© 2000 International Monetary Fund

August, 2000
IMF Staff Country Report No. 00/97

Ireland: Staff Report for the 2000 Article IV Consultation

As required under Article IV of its Articles of Agreement, the International Monetary Fund conducts periodic consultations with its member countries. In the context of the 2000 Article IV consultation with Ireland, the following documents have been released and are included in this package:

- the staff report for the 2000 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on **May 15, 2000,** with the officials of Ireland on economic developments and policies. **Based on information available at the time of these discussions, the staff report was completed on July 12, 2000.** The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF;

- a staff statement **of Aug 2, 2000** updating information on recent economic developments;

- the Public Information Notice (PIN), which summarizes the **views of the Executive Board as expressed during the August 2, 2000, Executive Board discussion** of the staff report that concluded the Article IV consultation.

Further background documentation prepared by IMF staff for the consultation may be published separately at a later date. The policy of publication of Article IV staff reports and PINS allows for the deletion of market-sensitive information.

The Article IV staff report is published—both in hard copy and on the IMF's website (http://www.imf.org)—as part of a pilot project. To assist the IMF in evaluating the pilot project for release of Article IV staff reports, reader comments are invited prior to October 5, 2000, and may be sent by e-mail to Pilotproject@imf.org.

Copies of this report are available to the public from

International Monetary Fund • Publication Services
700 19th Street, N.W. • Washington, D.C. 20431
Telephone: (202) 623 7430 • Telefax: (202) 623 7201
E-mail: publications@imf.org • Internet: http://www.imf.org

Price: $15.00 a copy

International Monetary Fund
Washington, D.C.

INTERNATIONAL MONETARY FUND

IRELAND

Staff Report for the 2000 Article IV Consultation

Prepared by the Staff Representatives for
the 2000 Consultation with Ireland

Approved by Jacques R. Artus and G. Russell Kincaid

July 12, 2000

- The discussions were held in Dublin during May 5–15, 2000.
- Meetings were held with Mr. McCreevy, Minister of Finance, Mr. O'Connell, Governor of the Central Bank of Ireland, other senior officials, and representatives of the Economic and Social Research Institute, the social partners, and the financial and academic communities.
- The mission team comprised Messrs. Tweedie (RES) (Head), Hagemann and Aitken, and Ms. Koliadina (all EU1). Ms. Gulde-Wolfe (MAE) participated in the mission to discuss the main conclusions of the Financial Sector Assessment Program (FSAP) report for Ireland. Messrs. Bernes and Charleton, Executive Director and Alternate Executive Director for Ireland, respectively, participated in the meetings.
- The authorities expressed their intention to continue to participate in the pilot project for publication of the staff report.
- Ireland has accepted the obligations of Article VIII, Section 2, 3 and 4. It maintains an exchange system free of restrictions on the making of payments and transfers for current international transactions.
- Ireland provides core macroeconomic data to the Fund in a comprehensive fashion. However, further improvements in timeliness and coverage of some key indicators would allow more effective monitoring and analysis of economic developments.

Contents Page

Executive Summary ... 4
I. Introduction ... 5
II. Background ... 5
A. Recent Economic Developments ... 5
B. Financial Developments and Policies ... 13
III. Report on the Discussions ... 22
A. Economic Outlook and Risks ... 22
B. Macroeconomic Policies ... 26
C. Incomes Policies ... 30
D. Structural Policies ... 31
E. Financial Sector Issues ... 32
IV. Staff Appraisal ... 34

Text Boxes
1. Explaining Ireland's Economic Success ... 6
2. How Serious Are Risks Associated with the Property Boom? ... 16
3. Assessing the Stance of Fiscal Policy ... 21
4. Responding to Overheating under EMU ... 23
5. Financial Sector Stability Assessment ... 33

Tables
1. Selected Economic Indicators ... 38
2. General Government Finances ... 39
3. Stability Program ... 40
4. Indicators of External and Financial Vulnerability ... 41

Figures
1. Growth and Inflation ... 7
2. Contribution to GNP Growth ... 8
3. Balance of Payments, Saving, and Investment ... 10
4. Labor Market Developments ... 11
5. Employment and Unemployment ... 12
6. Exchange Rate Developments ... 14
7. Asset Prices ... 15
8. Monetary and Credit Indicators ... 17
9. Interest Rate Developments ... 19
10. General Government Finances ... 20
11. Comparisons of Key Indicators with Other Euro Area Countries ... 24
12. Comparison of Fiscal Indicators with Other Cyclically-Advanced Euro Area Economies 29

Annexes

I. The National Development Plan, 2000-2006 ... 42
II. Alternative Medium-Term Scenarios ... 44

Appendices

I. Basic Data ... 46
II. Fund Relations ... 47
III Statistical Issues ... 48

EXECUTIVE SUMMARY

Ireland is now in its seventh year of spectacular economic growth. Staff estimates suggest real GNP will expand by close to 8 percent in 2000, in line with the average since 1994. This performance has been associated with rapid growth in employment and disposable incomes, and a marked strengthening in the public finances. This record primarily reflects fundamental improvements in economic performance, but growth has also been boosted over the past 2-3 years by stimulatory macroeconomic policies, mainly associated with the advent of EMU.

Overheating pressures have become more pronounced since the last consultation. Inflation has accelerated sharply to over 5 percent. Higher fuel prices and a tobacco tax hike account for part of this increase, but underlying inflation has also increased. Widespread labor shortages are putting upward pressure on wage rates, and there are significant infrastructure bottlenecks. Property prices continue to rise rapidly, and property-related lending is fueling strong growth in private sector credit.

Ireland's medium term prospects remain favorable. However, overheating in the short term poses a significant risk to this outlook. A sustained acceleration of inflation could weaken the social consensus underlying the latest national wage agreement, sparking increased industrial unrest and threatening the stability that has been central to Ireland's success. More generally, wages and prices could overshoot sustainable levels, setting the stage for a painful economic adjustment later. The domestic property price boom adds to these risks directly, and represents a potential destabilizing element in its own right.

The authorities are giving high priority to alleviating supply side constraints. The National Development Plan for 2000-06 envisages a substantial increase in public investment outlays. Recent fiscal measures have sought to increase work incentives and raise participation rates. The government is also taking steps to increase the supply of housing. The mission welcomed these initiatives. However, it felt that, in view of the short-term risks from overheating, a tighter fiscal stance was warranted to help restrain excess demand. There was also broad agreement that pressures for public sector wage increases beyond those envisaged in the latest agreement should be firmly resisted.

Beyond the immediate issue of overheating, the mission emphasized the importance of putting in place mechanisms to allow greater flexibility in public sector wage determination and eliminate the reliance on tax trade-offs. The mission also urged further progress toward a multi-year budgetary framework, which would help to maintain fiscal discipline, ensure medium-term sustainability and guide private expectations of the orientation of fiscal policy.

The mission stressed that the rapid growth in private sector lending pointed to a need for extreme vigilance on the part of market participants and supervisors alike to ensure that financial system soundness is not compromised. A recent FSAP report concluded that the Irish financial system remains sound but urged the supervisory authorities to continue their efforts to ensure that credit institutions follow prudent lending guidelines and take adequate account of the potential impact on their portfolios of an external or domestic shock, including a downturn in the property market.

I. Introduction

1. **Ireland's economy has undergone a remarkable transformation over the past decade.** In terms of output growth, Ireland ranked first among OECD countries in the 1990s after being among the weakest performers in the first half of the 1980s. Growth took off in 1994 and has since averaged 8 percent on a GNP basis (almost 9 percent on a GDP basis).[1] As a result, per capita GNP reached about 90 percent of the EU average in 1999, up from 60 percent in 1993. Over the same period, inflation was generally subdued, unemployment fell by almost two-thirds, and the external current account remained in surplus, boosted by annual gross EU transfers averaging close to 4 percent of GDP. The public finances strengthened as the general government balance moved from deficit into sizable surplus, and the public debt ratio was cut in half. The dramatic turnaround in the economy raises the question of whether it can be attributed to a few key policy initiatives. Available studies of the Irish experience, however, suggest a more complex story (see Box 1).

2. **The rapid growth of the last few years has raised concerns about overheating risks.** At the time of the last Article IV consultation in August 1999, Executive Directors commended the authorities for Ireland's impressive and sustained economic performance. However, they generally agreed that capacity constraints were likely to become more binding, and that indications of inflationary pressures—in goods, labor, and asset markets—had grown. Against this background, they broadly agreed that a shift of policy emphasis toward containing inflationary pressures was appropriate.

3. **The minority center-right coalition government of Prime Minister Bertie Ahern has been in power since June 1997.** Elections must be held by May 2002, but could be called earlier.

II. Background

A. Recent Economic Developments

4. **1999 was another banner year for growth**. Staff estimates suggest real GNP grew by almost 9 percent (Table 1, Figures 1 and 2). Private consumption was boosted by strong gains in real disposable incomes—up almost 50 percent since 1993—the wealth effects of rising house prices, and a sharp decline in borrowing costs. Investment outlays also remained

---

[1] Multinational firms contribute substantially to Irish output, and the associated factor outflows create a significant difference between measures of output and income. As a result, real GNP tends to be preferred to real GDP as a measure of economic growth for Ireland.

Box 1: Explaining Ireland's Economic Success

Ireland's strong economic performance in recent years is all the more remarkable when viewed against the background of the near-crisis situation in the mid-1980s. At that time, the fiscal deficit was over 12 percent of GDP, the public debt ratio reached 110 percent of GDP, and the unemployment rate peaked at 17 percent. Recent studies of the Irish experience[1] attribute the subsequent turnaround to a number of mutually reinforcing factors, some of which significantly pre-date the recent boom.

- **Long-standing outward orientation of trade and investment policy has been pivotal**. The shift away from a protectionist import-substitution strategy dates back to the 1960s. The Anglo-Irish Free Trade Agreement of 1965 and EC entry in 1973 were two landmarks. Trade liberalization was accompanied by consistent pursuit of an industrial policy that actively encouraged foreign investment in export-oriented manufacturing industries through tax and financial incentives and a stable regulatory environment.

- Building on this foundation, the **advent of the single European market played a major role** in broadening market access, promoting efficiencies, and encouraging FDI inflows. Ireland benefited from a sharp increase in U.S. FDI flows into the EU from the late 1980s seeking to take advantage of the single market. In addition to a welcoming policy environment, the availability of a relatively low cost, skilled, English-speaking workforce, and the links established by decades of migration made Ireland an attractive destination for U.S. investment.

- **A large increase in the allocation of EU structural funds to Ireland from 1989 onwards** helped to support demand, ease economic adjustment, and upgrade the physical infrastructure, thereby boosting potential growth and adding to Ireland's attractiveness for foreign investment.

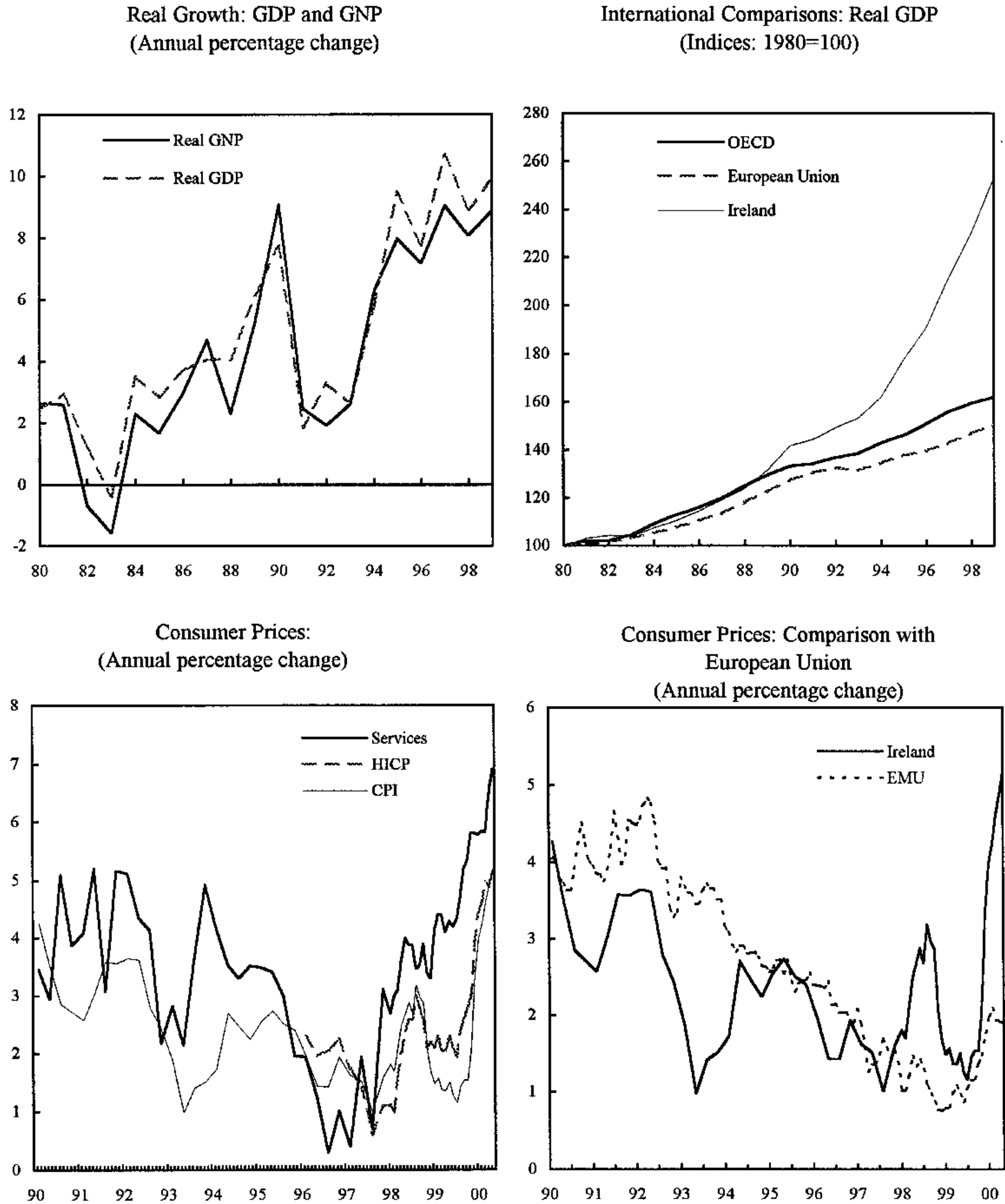
- **Decisive action in 1987 to address the fiscal crisis was critical**. Fiscal consolidation focussed on spending cuts rather than tax increases (though a tax amnesty led to a revenue windfall in 1988 and raised the tax base). These actions coincided with a dramatic improvement in the external environment, reflecting falling world interest rates, the 1986 exchange rate realignment, appreciation of sterling, and a strengthening in external demand. Monetary discipline was maintained through Ireland's participation in the ERM.

