



# A Strategy for Growth

Medium-Term Economic Strategy  
2014 – 2020

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#MTES2020

December 2013



BAILE ÁTHA CLIATH  
ARNA FHOILSIÚ AG OIFIG AN tSOLÁTHAIR

Le ceannach díreach ó  
FOILSEACHÁIN RIALTAIS,  
52 FAICHE STIABHNA, BAILE ÁTHA CLIATH 2.

Fón: +353 1 647 6834 nó 1890 213434  
Facs: +353 1 647 6843  
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ECONOMIC STRATEGY 2014 – 2020

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2014 – 2020

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## Preface

Our country is emerging from the deepest economic crisis in our history.

Through the hard work and sacrifice of the people of Ireland, we have now exited the bailout programme which was forced on our country as a result of disastrous economic mismanagement.

The purpose of this Medium-Term Economic Strategy is to point the way to a stable and prosperous future, and away from the failed policies of boom and bust that have cost us so dearly.

This Strategy sets out how we will build and sustain a competitive economy that can pay its own way, serve our society, and that can survive and thrive in a reformed eurozone and an increasingly globalised international economy.

It provides an overall framework for social and economic policies that are being developed and implemented by every member of the Government.

At the heart of this Strategy are the interests of our people.

We are committed to healing the wounds left behind by the crisis:

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**By helping to create jobs so that we return to full employment**

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**By tackling the problems of excessive household debt and mortgage arrears**

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**By giving opportunities to our children to live and work at home, including for those who have had to emigrate**

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**By ensuring that we have well-managed public finances and a stable and effective banking system**

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**By generating the resources to protect the vulnerable in our society, to eliminate poverty and to provide the public services that our citizens deserve**

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**By ensuring that the fruits of recovery are enjoyed by all of our people, in all parts of our country.**

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The future will still contain some difficult choices.

We must face these choices honestly if we are not to see a return to the failed politics and economic despair of the past.

But we face those choices with hope, with optimism for the future and with faith in the Irish people.

We want Ireland to be the best small country in the world in which to do business, in which to live, to bring up children and to grow old with dignity.

We believe this is a realistic goal and we are serious in our ambition to achieve it.



Enda Kenny T.D.  
Taoiseach



Eamon Gilmore T.D.  
Tánaiste

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## Section 01 Introduction

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## Introduction to the Medium-Term Economic Strategy



### On 15th December Ireland exited the EU IMF programme

Thanks to the sacrifices of the Irish people and their resilience during a period of substantial adjustment, significant progress has been made in restoring financial stability, fiscal sustainability and economic growth. While Ireland is now in a much better position than three years ago, stronger economic growth is needed to reduce unemployment and reduce the debt overhang.

This Medium-Term Economic Strategy sets out the core components of the Government's strategy to continue the work of rebuilding the Irish economy, achieve sustainable economic growth, strong public finances, and enduring job creation.

It explains how the Government will ensure that the failed policies of the past are consigned to history and the economy will be managed and developed on a sustainable basis, for the benefit of all.

Ireland has experienced a long and deep financial crisis. The failed policies of the last decade forced Ireland to seek external financial assistance.

After a period of strong export-led growth between 1994 and 2002, a credit-fuelled property bubble sucked labour and other resources into an over-expanded construction sector. The banking crisis which followed was accompanied by a loss of around 10 per cent in real output (with domestic demand falling by about 25 per cent), and the emergence of a major gap in the public finances over and above the cost to the sovereign of repairing the banking system.

The consequent loss of international confidence in the reputation and creditworthiness of our financial system and in the sustainability of our public finances ultimately forced the previous Government to seek external financial assistance from the IMF and our EU partners in November 2010.

The new Government elected in March 2011 renegotiated key aspects of the EU IMF Programme of Support to improve its financial, political and social sustainability. The most notable changes in this regard were the reduction in interest rates and the extension of maturities on EU loans, the replacement of the Promissory Notes as part of the liquidation of IBRC (formerly Anglo Irish Bank), the use of the proceeds from the sale of state assets for investment, the reversal of the cut to the minimum wage and the abandonment of further income tax increases committed to by the previous Government.

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## Since March 2011, important progress has been made

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Following strong implementation of the revised EU IMF Programme, the Irish economy is now emerging from a deep and prolonged recession. Signs of an economic recovery are increasingly evident.

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On the external front, the substantial improvement in competitiveness in recent years is underpinning an expansion of service exports in particular.

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Domestic demand is also stabilising after a sharp decline. Although the savings rate remains elevated, households are now more confident about making purchases and companies are investing more, reflecting their perceptions that economic conditions are improving.

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Next year, GDP is projected to increase by 2 per cent, with both domestic and external demand making a positive contribution.

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Recovery is perhaps most clearly evident in the labour market. The economy added nearly 60,000 jobs in the year to the third quarter of 2013, and the unemployment rate is now at its lowest level since 2009.

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Following a major restructuring and recapitalisation of the banking system, predominantly from State resources, financial sector stability has been restored, confidence is improving and deposits and other private capital are returning to the Irish banking system. Irish banks are issuing securities in the capital markets to fund themselves and the State has started exiting its investments.

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Stability is also returning to the public finances. The general government deficit is being reduced in a gradual, phased manner through a combination of tax and spending measures and the resumption of economic growth. The ratio of public debt to GDP is set to peak this year, and move onto a downward trajectory from next year onwards.

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While challenges clearly remain, policies designed to correct the public finances, to address the high levels of public and private indebtedness, to improve competitiveness and to stabilise the banking system are bearing fruit.

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After exiting the EU IMF Programme, the Government is focused on maintaining the reform momentum to achieve the goals of creating more jobs to enhance living standards and ultimately to achieve full employment.

This will, in turn, create resources for the delivery of a sustainable, adequate and reformed system of social supports and services for those who have completed their working years or who have caring responsibilities or a long-term disability.

## Economic Outlook & Scenarios



While economic recovery is underway, it is clear that the crisis will cast a long shadow. Legacy effects – such as high levels of indebtedness (household, corporate and public) and unemployment – will take time to work through and risks to domestic and international demand make medium-term forecasts subject to a high level of uncertainty.

There are, nonetheless, good reasons to be confident that the growth potential of the Irish economy remains strong. Ireland continues to be an attractive location for investment. The labour force is relatively young,

flexible and well-educated. Ireland has continually restated its commitment to the European Union and to membership of the euro area, which presents a potential for much greater growth and stability as Ireland takes advantage of the enormous market on our doorstep. Social cohesion has remained strong, the fiscal adjustment has been achieved as fairly as possible, and industrial peace has been maintained. The taxation regime is predictable and competitive, and Ireland has a pro-enterprise political and regulatory environment, a growing scientific base

and technological infrastructure, all of which encourage investment.

With sizeable macroeconomic adjustments still underway, the European Commission Autumn 2013 forecasts project euro area GDP will contract by 0.4 per cent in 2013 and grow by 1.1 per cent in 2014 before accelerating to 1.7 per cent in 2015. A return to growth in the euro area and a strengthening of growth in the UK and the US will be beneficial for Ireland given the high share of these three regions in terms of Irish exports.

**Table 1: BASELINE MACROECONOMIC & FISCAL PROJECTIONS 2013-2020**

	2013	2014	2015	2016	2017	2018	2019	2020
Real GDP growth	0.2	2.0	2.3	2.8	3.5	3.5	3.5	3.0
Unemployment	13.5	12.4	11.8	11.4	10.6	9.6	8.7	8.1
General government balance (% GDP)	-7.3	-4.8	-3.0	-2.4	-1.0	0.5	0.4	0.0
Structural budget balance (% GDP)	-6.5	-5.0	-3.1	-2.7	-1.4	0.0	0.0	0.0
Gross General Government Debt (% of GDP)	124	120	118	115	110	104	98	93

Source:  
Department of Finance

Note  
GGB path post-2016 is a technical assumption and indicates the GGB required to support achievement of our Medium-Term Objective (MTO) of structural balance by 2018 and its maintenance thereafter. Structural balance estimates are contingent on the estimated output gap which is subject to revision.

1

Estimates of the supply-side are subject to a wide margin in an Irish context. Different methodologies will lead to different results.

2

It is worth noting, however, at Budget time, the unemployment rate was projected to reach 11.4 per cent by 2016; better-than-expected figures since then mean that this figure could potentially be outperformed.

Appendix 1 to this document sets out two macroeconomic scenarios for Ireland covering the period 2013-2020. Table 1 shows projections for key variables from the 'baseline' scenario. It is however important to note that (i) these are baseline projections based on current trends and do not represent targets and (ii) the unemployment rate forecasts are based on the last published forecast figures to 2016 of the Department of Finance which were prepared before the release of third quarter Quarterly National Household Survey (QNHS) data on November 26th 2013. Given the stronger than anticipated outturn in that release, there may be some upside potential to the estimates for 2013 and later years.

The primary economic goal of the Government is to improve employment levels and household incomes, in a manner that is consistent with maintaining competitiveness and the stability of the public finances.

Between now and 2020, the economy is expected to grow, leading to more jobs and increases in living standards. The Department of Finance projects that the growth potential of the Irish economy is in the region of 3 per cent per annum over the medium-term, with broadly equal contributions from employment and labour productivity<sup>1</sup>. As a result, unemployment in the baseline scenario is expected to decline over the period of the Strategy, from a peak of 15 per cent to 8.1 per cent in 2020.

The Government's goal is to reduce unemployment to below 10 per cent by the end of 2016 and to achieve full employment (defined as an unemployment rate of approximately 5 to 6 per cent) by 2020. The 'high growth' scenario in Appendix 1 shows that these goals can be achieved with current baseline conditions in our trading partners, but they will also require determined implementation of appropriate Government policies, as set out in this document<sup>2</sup>.

This Strategy aims to return the public finances to balance in both headline and structural terms by 2018. Once Ireland achieves its budget target in 2015 of a deficit below 3 per cent of GDP, the application of continued budgetary rigour – combined with the positive impact of expected economic growth – will lead to reductions in the Government deficit and public debt consistent with the requirements of domestic and EU fiscal rules, without necessarily requiring further austerity measures. By 2020, the gross debt-to-GDP ratio is expected to fall to just over 90 per cent of GDP, close to the current euro area average.

## A Three-Pronged Strategy for Growth & a Job-Rich Recovery



Ireland must not repeat the mistakes of the past, when a domestic property bubble led to an over-reliance on a single domestic sector (construction), and exposed the public finances to excessive risks.

Ireland has learned the hard way the need for more effective regulation of the financial system; for greater budgetary discipline; for more responsible politics; for relentless pursuit of cost control; for innovation in both public and private sectors and for a highly-skilled and adaptable workforce to maintain our competitiveness and fuel productivity growth.

The Government is, therefore, committed to a strategy of export-led growth, as essential to sustainably enhance employment opportunities and living standards in a small open economy.

This strategy is based on three pillars:

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01

### **Ensuring Debt Sustainability.**

Confidence in the sustainability of public finances is a pre-condition for a strong and lasting economic recovery. The financial crisis and inappropriate fiscal policy left Ireland with very high public debt. Through a combination of rigorous new debt, deficit and spending rules, institutional reforms and better management of public spending, gross public debt will be brought down to safer levels (just over 90 per cent by 2020). At the same time, the Government will preserve the competitiveness of our tax system and efficiently deliver the public services and infrastructure needed to support a high quality of life and strong economic growth.

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02

### **Financing Growth.**

Rigorous management of the public finances will support strong growth if accompanied by measures to ensure adequate flows of domestic and international finance into enterprise and investment opportunities in Ireland and to resolve legacy debt problems of households and enterprises. The Government will continue to repair and restore trust in the banking system, prioritising credit availability at competitive interest rates for productive enterprise and sustainable investment. At the same time, the Government will responsibly open up new, innovative sources of non-bank finance for job creation and infrastructure development.

---

03

### **Supporting Employment and Living Standards.**

The immediate priority is to ensure the recovery continues to be jobs rich. In the medium to long-term, growth in Ireland depends on continually improving productivity, which, in turn, depends on investment in people, and boosting competition and innovation. Being part of the euro zone presents not just opportunities but domestic challenges. In this context, within a currency union, the Government needs to make our economy more resilient in the face of international shocks. Barriers to growth will be identified and removed in the key sectors of our economy. The Government will open up sheltered sectors of the economy to competition and investment, and intensify efforts to enhance the capacity of Ireland's workforce, through investment in education and training, and through measures to support people to set up business or move between jobs and sectors as the economy grows.

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This Medium-Term Economic Strategy sets out the Government's intentions to drive ahead with its reform programme under each of these three pillars. The Government's purpose is to ensure a job-rich recovery and to set Ireland on the path to sustainable prosperity, which will provide jobs and opportunity for our people, provide high quality public services, and encourage innovation in business and across society. This will enable the building of a fairer Ireland by helping to reduce inequality and improve poverty outcomes across society, with a particular emphasis on child poverty in line with the commitment in the Programme for Government.

# Ensuring Debt Sustainability

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# 02

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## Section 02 Ensuring Debt Sustainability

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Current State of Public Finances

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## Introduction



The financial crisis and its impact on the economy and public finances has left Ireland with very high public debt. Confidence in the sustainability of our public finances is, therefore, a pre-condition for a strong and lasting economic recovery.

There are a number of reasons for this. Higher levels of debt tend to increase sovereign borrowing costs. Because sovereign borrowing costs typically set the floor for the rate at which households and firms can borrow, imbalances in the public finances may push private sector borrowing costs upwards, dampening investment and growth.

High levels of public indebtedness also absorb a larger portion of government revenue through debt servicing needs, ultimately resulting in lower expenditure in other areas including growth-enhancing areas.

In the context of high deficit and debt levels, fiscal adjustment and the consequent restoration of sound public finances are crucial for restoring lost credibility and strengthening investor confidence. Confidence that the debt burden will be resolutely reduced over time is needed to support durable market access, both on reasonable terms and across a broad investor base. This is an absolute prerequisite for building a strong economy that can support good jobs and provide the public services needed to meet demand.

## Current State of the Public Finances



Significant progress has been made in addressing the underlying problems of the public finances. Since the crisis began, over €30 billion of fiscal adjustments have been introduced, equivalent to just over 18 per cent of GDP.

