interest payments. This is somewhat above what it paid during the 2000s, when the economy was booming and indebtedness was low. It is significantly above what it paid in the late 1990s during the Celtic Tiger years. At the same time, it is around average historically (see Fitzgerald and Kenny, 2019: 27). Repayments will likely increase only slightly next year, and are due to actually fall in the years after. Longer-term forecasts also predict lower debt servicing costs, despite rising demographic pressures (IFAC, 2020b: 105). This would suggest space for net spending measures - to address the policy issues raised above - in the coming years.

This benign financial outlook exists despite the fact that Ireland is expected to continue to run sizeable deficits with a level of public indebtedness close to historic highs. The reason is that the ECB has committed to buying member states public debt so as to keep borrowing and hence servicing costs low, unlike in the last crisis. This is among the reasons that low interest rates are expected to persist.

Most of Ireland's debt is fixed interest debt, so that a rise in interest rates will not increase the debt-servicing burden of historic borrowings. A risk going forward is that interest rates rise, so that when the state issues new debt to roll over previous borrowing, it has to borrow at higher costs. The worst-case scenario is that other countries recover, but Ireland does not. This is because ECB monetary policy is calibrated according to the Eurozone as a whole, not to Ireland's specific needs. As other countries recover, inflation is likely to grow. As inflation increases, the ECB will raise interest rates, as required by its mandate to control inflation at the Eurozone level. If Ireland were somehow left behind in the recovery, then it would have rising costs of servicing its debt, but without the nominal economic growth to facilitate higher debt repayments that other countries would have. The larger borrowings are today, the worse the impact of an adverse and uneven recovery would be.

A more likely scenario is that Ireland recovers at the same time as other countries. As inflation increases in Ireland and elsewhere in the Eurozone, the ECB is likely to increase interest rates. Rising inflation is likely across the Eurozone during a recovery, as households spend the savings they have been accumulating since the crisis. In such a context, the actual cost of servicing our debt may be limited. For instance, suppose both inflation and interest rates were to increase by two percentage points. Although the government will be paying more each year in interest to service that debt, inflation will erode the value of the debt. The actual, real increase in debt servicing costs will be much lower.

Again, there is a risk is that Ireland does not recover as other economies do, so that it has neither economic growth nor inflation to alleviate the burden of servicing its borrowings. However, it is difficult to see why Ireland would fail to recover along with the rest of the Eurozone.

It is therefore our view that it is prudent to borrow now to avail of low interest rates. So long as the fiscal rules are suspended, the main indicator the government should concern itself with is debt servicing costs. The level of the debt and deficit is the not the main channel through which state borrowing imposes a burden on the economy. When the fiscal rules are reinstated, the government will need to close the funding gap. An important area of funding shortfall relative to peer countries is low levels of revenue collected from employers PRSI. This will be an important funding source to tap going forward.

Socioeconomic priorities

Inequality

It is clear that COVID-19 is disproportionately affecting younger workers and low paid workers. The hardest hit sector has been hospitality, where many low paid and young workers are employed. Many retail workers also required supports at the height of the lockdown, but that sector has since rebounded. Measures such as the Temporary Wage Subsidy Scheme and Pandemic Unemployment Payment (PUP) implemented early into the crisis have been progressive in that lower-income groups have benefited more.

Beyond the immediate effects, the longer-term distributional consequences of COVID-19 are as of yet unclear. Employment losses, as intimated above, have been heavily concentrated among less educated groups. At the same time, many younger workers are not in the lower part of the income distribution. Given the scale of the job losses and the concentration of those losses among less educated groups, a fall in that group's income is likely to increase inequality. The government should equality-proof its budgetary strategy so inequality is not increased. No single policy can achieve equality-proofed budgeting on its own. In the immediate term, equality-proofing could entail revisiting the reduction of PUP, or benchmarking social welfare increases to mean or median earnings. Any policy change should be tailored to ensure no adverse employment effects.

The government should also consider significantly increasing investment in apprenticeships and vocational training, especially in growing industries and outside of major cities.