- **Other domestic factors have contributed**. Rapid labor force growth was made possible by demographic factors (the result of a late baby boom), rising female participation, and the advent of net inward migration flows in recent years. The average skill level of the labor force has been boosted by improved public education since the early 1960s. Successive national wage agreements since 1987 have promoted wage moderation and a relatively harmonious industrial relations environment. Deregulation helped reduce domestic costs and increase competitiveness.

- **Ireland also benefited from its close links with the buoyant U.S. economy and from the global high tech boom**. FDI flows have been concentrated in high-growth sectors, notably electronics (including software), health care and pharmaceuticals. Ireland entered these sectors relatively early, and agglomeration effects have probably been important in attracting new foreign investment. There also appear to have been positive spillovers in terms of skill and technology transfers from the foreign sector to "new" indigenous industries.

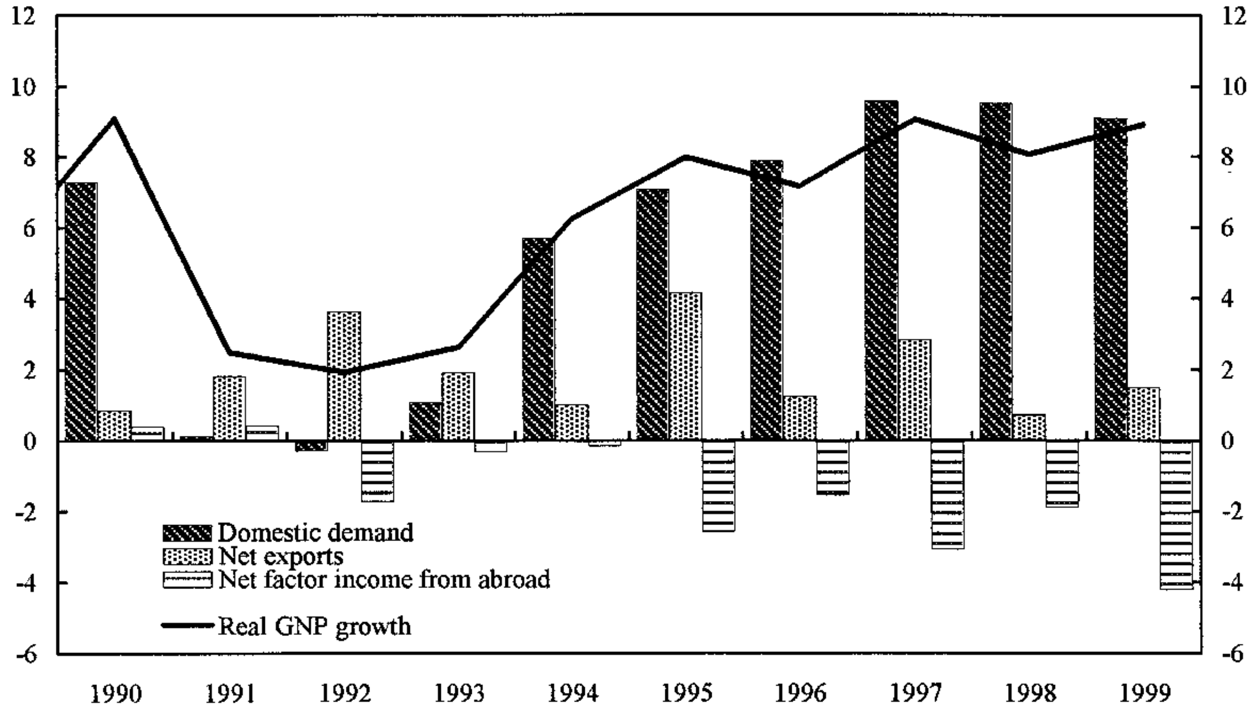
[1] See, for instance, Duffy *et al.* (1997), *Medium Term Review: 1997-2003*, The Economic and Social Research Institute, Chapter 3; *OECD Economic Surveys: Ireland 1999*; and Frank Barry, ed., (1999), *Understanding Ireland's Economic Growth*, (MacMillan Press LTD).

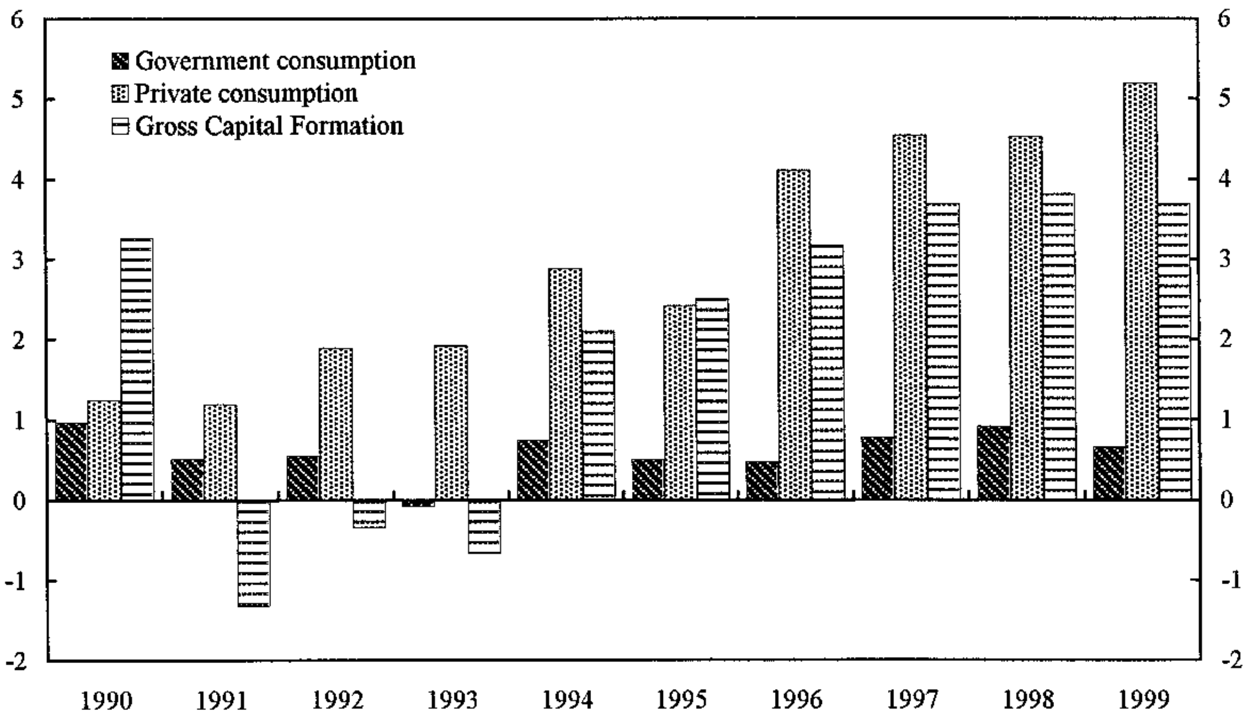
Figure 1. Ireland: Growth and Inflation



Sources: IMF, International Financial Statistics; Department of Finance; Central Bank of Ireland, Quarterly Bulletin; and OECD, Main Economic Indicators.

Figure 2. Ireland: Contribution to GNP Growth, 1990-99





Sources: Central Statistics Office and staff calculations.

extremely buoyant. The external current account position deteriorated to near balance in 1999 from a 2 percent of GDP surplus in 1998 as a rise in the trade surplus with non-euro area countries was more than offset by higher profit repatriation by foreign-owned enterprises and a decline in EU transfers (Figure 3). Export growth initially slowed amid weaker external demand, but rebounded later in the year. Import growth moderated somewhat.

5. **Available indicators for 2000 suggest activity is still expanding at a torrid pace.** Consumer confidence remains near record levels, and retail sales volumes were up 15 percent in the first four months of 2000 (year ago basis), boosted by a surge in new car sales. Business confidence is high, though survey data suggest that labor and supply shortages are increasingly constraining growth. Tax receipts through June were up 14½ percent on year ago levels.

6. **Rapid employment growth has been a defining feature of the expansion.** After averaging 4 percent in 1994-97, annual employment growth has since accelerated to over 6 percent, pushing the employment rate above the euro area average (though it remains below rates in the United States and the United Kingdom—Figure 4). Labor force growth has remained strong, reflecting rising female participation, demographic factors, and net inward migration (Figure 5). The unemployment rate fell to 4.7 percent in the first quarter of 2000. Short-term unemployment appears to have stabilized at about 3 percent, while long-term unemployment fell to just 1.7 percent.

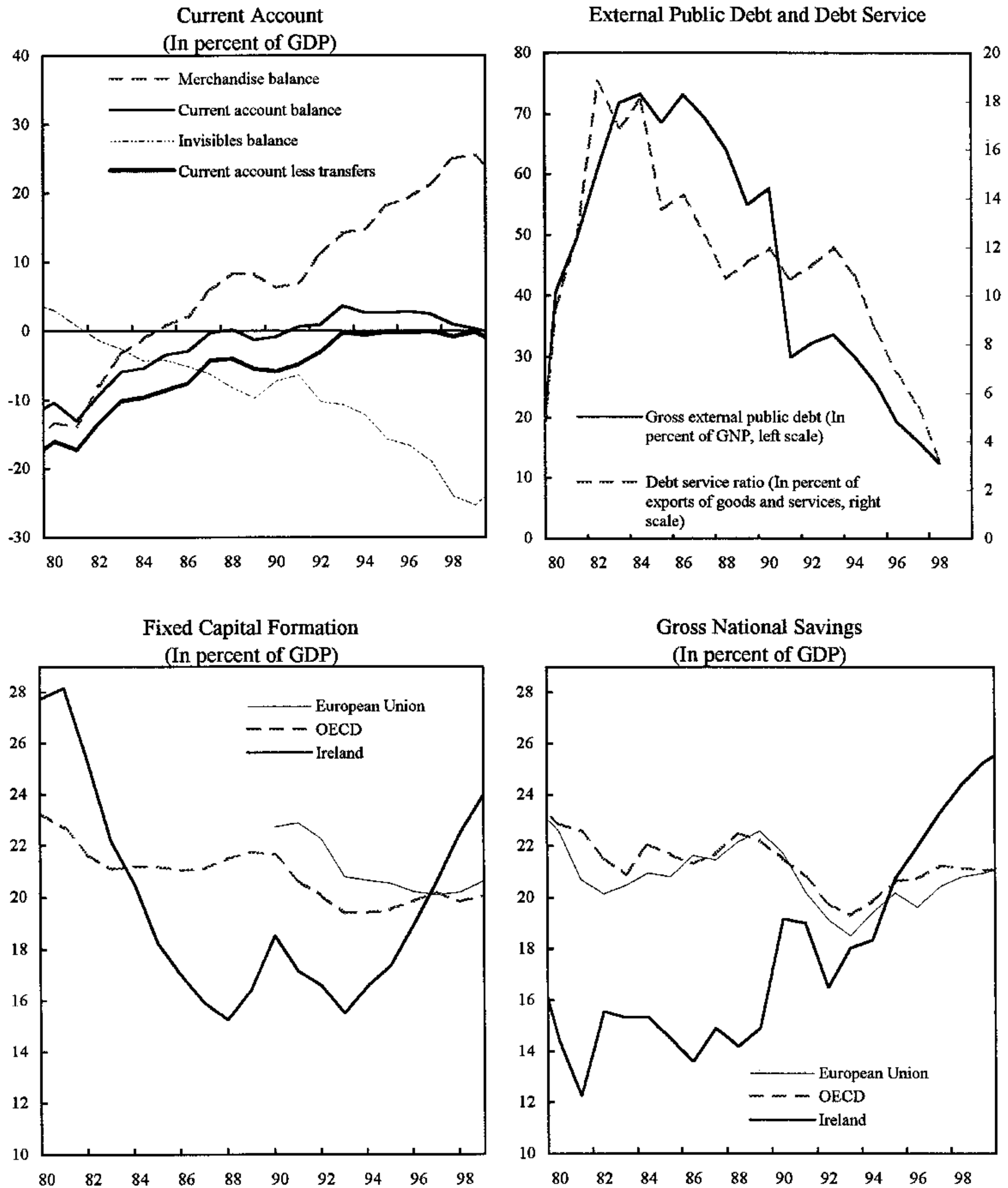
7. **Labor shortages are widespread across both skilled and unskilled categories, and have put upward pressure on wages.** Available data suggest average hourly earnings accelerated markedly in 1998 and the first half of 1999 (Table 1). Incomes policy since 1987 has centered around a series of multi-year national agreements targeting wage moderation in exchange for understandings on other policies, including tax cuts. These accords are generally thought to have had most impact on public sector wage formation, given lower unionization levels in the private sector. Wage increases through mid-1999 exceeded the guidelines under the last national agreement despite higher tax relief,[2] raising questions about the capacity of current arrangements to deliver wage restraint in a tight labor market (Figure 4).