These policy measures have resulted in a decline in the underlying general government deficit, from a peak of 11.2 per cent of GDP in 2009 to a projected 4.8 per cent of GDP in 2014. The deficit has been reduced in a gradual, phased manner consistent with the dual needs of supporting economic activity as well as repairing the public finances.

Looking to 2014, this is the first time that the Government has sought to surpass the deficit targets set in 2010 and is reflective of the prudent fiscal management that has been in evidence since the Government was elected. Ireland's credibility is being restored, and this is reflected in the decline in our borrowing costs in recent years.

2014 also represents the first time since the crisis began that the Government is planning to achieve a primary surplus, i.e. State revenues greater than expenditure when debt interest costs are excluded. This is a key metric from a debt sustainability perspective. The debt ratio is estimated to peak at around 124 per cent of

GDP in gross terms (at 99 per cent in net terms) at end 2013.<sup>3</sup> Continued fiscal prudence, coupled with economic growth and the effect of stock flow adjustments (the running down of cash balances), are expected to bring the debt ratio down to just over 90 per cent by 2020.

## Where We Need to Get To

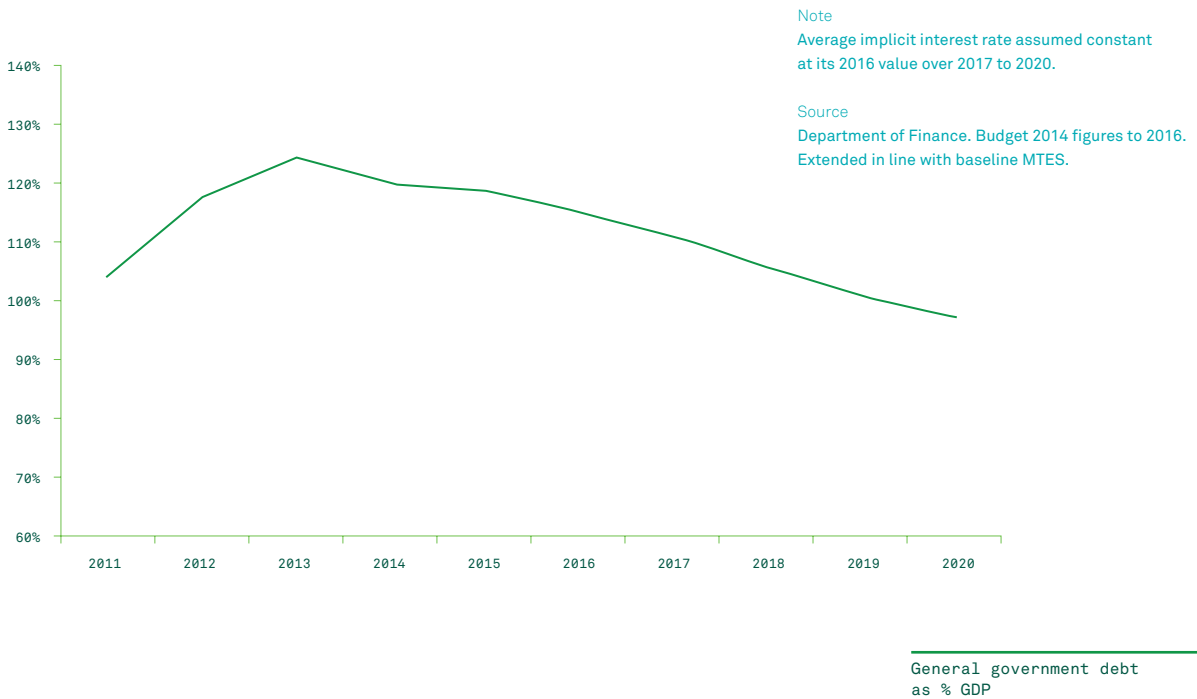


Over the medium-term, economic recovery must continue to be supported by putting the sustainability of our public finances beyond doubt. By 2018, the Government aims to be running a balanced budget in both structural and headline terms. The debt-to-GDP ratio will be on a declining path, helped *inter alia* by primary surpluses and a growing economy.

As Ireland's debt ratio is projected to peak in 2013 and remain on a downward trajectory thereafter, compliance with the debt correction rule – requiring a reduction in the portion of the debt in excess of 60 per cent of GDP by 1/20th on average per annum – should be achieved once the structural balance in the public finances is achieved in 2018 and maintained thereafter. The gross debt ratio is projected to fall to just over 90 per cent by 2020.

While there are specific fiscal risks to the forecasts, the major risk remains the macroeconomic outlook. The path of fiscal recovery is dependent on economic growth materialising both domestically and internationally. Therefore, within the strict overall budgetary constraints, taxation and expenditure policy must be oriented to continue to support economic growth and job creation.

Figure 1: DEBT PATH UNDER BASELINE SCENARIO



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## What We Need to Do



### Complying with Domestic and EU Fiscal Rules

Fiscal policy in Ireland is formulated within the boundaries of both the Stability and Growth Pact (the Pact) and the Treaty on Stability, Co-ordination and Governance (TSCG). Ireland is currently subject to the requirements of the corrective arm of the Pact; within a multi-annual correction framework, interim targets for the headline deficit have been set. To date, we have consistently overachieved against these deficit targets.

For 2014, a general government deficit of 4.8 per cent of GDP is targeted, well within the 5.1 per cent of GDP ceiling set under the corrective arm of the Pact. Thereafter, the Government is fully committed to correcting the excessive deficit in 2015 by reducing it to under 3 per cent of GDP.

Once the excessive deficit is corrected, Ireland will be subject to the requirements of the preventive arm of the Pact. This involves making progress towards the medium-term budgetary objective (MTO), which is for a balanced budget in structural terms. In compliance with the requirements of the Pact

and the TSCG, Ireland should achieve its MTO by 2018.

Provided potential revenue growth is reasonable, then modest expenditure increases, taxation reductions or a combination of both can be achieved over the medium-term, while at the same time progress towards a balanced budget in structural terms can be facilitated. This underlines the importance of measures designed to boost the growth potential of the economy, as this will give the Government greater discretionary resources to pursue economic and social policy objectives. Moreover, a reasonable potential growth rate should be sufficient to comply with the requirements of the debt correction rule (i.e. the so-called 1/20th rule).

### Ensuring Higher Levels of Budget Transparency

Complementary to the European fiscal rules are the considerable improvements that have taken place domestically in the area of fiscal governance. The Irish Fiscal Advisory Council (IFAC) has been established with a mandate to assess compliance with fiscal rules

and to assess if the fiscal stance is conducive to prudent economic and budgetary management. In addition, the IFAC has the role of independently endorsing the macroeconomic forecasts on which the Budget and Stability Programme are based. This helps to ensure transparency and openness in the forecasting process. The oversight role for IFAC will help steer the course of fiscal policy and provides for greater governance and accountability.

In addition, binding multi-annual expenditure ceilings have been introduced which boost transparency and facilitate a more efficient allocation of resources. These expenditure ceilings are in part informed by periodic comprehensive expenditure reviews that examine expenditure across the full spectrum of Government programmes and focus particularly on establishing what is being delivered with public resources and identifying where there are opportunities to improve efficiency and effectiveness.



### Reinforcing a Competitive and Fair Taxation Policy

At its most basic level, tax is the price we must pay for the services and income supports provided to society by Government. At the same time, good tax policy requires taxes that are structured to support or, at the very least, not inhibit economic growth.

The crisis exposed considerable shortcomings in the structure of Ireland's tax system. This was characterised by both an over-dependency on cyclical property transaction taxes such as stamp duty and a systematic narrowing of the income tax base as a matter of policy over a decade. The net result was a collapse in revenue

from transaction taxes and significant weakness in income tax – in 2009 some 44 per cent of income taxpayers paid no income tax. This was structurally unsustainable.

Since 2009, significant progress has been made in addressing the frailties of the tax system. In that period, policy measures amounting to €11 billion have been introduced across the entire system. While tax rates other than corporation tax have increased, there has been a significant emphasis on base broadening through the abolition or curtailment of tax reliefs such as those relating to property investment and interest relief as well as increases in minimum tax rates

for high earners. Over the period, this approach has meant that those at the top of the income distribution made the greatest contribution to the fiscal adjustment - most recently through the capping of the tax relief on funding pensions in excess of €60,000.<sup>4</sup>

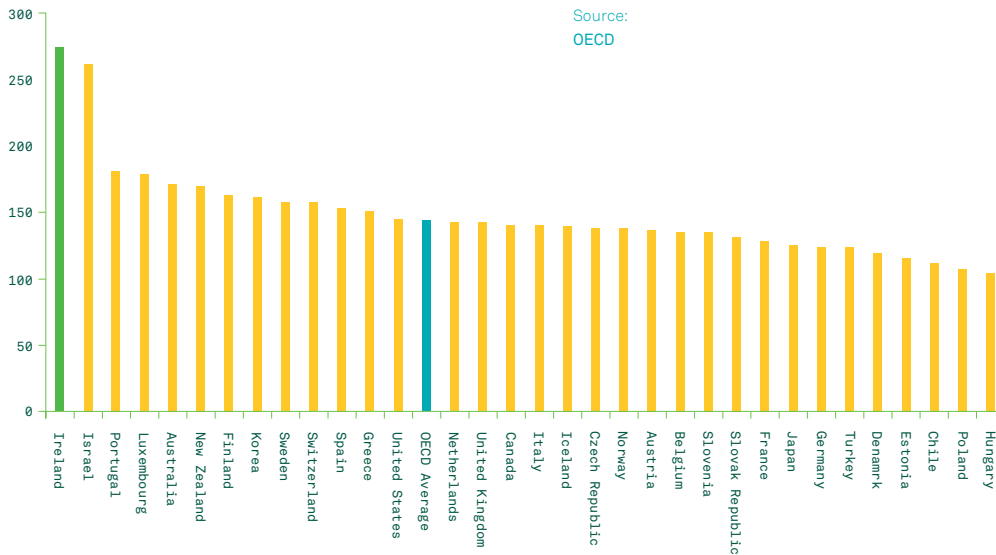
In addition to the curtailment of tax reliefs which are generally availed of by higher earners, the tax system has become more progressive since 2009, meaning that those on higher incomes pay proportionately higher rates of tax on their income than those on lower incomes.

Figure 2 shows a comparison of progressivity of tax systems across OECD member states and shows

**Figure 2: PROGRESSIVITY OF INCOME TAX – OECD MEMBERS 2012: SINGLE TAXPAYERS**

Note  
Data for single taxpayers, no children, comparing ratio of income tax and employee Social Security Contribution as proportion of wages at 167% and 67% of average wage for 2012.

Source:  
OECD







Ireland to have the most progressive income tax system. The Government is committed to maintaining this strong progressive structure and will continue to ensure that the taxation base remains competitive so as to ensure as wide a revenue base as possible in order to fund the provision of public services. We will also have regard to the appropriate balance between personal taxation and social insurance contributions over the period of this strategy.

The taxation of property has also been transformed. Transaction taxes on property are now at relatively modest levels while a less cyclical tax measure, the Local Property Tax, has been introduced. Property incentives have been largely abolished while mortgage-interest relief is being phased out. Capital tax rates have been increased and reliefs reduced. Carbon tax, VAT and excise duties have also been increased.

The rationale for this approach is very clear. It has been to ensure that core income tax rates did not increase and that the corporation tax rate could be kept at 12.5 per cent. These are key to attracting foreign direct investment (FDI), creating employment and underpinning economic recovery.

Accordingly, there are a number of strategies and actions that will be employed to ensure the tax system is used to meet the dual objectives of funding the provision of efficient and effective public services and at the same time encouraging well balanced economic growth, both taking into account the overriding fiscal parameters.

To this end, the Government will:

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**Maintain an economically rational and sustainable approach to tax policy consistent with the dual mandate of funding public services and supporting economic growth.**

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**Support economic growth by ensuring any tax increases be effected in the first instance by base broadening through the elimination or curtailment of overly-generous, poorly targeted or otherwise unaffordable tax reliefs.**

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**Avoid increases in income tax rates consistent with fiscal obligations. The Government must ensure that work pays.**

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**Maintain 100 per cent commitment to the 12.5 per cent corporation tax rate: it is settled policy and will not change.**

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**Continue to be a key influencer of developing international tax policy on tax competition and transparency<sup>5</sup>.**

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**Keep indirect taxes under review including in the context of developments at EU level and with a view to minimising cross-border distortions.**

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**Use the tax system in limited circumstances where there are demonstrable market failures and where a tax-based incentive is more efficient than a direct expenditure intervention.**

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**Time-limit all tax expenditures and subject those with higher costs to *ex-ante* evaluation.**

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**Conduct a regular programme of tax relief reviews using public consultation as appropriate and publish the results.**

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**Bolster our tax law and administration where necessary to tackle non-compliance and aggressive tax avoidance so as to support fairness.**

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The MTO is complemented by the 'expenditure benchmark', which helps ensure control of General Government expenditure, net of discretionary measures and excluding interest and the effects of cyclical unemployment growth. It provides that GG expenditure (including the local authority sector and other GG subsectors) does not grow faster than the combined effect of the average potential growth rate of the economy when a Member State is at its MTO and the GDP deflator. When a Member State is not at its MTO, GG expenditure growth is constrained by incorporating a 'convergence margin', calculated to ensure that the required annual adjustment towards the MTO in structural terms is achieved.



## Maintaining Discipline in Public Spending

On the expenditure side, continued restraint will remain necessary to avoid exposure of the State's finances to any possible future economic downturns. The expenditure plans for 2014 and 2015, as set out in Budget 2014, will support the achievement of the target of a 2.9 per cent of GDP underlying general government deficit by 2015. From 2016 onwards, the Government is projecting that there will be some space to allow for modest and gradual growth in public spending<sup>6</sup>.

Considerable progress has been achieved in recent years in returning Government expenditure to a sustainable, affordable path. This required some very difficult but necessary decisions that led to a reduction in day-to-day spending on public services across central Government from €53.4 billion in 2008 to €49.6 billion for 2014. Through the parallel process of public service reform, significant efficiency improvements have offset a great deal of the impact of the spending reductions. In this way, notwithstanding the reductions in expenditure and a lowering of public service employment by almost 10 per cent in the last five years, increased service demands have been met, most notably in health, education and social protection.