Social inclusion

COVID-19 and the lockdown exposed the scale of the deprivation faced by particular marginalised groups living in Ireland, as well as the challenge in accessing certain services in the areas of health, education and social welfare. For instance, Travellers, Roma, asylum seekers and older people, who are already at risk of health inequalities, have been disproportionately affected by the virus. This has been due in part by inequalities in terms of access to health care, as well as living conditions. In addition, the sectors of the labour market that have been hit hardest by job loss (as mentioned previously, including hospitality, retail, food and service industries) are more likely to consist of workers from particular marginalised groups, including lone parents, migrants, people with disabilities and young people/students.

After the last financial crash, Ireland adopted an austerity approach that focused predominately on job activation and cutting spending to balance budgets. Such decisions disproportionately impacted at-risk populations; for example, as cited by forthcoming TASC research on Traveller children and education, Traveller-specific educational supports were

cut by over 80 percent post-2008 despite the fact that Travellers remained among the most educationally disadvantaged groups in Ireland (Harvey, 2013). TASC recommends that budgetary decisions should be proofed to ensure that they do not further marginalise particular populations moving forward.

Childcare

Childcare is an area which is relevant to inequality, low pay, and social exclusion. Spending on the sector in 2019 was just under 0.3 percent of GNI* (Sweeney and Oliveira Santanna, forthcoming 2020). This leaves Ireland at or near the bottom in terms of public spending on the sector in international rankings. Sweden, by contrast, spends 1.8 percent of GDP on the early year's sector. As a result, the Irish system is unaffordable. High childcare costs are also a major barrier to paid employment, especially among lower income women. According to the OECD tax-benefit model, 59 percent of income from entering employment would be used on childcare fees for the typical single person with two children (ibid). Ireland should move to increase the funding toward the sector along international norms. Funding increases should depend on implementing minimum rates of at least the Living Wage, together with caps on fees. Over the medium term, the current policy whereby the state pays the wages of sector through EWSS could become permanent as a national system of early years care is created.

Healthcare

TASC supports the move toward Sláintecare. Recent academic and forthcoming TASC research shows a trend toward privatisation in the areas of nursing and home care. From about a fifth in the early 1980s, almost 70 percent of nursing home beds today are private (Mercille, 2018). Spending on private providers has likewise risen from one percent in 2006 to about two fifths of spending on home care (Mercille and O'Neill, 2020). Though this shift is likely to yield cost savings, it also contributes to a deterioration of pay and conditions of carers in the sector. Such policies are at odds with the current public sentiment to value care workers. Adequate funding should be put in place to expedite the move toward Sláintecare and support care workers.

Housing

TASC is currently undertaking research projects on housing, but which are still in the early phase. TASC supports significant increases in funds allocated toward new builds of public housing. This could be up to €1 billion per annum if capacity exists to increase output by that level. It may be necessary to support funding for new builds through increases in funds allocated toward training. For instance, there is strong evidence that labour shortages are a major impediment to increasing supply.

Climate

Budget 2021 must recognise the mounting challenge that Ireland faces in meeting its commitments and obligations in relation to the Paris Agreement and the 2030 Agenda for Sustainable Development. However, in meeting its commitments under the Paris Agreement on Climate Change, the Government must not exacerbate inequality or poverty. The design of any carbon tax must not increase energy poverty and at present the necessary data is not available to ensure this.

The Republic remains a laggard in terms of climate action internationally. This comes with an inherent cost. Fines and the cost of carbon credits could amount €7bn by 2030 (Gabbatiss, 2019). In order to reach our targets, the most recent Climate Change Advisory Council indicates that additional government investment is needed in: public transport, retrofitting of local authority buildings and housing, and essential adaptation measures (CCAC, 2019).

Given the risks that an ill-designed carbon tax hike could have on people living in vulnerable situations; cognisant that there are currently no indicators or measures in place to track energy poverty, nor is there an up to date national energy poverty strategy; and considering the potential negative impact of a tax that brings hardship on social approval for climate action in Ireland, TASC recommends that there be no increase in carbon tax in this budget. In order to realise a just transition in communities all across Ireland and build social approval for climate action, TASC recommends that green expenditure be channelled into community initiatives that help to stimulate local development, build create local and enable the growth of cooperative or community owned businesses. To achieve this, Budget 2021 should make provision for local community consultations or Just Transition Community Dialogues to facilitate bottom up policy creation. The budgetary impact of such a policy would be modest – of the order of €15 million.

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