8. **Inflation has accelerated sharply in recent months**. On a harmonized basis, inflation reached 5.1 percent in May, the highest in the euro area and up from about 2 percent

---

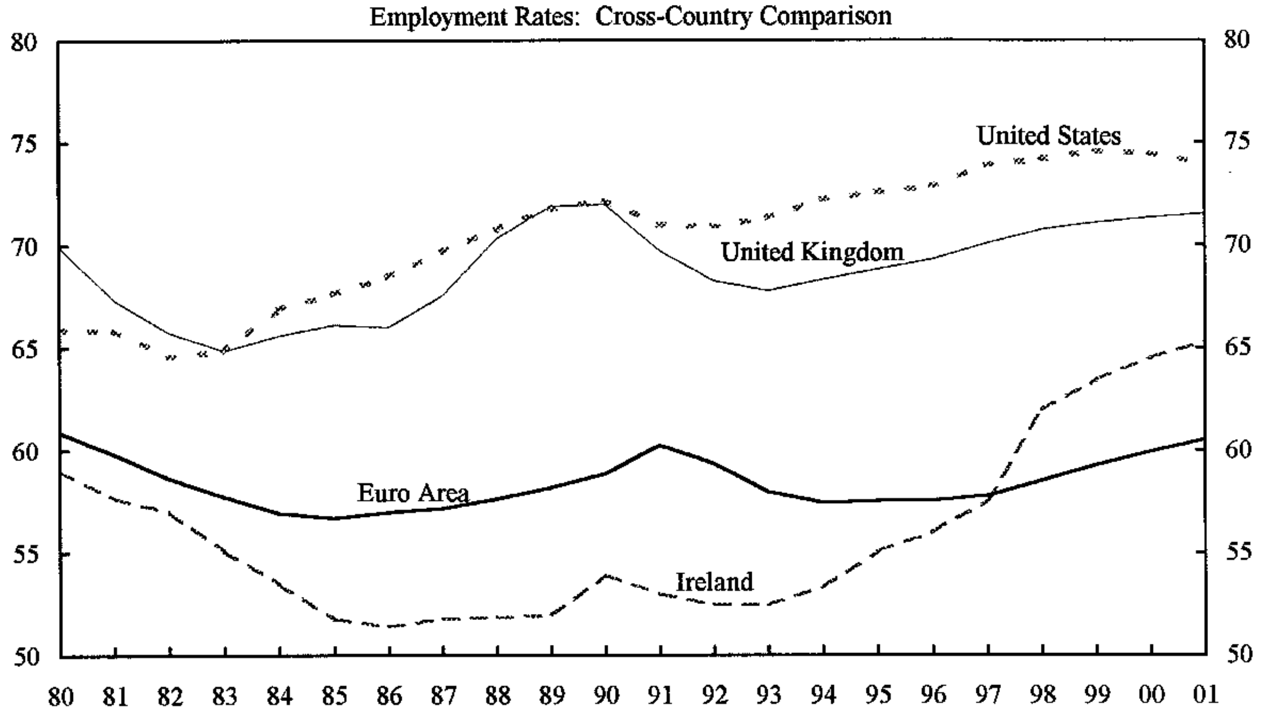
[2] The *Partnership 2000 for Inclusion, Employment and Competitiveness* covered the three-year period through March 2000 and specified a cumulative pre-tax wage increase of 9 ¼ percent in exchange for personal tax reductions of 1 percent of GDP. In the event, tax reductions of some 2½ percent of GDP were granted over the life of the agreement.

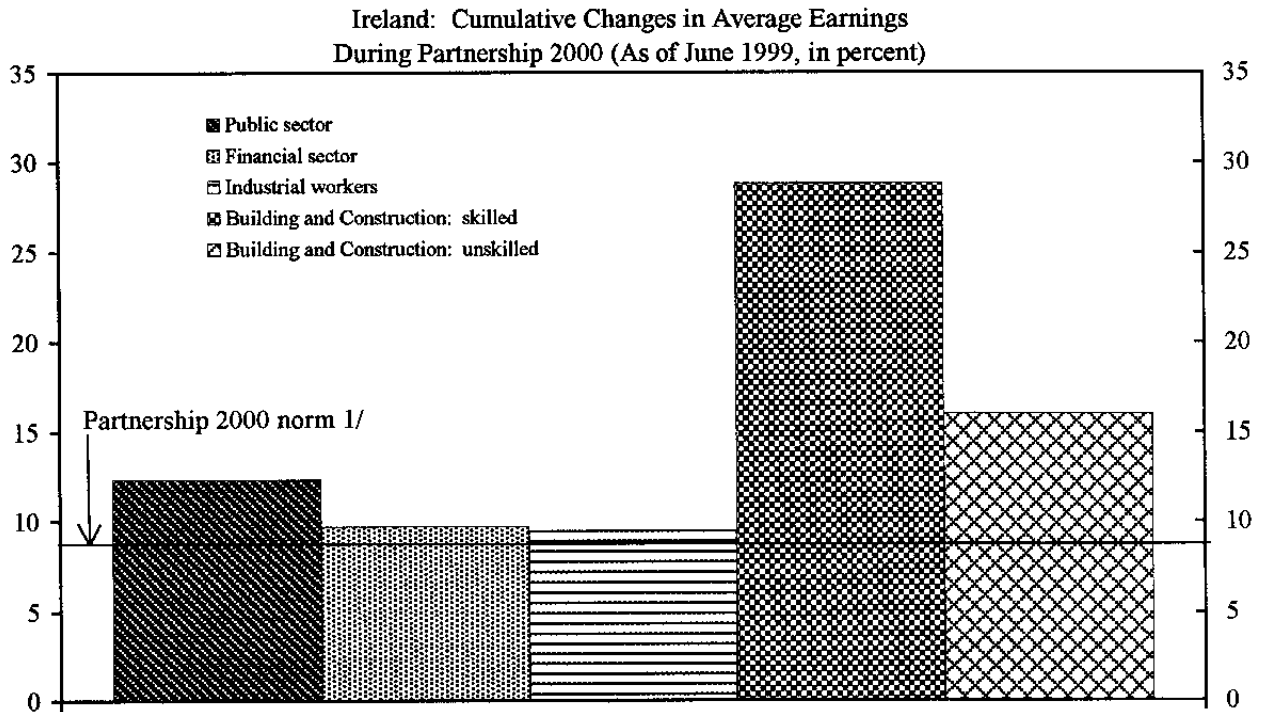
Figure 3. Ireland: Balance of Payments, Saving, and Investment



Sources: IMF, World Economic Outlook; Department of Finance; Central Bank of Ireland, Quarterly Bulletin; and OECD, Quarterly National Accounts.

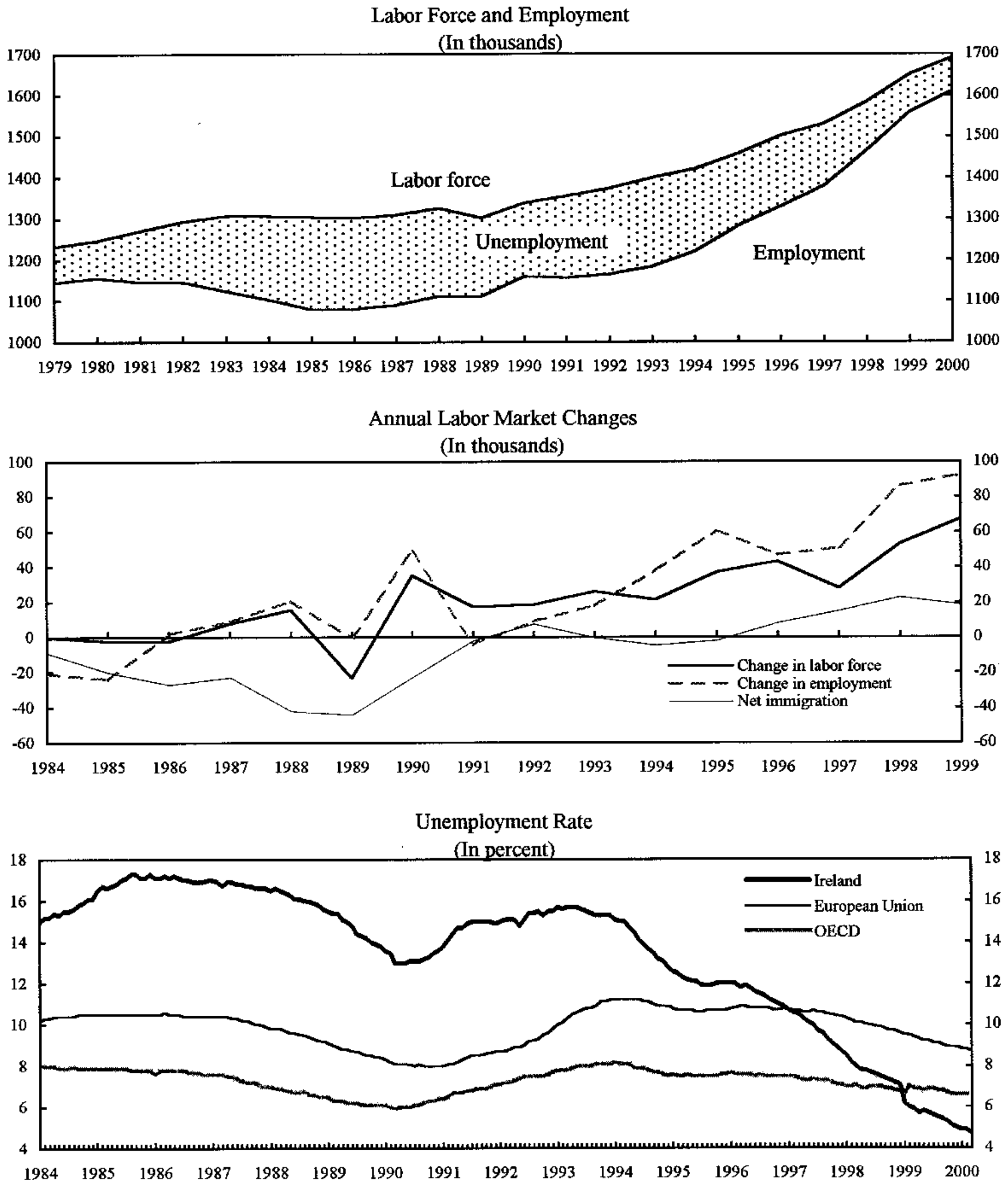
Figure 4. Ireland: Labor Market Developments





Sources: OECD, the Central Statistics Office, and staff estimates.
1/ Partnership 2000 specified a cumulative pre-tax wage increase of 9¼ percent.

Figure 5. Ireland: Employment and Unemployment



Sources: OECD, Central Statistics Office, Census of Population, Labor Force Surveys, and Live Register Statements; and Department of Finance.

in mid-1999 (Figure 1).[3] Higher energy prices and a tobacco tax hike accounted for about 2 percentage points of the increase. However, central bank estimates put the underlying inflation rate (excluding temporary factors) at over 4 percent, and underlying services inflation at more than 7 percent, up from 3 percent in early 1998. [4] Goods price inflation remained subdued despite the depreciation of the euro, though recent data show some signs of a pick-up. Consumer survey data also point to a marked increase in inflationary expectations.

9. **At least until very recently, the adverse effects of rising inflation on competitiveness have been outweighed by the weakness in the euro.** Staff estimates suggest that strong productivity growth in the manufacturing sector has contributed to a steady depreciation of Ireland's real effective exchange rate on a ULC basis (Figure 6). This primarily reflects unusually high productivity growth in a few key traded sectors, but the CPI-based real effective exchange rate and recent export trends also suggest that competitiveness vis-à-vis non-euro area trading partners remains strong. Competitiveness within the euro area has probably begun to erode, but from a favorable starting point. There is little evidence so far that investment flows have been significantly affected by competitiveness concerns, as FDI inflows almost doubled in 1999.

10. **Excess demand pressures have been manifested also in rapid property price increases** (Figure 7). House price inflation has moderated somewhat from its peak but still exceeded 20 percent (12-month basis) in April 2000, the fourth year in a row of rapid price increases. Housing demand has been boosted by demographics, net migration inflows, rising real incomes, and falling mortgage interest rates. However, demand also may be driven in part by expectations of further price increases (see Box 2). Commercial real estate prices also have been rising strongly, with office vacancies at historic lows and capital values up 30 percent on a year ago basis in December 1999. Equity prices have been relatively subdued on balance over the past two years after earlier strong gains.

B. Financial Developments and Policies

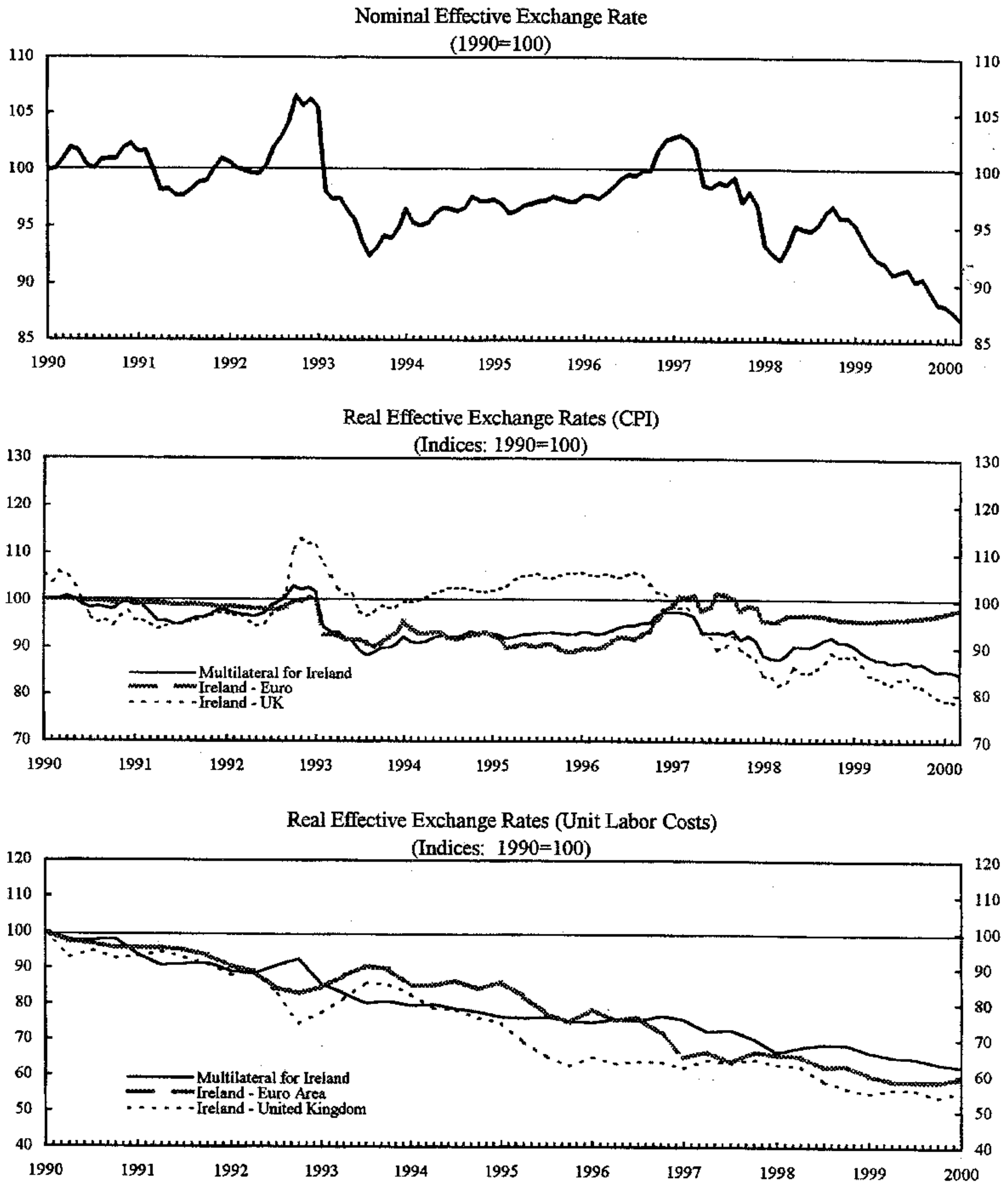
11. **Monetary conditions are more expansionary than at any time in the past decade** (Figure 8). Interest rate convergence in the run-up to Stage 3 of EMU implied a loosening of monetary conditions, which was compounded by the ECB's move to cut official rates by 50 basis points in April 1999 and the weakening of the euro against other major currencies.