Expenditure pressures:

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**The Live Register increased from 161,722 in November 2007, peaked at 470,284 in July 2011, then fell to 391,507 in November 2013, and expenditure on the live register has increased from €1.4 billion in 2007 to projected expenditure of €3.3 billion in 2014;**

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**The health sector has experienced increased demands with the numbers on medical cards increasing from 1.27 million in 2007 to 1.85 million in 2014;**

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**In the same period the number of primary and secondary students has increased by 75,000 to 855,300 with the number of full time third level students increasing by 17,000 to 164,000.**

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Future spending will continue to prioritise measures that contribute to economic growth and job creation, while protecting and supporting the most vulnerable in society. Making these well-informed spending choices requires the availability of quality analysis on needs and on the effectiveness and impact of expenditure measures.

To this end the Government undertook a Comprehensive Review of Expenditure (CRE) in 2011 which examined spending right across the spectrum of central Government and which informed the expenditure decisions for the 2012 to 2014 period.

The next Comprehensive Review of Expenditure will be undertaken in advance of Budget 2015. This will again allow for a detailed examination of current expenditure across all areas of Government, and it will build on the knowledge and experience gained from previous reviews and other evaluations. It will examine spending trends and pressures, and help to identify ways of addressing the challenges arising in the context of fiscal policy. The purpose of the CRE will be to inform Government decisions on future budgetary matters and allow for the Government's recalibration of ministerial expenditure ceilings in light of changing priorities and evaluations of expenditure.

## Making Space for Public Capital Investment

In recent years the Exchequer capital programme has continued to address priority infrastructure deficits and to invest in Ireland's future. This has been done at a time when fiscal consolidation was a necessity and resulted in lower levels of resources being available for capital investment. However, this reduction must be viewed in the context of a significant level of investment in the preceding decade which saw most of the critical infrastructure needs met.

Since its infrastructure investment plan was launched in 2011, the Government has been able to announce a number of increases to its capital plans through the use of the proceeds from the sale of State assets and the Lottery licence transaction and the introduction of a new Public Private Partnership (PPP) programme. As the economy recovers, capital investment requirements can again be reviewed from the perspective of sustaining and enhancing economic growth.

PPPs will continue to be used as a delivery mechanism for infrastructure delivery, while ensuring value for the State. Much has already been done in this area and Ireland is successfully delivering a PPP programme announced by Government in July 2012.

During 2014 – and in parallel with the review of current expenditure – there will be a review of the capital investment framework to provide an updated outlook on the pipeline of capital support and identify key areas in which the Government will prioritise its investment over the medium-term. This review will assist the Government in identifying the priority areas for investment that will ensure that, in an affordable way, Ireland has the infrastructural capacity to support and sustain economic growth. t

The Ireland Strategic Investment Fund (ISIF) will further support capital expenditure priorities through commercial investment.<sup>7</sup> In addition European Structural and Investment Funding will be available over the period 2014–2020<sup>8</sup>.

### Reforming the Public Service

Public Service Reform has been a key element of the Government's strategic response to the economic crisis and has set out an ambitious agenda for reform across all areas of the public service.

Considerable progress has been made over the past number of years through reducing costs, improving productivity, delivering a greater number of services online and implementing shared services. The Exchequer Pay Bill, which peaked in 2009 at €17.5 billion will decline to €13.6 billion in 2014. In addition, these measures have been taken during a period of unprecedented demand for public services, while the number of public servants has been reduced from 320,000 in 2008 to under 290,000 by the end of this year.

Alongside the overall Reform Plan, all Departments and major offices have their own Integrated Reform Delivery Plans, which set out the key actions required to ensure the successful delivery of the cross-cutting reforms in the Public Service Reform Plan, as well as sector-specific reform initiatives and actions from the Haddington Road Agreement which will deliver further

savings to the pay and pension bill of €1 billion by 2015.

With implementation of the Public Service Reform Plan underway, it is now timely to consider how the Government can build on what has been achieved to date. A renewed Reform Plan is currently in development and will set out ambitions for the coming years.

Given the fiscal situation, the primary focus of the current phase of reform has necessarily been on cost reduction and efficiency measures. As we reach a more sustainable fiscal position, the next phase of reform will have the goal of providing a Public Service that achieves further efficiencies and positive outcomes for all stakeholders, including citizens, businesses and public servants themselves.

In the context of closely-managed expenditure ceilings, further innovative solutions will be needed to ensure that high performing services can be delivered and that people with the necessary skills and capacities to deliver productive, cost-efficient and high-performing public services can be recruited and retained.

A new Public Service Reform Plan covering 2014 to 2016 will be published early in 2014. This will set out the ambition for the next phase of Public Service Reform, outlining both cross-cutting and sectoral reforms.



With respect to the Health sector, which will remain a key priority going forward, Future Health: A Strategic Framework for Reform of the Health Service 2012-2015, provides a structure which sets out the main healthcare reforms that will be introduced in the coming years.

Future Health will deliver a major reshaping of the health system by restructuring service delivery, and improving organisational, financial, governance and accountability systems across the board – in the primary, community and hospital sectors. The approach to reform is constructed around four pillars:

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#### Health and Wellbeing

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#### Service Reform

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#### Structural Reform

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#### Financial Reform

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Future Health will be complemented by a Government White Paper on Universal Health Insurance, to be published early in 2014. In addition, the implementation of generic substitution and reference pricing has been prioritised by the Department of Health, the Health Service Executive and the Irish Medicines Board.

The Health (Pricing and Supply of Medical Goods) Act 2013 also includes a process for the review of existing prices outside of reference pricing. Each medicinal product, which was on the Reimbursement List when the legislation was commenced, must be reviewed by the HSE within three years to determine whether it should remain on the list and, if so, the price that should apply.

#### Completing the Separation of Banking from Sovereign Debts

It is Government policy to continue to dispose of its holdings of banking assets. In 2013, we have already realised €4.4 billion from the sales of debt and equity securities in Government supported banks and Irish Life.

The baseline debt path is the same position as in the Budget 2014 publication and therefore includes neither the proceeds of the sale of the Bank of Ireland preference shares nor any further receipts as the timing and quantity of sales is difficult to predict. The further disposal of any such assets, would be likely to have a beneficial impact on the debt path. In tandem to potential private sector disposals, the Eurogroup has agreed that retroactive recapitalisation may be decided on a case-by-case basis as part of the European Stability Mechanism's Direct Bank Recapitalisation instrument (DBR). Significant work remains to be

done on the details of this instrument. Looking to the future, the Government will strengthen national bank resolution legislation to further protect taxpayers from future banking losses by ensuring that, in line with forthcoming European legislation, creditors earning a risk premium on their investments take losses before taxpayers.

The Government is also working with our European partners towards banking union, which will provide additional protection to taxpayers by ensuring consistent regulation by the European Central Bank. It will also provide for a single resolution mechanism, which will ensure timely and least-cost resolution of impaired banks. The completion of banking union is intended to break the link between the sovereign and the banking sector in such a way that investors lend to banks and charge an appropriate risk premium for such lending, according to the financial and capital position of the bank in question, as opposed to the strength of the public finances in the bank's Member State. This should lead to convergence in the cost of credit across the EU.

#### Providing for an Ageing Population

Ensuring adequacy of income in retirement for the Irish people is a central objective for the Government.

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A key challenge for the State is to ensure a sustainable and flexible approach to pensions over the medium and long-term that delivers an adequate income in retirement. Current projections, including the Actuarial Review of the Social Insurance Fund published in 2012, show an increase in the proportion of retirees in the medium and long-term, which will place an additional burden on public and private sector pension schemes and the State pension system. The additional burden can already be seen in the resources required to fund State pensions, which increased by over €190 million in 2013 alone. Pressures of this magnitude or greater will continue in the medium-term and will therefore be central to any future restructuring of the tax (including USC) and PRSI systems. However, a number of important reforms have already been undertaken by the Government to address issues of sustainability.

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#### **State Pensions**

The Government has brought in necessary changes to the age of qualification for State Pension schemes. From 2014, the age of entitlement to all pension age schemes will be set at 66 years and the State Pension Transition will be discontinued. Further increases in the qualification age for the State Pension will take place in 2021 (age 67) and in 2028 (age 68). The Government has also increased the number of social insurance contributions required to qualify for a State Pension and ensured that those who contribute during their working life benefit more in retirement. It has also reduced the deficit of the Social Insurance Fund through measures, including broadening the PRSI funding base, but significant challenges remain.

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#### **Private Occupational Pensions**

Private occupational pension schemes have faced significant challenges during the economic crisis. The Government has taken a number of steps to address the sustainability of defined benefit pension schemes, including increasing options for scheme restructuring, the issuing of sovereign amortising bonds, and measures to improve risk sharing between scheme members which will ensure fairer outcomes when such schemes and/or the relevant employers become insolvent. Improvements were made to the regulatory structure to provide for a requirement for defined benefit schemes to have a reserve to protect against the risk of volatility in the financial markets.

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#### **Public Service Occupational Pensions**

Since 2009 progressive reductions to the pay of public servants and to the pensions of public service pensioners have reduced pension and lump sum awards to ensure their better sustainability. Since January 2013, a new Single Public Service Pension Scheme applies to all new public servants. The main features of the new scheme are benefits based on career-average earnings rather than final salary, valorisation of accrued pension rights based on the CPI and steadily increasing retirement ages.

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#### **Proposals to Further Ensure Sustainability**

The OECD published a comprehensive review of the Irish pensions system in 2013 setting out a range of recommendations aimed at enhancing the long-term sustainability and coverage of pension provision in Ireland. While the OECD acknowledged an overall good level of State Pension provision in Ireland, it also recommended the need to supplement this by way of a universal employment related supplementary mandatory/quasi mandatory pension scheme. The Government supports the introduction of such a scheme in principle and having reflected on the OECD's recommendations, will bring forward detailed proposals setting out its long-term plans in this area early in 2014.

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# Financing Growth

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# 03

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## Section 03 Financing Growth

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### In this section:

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Introduction

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Current State of Financial System

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Where We Need to Get To

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What We Need to Do

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## Introduction



Since the onset of the financial crisis, credit availability has been severely constrained. The impact has rippled across various sectors of the economy including households, SMEs and infrastructure financing. In particular, households, many with high levels of debt and some in arrears, are also constrained in their capacity to borrow. SMEs also face difficulties in accessing finance to fund investment and growth.

In both instances, excessive debt overhang and consequential deleveraging are adversely affecting credit conditions. This is a critical impediment to stimulating demand, enabling growth and fostering innovation. The financial and fiscal challenges faced by the State in the period since 2008 have also triggered a substantial reduction of public expenditure on infrastructure investment. Government has taken a number of actions to assist in the financing of the economy, launching a suite of new and innovative products and initiatives, but more needs to be done.



## The Current State of the Financial System



### Irish SMEs Face Credit Constraints

Businesses in Ireland are overly-reliant on bank lending. This is common across Europe where approximately 80 per cent of debt financing to the economy is provided by banks.

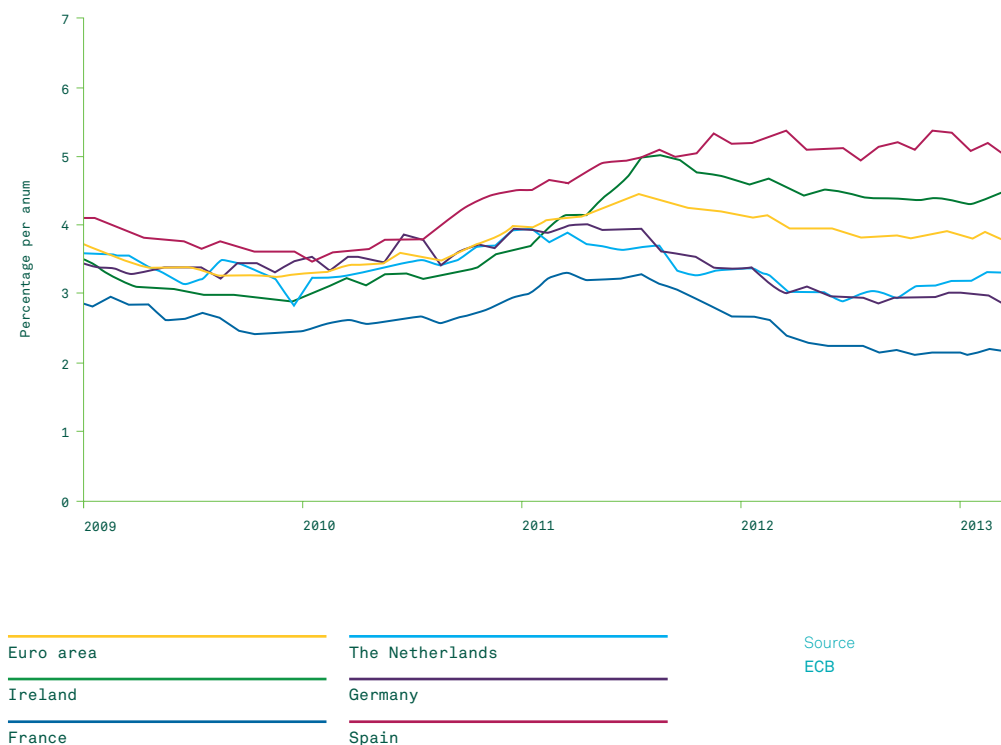
As a result, Irish SMEs are heavily exposed to the difficulties faced by Ireland’s pillar banks and non-pillar banks since the onset of the financial crisis. The challenging environment is illustrated by the fact that credit advanced to Irish resident SMEs (excluding the financial and property

related sectors) has fallen over 20 per cent from €32.4 billion to €25.1 billion between September 2010 and September 2013.

Difficulties faced by SMEs accessing financing are not purely an Irish phenomenon. Irish SMEs have been disproportionately exposed due to their reliance on Irish banks facing balance sheet constraints, foreign banks focusing on their home markets and a lack of alternative sources of financing.

The period since 2008 has also witnessed an increased fragmentation of European financial markets with the result that the cost of credit for entrepreneurs and SMEs in Ireland is higher relative to other European trading partners where the sovereign enjoys a higher credit rating. This considerable divergence in credit conditions has created a strong competitive disadvantage for Irish entrepreneurs and enterprises (see figure 3 below).