---

[3] The EU Harmonized Index of Consumer Prices (HICP) excludes items that comprise about 8 percent of the national basket, including mortgage interest payments. On a national basis inflation was 5.2 percent.

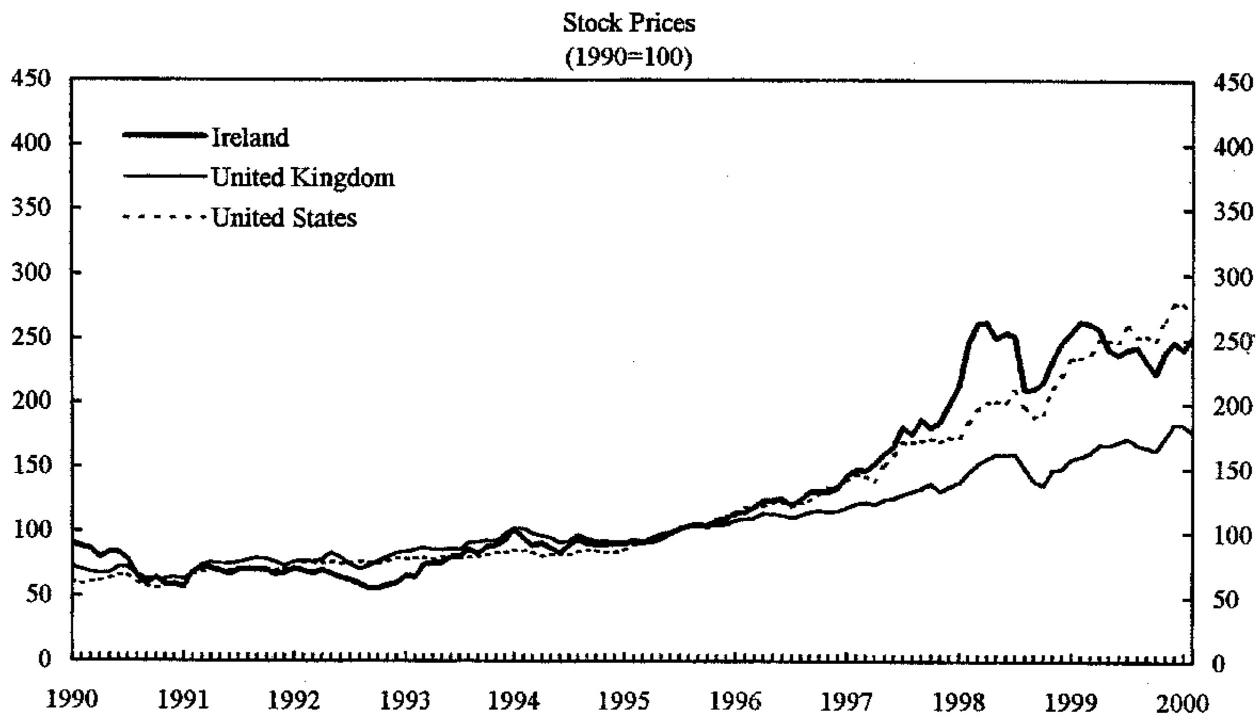
[4] See Central Bank of Ireland Bulletin, Summer 2000, pp. 29–30. By way of comparison, service price inflation for the euro area is below 2 percent.

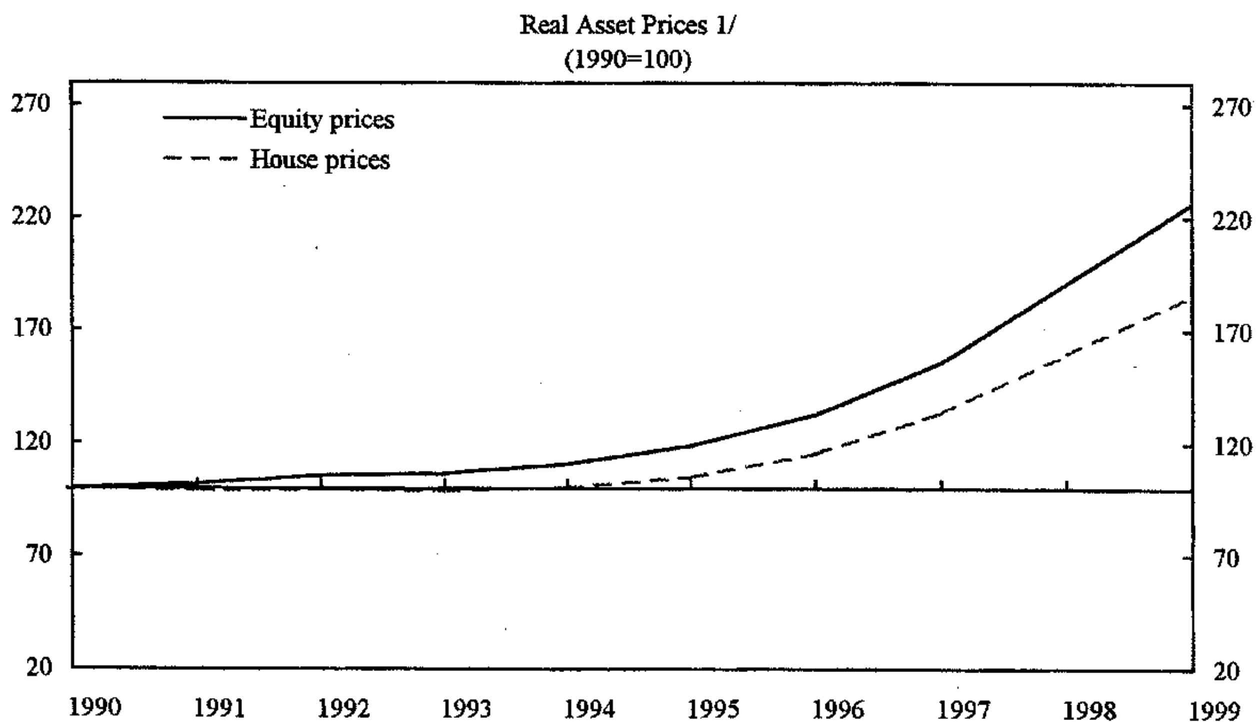
Figure 6. Ireland: Exchange Rate Developments



Sources: IMF, INS, International Financial Statistics, and Fund staff estimates.

Figure 7. Ireland: Asset Prices





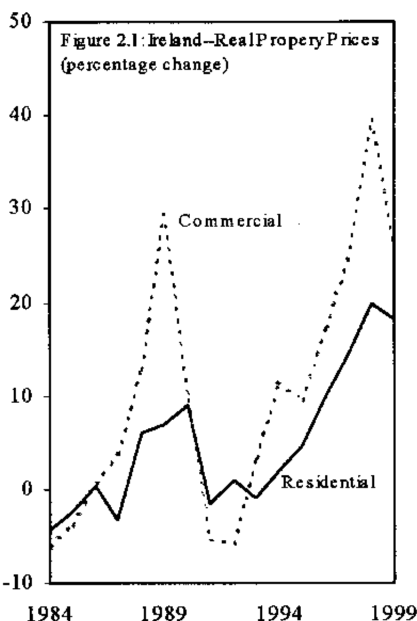
Sources: IMF, International Finance Statistics; and Central Statistics Office.

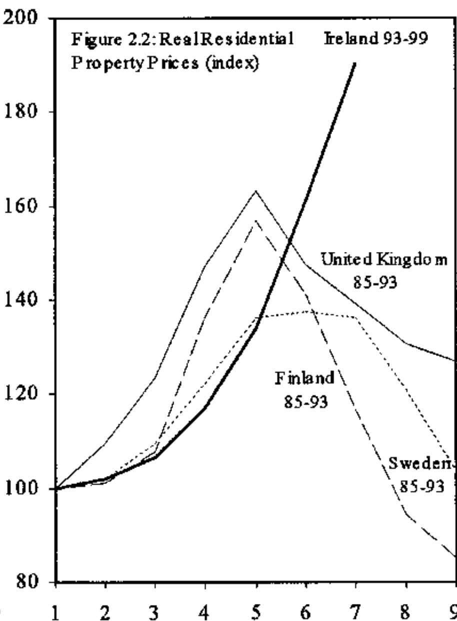
1/House prices for Ireland refer to new house prices.

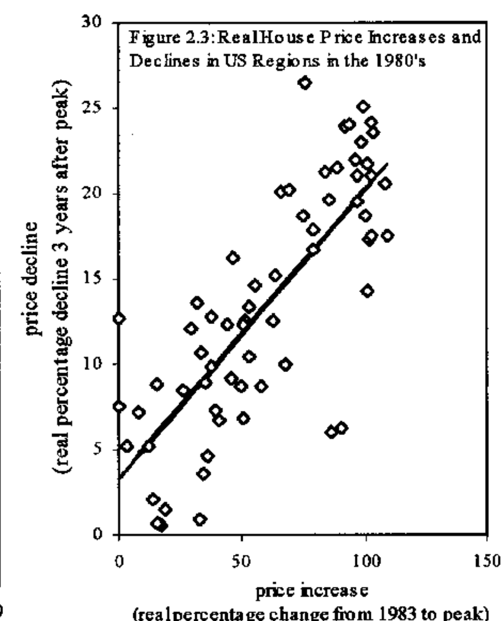
Box 2: How Serious Are Risks Associated with the Property Boom?

Since the early 1990's, Ireland has experienced a dramatic increase in property prices, as rapidly growing demand has outpaced relatively inelastic supply (Figure 2.1). Much of the increase in demand for housing reflects demographic factors, strong employment growth, and lower interest rates. However, it is less clear that fundamentals alone can justify the rapid increase in house prices.[1] The usual method for making such assessments is to relate historical price developments to a basket of observed fundamentals (see Chapter III of the Winter 2000 WEO). However, this method rarely yields conclusive results and in any event is difficult to apply to cases such as Ireland where the change in the economic environment has been dramatic.

Beyond the influence of fundamentals, sustained rapid price increases over several years may lead to self-fulfilling expectations-driven demand followed by price overshooting.[2] Comparisons with other high-growth episodes, while by no means conclusive, are informative. Cumulative real estate price increases in Ireland exceed those of several countries, notably the United Kingdom, Sweden, Finland, and Norway, that experienced unsustainable property booms in the late-1980s (Figure 2.2). The US has also experienced a variety of regional house price developments against the background of a common monetary policy. Price increases in the 1980s in many regions (particularly New England and California) were also very rapid,







followed by dramatic collapses. The regions with the largest increases also suffered the largest collapses, consistent with expectations-driven demand (Figure 2.3). While several euro-area countries and US regions have sustained property booms in the 1990s without price collapse (Finland, Netherlands, Norway, Colorado, Oregon, Utah), none have been on par with Ireland's; in fact, no industrial country in the last 20 years has experienced price increases on the scale of Ireland without suffering a subsequent fall.

If Irish real estate prices were to fall, the aggregate demand effects would probably be substantial, given the high rate of house ownership in Ireland. It is not currently considered that such a decline would pose a threat to the Irish banking system. Average household indebtedness is still moderate; falling interest rates have kept the mortgage repayment burden well below that during the UK boom, and Ireland's volume of mortgage debt remains below that observed in other countries at their house price peaks.[3] However, Ireland's relatively low indebtedness also may suggest that mortgage lending can continue to expand rapidly for some time before debt level concerns become a binding constraint. Given this, the risks may arise not so much from a price decline now, as from the possibility that rapid price increases may persist, increasing the potential for overshooting and a future price reversal.