**Figure 3: AVERAGE INTEREST RATES ON SHORT TERM LOANS (<€1 MILLION)**





**Infrastructure Financing Has Also Become More Difficult**

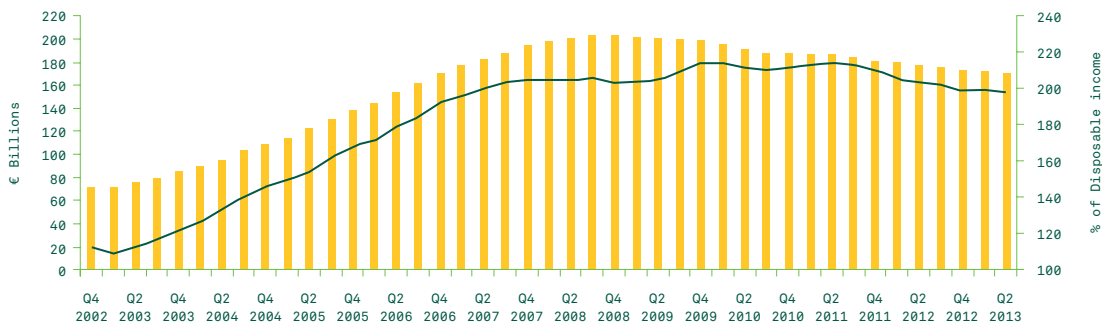
Bank financing for infrastructure development has also become more difficult to source. This can be attributed to a combination of fiscal constraints and changing banking regulation. It should be noted that the infrastructure financing environment in Ireland, in more recent times, has improved alongside the improvement in Irish sovereign yields. International banks and institutional investors are re-engaging in the Irish market, thereby assisting in the delivery of Ireland’s PPP pipeline.

However, the changing landscape of banking regulation makes the long dated nature of infrastructure investment less attractive for banks. While banks continue to provide the majority of funding for infrastructure projects alongside the EIB, there is a growing need to attract institutional investors including Irish and international pension funds and capital market participants whose investment needs are better matched to the long duration, stable cash flow profile of infrastructure investment.

**Irish Households Are Deleveraging**

The period since the mid 1990s witnessed a rapid increase in the levels of personal debt in Ireland. Central Bank data show that the total volume of household liabilities increased rapidly throughout the 2000s peaking at €203.8 billion in Q4 2008<sup>9</sup>. As a result the household debt<sup>10</sup> to disposable income<sup>11</sup> ratio, which is an indicator of household debt sustainability, rose sharply from Q4 2002, peaking at 223.9 per cent in Q4 2009 (Figure 4). This high level of household debt, alongside high unemployment and high mortgage arrears, impacts negatively on domestic

**Figure 4: IRISH HOUSEHOLD DEBT AS A PERCENTAGE OF DISPOSABLE INCOME**



Irish household debt (lhs)

Irish household debt as percentage of gross disposable income (rhs)

Source: Central Bank of Ireland, Central Statistics Office (Ireland).



demand. While recent figures from the Central Bank indicate that the household debt to disposable income ratio has now begun to decrease, it remains high by European standards<sup>12</sup>.

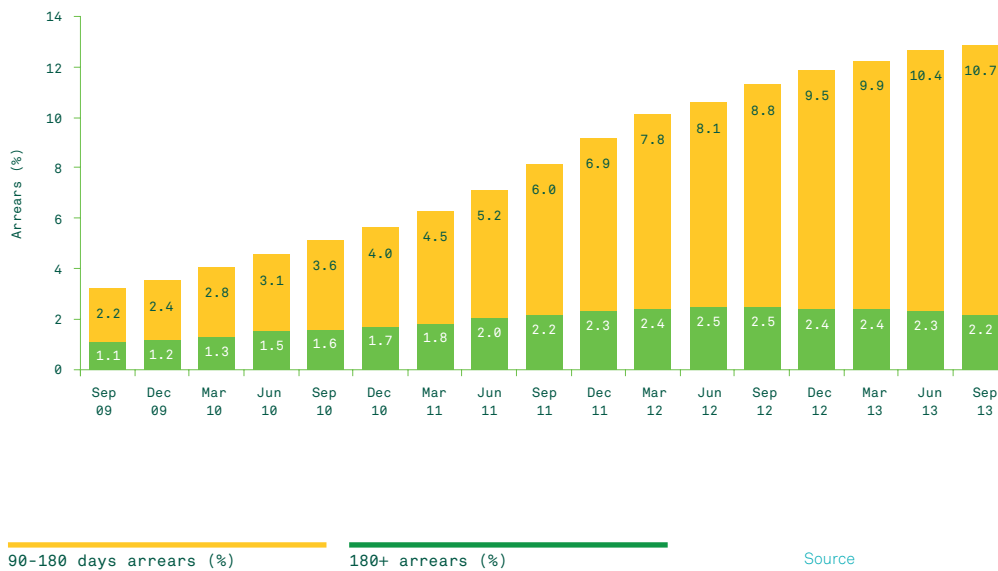
A feature of the economic crisis has been the rise in mortgage arrears, with the percentage of owner occupied mortgages in arrears for 90 days plus, increasing steadily from 3.3 per cent in Q3 2009 to 12.9 per cent in Q3 2013 (see Figure 5). High levels of mortgage arrears not only impose large financial and social costs on individual house-

holds but also exert sizeable economic costs. One of the primary objectives of Ireland’s new Personal Insolvency legislation is to create a modern and equitable framework that will both assist individuals in resolving their debt-related difficulties and also encourage their productive participation in both the economy and society.

The collapse of the residential property market since the peak of 2007 has been mirrored by a similar collapse in new mortgage lending. Recent evidence suggests an improvement in this

area with the value of mortgage lending in Q3 2013 at €750m - an increase of 13.1 per cent on Q3 2012.<sup>13</sup> Nevertheless new mortgage lending remains constrained by legacy issues such as affordability, negative equity, arrears and borrowers’ unwillingness to move house if it means ceding the advantages of tracker mortgages.

**Figure 5: MORTGAGE ARREARS STATISTICS (BY NUMBER) – PRIMARY DWELLING HOUSE**



## Where We Need to Get To



### The Government is Reforming the Financial Sector

Government has developed a range of policies designed to restructure the Irish banks, improve access to finance for viable businesses, secure increased investment in infrastructure and address the problems of mortgage arrears and high household debt. These initiatives have included:

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**Government sanctioned lending targets to SMEs for both Bank of Ireland and AIB;**

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**A suite of State-sponsored financing instruments that provide a broader range of capital, equity, and debt funding across all stages of the business cycle.**

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**Soon to be published legislation to establish the Ireland Strategic Investment Fund (ISIF) which will absorb the resources of the National Pensions Reserve Fund (NPRF) and redirect them to commercial, Ireland-focused investments that support economic activity and employment;<sup>14</sup>**

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**Establishment of NewERA to work with stakeholders and accelerate investment in strategic infrastructure;**

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**Intensified engagement with the EIB in order to increase the scale of EIB funding for economic activity in Ireland (infrastructure and SMEs); and**

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**An integrated mortgage arrears strategy incorporating Personal Insolvency, a Mortgage Advisory Service, the Mortgage to Rent Scheme and intense engagement with the banks.**

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While the financial sector has already been through radical transformation, much more needs to be done to support the economic recovery.

Ireland must have a financial system that engages effectively with, and serves the needs of the real economy. In particular, Ireland must have a more diversified and stable financial system premised on a competitive and profitable banking sector and increased direct capital market financing of both infrastructure and enterprises, with greater involvement by institutional investors and alternative financial markets.

In this context, Ireland will aim to be a world leader in the provision of a diverse and innovative suite of financial products to SMEs. Ireland will also have resolved the problem of debt overhang within households and the SME sector. Similarly, Ireland will also be to the fore in both expanding the range of funders involved in infrastructure development and also designing responsible innovative financing structures. NewERA and the ISIF will play a catalytic role in accelerating investment in strategic infrastructure and providing commercial financing and investment in areas that support economic growth and employment.

Finally, the financial system will also provide a suite of appropriate products to meet sustainable demand for credit and will better embrace technology in the delivery of payment and other banking services to households. State institutions and enterprise agencies will continue to play a strategic enabling role, channelling investment into potentially high growth, strategic and innovative sectors of the economy. This role may diminish over time as private sector players replace State support.

## What We Need to Do



Achieving the goal of a well-financed economy will necessitate policy makers and other relevant stakeholders improving the effectiveness and competitiveness of the financial system – markets, institutions and financial instruments – in both attracting available domestic and international savings and channelling them towards the financing of infrastructure, enterprises (including SMEs) and households.

In parallel, Government must continue to use its agencies and resources to support enterprises to innovate, grow and develop their capacity to internationalise, enabling them to become world class and capable of competing on global markets. The key pillars and strategies to achieve this are summarised in the sub-sections below.

### A new banking landscape

Banks will continue to be the key players in the financing of the economy. This highlights the need to complete the necessary restructuring of the Irish banking sector in a manner that will underpin a return to both sustainable profitability and private ownership. The right-sizing of the banks, in conjunction with the emergence of a new national and European regulatory environment, ensures that the banking landscape that will emerge in the period 2014-2020 will be markedly different to that of the pre-financial crisis era.

Strengthening the role of the banking sector in supporting enterprise and infrastructure development will, in part, be dependent on reasserting the key intermediary and transmission roles of banks and encouraging activities, in partnership with other financial institutions, that strengthen their core capacities and functions. In relation to both infrastructure and enterprise development, there is clearly considerable potential in developing new innovative financing structures involving a more diverse range of bank and non-bank actors.

There is a need to foster an environment for increased competition in the retail banking sector. While considerable restructuring of Ireland's banking system has been necessary in recent years, there has been a deterioration in competition in the retail banking sector, as the global financial crisis has resulted in some foreign banks either scaling back lending activities or exiting the Irish market entirely to focus on their home markets. These issues will be addressed by seeking to attract more institutions into the financial system and scaling back the role of the State within the sector.

The Government will work with the Central Bank to provide a transparent, responsible and welcoming regulatory landscape to attract foreign banks and financial institutions with responsible lending practices to

Ireland, including those establishing branch networks and those providing digital banking or non-bank lending.

Over the course of this Strategy measures will be undertaken to enhance:

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### Customer mobility and protection

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### Entry of competitors into the financial services market; and

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### Responsible lending and resolution strategies.

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It is also expected that the delivery channels for bank services – payment over the counter and other client facing services will change dramatically over the term of this Strategy through, for example, ongoing advances in digital banking. Consequently Government will work with the Central Bank of Ireland, banks and other new providers of finance to ensure Ireland's system can be restructured to become best in class and also a hub for global payment services. There is a need for further mortgage products which can facilitate trading up and trading down with negative equity and options for customers with tracker mortgages to increase mobility and availability of properties for sale.

Ireland will compare its financial system to other financial systems, adopting good practices



where appropriate while learning from mistakes made in other countries. This could include learning from countries where the development of more diversified infrastructure financing markets has generated improvements to certain aspects of the funding of infrastructure or markets where a more diversified secondary market for mortgage and SME lending exists due to greater involvement from institutional and retail investors.

In parallel, the strategy of attracting the R&D operations of multinational banks will be scaled up in order to establish Ireland as an international centre of financial innovation particularly in relation to how SMEs are funded through their business life-cycle.

### Deleverage Household Debt

A comprehensive plan has been put in place to deal with those with excessive household debt. There will continue to be full and determined implementation of the Government's strategy incorporating Personal Insolvency, a Mortgage Advisory Service, the Mortgage to Rent Scheme and more intense engagement with the banks and credit unions. Increasing employment will help but in any event it is imperative that unsustainable debts are managed and dealt with so that domestic demand contributes to economic growth. Targets have been set for the banks to agree sustainable long-term solutions for households and these targets must be met.

### Non-Bank Funding

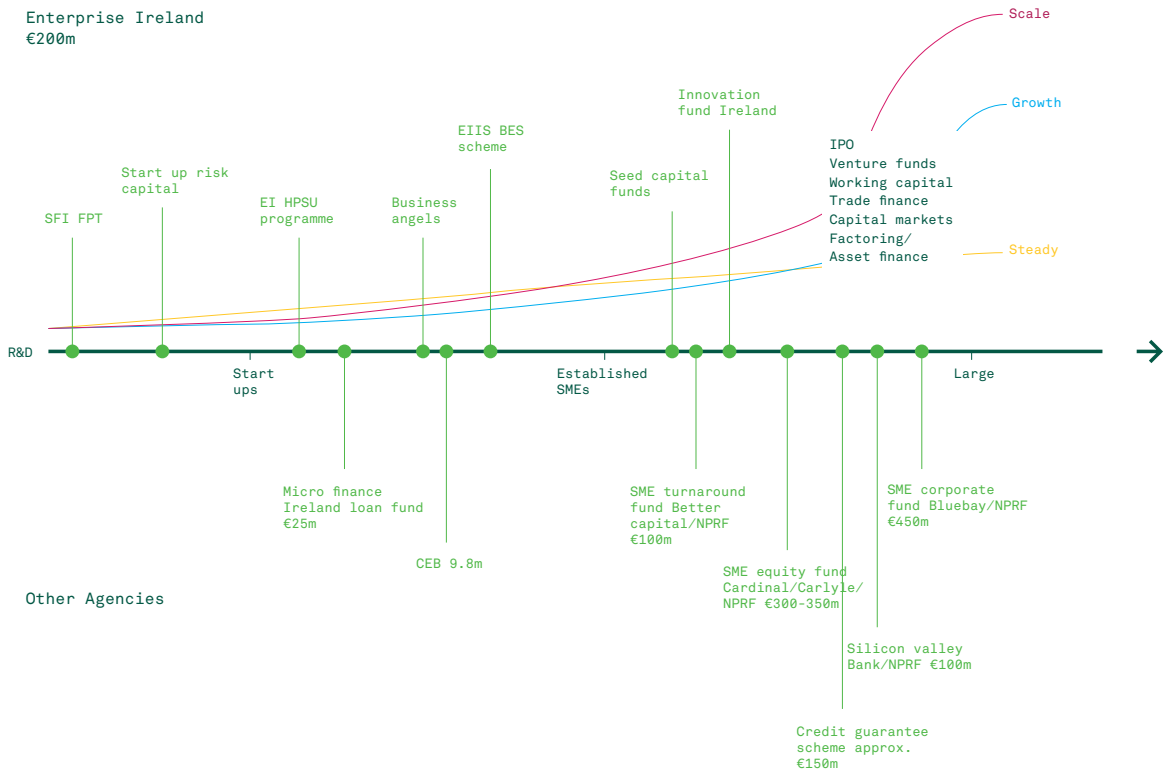
Ireland needs to develop a more diversified and stable financial system with increased direct capital market financing and a greater involvement by institutional investors and alternative sources of finance. There are two broad strands to this: firstly measures that will reduce capital and funding pressure on banks and, secondly, initiatives that will connect non-bank lenders directly to enterprises.