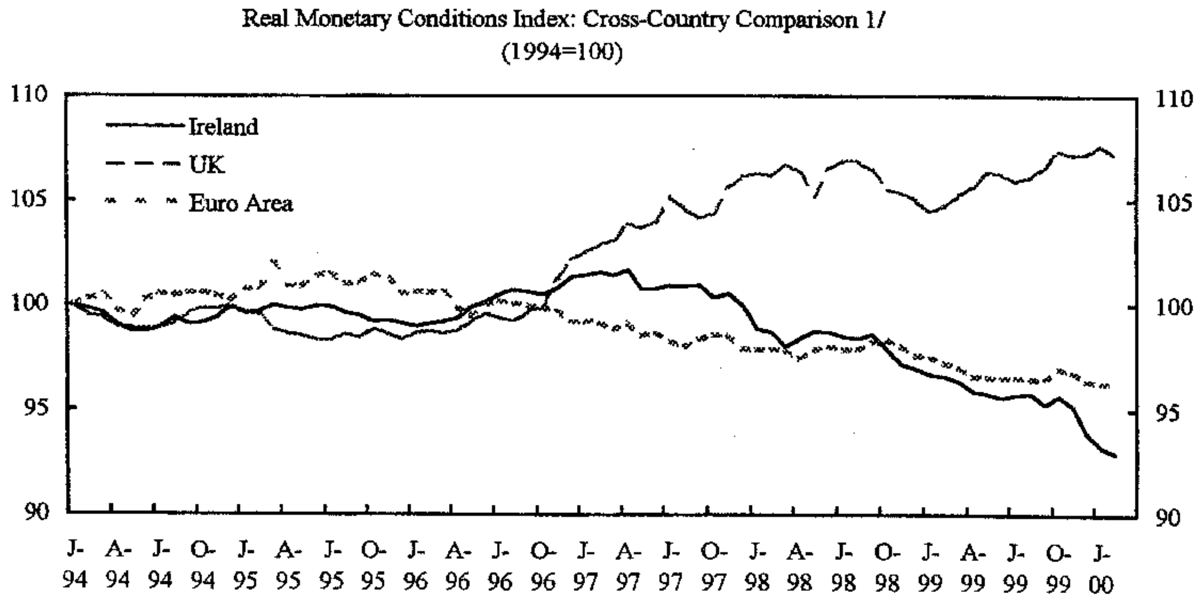
---

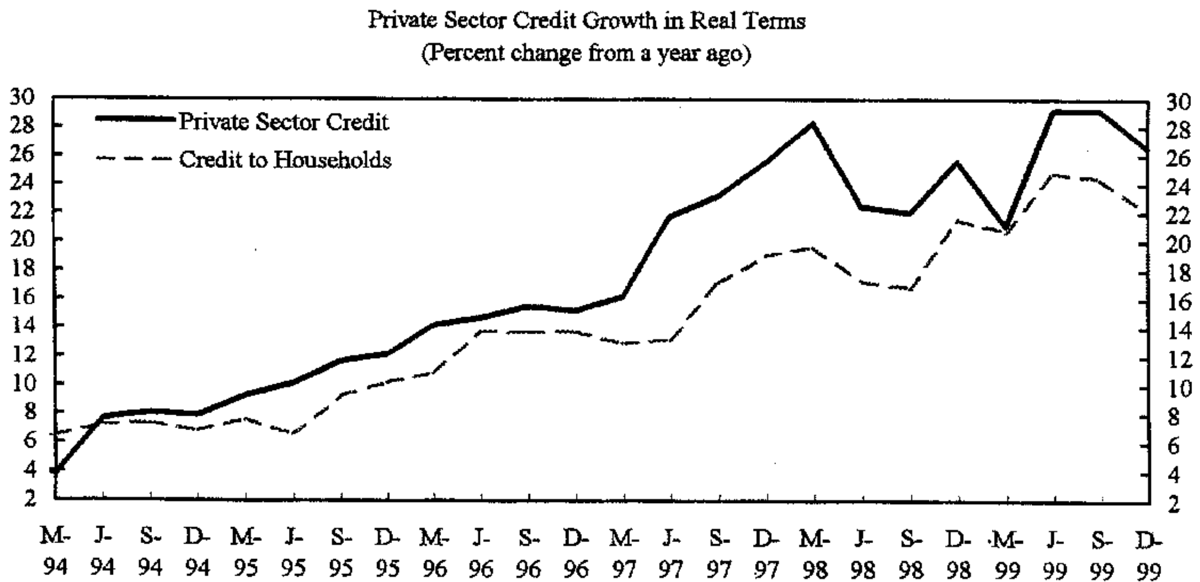
[1] These issues will be examined in the Selected Issues paper *Ireland's Property Boom from an International Perspective*.

[2] There is some evidence that demand in Ireland has increasingly been driven by expected future house price increases (Bacon, *The Housing Market in Ireland: An Economic Evaluation of Trends and Prospects*, June 2000).

[3] The European Central Bank (*Asset Prices and Banking Stability*, April 2000) concluded that there appears to be no major systemic threat to the Irish banking system from a decline in real estate prices. A similar conclusion was reached by the recent FSAP mission, on the basis that major banks are well capitalized and have relatively diversified portfolios.

Figure 8. Ireland: Monetary and Credit Indicators





Sources: IMF, Central Bank of Ireland and staff calculations.

1/ The index is defined as a weighted average of the percentage point changes in the real short-term interest rate and the real effective exchange rate from the base period. Relative weights are 4 to 1 for both Ireland and the United Kingdom and 7 to 1 for the Euro Area. The appropriate weights for Ireland are uncertain given the unusually large size of trade relative to GDP, and the uncertain effect of Ireland's entry into EMU. However, the broad conclusions about the evolution of monetary conditions in Ireland are not particularly sensitive to the choice of weights.

The ECB has since raised rates by a cumulative 175 basis points, but staff estimates suggest that real monetary conditions in Ireland continued to loosen as a result of the further depreciation of euro and the rise in domestic inflation (Figure 9). Private sector credit has expanded at a very rapid pace over the past three years, and was up 24½ percent in the year ended May 2000.[5] This may partly reflect a stock adjustment given initially low private debt levels; the credit-to-GDP ratio reached 87 percent by end-1999, close to the euro-area average of 95 percent.

12. **The public finances strengthened further in 1999, as buoyant tax receipts and savings from lower unemployment and interest rates more than offset budgetary overruns in other areas.** The general government surplus reached 3.7 percent of GDP before adjusting for one-off costs associated with settlement of pension liabilities for the telecommunications company and postal services (Table 2, Figure 10). On the same basis, the primary surplus exceeded 6 percent of GDP, up from 5.5 percent in 1998, while the general government debt-to-GDP ratio dropped to 50 percent, half its 1993 level. As in previous years, stronger-than-expected tax receipts were partly offset by spending overruns, notably on public sector wages. The rapid pace of output growth in recent years complicates assessments of the fiscal stance. However, using Fund methodology and based on *ex post* outcomes, staff estimates of the primary structural balance suggest the fiscal stance remained broadly neutral in 1999, as it was in 1997–98 (see Box 3).

13. **The fiscal surplus is expected to be broadly unchanged in 2000.** The budget included sizable personal income tax cuts of 1.3 percent of GDP, reflecting lower tax rates, a reduction in the proportion of taxpayers subject to the top rate (from 46 to 37 percent), and a partial move toward individualization of the tax bands aimed at encouraging increased female participation. The latter move proved controversial as it was viewed as discriminating against single-earner households, and the government subsequently introduced a new "home carer" allowance for single-income families with dependents, watering down somewhat the incentive effects of individualization. The standard corporate tax rate was further reduced from 28 to 24 percent in line with the government's plan to unify the rate at 12 ½ percent.[6] The budget also included significant increases in spending on social services and infrastructure, the latter reflecting the government's commitment to address infrastructure needs under the *2000-06 National Development Plan* (NDP) (see Annex 1). Staff estimates suggest the structural primary surplus would decline by ¾ of 1 percent of GDP in 2000.

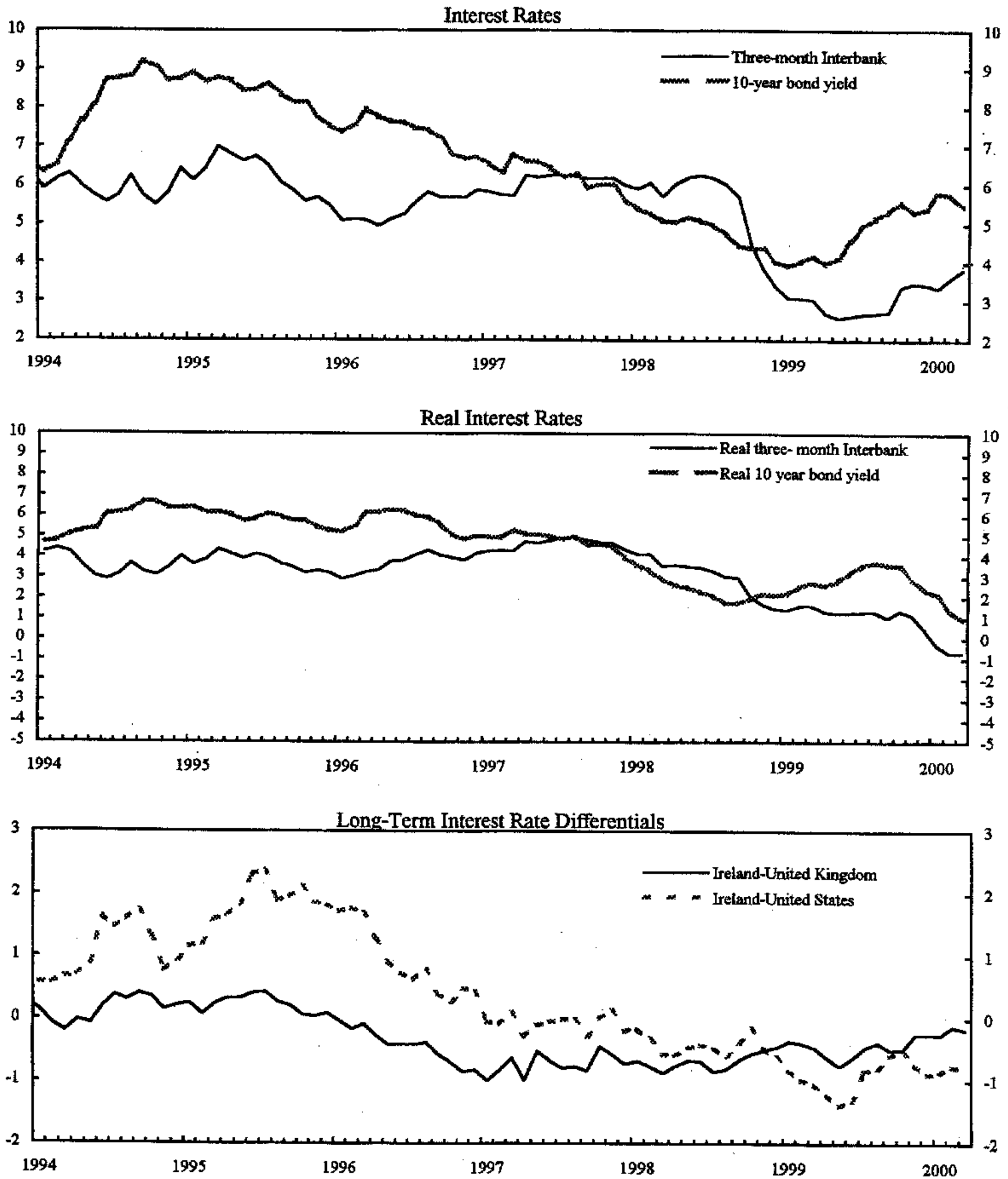
14. **In early 2000, agreement was reached on a new multi-year national wage accord.** The *Programme for Prosperity and Fairness* (PPF) takes effect in the public sector in

---

[5] Adjusted for lending to non-bank entities in the International Financial Services Center.

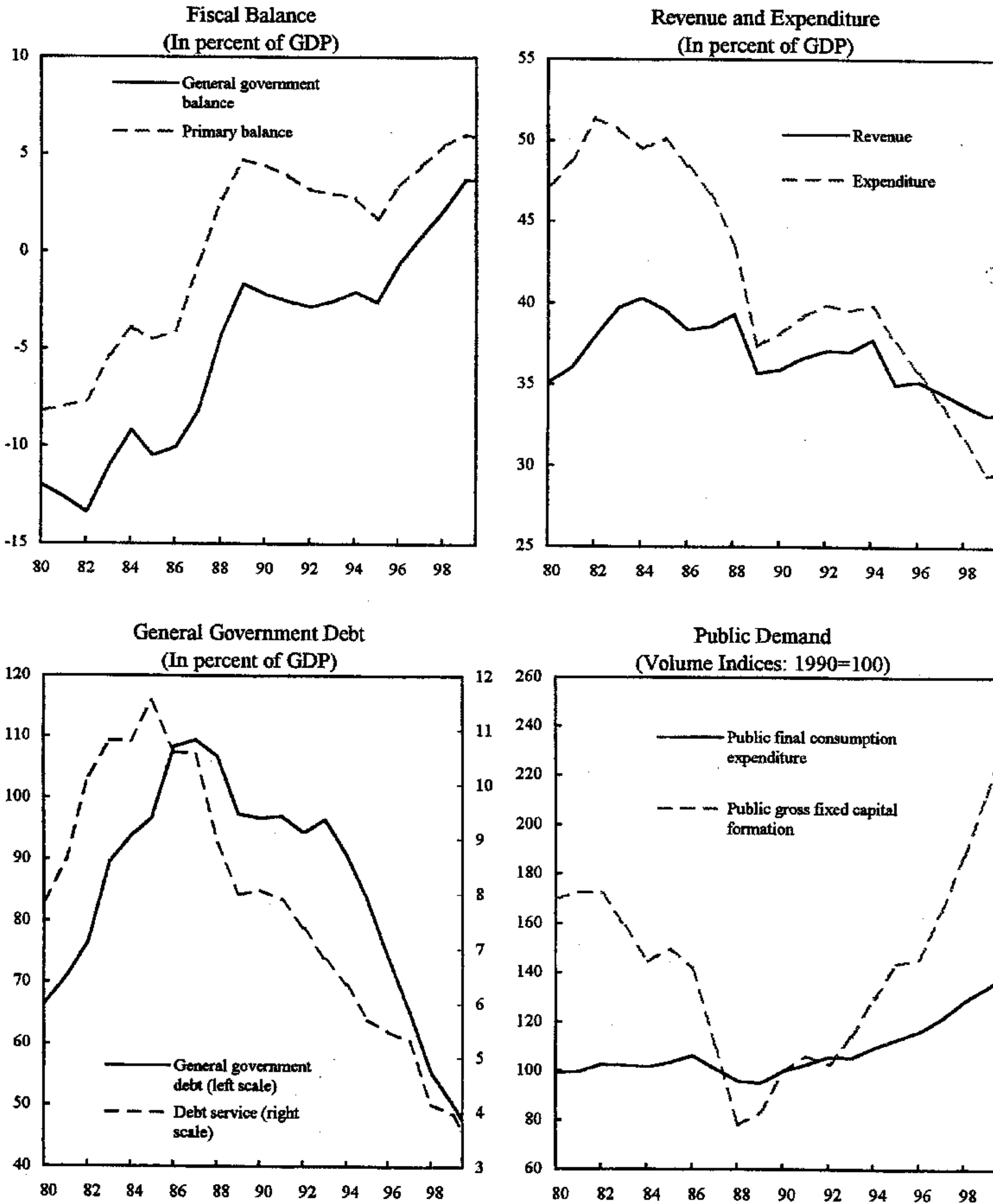
[6] As agreed with the European Commission, the 10 percent rate applying to manufacturing and certain internationally traded services will be unified with the standard rate by 2003.

Figure 9. Ireland: Interest Rate Developments



Sources: Central Bank of Ireland, Quarterly Bulletin; and IMF, Surveillance Database.

Figure 10. Ireland: General Government Finances, 1980-99

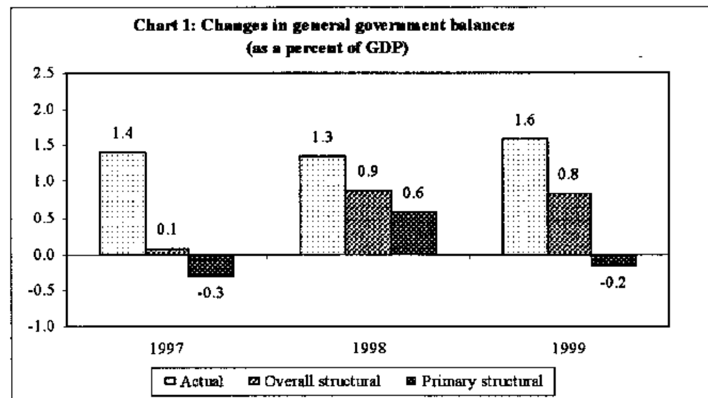


Sources: Department of Finance, Economic Statistics.

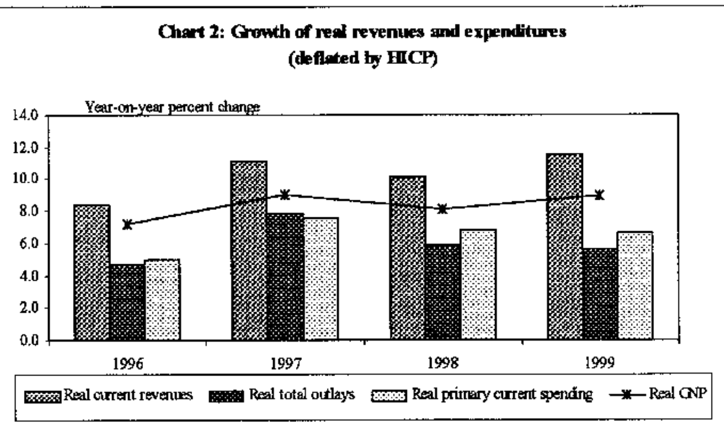
Box 3: Assessing the Stance of Fiscal Policy

Rapid output growth since the mid-1990s has been associated with a marked strengthening in the public finances, as the general government balance improved by more than 6 percent of GDP since 1995. Notwithstanding this, some have argued that discretionary fiscal policy has been pro-cyclical.[1] This apparent contradiction raises questions about how the fiscal stance should be assessed in a rapidly growing economy such as Ireland.

A traditional approach is to look at changes in the structural balance (SBB), i.e., the general government balance adjusted for the effects of the economic cycle. Staff estimates of the SBB suggest that fiscal policy has been contractionary in recent years (Chart 1). A variant of this approach is to focus on the primary SBB, i.e., excluding interest. This may be justified on the grounds that interest payments have weaker multiplier effects (taking account of the fact that part of the public debt in Ireland is held abroad). Staff estimates show an unchanged primary SBB since 1996, suggesting that fiscal policy has been broadly neutral. The SBB approach relies on estimates of potential growth, which normally would be stable but is more uncertain in Ireland. If recent potential growth were lower than staff estimates suggest (7 ½ percent in 1997-99), for example, the SBB measures would show a looser fiscal stance than indicated above.



An alternative approach is to focus on discretionary measures by comparing actual budgetary outcomes with those implied under a "no policy change" setting. If the actual budgetary outcome exceeds the simulated "no policy change" balance, the stance would be interpreted as expansionary. Based on such a methodology, Duffy *et al.* (1999) estimate that fiscal policy has been pro-cyclical, with an estimated fiscal impulse of 3¾ percent of GDP in 1997-99.



The "no policy change" approach requires difficult judgments as to what measures are discretionary. Nonetheless, an examination of the discretionary element in recent budgets provides useful insights into how fiscal policy has been conducted. During 1997-99, for example, the government has been able to provide "discretionary" tax relief of over 3 percent of GDP, and increase real primary current spending on average by 7 percent a year, while at the same time achieving a significant reduction in the public debt ratio (Chart 2). This outcome partly reflects the benefits of rapid economic growth and declining interest rates that have effectively allowed fiscal policy to achieve multiple objectives.

From the perspective of assessing the impact of the fiscal stance on aggregate demand, however, it is the overall effect of fiscal policy and not just the discretionary element that is the most relevant concept. For example, "discretionary" tax cuts that offset the effects of fiscal drag, or spending programs that boost public spending growth in line with potential may be judged expansionary under a "no policy change" approach, even if they imply no net addition to demand. For these reasons, and despite its shortcomings, the staff has used the SBB approach when assessing the overall fiscal impulse. As discussed above, this approach suggests that the fiscal stance was broadly neutral during 1997-99.

---

[1] See, for example, Duffy *et al.* (1999), "Medium-term Review 1999-2005," *Economic and Social Research Institute;* Cronin and McCoy (1998), "Measuring Structural Budget Balances in a Fast-growing Economy: The Case of Ireland", *Indicators of Structural Budget Balances,* Special Issue of Contributi All'Analisi Economica, Banca d'Italia; Lane (1998), "On the Cyclicality of Irish Fiscal Policy," *The Economic and Social Review*, Vol. 29; and the Central Bank of Ireland Spring 2000 Bulletin (pp. 6-7).

October 2000 and covers the 33 months through mid–2003. It envisages cumulative wage increases of 15½ percent, income tax reductions that would boost disposable incomes by a further 10 percent, and increased public spending on social services and infrastructure. The PPF also introduced a national minimum wage of IR£4.40 (workers under 18 are entitled to 70 percent of the adult rate), equivalent to 58 percent of the average industrial wage as of June 1999.[7] The rate will be raised to IR£4.70 in July 2001 and IR£5 in October 2002.

III. Report on the Discussions

15. **After a decade of remarkable success, Ireland finds itself at the cutting edge of the debate over the risks and policy challenges facing small cyclically-advanced economies in the euro area** (see Box 4). Overheating signs are more pronounced in Ireland than elsewhere in the euro area (Figure 11), consistent with staff estimates that the economy is operating well above potential.[8] These developments raise questions about the policy options available to contain excess demand pressures in the context of EMU. Related policy challenges involve alleviating the supply side constraints on future sustainable economic growth, and how to handle possible conflicts between demand- and supply-side objectives in the short-term. The discussions focussed on these issues.

A. Economic Outlook and Risks

16. **There was broad agreement that growth was unlikely to moderate significantly in the near term.** Macroeconomic policies remain highly stimulatory, and rapid gains in real incomes and household wealth continue to drive domestic demand. The staff projects that real GNP will increase by close to 8 percent in 2000,[9] reflecting further strong expansion in private consumption and investment spending. External demand may strengthen further given the recovery in the European Union and the ongoing pick-up in global demand. However, limits on available capacity are expected to constrain Ireland's ability to meet this demand in the short run, and a further moderate deterioration in the current account balance is projected.

17. **The authorities and the mission also agreed that sustainable output growth in coming years would be well below its recent rapid pace.** The natural rate of increase in the

[7] By way of comparison, the national minimum wage in the United Kingdom, which was introduced in April 1999, is equivalent to 37 percent of the average industrial wage.

[8] Staff estimates suggest that output exceeded potential by more than 4 percent in 1999. However, given the rapid structural changes over the past decade, and Ireland's relatively elastic labor supply, these estimates are subject to considerable uncertainty. For a discussion of the methodology used by the staff, see Potential Output Growth in Ireland, which appeared as a background study to the 1999 consultation report for Ireland.

[9] Real GDP growth would be almost 9 percent, above the June consensus of 8 percent.

Box 4: Responding to Overheating under EMU

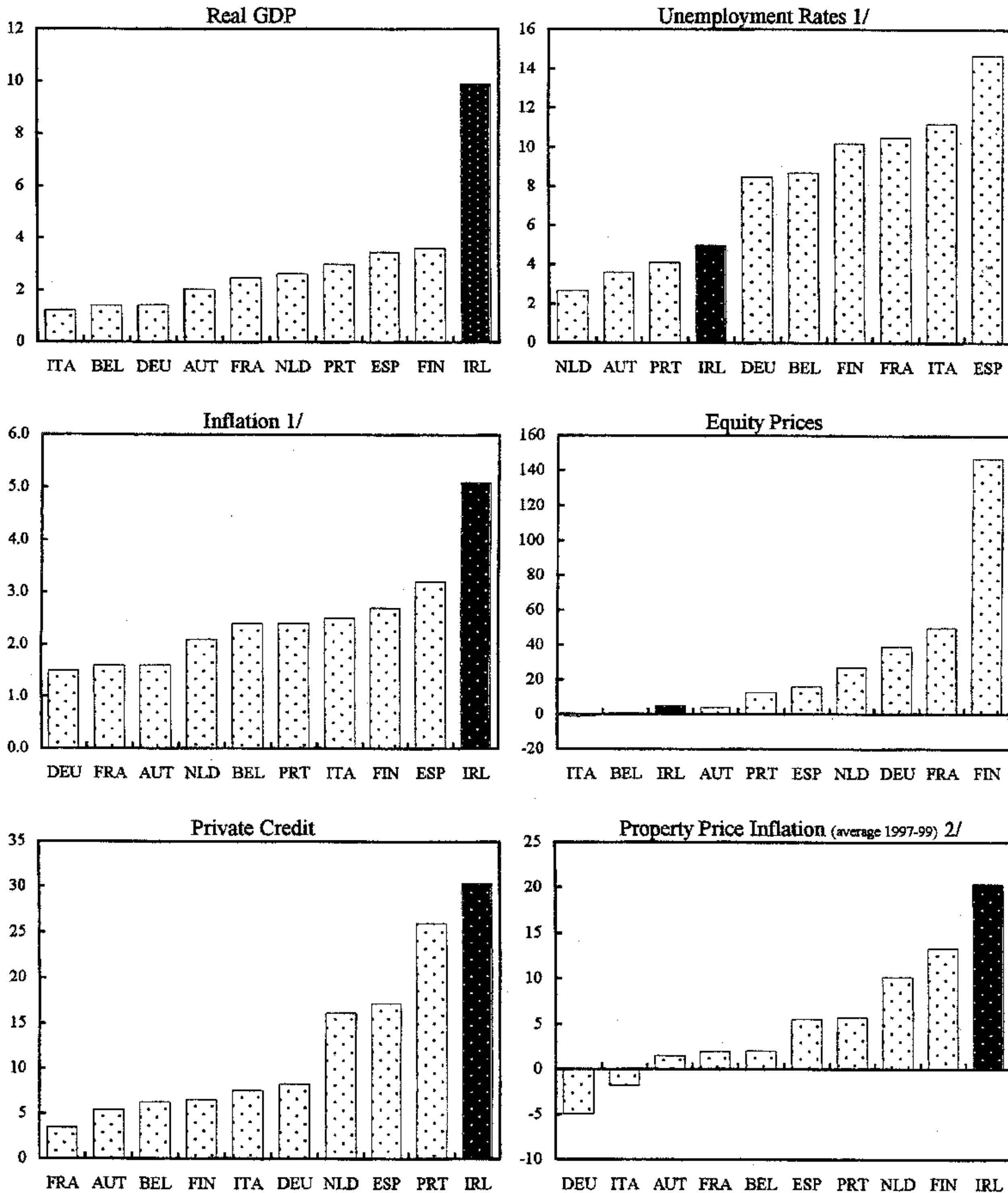
In recent years, a number of the smaller euro-area economies—Finland, Ireland, the Netherlands, Portugal and Spain—have experienced buoyant output growth, sharp falls in unemployment and, in some cases, rapid increases in consumer and asset prices and in bank credit. These developments have raised concerns about possible overheating. A forthcoming cross-country staff study considers the risks posed by overheating in the context of EMU and the policy options to address those risks.

In principle, **overheating within a monetary union need not be resolved in dramatic fashion.** Excess demand is likely to generate wage and price inflation that, with a fixed nominal exchange rate, will lead to real exchange rate appreciation, loss of competitiveness, and—within the economy—a shift in production from tradables to nontradables. The associated costs may be relatively low, especially if adjustment were gradual. On the other hand, if asset prices rise to unsustainable levels, a subsequent collapse might provoke significant problems for the banking sector that could feed back into declines in output. The direct impact of the asset price decline on consumption and investment also could be large if, as in Ireland, real estate accounts for a large share of household assets. Also, structural rigidities in labor markets could generate long wage cycles, in which real wages continue to rise even after labor market tightness begins to ease, resulting in deeper and longer-lasting unemployment than otherwise would be the case. Finally, with monetary policy set for the euro-area as a whole, there is a risk that monetary conditions could be tightened in response to area-wide demand pressures just as demand begins to wane in the more cyclically advanced economies, tending to exacerbate the cyclical downturn.

In the absence of monetary policy, **adoption of a contractionary fiscal policy** is an obvious choice to address excess demand. Certainly, there is no case for a pro-cyclical fiscal stance, and a compelling case exists for taking advantage of strong cyclical conditions to make rapid progress on medium-term structural fiscal goals. The more difficult issue is the extent to which a discretionary fiscal contraction is appropriate and politically feasible, particularly where the medium-term fiscal position is already sound. Two factors militate against such a policy. First, there are difficulties in judging the extent to which higher inflation represents a "problem" as opposed to part of a normal adjustment process that should not be resisted through fiscal or other means. Second, as a group the cyclically-advanced countries tend to be relatively small and open, implying a smaller fiscal multiplier and therefore a need for larger fiscal tightening. Nevertheless, depending on the particular situation, the time may come when demand pressures and economic dangers are sufficiently clear that the costs of an appreciable discretionary fiscal contraction are worth bearing. These considerations are applied in the main text to the case of Ireland. It is concluded that the dangers have indeed reached the point where discretionary fiscal tightening is warranted, notwithstanding the fact that the budget is already in surplus and that fiscal policy is constrained by the use of tax trade-offs to promote wage moderation.

Structural policies also have a role to play, albeit not in a strictly counter-cyclical sense, but rather as a means of preventing rapid demand, credit and asset price increases from generating long wage cycles and destructive banking sector events. Given the lags between when structural policies are introduced and when they have an impact, the case for early action on the structural front is clear. This has particular relevance for Ireland, given the role that increased competition can play in moderating rapid services price inflation, and given the dramatic boom in property prices. There are also questions about the rigidities implicit in the Irish wage formation process, particularly as it relates to public sector wages.

Figure 11. Ireland: Comparisons of Key Indicators with Other Euro Area Countries, 1999
(Growth rates, in percent, unless otherwise indicated)



Source: WEO and staff estimates.

1/ Panels for inflation and unemployment rates show 12-month inflation through May 2000 and the level of unemployment in January 2000, respectively.

2/ For Austria, Belgium, France, Germany, and Italy averages are for 1997-98.

labor force is expected to slow, and room to lower unemployment further is uncertain. Scope exists to increase participation rates, particularly among females, though prospective additions from this source may be increasingly difficult to secure as overall female participation has now reached the EU average. (However, it remains significantly below average for the 35-64 age group.) Inward migration also remains a potential source of labor force growth, but limited availability of affordable housing and other infrastructure bottlenecks may discourage such flows. On balance, the staff expects real GDP growth to moderate gradually over the medium term to 4 ½ - 5 percent (see Annex 2), still well above the EU average reflecting Ireland's favorable demographic profile and high productivity growth.