Europe's lack of a robust securitisation market is a key constraint on credit flows. Reigniting this market will require action at both the national and European level. It is important that Ireland actively promotes initiatives by EU institutions in supporting SME

securitisations as this can play a key role in kick-starting these markets to generate funding sources for banks, particularly in countries where banks and/or sovereigns are credit-rating challenged at present. In this way, EU institutions can contribute to addressing the fragmentation of SME funding markets. However, this has to be matched by action at the national level, and there is an onus on government and the national regulator to proactively work with industry to develop concrete measures that will support the development of quality, simple and transparent securitisations.

Irish enterprises and entrepreneurs must also be encouraged to shift from an overreliance on debt towards a greater use of private equity in growing and scaling their businesses. In relation to venture capital and seed funds, public policy needs to create an environment in which private sector investment ultimately becomes a greater source of seed and venture capital funding. In certain key sectors, the venture capital industry has remained relatively robust, despite the financial crisis, with, for example technology companies in Ireland attracting four times as much venture-capital funding per capita as the European average since 2003<sup>15</sup>.

Figure 6: SELECTED SME FINANCING INSTRUMENTS



Stimulating increased levels of direct funding by capital markets is also a key priority. Drawing on successful bespoke private placement markets, e.g. the German *Schuldscheindarlen* market, there is an opportunity for Ireland to establish a national private placement regime that will develop direct funding sources to SMEs and Mid-Caps. Similarly there is considerable potential to create a more diversified funding environment for Irish SMEs by seeking to connect retail investors to productive investment through the development of a retail “mini-bond” market.

There is also a need for co-ordinated and focused policies at the national and EU levels that are designed to incentivise dynamic companies – both SMEs and larger corporations – to continue to grow and scale using the IPO route to raise development finance as opposed to a trade sale exit.

Ireland also needs to create the appropriate regulatory and legislative environment to facilitate specialised debt funds (funds of loans) providing direct capital market funding to SMEs. These types of funds can also play a role in increasing the efficiency and liquidity of the secondary market for

loans to SMEs originated by banks thus providing incentives *ex ante* for more SME loan origination primarily by the banking sector. Finally, there is potential to be explored in further developing markets for alternative forms of financing, such as peer-to-peer lending and crowd-funding.

Overall there is a need to actively encourage enterprises and entrepreneurs to be more creative in their use of funding instruments at all stages of their development and to recognise bank and non-bank funding as complementary sources of financing.

A number of other EU states have well established state investment banks e.g. KfW (Germany) and ICO (Spain), others including the UK and France have recently set up new institutions – see BPI France and the British Business Bank – while Portugal has recently announced its intention to establish a new promotional institution (Banco de Formento).



### Ireland Strategic Investment Fund

Following the enactment of legislation to put the ISIF and NewERA on a statutory footing, which is expected to happen early in 2014, additional financing will become available for SMEs and strategic infrastructure. Provided sufficiently competitive funding can be secured, this additional source of financing will be further developed to establish a Strategic Investment Bank tailored to meet the financing needs of a dynamic innovation orientated economy that will:

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**Co-ordinate and drive strategic development within the economy through the provision of long-term funding and capital to enterprises including SMEs<sup>16</sup> and strategic infrastructure; and**

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**Function as a catalyst to attract private sector investment in sectors that are of long-term strategic importance to the State to support economic growth and employment.**

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The on-going discussions with KfW (Germany) allied to the EU's emphasis on the need to increase co-operation between the EIB and National Development Banks provides a new supportive framework in which to consider establishing a new strategic investment institution.

### NewERA

In 2011, NewERA was established on an administrative basis to support a commercial investment programme in vital economic infrastructure. In the process it has significantly reformed how the State manages its portfolio of semi State companies (such as ESB and Bord Gáis). NewERA has had a key role in the establishment of Irish Water and in the State asset disposal programme in order to raise new funds for reinvestment into the economy.

NewERA will be established on a statutory basis in 2014. It will continue to be central to the Government's job plans by identifying and advising on opportunities for the commercial investment programme in vital economic infrastructure. In addition it will have a role in the provision of independent advice on all aspects of the business, operations and governance of commercial semi-states under its remit.

A working group chaired by the Department of Public Expenditure and Reform has been established to progress the Programme for Government commitment to move towards a full holding company structure, building on the work that has already been undertaken by NewERA in this regard and will report to Government on a periodic basis.

### New Models of Infrastructure Financing

With respect to infrastructure financing, there will be continued focus on expanding the number of funders participating in the market, including both international and domestic institutional investors. Through continued engagement with the entire market, specific needs can be identified and appropriate funding models that best suit market requirements will be developed, while continuing to ensure value for the State. This will require developing and embracing new financing structures and opportunities as they arise. An increase in the number of funders participating in the market will create downward pressure on pricing and provide sufficient market funding to meet the infrastructure project pipeline.

The ISIF will seek to leverage and maximise its resources by attracting private sector co-investment. This will be achieved by the ISIF having a commercial investment mandate and as such its participation in a particular investment will provide comfort to other private sector co-investors. In seeking to create projects of sufficient scale to attract institutional interest, Ireland will build on the success of the project bundling approach used for PPPs in the schools and the roads sectors, and analyse the potential for the further development of this approach.



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## Working Capital for Exports

Given the need to continue to grow the export sector, it is essential that export-orientated firms have access to the various finance and working capital for exporters' products that are well established in competitor countries. The State, working with the EIB and other potential investors, is developing a platform that will support the growth of the export sector through the provision of a suite of tailored and customised financing products.

## Debt Restructuring

For a significant number of viable SMEs the capacity to access financing is constrained by debt overhang related in particular to property exposures. Restoring confidence and unlocking demand for the finance that is required to invest in growth will necessitate the adoption of an innovative and coordinated strategy to facilitate debt restructuring in a manner that meets the needs of all stakeholders, including SMEs, banks and the State. This strategy will comprise a number of inter-related policy strands namely:

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**An improved bankruptcy and corporate insolvency framework for companies with a reasonable prospect of survival, providing easier access to the courts. This should enable viable businesses restructure their debts and grow in the future;**

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**The introduction of standardised debt restructuring options for SMEs, encouraging banks to engage and helping to reduce the transaction cost of debt workouts; and**

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**An SME Equity Investment Fund using public and private funding on commercial terms, to repair the balance sheets of viable but constrained businesses through a combination of equity investment and debt restructuring.**

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## Data Infrastructure

Improving SMEs access to non-bank lending will require public bodies and private actors to collaborate in improving the data infrastructure for SME finances so as to both enhance the quality of the information publicly available and reduce the financial and administrative costs associated with accessing these data.

Building on the planned introduction of a new Credit Registry, there is considerable competitive advantage to be garnered from developing a comprehensive credit risk database that would combine information from various sources including private sector participants such as banks, leasing companies, credit insurers and national credit bureaus.

Additional credit relevant information given by individual SMEs on a voluntary basis could also be uploaded to an on-line portal and

made available to either the general public or on a private basis to interested third parties pre-selected by the SMEs. Such a portal could be developed by the private sector in line with similar internet-based social media exchanges and messaging systems.

## Public Private Partnerships

We will continue to ensure that PPPs are considered for all major infrastructure projects as provided for in the Public Spending Code and in PPP Guidance.

## Infrastructure Project Pipeline

The Government will continue to operate a multi-annual budgeting approach to infrastructure investment and publish five year Exchequer investment envelopes. A new infrastructure investment framework will be published in 2015 following a review of Exchequer infrastructure requirements. This will include consideration of the use of PPPs as a delivery mechanism where appropriate.

# Supporting Employment & Living Standards

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# 04

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## Section 04 Supporting Employment & Living Standards

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### In this section:

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Introduction

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Where We Are Now

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Where We Need to Get To

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## Introduction



It is essential that the recovery creates rising levels of employment and living standards, and does not leave behind those most affected by the economic crisis.

In the short to medium-term, the priority must be to grow employment levels through further improvements in competitiveness, and to make sure that people are supported to create businesses or take up new job opportunities as they arise.

In the longer term, the key to increasing living standards is through raising productivity. In turn, higher productivity is achieved through innovation and investment in people – creating higher value products and finding better, more efficient ways of doing things. Ireland must focus on policies to improve innovation and thus productivity and competitiveness.

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## Where We Are Now



The loss of employment is the most prominent legacy of the economic crisis. At its peak, employment in Ireland reached 2.16 million people, before 330,000 jobs were lost between 2008 and 2012; the majority during the initial stages of the recession.

Employment is recovering and that recovery is strengthening, with unemployment down from a peak of 15.1 per cent to 12.8 per cent (on a QNHS basis). There has been significant growth in employment since mid-2012.

The turnaround in part reflects the improvements in Ireland's competitiveness in recent years. We have made advances in reducing key costs for business, taking them back to levels last seen in 2002. This improvement has been driven by factors including relative improvements in labour costs, reductions in property costs, more extensive use of technology and falling prices across a range of professional and business services. We have increased productivity, with cumulative growth rates since the crisis well above the OECD average.

Progress has moved us three further places up the table to 17th in the IMD's 2013 World Competitiveness Report.

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**We were 3rd for the availability of skilled labour**

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**1st for a flexible workforce**

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**1st for attitudes to globalisation**

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**1st for incentives for investment**

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But further progress is needed as some factors in Ireland continue to remain out of line with our key competitors, including costs of energy, waste and legal services.

## Where We Need to Get To



Our vision is to make Ireland the best small country in which to do business. We will create an environment that fosters entrepreneurship and the growth of new enterprises; one that attracts talented people and investment from overseas, creates an open, diverse, flexible and innovative workforce and enables all enterprises in Ireland to thrive, regardless of their size or sector, whether they are trading locally or internationally.

We will aim to further enhance Ireland's share of world trade and mobile FDI. We also want to foster an innovative, competitive and entrepreneurial indigenous enterprise sector that competes on international markets. We will invest in our people and continue to reform our education and training system. Our objective is to ensure that our people are equipped for the jobs of tomorrow, and have the skills to move between employment opportunities in a dynamic and changing world.

Our Action Plan for Jobs set a target of 100,000 additional jobs by 2016. Our Plan is working, as is shown by the recent strong growth in employment. Under this Medium-Term Strategy, we aim to return the country to full employment by 2020.

Under the Department of Finance's baseline macroeconomic scenario, employment levels are now projected to return to nearly 2.0 million by 2016, and to over 2.1 million by 2020 – exceeding the Government's previous targets under the Action Plan for Jobs and the previous employment peak reached in 2007. Under the same scenario, unemployment will fall to 11 per cent by 2016, and to 8 per cent by 2020.

It remains the Government's ambition to exceed these baseline projections. The Department of Finance High Growth Scenario (outlined in Appendix 1) shows that this ambition is realistic by identifying the potential additional impact of appropriate domestic policy changes. Under this scenario the unemployment rate is projected to fall to 10 per cent by 2016 and to under 6 per cent by 2020.

We have identified the following policy areas as key to achieving this ambition over the coming years:

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**Creating an Environment Conducive to Job Creation and Innovation**

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**Helping the Unemployed Back to Work**

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**Meeting the Future Skills Needs of the Economy**

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**Increasing Competition through Better Regulation.**

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## Creating an Environment Conducive to Job Creation and Innovation



Ireland has a well-established reputation for having an environment conducive to doing business and to supporting job creation. We have developed world-class companies in Agri-business and ICT. We have been extremely successful in targeting FDI which has catalysed industrialisation, the expansion of exports and helped to diversify economic activity.

If we are to fulfil the employment needs of our population and the aims of this Strategy, we need to do better. We need to accelerate the re-balancing of the economy towards internationally-competitive, export-oriented sectors that can generate employment and foreign earnings, and we must remove any remaining barriers to growth and employment creation in those sectors most capable of strong expansion. Across the economy, sectors can better position themselves to take opportunities presented in an increasingly digital world – for example, using technology to overcome geographic isolation and to access new markets.

We need to continue to focus on improving our international competitiveness and upgrading our infrastructure. In order to win new international markets everyone, in both the private and public sector, must constantly improve productivity, through measures such as continuous innovation, greater use of technology and adoption of best practice.

We also need to continue and sustain a workplace relations environment, characterised by harmonious industrial relations, that is inclusive and responsive to change, and thereby supports job creation.

In 2012, led by the Department of Jobs, Enterprise and Innovation and Forfás, the Government initiated an annual Action Plan for Jobs process. The Action Plan for Jobs includes all Government Departments and agencies, involves a deep collaboration with industry and, crucially, sets transparent quarterly targets for delivery of measures to cumulatively improve the environment to conduct business and grow jobs.

The original Action Plan for Jobs set a target of having 100,000 extra people in work by 2016 compared to the start of 2012, and to have 2 million people in employment by 2020. The target for 2020 has now been overtaken by this Medium-Term Economic Strategy, and a new target will be reflected in the Action Plan for Jobs 2014 plan to be published early in the new year.

The third annual Action Plan is currently being finalised by the Government for publication in the New Year. It will identify specific additional policy measures in a number of key areas.

### Innovation

Ireland offers a business environment that is regarded as being conducive to innovative firms<sup>17</sup>. However Ireland still lags behind world leaders (i.e. Singapore and the United States) and European leaders (i.e. Germany, Switzerland and the Netherlands) and innovation in Ireland is too concentrated in foreign owned firms<sup>18</sup>.

We must find ways to foster greater innovation in domestically owned firms and in the delivery of our public services. It is important also to realise that innovation often does not involve step-change but rather incremental improvements.

Investment in Science, Technology and Innovation (STI) is an essential component of supporting an innovative and enterprising economy. It assists in creating and maintaining high-value jobs and attracts, develops and nurtures business, scientists and talented people ensuring Ireland is connected and respected internationally. The importance of investment in STI to Ireland's on-going and future economic and social development and well-being has been well recognised by the Government. We have progressed significant initiatives in respect of increasing the innovative capacity of the Irish economy through Science Foundation Ireland and the Research & Development (R&D) tax credit.



Investment is based on a two pronged approach. Firstly, investment in people, infrastructure and associated facilities to build the science base and secondly, direct support to the enterprise sector to build their capacity for research and development.

Having built up a very strong science base in Ireland, following a prolonged period of incremental and substantial investment in the area, STI policy has evolved in recent years and the current strategy is focused on accelerating the economic and societal return on our STI investment, further strengthening enterprise engagement with public research and driving more commercialisation of research.

We are now focused on realising the economic benefits of our investments to date in R&D by delivering on the Action Plans which have evolved in response to the Report of the Research Prioritisation Group, by strengthening our Intellectual Property (IP) framework, by brokering partnerships between firms and research institutes, and by reducing barriers for SMEs to engage in research, development & innovation.

The next Action Plan for Jobs will build on the State's investments in R&D infrastructures to further drive innovation by a number of actions including consolidating and building critical mass and international reputation in areas that underpin Ireland's enterprise base and enhancing collaborations between creative and design firms and other enterprises, academia and other public

sector bodies to deliver economic and social benefits.

It will also identify ways to use Government procurement in a strategic way to stimulate collaborative efforts between the public sector, research institutes and firms that will deliver innovative solutions.

### Entrepreneurship

There are 180,000 SMEs in Ireland today who employ almost half of Ireland's workforce. By building a supportive environment for entrepreneurship we will create a sustainable and growing indigenous SME sector.

Traditionally in Ireland starting and growing a business is considered less attractive by many than working in larger employers. We must continue to find innovative ways to encourage an entrepreneurial spirit by: (i) beginning from an early age in the education system to foster entrepreneurship; (ii) acknowledging the importance of the range of skills, capabilities and acumen to enterprise from good business management skills, vocational and technical skills, like apprenticeships, through to higher order university qualifications; (iii) developing policies which recognise failure is an integral part of a healthy entrepreneurial process; (iv) rationalising our support structures for start-up businesses so as to build a streamlined cohesive system encompassing both local and central governmental levels including through the new LEOs and Enterprise Ireland and in a way which does not encourage over

dependence on state supports;<sup>19</sup> (v) encouraging Higher Education institutions to place a strong emphasis on building entrepreneurship and supporting competitive enterprises; and (vi) building key clusters that will act as magnets for innovation and commercialisation of ideas.

We will work to find solutions so that more Irish companies can grow to scale and make a bigger contribution to economic growth and employment. This will involve dealing with the structural and cultural reasons, including access to capital and scaling issues during the growth business lifecycle that entrepreneurs seeking to scale-up can face.

### Building New Markets

As a small open economy, Ireland relies on its ability to sell its goods and services in overseas markets in order to achieve sustainable long-term growth and improved standards of living for all. As the centre of gravity in world trade shifts towards emerging markets, Ireland must respond by developing new trading relationships, with the objectives of achieving diversification in both markets and sectors, and of continuing to grow our exports, particularly among indigenous companies.

Ireland needs to have an ambitious approach to winning new markets by building a strong platform to help our enterprises succeed abroad. Winning in emerging markets requires enterprises to especially develop long-term relationships and therefore have the capability and be supported to





develop a long-term strategy and a network embedded in those new markets. Work continues across Government to promote Irish exports and investment into Ireland, including high-level trade missions and development of local market teams.

The next Action Plan for Jobs will set out additional measures to increase the number of indigenous firms exporting their products or services, to expand Irish-based companies' market share in existing export markets, and to gain a foothold for enterprises in new markets. A review is currently underway of the Export Trade Strategy, led by the Department of Foreign Affairs and Trade, which will inform further development of relationships with emerging markets.

### Seizing Sectoral Opportunities for Growth

Building a strong enterprise mix can ensure that Ireland is not overly reliant on a limited number of sectors for future growth and/or employment, is better protected from external shocks, and further underpins a sustainable model for economic growth.

The next Action Plan for Jobs will set out additional measures to:

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**Build on sectors where Ireland has particular strengths (e.g. Agri-food, ICT, International Financial Services);**

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**Capture sectors with emerging opportunities and untapped potential (e.g. Green Economy, Creative Industries, Healthcare Services);**

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**Place a renewed focus on mature sectors (e.g. Tourism, Retail and Wholesale, Construction);**

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**Promote competitive locally traded activities (e.g. Professional and Business Services, Personal Services); servicing the local economy will be the first step for most new entrepreneurs, and the development of a greater online trading capacity will thereafter facilitate broader trading possibilities including internationally for those firms; and**

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**Promote greater collaboration between indigenous and foreign-owned companies.**

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It will commit the Government to establishing clearly designated 'ownership' at Department and Agency level to deliver a cohesive, coordinated and comprehensive approach to develop sectors that cross areas of responsibility at Government Department/Agency level. These include Clean Technology, Creative Industries, Marine, Education Services and Healthcare Services (eHealth).

Complementary to the Action Plan for Jobs, a number of sector specific strategies are being developed and implemented to focus on supporting sectors with immediate employment potential.

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### Agri-Business

The agri-food and fisheries sector is an important indigenous industry and is recognised as a key driver for an export-led economic recovery. The future vision and strategy for the sector is encapsulated in Food Harvest

2020 (FH2020) which uses the 'Smart', 'Green', 'Growth' themes to achieve ambitious and challenging growth targets by 2020. These include growing the value of exports and value added product by over 40 per cent and increasing the value of primary output by over 33 per cent. These targets are being pursued collaboratively by the ministerial-led High Level Implementation Committee which coordinates and energises the state led response. Under its direction, the sector has performed strongly and as indicated in Milestones for Success 2013, the latest progress report, by end 2012, the value of primary production has risen by 25 per cent vis a vis the 33 per cent projected target for 2020, exports had achieved 13 per cent of the 42 per cent projected growth while value added has increased by 20 per cent (end 2011-latest data). FH2020 will be further underpinned by policy initiatives and investment under the new Common Agricultural Policy and Common Fisheries Policy, negotiated under the Irish Presidency.

In the last three years, agri-food exports rose by 28 per cent on the levels recorded in 2009, most notably in the dairy, beef, beverages, pigmeat and seafood sectors and are currently in excess of €9 billion, accounting for over half of manufacturing exports by Irish owned firms and reaching in excess of around 170 export destinations. In relation to the Food Harvest headline growth targets, CSO data indicate that the value of primary production has risen by 33 per cent (2013 advance estimate), exports have grown by



13 per cent (2012 data) and the outcome for 2013 is expected to be close to €10 billion. Current indications are that these growth figures have the potential to significantly increase with the higher output capacity following the abolition of milk quotas in 2015.

In addition to State involvement, there has been strong industry support and investment for the Food Harvest vision. Significant industry investment of the order of €600 million has been made particularly in innovation and technology in dairy processing, in new brewing, distillery and tourist-related projects and capital investments in the beef and sheepmeat areas. These investments act as a catalyst for other businesses and due to the comparatively high multiplier effect from this sector have a particularly valuable regional employment and development significance. An independent assessment of the employment potential arising from achieving the 2020 growth targets estimates that around 25,000 additional direct and indirect jobs could be created.

#### **Tourism, Hospitality, Arts and Culture**

This Government identified tourism as a key driver of economic growth and job retention and creation across the country. It is an export industry that brings money into the country, provides jobs in urban and rural areas and is

populated by many Irish-owned SMEs. We introduced initiatives to improve competitiveness such as the 9 per cent VAT rate, an air access strategy including the suspension of the travel tax and initiatives such as *The Gathering*. These initiatives have helped revitalise the industry. From a low in 2010, visitor numbers have increased by almost 14.8 per cent based on an estimated outturn in 2013 of 6.93 million approx. From a low in mid 2011 employment in the core tourism and hospitality areas of accommodation and food have increased by 14,900 (+13 per cent). Revenue has also increased by €127 million (+3.6 per cent) up to the end of 2012 and 2013 figures are expected to increase this figure further. As the tourism sector has now entered a period of growth, it is appropriate to review existing policy which is more than a decade old and consider its future direction. The policy review started in September 2013 and is expected to be completed in the 2nd quarter of 2014.

The policy will seek to build on the gains made in recent years and chart a course to achieving a significant increase in tourist visitor numbers, revenue and employment in the sector over the course of the next decade. The success of the Great Western Greenway and the positive reception in key source markets to the development of the Wild Atlantic Way (WAW) or Dublinne shows the potential of large inter-

national scale projects that leverage existing assets such as landscape and heritage to attract overseas tourists. Furthermore, the potential of festivals and events (cultural, sports and business) to contribute to tourism growth was reinforced during the Gathering.

Sport is not just about leisure and health. It is also a big business from major events to sports science and technology. The Government will seek to capitalise on the potential of sport as an industry to create jobs and growth.

The Government will also leverage the potential of the Arts and Culture and creative sciences sectors for job creation. There are particular opportunities to assist balanced regional development and rural development, including in Gaeltacht areas and in border areas, by developing our creative sectors and cultural and heritage tourism. This will be supported by an improved infrastructure for both visitors and citizens. Equally, creative sciences must be leveraged to play a greater role in further developing an innovative society and innovative industry.



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### **Construction Sector**

A properly functioning construction sector can play an important role in getting people back to work. The decline in the construction sector in Ireland in recent years has been unprecedented in its scale and duration, and the sector is widely seen as having 'over-corrected', particularly by comparison with international norms. Moreover, the country faces continuing infrastructure needs and specific demographic pressures.

Government is committed to playing its part in addressing the over-correction, to help bring the construction sector back to more appropriate and sustainable levels, thereby contributing further to job creation and supporting the domestic economy. At the same time, the sector must make maximum use of modern technology, techniques and skills, deliver to the highest quality standards, and demonstrate higher regulatory compliance levels.

Earlier this year, the Government published a policy statement setting out proposed actions in a range of areas to help address particular issues and obstacles in the sector. These include continued investment in public infrastructure, revised construction sector contracts, establishment of a statutory register of builders and contractors, improvements in the planning process, a greater focus on energy

efficiency and tackling the shadow economy in the sector. In addition, a framework for greater coordination of activity and consultation with industry is envisaged. Budget 2014 built on this progress by including a number of specific, targeted measures aimed at increasing activity levels, improving compliance and boosting employment. This work will be developed further in 2014 and beyond by addressing remaining challenges in the sector, such as developing an overall strategic approach to housing supply, identifying and implementing further improvements in the planning process to facilitate appropriate development, and seeking to improve financing options for development and mortgage provision.

### **Reforming Local Government to Support Enterprise and Job Creation**

The local government system is currently undergoing its biggest shake-up since its foundation. New legislation to be enacted in 2014 will replace 114 local authorities with 31 integrated authorities organised on the basis of municipal districts within counties.

As part of this shake-up of local government, new responsibilities for economic development will be devolved to local level. In particular, new enterprise support services will be embedded in local authorities in Local Enterprise Offices (LEOs) to help new local start-ups and micro businesses.

It will serve as a first-stop shop for all enterprises and signpost firms to the most appropriate support services, including brokering introductions to Enterprise Ireland for companies that have the potential to export.

Next year will also see an entirely new structure for delivering water services across Ireland. Instead of 31 separate water authorities, all with their own plans, we will have a single water utility company – Irish Water. Having a national service will cut out waste and reduce costs for local businesses. Investing in quality water infrastructure is essential for the future economic development of the country and for job creation.

The biggest change in local government is in its financing. The introduction of a local property tax has put local government finances on a sustainable footing for the first time. No longer will the provision of local services be fully dependent on inconsistent central Government funding and local business rates. The ability to vary the level of the local property tax will also give local Councillors clear responsibility for local government financing and will also promote local democracy in a way not seen before in Ireland.

## Helping the Unemployed Back to Work



Although progress has been made, the numbers of people out of work remain unacceptably high. This Government will continue to address the challenge of further reducing unemployment, in particular by focusing on our on-going strategy designed to tackle long-term unemployment, Pathways to Work (PTW), which is led by the Department of Social Protection. The service traditionally provided by the Department in providing income supports continues. However, the cornerstone of Government policy in this area is transforming the Department from a passive benefits provider to a public employment service that is actively assisting jobseekers to return to work; this approach will require significant resources. Over the duration of the Medium-Term Economic Strategy our approach to labour market activation will facilitate the reduction in unemployment through the following measures:

### **Intreo – Increasing Engagement with Job-Seekers**

The new Intreo one-stop shop for job-seekers - combining employment and income support services - will be fully rolled out by the end of 2014. The number of appropriately trained case officers in Intreo will continue to be increased to ensure that resourcing is commensurate with the scale of the problem.

The profiling of all individuals on the Live Register will be used to target interventions for those at higher risk of becoming long-term unemployed. New activation places will be added,

with an increasing share ring-fenced for both the long-term unemployed and those under 25 qualifying for the Youth Guarantee. In 2013, of around 264,000 activation places in employment, further education and training programmes, up to 84,000 places (32 per cent) were reserved for the long term unemployed.

These targets will be maintained and extended on a yearly basis to reflect the prioritisation of the long-term unemployed.

### **JobPath**

Complementary to the work of Intreo, the Department of Social Protection will outsource a new labour market activation service – ‘JobPath’ – to provide monthly engagement with the long-term unemployed. The service will be operational by the fourth quarter of 2014.

Under JobPath, every long-term unemployed jobseeker will receive intensive assistance to find, apply and prepare for employment. Where necessary, individuals will be referred to specific work experience or further education and training programmes to increase their employability. Payments to contractors will be on the basis of results, with performance in sustaining a person in employment the key metric.

### **Youth Guarantee**

In line with the European Union’s Youth Employment Initiative and the Youth Guarantee, we will implement a focused plan over 2014 and 2015 aimed at ensuring that young people under

the age of 25 who are unemployed or who are leaving education will receive an offer of employment, continued education, an apprenticeship or a traineeship.