18. **A key uncertainty was the outlook for inflation.** With the economy already above potential, and widespread signs of continued strong demand, the mission saw a risk that inflationary pressures would be greater than had been envisaged in the official and most private sector forecasts. The persistent weakness in the euro during the first five months of 2000 had accentuated these risks. Nonetheless, all agreed that the acceleration in headline inflation had been exaggerated by temporary factors, and the authorities also noted that traded goods price inflation had been remarkably subdued given the weakness in the euro. The staff's baseline forecast has headline inflation peaking at about 5 ½ percent in coming months and declining in late 2000 as the effects of higher fuel prices and the tobacco tax rate hike fade. Services and non-traded goods price inflation may increase further, given the staff's estimate of a positive output gap. However, the forecast assumes that higher headline inflation does not spill over into a wage-price spiral, and that traded goods price inflation does not accelerate significantly.

19. **There was a shared concern that sustained high inflation would pose a risk to Ireland's otherwise very favorable economic outlook.** Somewhat higher inflation in Ireland than in the euro area as a whole was to be expected given productivity differentials.[10] In addition, Irish inflation may need to exceed the euro area average for a period as part of a broader price-level convergence, and given the assessment that the Irish pound entered the euro area at a relatively favorable rate. However, were the consensus underlying the national wage agreement to erode, increased industrial unrest could undermine the stability that has been key to Ireland's success in attracting foreign direct investment. Given the domestic resource strains, and with the euro remaining well below most estimates of its medium-term equilibrium level, there was also a risk that domestic wages and prices could overshoot sustainable levels, setting the stage for a painful economic adjustment later if the euro were to strengthen substantially. The domestic property boom added to these risks through its impact on wage pressures and domestic demand. The mission also stressed that the property boom

---

[10] As discussed in the 1999 Article IV report, staff estimates suggested that Ireland may be able to sustain CPI inflation about 1 percentage point above that in the euro area and average wage inflation of about 5 percent over the medium term without a loss of competitiveness.

could be a destabilizing influence in its own right, through a dynamic of unsustainable house price increases followed by a large decline.

20. **The mission also emphasized the risks posed by a negative external shock.** Ireland emerged largely unscathed from the Asian crisis but it would be more affected by a sharp slowdown in the United States, particularly one associated with a large correction in high tech stocks and an abrupt rise of the euro against the dollar and sterling. Investment and trade linkages with the buoyant U. S. economy have contributed importantly to recent growth, and linkages with the United Kingdom—though diminished over the years—remain strong. A particularly worrisome scenario would be if the weak euro and buoyant domestic and external demand conditions were to persist for a while longer, allowing overheating pressures to intensify and increasing the economy's vulnerability to a subsequent shock. Annex 2 illustrates such a scenario using a small country module of MULTIMOD estimated for Ireland, and the assumptions of the alternative global economic scenario presented in the Winter 2000 WEO. Such a scenario cannot capture the full range of possible spillover effects, including potential interactions with the domestic risk factors noted above, but it nonetheless suggests that Ireland could suffer a steep slowdown in the event of such a shock.

B. Macroeconomic Policies

21. **There was agreement that monetary conditions were excessively easy for Ireland's cyclical position.** While interest rate convergence as a result of euro area participation was anticipated, the subsequent decline in the euro and sustained strength of sterling had further increased Ireland's competitiveness. In addition, the fall in mortgage rates was reinforced by the entry into the market of the Bank of Scotland in August 1999. Officials noted that real interest rates were very low, particularly viewed against the high rates of economic growth and property price inflation. Recent interest rate hikes by the ECB went in the right direction from a domestic perspective, but all agreed that interest rates were unlikely in the foreseeable future to reach appropriate levels for current demand pressures in Ireland.

22. **The authorities noted that fiscal policy had sought to strike a balance between the goals of implementing tax and spending measures to improve supply side responses and contribute to the social consensus, while not adding excessively to domestic demand.** Thus far, the government had been able to achieve a substantial strengthening of the public finances, while pursuing tax reductions aimed at preserving competitiveness, improving work incentives, and reducing the tax burden. In coming years, fiscal policy would be governed to a significant degree by the tax and spending commitments under the PPF and the NDP. Taking account of the stronger-than-expected fiscal outcome for 1999, the authorities

felt that these commitments could be accommodated within the budgetary surpluses envisaged in the Stability Program (Table 3).[11]

23. **While broadly supporting these objectives, the mission considered that a tighter fiscal stance was needed in view of the overheating risks and easy monetary conditions.** The 2000 budget implied a decline in the structural primary surplus of ¾ of 1 percent of GDP, and there would be a similar decline on the same basis in 2001 if the actual surplus is in line with the 2.8 percent of GDP envisaged in the Stability Program. Thus, staff estimates suggested a fiscal loosening over the two years combined of about 1½ percent of GDP, which was inappropriate given cyclical considerations. The mission acknowledged the already-sizable fiscal surplus and that the fiscal multipliers were probably relatively small, [12] suggesting that it would not be feasible or desirable to attempt to eliminate overheating pressures using fiscal policy alone. However, the mission argued that explicit adoption of a tighter fiscal stance in 2001 would be important to signal the authorities' commitment to address overheating risks, to help lean against the current excess demand pressures, and to provide more room for future fiscal easing in the event of a slowdown.

24. **Concretely, the mission stressed the importance of avoiding budget overruns in 2000, and using any dividend from stronger-than-expected tax receipts to further reduce the public debt. For 2001, there should be an increase—perhaps of the order of 1 percent of GDP—in the actual fiscal surplus from 3.7 percent of GDP in 2000 to about 4 ½ percent of GDP in 2001.** This would ensure a similar improvement in the structural primary balance and would imply a significantly tighter stance than envisaged in the Stability Program. Staff estimates suggest that such an increase would allow for real non-interest current spending growth of about 5 percent, assuming no further decline in the revenue ratio in 2001. The authorities indicated that they fully intended to preserve any fiscal over-performance in 2000, but that the appropriate stance for 2001 would need to be kept under review in light of ongoing developments. The mission strongly supported the government's plans under the NDP to increase public investment in areas critical to relieving infrastructure bottlenecks. However, consistent with these objectives, the mission felt there should be scope to tailor current and capital spending increases to focus on priority areas and avoid adding to near-term resource pressures (see Annex 1).

---

[11] The Stability Program for 2000–02 was finalized before the fiscal outcome for 1999 was known and before negotiations on the PPF had been concluded. The Program envisaged general government surpluses of about 3 percent of GDP (before pension pre-funding and associated one-off costs), and included a contingency for the effects of the PPF.

[12] Available estimates put the short-term fiscal multiplier in the range of 0.6–1.0. These estimates should be treated with considerable caution, however, given the dramatic improvement in the public finances over the past decade and the advent of the European currency union.

25. **The authorities remained committed to reducing the tax burden and improving work incentives.** Over the last three budgets, the government had removed more than 16 percent of taxpayers from the tax net, lowered tax rates, and largely completed a shift to a full tax credit system through standard rating of personal tax allowances. The move toward individualization was a further important step, upon completion of which only 17 percent of taxpayers would be subject to the top tax rate. While supporting these initiatives, the mission noted that the overall tax burden in Ireland was already relatively low, suggesting that tax reductions may be less of a priority at present than in some other countries (Figure 12). This did not mean that further efforts should not be made to improve incentive structures by reducing high marginal tax rates, but it did suggest that consideration be given to revenue-neutral changes, for example, by combining income tax cuts with other reforms such as the introduction of a property tax (see below).

26. **The mission also cautioned against granting large income tax cuts at a time when disposable incomes were already rising strongly.** This suggested that it would have been better not to have front-loaded the tax cuts under the PPF (staff estimates put the total cost of the personal income tax cuts agreed under the PPF at about 2 ¼ percent of GDP, of which more than half was granted in the 2000 budget). The mission agreed that the remaining tax commitments under the PPF should be respected so as not to jeopardize the wage agreement. However, pressures to provide larger tax reductions should be resisted as this would tend to add to inflationary pressures. These considerations highlighted the current tension between the policy of trading off tax cuts for wage moderation on the one hand, and the need to reduce excess demand pressures through a tighter fiscal stance on the other.

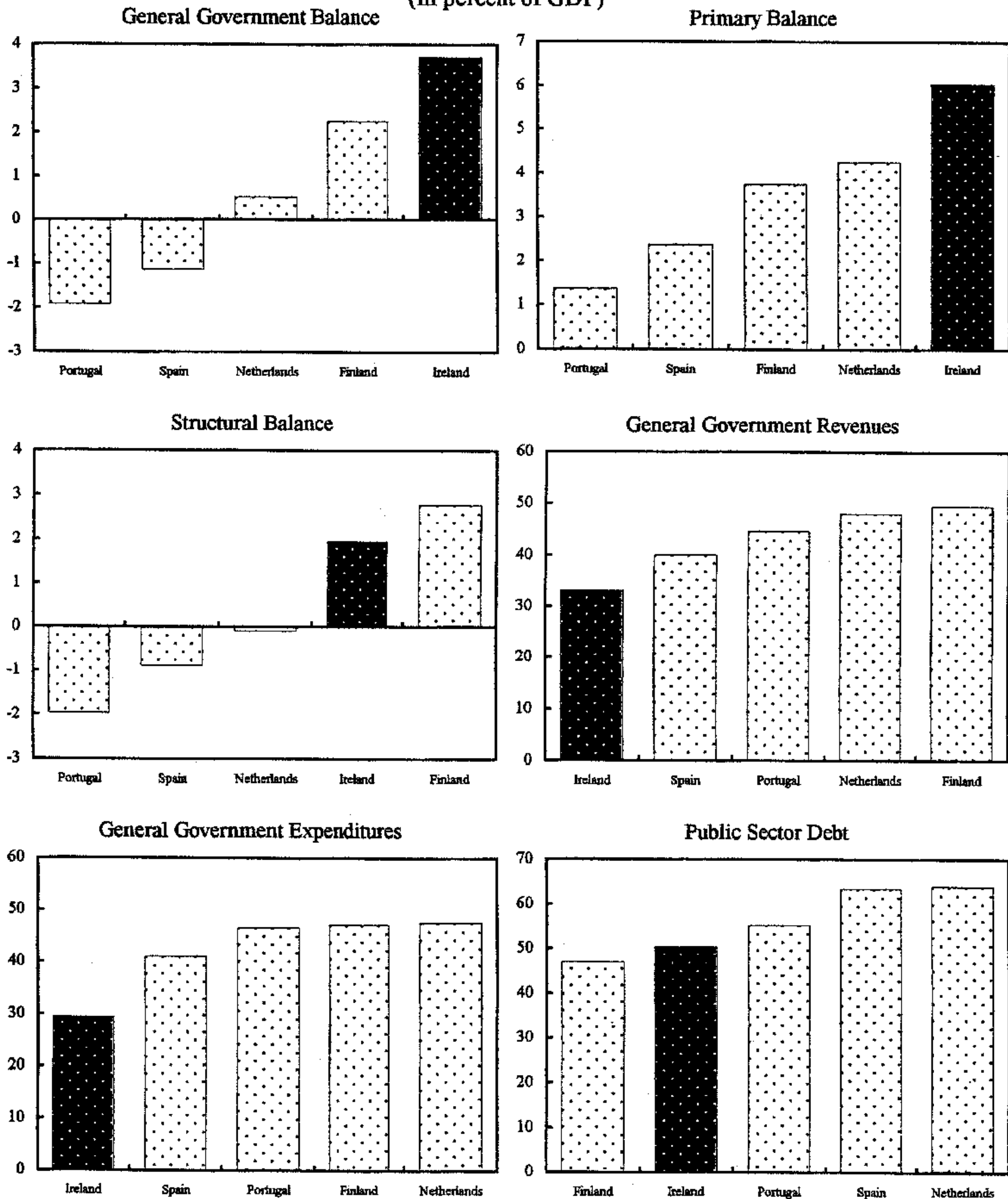
27. **In the view of the authorities, the Stability Program together with the PPF and NDP provided adequate guidance as to the orientation of fiscal policy in coming years.** Accordingly, the government had decided not to proceed with its previous plan to introduce a multi-annual budgetary framework through publication of agreed financial envelopes on departmental spending. They also had relaxed somewhat the 4 percent ceiling on average net current spending growth over the life of the current administration.[13] The mission expressed concern that these developments left fiscal policy without a clear medium-term orientation that could help ensure maintenance of fiscal discipline and guide private sector expectations.

28. **The mission strongly supported the new National Pensions Reserve Fund, draft legislation for which was presented on June 14.** This legislation establishes the framework under which the government will automatically set aside at least 1 percent of GNP a year to

---

[13] The ceiling already did not imply a particularly tight constraint as it included interest outlays—which have been declining rapidly—and net social security outlays, which are currently negative. On a general government basis, annual growth in non-interest current spending averaged 9 percent during 1997-99.

Figure 12. Ireland: Comparison of Fiscal Indicators with other Cyclically Advanced Euro Area Economies, 1999
(In percent of GDP)



Source: WEO.

partially pre-fund future social welfare and public service pension liabilities.[14] The funds are to be managed independently with a strict commercial mandate, and with no drawings until 2025.

C. Incomes Policies

29. **The multi-year centralized wage agreements are the cornerstone of the authorities' strategy for promoting wage moderation and economic stability.** The authorities felt that the PPF provided wage increases that were broadly appropriate, and within the range that the economy could afford given the growth outlook. The authorities and the mission agreed that demands for higher wage settlements than envisaged under the PPF could not be accepted as this would undermine the overall agreement.[15] While the authorities remained optimistic that inflation would peak in coming months, the pick up in inflation had provoked union demands for immediate cuts in consumption taxes to curb headline inflation. The mission noted that such measures would provide at best temporary relief on inflation, and would add to rather than ease demand pressures.[16]

30. **The authorities noted that the PPF incorporates significant improvements over previous multi-year agreements as regards the public sector.** First, it removes scope for local bargaining, which in the past had allowed individual unions to secure wage increases above the agreed norms, prompting demands by other groups to re-open negotiations.[17] Second, it provides for the establishment of a Benchmarking Body to review remuneration across the public sector. This initiative followed a November 1999 Review of Public Sector Pay Determination that recommended elimination of fixed relativities, and greater decentralization of pay management. A report is expected by end-2002, with any recommended wage increases to be considered in the next agreement. Third, the PPF links the last phase of the wage increase to specific performance targets under the public sector modernization program.