This will involve active engagement with the young unemployed, the development of personal progression plans to support their transition into employment and the provision of appropriate education, training and employment supports.

### **Tax and Welfare – Incentives to Work**

In order to simplify and improve the understanding of the tax and welfare codes and to ensure that there is a strong benefit from returning to work for the unemployed, the Government has established an Advisory Group on Tax and Social Welfare. This Group will make recommendations for consideration by the Minister for Finance and the Minister for Social Protection on how to amend our tax and welfare systems to ensure that work always pays and to address work disincentives for atypical workers. The Government also aims to simplify the applications process for the Family Income Supplement (FIS) payment, and to encourage employers to increase awareness of the scheme. These measures will be reflected in the next Pathways to Work programme. The Department of Social Protection has already made major operational improvements to administration of the FIS system which have minimised delays.

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## Meeting the Future Skills Needs of the Economy



Core to Ireland's success will be its people. Our highly adaptable and effective workforce has proven to be one of our competitive advantages in the past. A key element of the Government's growth and employment strategy is ensuring that we continue to have the right skills to attract, retain and grow job opportunities and investment. A well-educated workforce will support Ireland's recovery and remains the principal means by which we can deliver high standards of living for our citizens. Investment in education is essential to ensure that everyone can contribute to society, and to our culture. To maintain our economic differentiation, it will be crucial that Ireland's education and continuous training policies are aligned with the needs of enterprise and the new economy.

Through on-going collaborative efforts between, in particular, the Departments of Education and Skills, Jobs, Enterprise and Innovation and Social Protection the skills base of the Irish workforce is constantly evolving. The Government's Pathways to Work strategy and the Action Plan for Jobs provide the overall framework for this work.

Our further education and training system is being restructured to better provide high quality, flexible and responsive education and training programmes for young people and adults, and targeted re-skilling opportunities

to support those who have lost their jobs to get back into employment. Significant reforms are currently underway to ensure that the nature of teaching and learning in our schools is better adapted to needs of all students into the future. Our starting point will continue to be a focus on ensuring that we have the best quality teachers in all of our schools.

Ensuring that all our school pupils have the essential life skills like literacy, numeracy, language skills and scientific competence will continue to be accorded priority. This will be increasingly complemented by an emphasis on developing the intellectual capacity of children to innovate, solve problems and apply their own intelligence in a creative manner – supported by digital technology and high quality broadband connectivity to every second level school.

Ireland's capacity to compete internationally will need a higher education sector with a reputation for innovation, quality and a capacity to work with enterprise to transform intellectual capital into economic value. An increasingly competitive international economy requires that Ireland's education system adapt and provide skills which allow Irish graduates to compete for employment with others from around the world and to set up businesses of their own which can compete internationally. To make this possible,

the effectiveness and sustainability of our higher education system are essential.

The higher education sector will see greater consolidation and collaboration between higher education bodies. There will also be greater accountability for performance for the delivery of national priorities and monitoring of the performance of the system as a whole.

Higher education institutions will be encouraged to identify their strategic niche and mission and to agree with the Higher Education Authority (HEA) a performance compact aligned with funding.

Reforms to our education system will not be targeted only at those currently at school or affected by unemployment. We must also endeavour to continue developing the skills of people who are currently at work. The rapid pace at which technology is advancing and new industries emerging make this objective an imperative for small, open economies such as ours.

## Competition and Regulation



Competition policy must play a central role in the structural reform programme for the economy. Increased competition is key to ensuring better choice, better quality services and lower costs. It ensures that Irish firms are equipped to compete on international markets, that investment is productive and that consumers reap the benefits. Introducing competition into previously sheltered sectors is a necessity in a rapidly globalising economy.

Monopolies belong in the past and competition is now the norm in modern democracies. Competition policy is a key driver of competitiveness, productivity and innovation. When properly regulated, competition results in better value and more choice for people. We are committed to pursuing policies that will:

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**Lower the cost of doing business in Ireland for all firms, including internationally trading firms**

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**Offer consumers more choice and ensure consumers get value for money**

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**Spur product and service innovation among suppliers**

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Improving the effectiveness of economic regulation is also a priority in the medium term. The Government recognises that effective regulation is essential for Ireland to be internationally competitive and an attractive place to do business.

To assist in improving the regulatory environment in Ireland, Government published a Policy Statement on Economic Regulation in July 2013. The Statement outlines a strategic framework to address the challenge faced by regulated sectors in balancing their diverse and often conflicting objectives to ensure quality services for end users and the efficient delivery of infrastructure investment. Sectoral departments have been tasked with implementing the actions set out in this Statement.

At the core of competition and regulatory policy in the medium term will be our objective to build upon the important reforms undertaken in recent years. We will achieve this by focusing further efforts in the sectors where opportunities for further reform have been identified.

### Energy

Energy is an important part of economic activity and the price paid for energy is a determining factor in the competitiveness of the entire economy. In 2011 electricity accounted for 36 per cent of final energy use in industry, with oil and gas accounting for approximately 25 per cent and 28 per cent respectively. As Ireland is highly import-dependent for oil and gas, we are a price-taker when purchasing these commodities. Fuel prices, network costs and the costs of accommodating renewable energy are the primary drivers of the cost of electricity in Ireland. Our electricity is

bought and sold on a single, wholesale market, the Single Electricity Market (SEM), which aims to increase competition and efficiency and secure our supply of electricity. Work is continuing to develop an integrated European market.

Future strategy in the energy sector will involve the sale of some of the ESB's non-strategic generation capacity and the sale of BG Energy, following its separation from BG Networks, all of which will enhance competition in the generation and supply of electricity. There will be a strong state presence in the ownership of electricity and gas networks and in the generation and supply of electricity.

Our climate change targets, set at EU level, will be important in shaping our energy policies and the energy sector. It is important that the targets, and the policies and measures necessary to meet them, are sustainable. They will involve a significant shift towards renewable energy and energy efficiency. There continues to be substantial employment potential in the area of retrofit and the reduction of energy consumption.



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## Professional Services

Studies into competition in professional services were conducted by the Competition Authority in eight professions: architects, dentists, engineers, optometrists, veterinary surgeons, medical practitioners and solicitors and barristers. The two most significant were identified as the legal and medical professions.

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### Legal Services

Government has undertaken to “establish independent regulation of the legal profession to improve access and competition, make legal costs more transparent and ensure adequate procedures for addressing consumer complaints”. This complements the relevant structural reforms to which the Government is committed under the EU/IMF/ECB Memorandum of Understanding. All of these undertakings are being given priority and expression in the Legal Services Regulation Bill 2011 under which, inter alia, there will be

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**A new, independent, Legal Services Regulatory Authority with responsibility for oversight of both solicitors and barristers. The Authority will have a lay majority and a lay chair and will be appointed through nominating bodies;**

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**Greater transparency in relation to legal costs and statutory principles will be put in place for the assessment of legal costs;**

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**An independent complaints system to deal with complaints against solicitors and barristers. This will provide a first port-of-call for the public, independent of the professional bodies. There will also be an independent Legal Practitioners’ Disciplinary Tribunal that will be able to deal with more serious complaints including allegations of fraud and the misappropriation of funds. We remain more committed than ever to following through on this reform in the post – programme period.**

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### Medical Services

In 2010, the Competition Authority found that a number of restrictions on competition exist among General Medical Practitioners (GPs) in Ireland and identified serious problems in the manner in which the General Medical Services (GMS) contracts for GPs operated. This had resulted in a limited number of GP practices, reduced patient choice and less pressure for GP practices to compete on price for private patients. Problems were also identified with GP advertising and GP training. The Competition Authority made seven recommendations. Implementation of these will continue to be overseen by the Government.

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## Transport

As an island nation, Ireland is heavily dependent on external trade links as an economic driver. Ensuring that our external and internal connectivity functions well so that enterprise can get its products and services to market is therefore crucial in terms of our medium-term economic strategy. The efficient movement of people is equally important in terms of labour market efficiencies, the attractiveness of Ireland for investment and indeed quality of life issues. Targeted investment to both enhance capacity, particularly to ease urban congestion, and to maintain and improve the efficiency and effectiveness of the existing network, will be continued. Competition will improve productivity and help to bring down price in the transport industries. The developments in Ireland’s airline industry in recent decades support this analysis.

While significant improvements have been made in the last decade, Ireland has some distance to go to bring its global competitiveness rating to a satisfactory level. Work is currently underway on the Strategic Framework for Investment in Land Transport (SFILT) and important conclusions emerging from this include the following:

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**Competitive and efficient transport is vital for both domestic and export sectors and a well-functioning world class transport infrastructure remains a key factor for FDI.**

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**We must ensure continued investment in our transport network in order that we can maintain the gains achieved to date and avoid any degradation of our existing infrastructure.**

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**As our economy continues to grow, there is a risk that congestion will emerge, leading to increased costs for industry. Therefore, it will be necessary to ensure that any emerging infrastructural bottlenecks are addressed and that spatial planning policy supports the delivery of efficient public transport.**

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#### **Ports**

Our ports sector is of critical importance to our ability to compete internationally. Activity has picked up in our ports in recent months and several new shipping lanes to Britain, France and Spain will commence soon.

The National Ports Policy introduces a clear categorisation into the ports sector: Ports of National Significance (Tier 1); Ports of National Significance (Tier 2); and Ports of Regional Significance. Ports of National Significance - Dublin, Cork and Shannon-Foynes have clear potential to lead the development of future port capacity in the medium and long term. They all have significant plans for future development. The Ports Policy provides clear direction to planning authorities, funding bodies and other Government and European agencies that future ports capacity development should be focused on these ports. While we have sufficient capacity in our ports for the foreseeable future, developments will

be necessary to improve infrastructure and respond to the trend of using deeper and larger vessels.

The Competition Authority has recently published a study of competition within the Irish ports sector which demonstrates the existence of competitive conditions within and between ports. The study contains a number of recommendations designed to further strengthen competition in the sector and these will be considered in the context of the implementation of the National Ports Policy.

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#### **Public Transport**

The objective of Government is to ensure a system of public transport throughout the country that is as integrated, as efficient and as widespread as possible, providing an alternative to private car use where required and feasible. Public transport has gone through a challenging period as passenger numbers fell, fuel costs increased and the level of State subvention fell. Despite this there have been significant improvements in the quality of the services provided.

In an important first step towards a more competitive public transport market, from 2016 approximately 10 per cent of the publicly subvented market will be tendered out. Dublin Bus, Bus Eireann and any other bus operator will be able to tender for the contract to operate these routes.

The winner will be expected to provide a better service for the same subsidy or the same service for a lower subsidy - a win for passengers and the taxpayer.

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#### **Aviation**

Because Ireland is an island, air connectivity is vital for our economic development. Significant progress has been made since the Government came to office in terms of restoring air links both across the Atlantic, to Europe, the Middle East and beyond and in respect of the separation of Shannon as a stand-alone State Airport. A new aviation policy is expected to be completed in the second quarter of 2014. The key issues being dealt with as part of that process are:

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**The future of the State airports at Dublin, Cork and Shannon;**

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**Funding arrangements for regional airports, following the end of the current funding programme in 2014;**

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**Access to the air transport market – the extent to which third country carriers will have access to the air transport market into and out of Ireland in competition with incumbent national and EU airlines;**

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**Restructuring the institutional arrangements for economic and safety regulation of the aviation sector; and**

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**How best to ensure the further development of the leasing sector and other aviation-related industries and services.**

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## Sustainable Development



Future investment in transport infrastructure will be considered as part of the national programme of investment in infrastructure. This will form part of the review of capital expenditure, along with other key elements of our infrastructure such as water services, rural development, housing, urban regeneration, energy, communications, enterprise support, health and education. Sustainable Development will be at the core of our development strategy, recognising that economic growth, social cohesion and environmental sustainability must be advanced in a mutually supportive way. Our commitment to sustainable development, and the associated economic benefits, is set out in the Government's strategy "Our Sustainable Future".

## Broadband



High-speed broadband is core to our competitiveness. As a knowledge and services oriented economy trading worldwide, our workforce needs to be better connected than most. Ensuring fast connectivity is not only about jobs – it is also increasingly a conduit for all aspects of modern society – citizenship, education, healthcare, learning, culture and leisure. Building on the National Broadband Plan, "Delivering a Connected Society" (August 2012), the Government will in 2014 announce full details of the State's investment plan to bring high-speed broadband to less populated parts of the country which will not be serviced by the commercial market. Rollout of services based on this investment will commence in 2015.

## North/South Co-operation and the Island Economy



In the context of the recent transformation of relations with Northern Ireland, there is scope for further improvements in economic cooperation between both parts of this island. Significant progress has been made in a number of sectors, such as the all-island energy market, and a number of North-South bodies exist under the Good Friday and St. Andrew's Agreement, including InterTradeIreland and Tourism Ireland, and there are strong business linkages between North and South. The Government will continue to work with the Northern Ireland Executive, including through the North-South Ministerial Council, to identify opportunities for further cooperation to the mutual benefit of both economies.

## The European and International Dimension to Ireland’s Prosperity



As a small open economy, our relations within Europe and across the world are crucial to our economic prosperity.

A successful, well-functioning European Union is essential to the performance of the Irish economy, particularly given the on-going deepening of Economic and Monetary Union in the areas of fiscal policy and banking.

The efficiency and effectiveness or otherwise of measures agreed at EU level impacts directly on a myriad of sectors of the Irish economy from agriculture and food, to financial services. A growing Europe is central to demand for Irish goods and services: the EU is the destination for more than half of Ireland’s exports and the source of more than half our imports.

Building on the widely acknowledged success of the 2013 Presidency, the Government will intensify its strategic engagement with Europe both with the Institutions of the Council, Parliament and Commission, but also with other Member States in order to contribute effectively to shaping a strong, growing and competitive Europe. Work will be completed in the first quarter of 2014 on a revised strategic approach to Ireland’s engagement with the European Union resulting in more structured engagement with partners on a more focused set of interests and priorities.

The election of a new European Parliament in May 2014, and the subsequent appointment of a new Commission and European Council President, will afford an opportunity for renewed effort in a number of key areas of particular priority to Ireland, among them Banking Union, completion of the Digital Single Market, and the Transatlantic Trade and Investment Partnership negotiations.

As an exceptionally open economy, international trade, investment and tourism are crucial to our economic progress and well-being. Ireland will continue to identify, develop and pursue key international markets for our goods and services. A number of important initiatives are in place or planned to help advance this agenda over the coming years. These include:

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**A ten year programme of enhanced cooperation between Ireland and Britain, agreed by the Taoiseach and the British Prime Minister in 2012, under which extensive bilateral collaboration is progressing across key areas of economic activity, including on foot of a jointly commissioned study of the economic relationship, published in July 2013;<sup>20</sup>**

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**Targeting of a number of key country markets for special engagement including Government led trade missions and the negotiation and conclusion of significant long-term strategic partnership frameworks with a number of emerging priority markets, including China (2012) and, most recently, Japan (2013);**

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**The work of the Export Trade Council which oversees delivery of the Trade, Tourism and Investment Strategy;**

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**A review of the current Trade, Tourism and Investment Strategy to examine targets and priorities in the light of any changed circumstances of the last few years, which is nearing completion;**

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**A review of Ireland’s Foreign Policy and External Relations which, inter alia, is expected to take greater account of economic and trade priorities in the future.**

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## A Better Country for our Children and Young People



Promoting and securing sustainable economic growth is a key prerequisite to ensuring a well-functioning and inclusive society and especially to improving the lives of our children, young people and families.

By building a prosperous economy, this Strategy aims to promote the economic security of Irish families through increasing the number of parents in employment and by providing increased employment opportunities at home for Irish young people.

A successful economy will also enable us to fund investment in quality supports and services for children and families, including new and future initiatives in the areas of early years services, childcare, education, access to healthcare, child protection and children and family services.

The estimated total population of 0-19 year olds in Ireland is 1.28 million in 2013, which represents an increase of 11.7 per cent since 2001. The estimated population of 0-4 year olds increased by 33.8 per cent over that period.

Our increasing child and youth population is a significant resource for our country. There is clear international evidence that investing in people during their early years pays significant dividends for individuals and for society as a whole. Ensuring the best possible outcomes for this group is therefore an important element in our future economic planning.

The Government's ambitious programme to achieve this will be set out in the new Children and Young People's Policy Framework which will be rolled out in early 2014.

# Policy Actions

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# 05

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## Policy Actions

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In this section:

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Policy Actions

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## Policy Actions



The sections below give a brief outline of selected policies underway.

This Strategy provides an overarching high-level integrated whole-of-government framework to drive and facilitate the development of appropriate sectoral and horizontal policies which will be refined over the next few months to take account of this Strategy. When reviewing and updating or publishing new strategy statements or plans, Government Departments and Agencies will ensure that they are aligned with this Medium-Term Economic Strategy.

In tandem with the increasingly successful ‘*Action Plan for Jobs*’ this high-level Strategy plots the path forward to ensure integrated policy making. The Strategy sets out new directions and strong associated governance systems to avoid repeating the mistakes of the past.

Government will monitor performance of relevant plans and initiatives on an on-going basis including through its cross-cutting mechanisms such as Cabinet Committees.



## Upcoming policy events, include:-

### 01 Fiscal Policies

Finance Bill (no 2)	Q4 2013
Stability Programme Update	Q2 2014
Budget 2015 and Finance Act 2015	Q4 2014
New Public Service Reform Plan	Q1 2014
Comprehensive Review of Expenditure	2014
Review of Capital Investment Framework	2014
Government Decision on Reforms to Increase Pension Coverage and Sustainability	Early 2014
White Paper on Universal Health Insurance	Early 2014

### 02 Financing Growth

Enactment of Bill to (i) Establish the Ireland Strategic Investment Fund and (ii) Put NewERA on a Statutory Basis	Q1 2014
Assessment of Establishing a Strategic Investment Bank	H1 2014
Assessment to Progressing NewERA to a Full Holding Company	H1 2014
Ensure Full Implementation of the Mortgage Arrears Strategy	2014 (on-going)
European Banking Union Transposition	2014 (on-going)
IFSC Strategy	Early 2014

### 03 Supporting Employment & Living Standards

Action Plan for Jobs 2014	Q1 2014
Export Trade Strategy	Early 2014
Tourism Policy Review	Q2 2014
Construction Sector Strategy	Q1 2014
Enact Legislation to Establish Local Enterprise Offices	Q1 2014
Pathways to Work 2014	Early 2014
Youth Guarantee	2014 (on-going)
Report from the Advisory Group on Tax and Social Welfare on In-Work Support	Q2 2014
Consider Competition Authority Recommendations on Ports Strategy	Early 2014
New Aviation Policy	Q2 2014
Children and Young People's Policy Framework	Q1 2014





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## Appendix

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## Appendix 1



### MTES Baseline Macroeconomic Scenario

The MTES Baseline macro-economic scenario is based on Budget 2014 projections out to 2016. Thereafter, output is profiled to grow by an average of 3.4 per cent per annum out to 2020, assuming steady growth in the world economy and continued improvement in cost competitiveness to support Ireland's share of global export markets. Provided labour productivity growth is sustained at around 1.5 per cent, average employment growth of 2 per cent per annum over 2017 to 2020 is expected. Under these assumptions, the economy is projected to add

238,000 jobs over the period 2014 to 2020, leaving total employment at over 2.1 million by the end of the decade. Longer-run labour force projections are subject to considerable uncertainty, given possible trends in net migration, population growth and labour force participation rates. On the basis of the above employment projections, alongside labour force growth of around 1 per cent per annum, these estimates are consistent with an unemployment rate of 8 per cent by the end of the decade.

The key macroeconomic aggregates under the Baseline scenario are outlined below.

The simulated path for the general government balance from 2017 onwards is prepared on a purely technical and indicative basis. Reflecting existing estimates of the output gap (prepared in line with harmonised European Commission approved methodology<sup>21</sup>) it profiles the minimum necessary headline balance needed to support the improvement in structural balance to achieve Ireland's Medium-Term Objective (MTO) of a balanced structural budgetary position in 2018.

**Table A1: BASELINE MACROECONOMIC ASSUMPTIONS**  
(% CHANGE UNLESS OTHERWISE STATED)

	2013	2014	2015	2016	2017	2018	2019	2020
Real GDP growth	0.2	2.0	2.3	2.8	3.5	3.5	3.5	3.0
Unemployment rate	13.5	12.4	11.8	11.4	10.6	9.6	8.7	8.1
Employment growth	1.6	1.5	1.3	1.3	2.0	2.1	2.2	1.8
Nominal GDP growth	1.2	2.9	3.7	4.4	5.2	5.4	5.5	5.1
General government balance (% GDP)	-7.3	-4.8	-3.0	-2.4	-1.0	0.5	0.4	0.0
General government debt (% GDP)	124	120	118	115	110	104	98	93

Source:  
Department of Finance  
Rounding may affect totals.

Note  
Certain year-on-year growth rates under "high growth" are below those under baseline, reflecting base effects. Notwithstanding the differences in rates of change, output and employment volumes remain higher under the "high growth" relative to baseline.



### MTES High Growth Macroeconomic Scenario

Making use of the ESRI's HERMES macro model, a 'high growth' scenario was modelled for the purposes of this Strategy to capture the economic impact of determined implementation of a selection of appropriate domestic policies. Additional dividend from labour market activation policies beyond those envisaged under current policy are modelled, together with; meeting climate change costs through carbon taxes (as distinct from income tax); a further-improved financial sector beyond that under the Baseline scenario (which would lower the cost of credit across the economy); improvements in educational attain-

ment (which raise human capital); and a re-balancing of taxation away from labour towards property. These are indicative simulations. Actual policy will be decided by the Government on the basis of available resources. The model suggests that if a suite of such policies were successfully implemented to support these conditions, output levels could be raised cumulatively by an average 1 per cent by 2020.

The 'high growth' scenario assumes no further improvement in trading partner growth beyond what is profiled under the Baseline. The public finance implications of the higher growth and employment levels envisaged under 'high growth' are estimated on a purely technical basis, assuming

an aggregate fiscal semi-elasticity of 0.5, whereby every €1 billion increase in real output translates to an improvement in the deficit of €500m.

Under the MTES 'high growth' scenario, by 2020 there are 18,000 more people employed relative to Baseline scenario assumptions, and the unemployment rate is projected to be 2 ¼ percentage points lower than would have been the case under Baseline assumptions. The significant improvement in projected unemployment takes account of the assumed impact of labour market activation measures (i.e. more of the jobs created are filled by the unemployed than under the Baseline scenario) as well as the higher increase in employment.

**Table A2: HIGH GROWTH MACRO-ECONOMIC ASSUMPTIONS**  
(% CHANGE UNLESS OTHERWISE STATED)

	2013	2014	2015	2016	2017	2018	2019	2020
Real GDP growth	0.2	2.3	2.5	3.1	3.7	3.6	3.5	2.9
Unemployment rate	13.5	12.2	11.3	10.2	8.9	7.5	6.4	5.9
Employment growth	1.6	1.7	1.6	1.6	2.2	2.1	2.1	1.7
Nominal GDP growth	1.2	3.2	3.6	4.6	5.3	5.4	5.4	5.0
General government balance (% GDP)	-7.3	-4.7	-2.8	-2.0	-0.5	1.0	0.8	0.4
General government debt (% GDP)	124	119	118	113	108	102	96	91

Source:  
Department of Finance  
Rounding may affect totals.

Figure A1: REAL OUTPUT (CONSTANT 2011 PRICES)

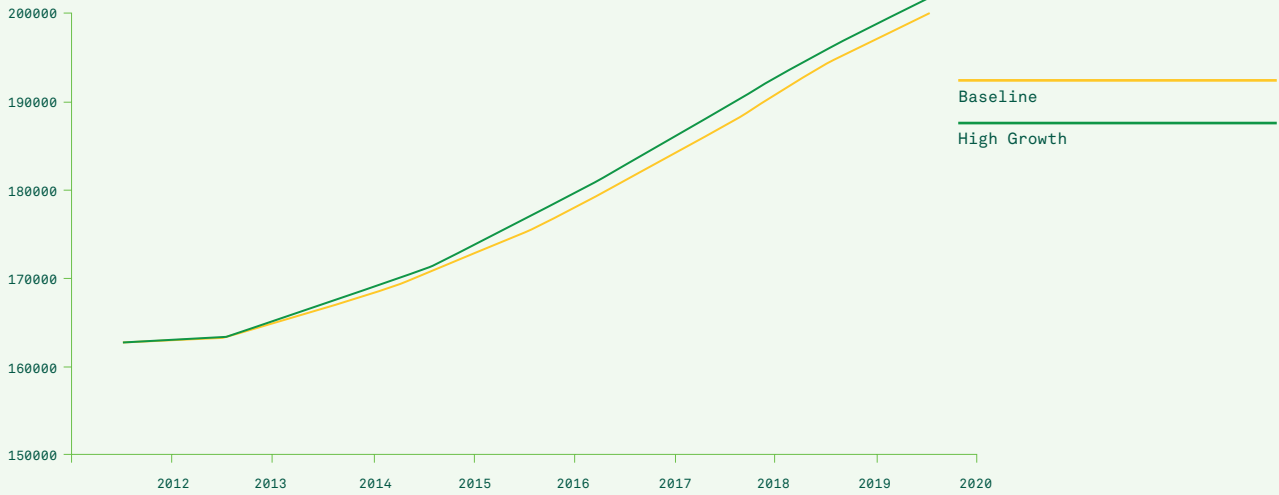
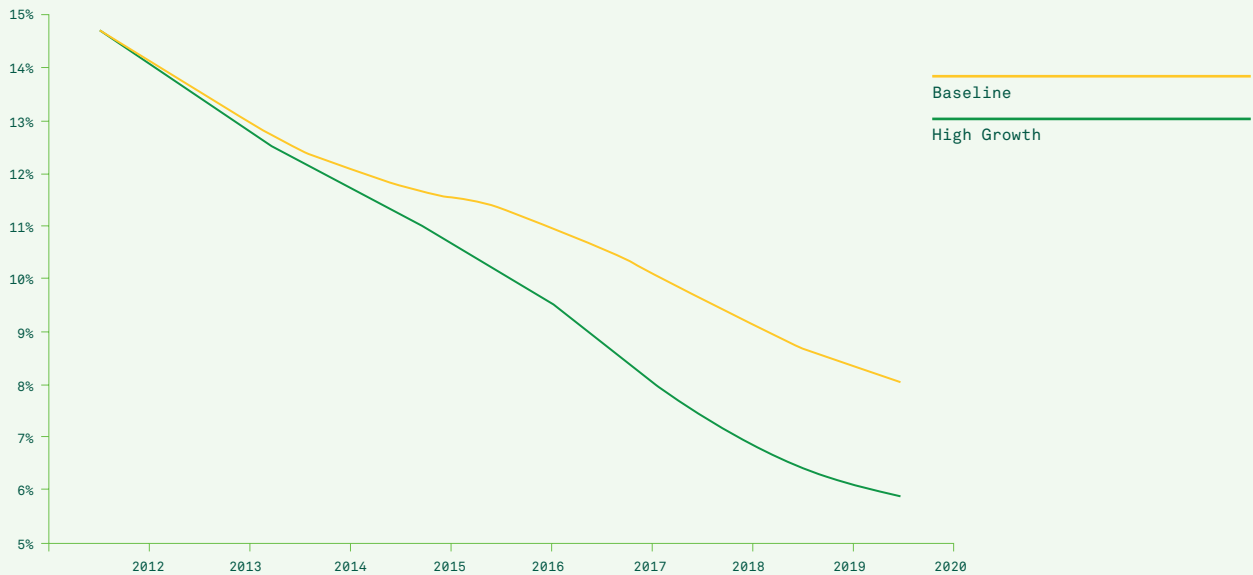


Figure A2: UNEMPLOYMENT RATES (% OF LABOUR FORCE)









Tithe an Rialtais,  
Sráid Mhuirfean Uacht,  
Baile Átha Cliath 2,  
Éire.

Government Buildings,  
Upper Merrion Street,  
Dublin 2,  
Ireland.

Fón/Tel: +353 1 676 7571  
Facs/Fax: +353 1 678 9936

Glaó Áitiúil/LoCall:  
1890 661010

[www.mtes2020.finance.gov.ie](http://www.mtes2020.finance.gov.ie)

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