---

[14] As discussed in a background paper for the 1999 Article IV consultation, demographic pressures are a less immediate concern in Ireland than in most other industrial countries given the relatively young population. The old age dependency ratio is expected to remain below 25 percent until 2016, but would then rise sharply to over 50 percent by mid-century.

[15] One major teachers union did not sign the PPF and has threatened industrial action in support of its claim for a 30 percent pay increase.

[16] On June 28, 2000, the government announced an anti-inflation package, including a temporary freeze on increases in public sector charges, temporary controls on liquor prices, and the establishment of a commission to consider further liberalization of liquor licenses.

[17] The PPF includes an additional 3 percent wage increase to settle claims from previous agreements.

31. **The mission noted that the present environment of labor market tightness and rising inflation would test the capacity of the centralized agreements to deliver wage moderation**. Increased wage pressures were inevitable to some extent. The question was whether existing mechanisms could absorb these pressures in a manner that did not lead either to a disruptive breakdown of the PPF, or to pro-cyclical tax and spending concessions. Excessive public sector wage increases could also add to pressures on private sector wages, with adverse consequences for inflation and competitiveness. There was broad agreement that the fixed public sector wage relativities implicit in the current system were not appropriate for a dynamic rapidly growing economy such as Ireland. The mission, therefore, urged the authorities to use the period of the PPF to put in place mechanisms to allow greater flexibility in public sector wage determination and eliminate reliance on tax trade-offs. The authorities agreed that fresh tax relief on the scale of that granted under the PPF would not be possible into the medium term.

D. Structural Policies

32. **With the tightening labor market, policy emphasis had shifted from job creation to upgrading skills and securing additional labor supply.** The government was actively engaged with targeted unemployed groups to support their reentry into the workforce, and had proposed the introduction of a skills-based immigration policy focussed initially on the information and technology, health care and construction sectors. On the training front, the 2000 budget announced the creation of a National Training Fund, to be financed by a levy on employers' social insurance contributions. Also, a Lifelong Learning Task Force will develop specific initiatives aimed at upgrading skills of low-paid workers and those facing the challenge of rapid technological change. In addition, the focus of foreign direct investment policy had shifted away from labor-intensive businesses and toward attracting higher-quality jobs and promoting better regional distribution.

33. **The continued rapid growth in house prices was a shared concern.** The NDP included substantial investment in social housing, roads and water services, and legislation was expected to be enacted in 2000 to streamline planning procedures. These measures would have a sizable impact over time, but in the short run there was no easy way to achieve better balance in the housing market. The mission stressed the dangers that an unsustainable property boom posed for macroeconomic stability and the financial sector. Given these dangers and the lags with which most feasible measures operate, the mission called for early consideration of the full range of measures affecting property incentives. In the mission's view, it was unfortunate that two otherwise desirable measures—a well-designed property tax, and water and sewerage charges—did not appear to be on the agenda. The authorities

have since announced additional measures, based on the recommendations of an external consultant, aimed at improving housing supply and discouraging speculative demand.[18]

34. **Progress toward deregulation and greater competition had been accelerated.** Public support for these measures reflected recognition of their potential benefits in reducing the cost and improving the quality of services, and reduced resistance to change given the buoyant job market. Electricity had been partly opened to competition and an independent regulator appointed, while liberalization of public transport was under active consideration. There had also been some limited moves to introduce greater competition in the Dublin taxi market and liquor licenses. The mission stressed the role that greater progress in these areas could play in counteracting upward pressure on services price inflation.

35. **The authorities expressed support for further trade liberalization in a multilateral context.** They also strongly supported efforts to increase market access for the least developed countries.

E. Financial Sector Issues

36. **In conjunction with the Article IV discussions, Ireland participated in the Financial Sector Assessment Program (FSAP).**[19] The FSAP found that the Irish financial system was sound, and that Ireland maintains a high degree of adherence to international standards and codes. Ireland's financial sector regulation and supervision had served it well in allowing the financial sector to grow while preserving stability, including during times of international financial turmoil. However, several current developments add to the challenges facing the supervisory and regulatory authorities in maintaining financial sector stability. These developments included the sustained rapid growth in private sector credit, associated in part with the property price boom, which could strain banks' internal risk control systems and lead to a decline in credit quality. The property boom posed particular risks for smaller institutions with less diversified portfolios. In addition, competitive pressures from abroad had increased, with a measurable impact on bank profitability, and ongoing financial sector restructuring had increased cross-ownership linkages among banks and other financial institutions. To address these challenges, it would be important that the central bank continue to pay close attention to

---

[18] The supply-side measures include fast-track planning and infrastructure provision for designated large-scale residential sites and a tax on landowners who delay development on these sites. Demand-side measures include an annual 2 percent tax on certain second-home and investment properties, with a flat 9 percent tax on the purchase of investment properties. However, the measures also include lower stamp duty rates for first-home buyers, which will tend to add to demand.

[19] The findings of the FSAP are provided in the forthcoming FSSA report, which is summarized in Box 5.

Box 5. Financial Sector Stability Assessment: Main Conclusions

Ireland volunteered to participate in the pilot Joint Bank-Fund Financial Sector Assessment Program (FSAP). A mission visited Dublin in February-March 2000 to assess financial sector vulnerabilities and observance and implementation of supervisory standards and best practices.[1] The mission prepared a FSAP report that formed the basis for the Financial Sector Stability Assessment (FSSA).

The FSAP found that Ireland has a sound and highly developed financial system that has been remarkably stable, including during periods of international financial turmoil. Banking sector capitalization and asset quality are high, and profitability levels generally exceed those for most European competitors. The overall framework of prudential regulation and supervision is well developed, and shows a high degree of observance of international standards and codes.

Nonetheless, current developments pose a considerable challenge for market participants and supervisors alike to maintain Ireland's record of financial stability. Some of these developments—financial sector innovation and increased competitive pressures—are not unique to Ireland; but the strong expansion of cross-border activities in the IFSC (Ireland is already the second largest hub in Europe for mutual funds.) and sustained rapid credit growth (related in part to the property market boom) add significantly to these challenges. Rapid credit growth has been fueled by sharply lower real interest rates and, as experience in other countries has shown, is likely to put stress on banks' internal risk control systems.

The FSAP found that the major banks have strong capital positions and are well diversified geographically and across sectors, making it unlikely that the relatively less resilient positions of smaller banks (which are domestically oriented and more dependent on mortgage lending) would have major systemic consequences. Also, the Central Bank of Ireland (CBI) has been active in alerting banks to the risks posed by rapid overall and property-related lending, and stress tests suggest a high degree of resilience to macroeconomic shocks and a fall in property prices. The FSAP concluded that the CBI's risk-based approach to supervision was fully appropriate but could be further strengthened by increasing the focus on systemic issues through, for example, a deepening of its analysis of macroprudential indicators. Also, the CBI should use its full arsenal of prudential requirements to ensure that smaller mortgage lenders are adequately capitalized and provisioned.

Cross-ownership linkages, particularly between banks and insurance companies, entail potential for contagion across sectors, which is especially relevant for Ireland given that supervision is still not unified. (Ireland has decided to unify supervisory entities, but the terms of its implementation are still pending.) Moreover, increasing cross-border insurance operations (including reinsurance) and the number of funds in the International Financial Services Center (IFSC) pose a challenge in maintaining the quality of insurance and funds supervision. The IFSC's impact on domestic economic and financial developments and the possible links between offshore and onshore activities will require continued effective prudential supervision. The FSAP recommended an urgent strengthening of insurance supervision, and stressed the role that formation of the new unified supervisory agency could play in facilitating such a strengthening and in reducing the risks of regulatory arbitrage and contagion, assuming adequate resources are made available. Ireland will continue to be affected by euro area arrangements in the fields of supervision and lender-of-last resort facilities, including measures to strengthen coordination of regulatory and supervisory practices, and arrangements for dealing promptly and effectively with any potential future problems in financial institutions.

The summary standards assessments contained in the FSSA will form the financial sector modules of the Report on Observance of Standards and Codes (ROSCs), which the authorities intend to publish following the conclusion of the Article IV consultation. Ireland complies with the Basel Core Principles on banking supervision, and broadly complies with all International Organization of Securities Commissions (IOSCO) principles that are relevant for a small market. The Irish RTGS adheres to all draft core principles for systemically important payment systems set out by the Basel Committee on Payment and Settlement Systems.

---

[1] The FSAP team was led by Mr. Baliño, and included Ms. Gulde, Ms. Kourelis, Mr. Morales, Ms. Mori-Whitehouse (Administrative Assistant) and Mr. Sastry (Research Officer), all from MAE; Ms. Koliadina (EU1); Mr. Abernethy (Chairman of the New Zealand Securities Commission); Mr. Gammaldi (Expert in Banking Supervision, Banca d'Italia); Mr. Lester (Expert in Insurance Supervision, World Bank); and Ms. O'Brien (Expert in Banking Supervision, OCC).

potential vulnerability areas, including those associated with the property sector, and use its full arsenal of prudential requirements to ensure that institutions are adequately capitalized and provisioned. The FSAP also recommended a strengthening of supervision over the insurance sector, which currently is the responsibility of the Department of Enterprise, Trade and Employment. In the latter connection, it would be highly desirable to move ahead with the plan to establish a unified supervisory agency.

37. **The authorities welcomed the FSAP, which they had found to be a very valuable process.** The central bank authorities were fully cognizant of the risks posed by current developments, and had been active in working with credit institutions to develop and refine stress tests that assessed the impact on their portfolios of a weakening in macroeconomic conditions. These tests suggested a high degree of resilience to macroeconomic shocks and to a fall in property prices. The authorities would continue to monitor the situation closely and would not hesitate to ask individual institutions to raise their solvency ratios if they felt this was warranted. General provisioning levels appropriately had been rising, but the authorities did not judge a mandated tightening of provisioning or capital requirements to be warranted by current risks. They noted that such measures could put Irish institutions at a competitive disadvantage. The authorities indicated that it was still planned to consolidate financial supervision into a single agency, but the decision on its location had not been taken.

IV. Staff Appraisal

38. **Ireland continues to achieve spectacular economic growth.** This performance partly reflects propitious policy decisions that have leveraged Ireland's natural advantages and attracted foreign investment into high growth sectors. This has sparked a virtuous circle of rapidly rising incomes and employment, and contributed to strong growth in private consumption and investment. Trade and investment links with the robust U.S. economy have also played a role.

39. **However, growth over the past 2–3 years has also been boosted by stimulatory macroeconomic policies.** Ireland's euro area participation conveys permanent economic benefits, but it has led, along with the depreciation of the euro, to an untimely easing of monetary conditions. During this period, fiscal policy was broadly neutral.

40. **Strains associated with the rapid growth have become more visible.** Labor shortages are widespread, putting upward pressure on wages. Underlying inflation has accelerated beyond a sustainable medium-term range based on productivity differentials, reflecting a sharp increase in non-traded goods and services prices. Physical capacity constraints are becoming increasingly acute, property prices continue to rise rapidly, and private sector credit is growing at a very high rate.

41. **There is little reason to expect demand growth to moderate significantly in the near term.** Private consumption has considerable momentum amid rising incomes, buoyant job growth, and the wealth effects of higher house prices. Real monetary conditions remain

highly accommodating, notwithstanding recent ECB rate hikes. The 2000 budget provided a sizable fiscal stimulus, and commitments under the PPF and the NDP have raised the public's expectations of further tax cuts and spending increases in coming years. Also, external demand continues to strengthen. On the supply side, however, pressing capacity constraints suggest that sustainable growth rates over the next few years will be significantly below the recent rapid pace.

42. **The growing imbalances between demand and supply represent the main risk to what is otherwise a very favorable medium-term outlook.** If inflation remains high, the consensus underlying the PPF is likely to be severely tested. Continued rapid house price inflation would heighten these pressures by further reducing home affordability for new entrants, and increasing wealth differentials across societal groups. Rapid property price inflation is a concern in its own right to the extent that demand is being driven by expectations of future price increases—a trend that could at some point be abruptly reversed. Overall external competitiveness remains relatively strong, reflecting the weakness in the euro, but rising wage and price pressures may set the stage for a difficult adjustment later if the euro were to appreciate substantially. Ireland's trading links with the United Kingdom and reliance on investment flows from the United States would make it particularly vulnerable to such a shock, especially one involving a serious U.S. slowdown.

43. **The government is appropriately giving high priority to alleviating supply side constraints.** These efforts promise a substantial pay-off over the medium term but will take time to have their effect, and in some cases may add to short-term demand pressures. For example, individualization of tax rates implies substantial tax relief for two income couples, while higher social service and infrastructure spending adds to short-term demand pressures and strains on labor resources. Inward migration may ease these strains but heightens pressures on the housing market.

44. **Given the overheating risks, fiscal policy should be tightened to restrain excess demand pressures.** For 2000, this suggests that budgeted spending limits should be strictly adhered to, and any excess tax receipts should be saved. For 2001, some increase in the fiscal surplus would be preferable, thereby ensuring an improvement in the structural primary balance. This would imply a significantly tighter stance than implied by the target in the Stability Program. Such a tightening should be achievable without undermining the government's commitment under the PPF to granting further moderate tax cuts, and to increase public investment in priority areas to relieve supply constraints.

45. **Strict adherence to the agreed wage increases under the PPF will be critical, and the government should firmly resist pressures for larger settlements by individual groups.** Beyond their immediate fiscal impact, any such slippages could put the overall framework at risk, raising the threat of a broad wage-price spiral and jeopardizing the stability that has been integral to Ireland's economic success. It will be important to use the period of the PPF to explore alternative mechanisms for public sector wage determination that avoid the rigidities inherent in the current process. The planned benchmarking exercise offers the

prospect of addressing entrenched relativities, but this should not come at the expense of overall public sector wage restraint. Reforms in the direction of more decentralized wage determination and eliminating reliance on tax trade-offs would be desirable.

46. **The government's plans to further simplify the tax structure are welcome.** Efforts in this area should focus on strengthening work incentives, particularly at the low end of the labor market. However, the pace and form of these measures, including the move to full individualization of personal income tax bands, should be tailored so as not to exacerbate demand pressures in the near-term. This suggests a greater focus on revenue neutral reforms. Further expansion of the new home carer's allowance does not seem desirable, as it would undermine the incentive effects of individualization.

47. **Further progress toward a multi-year budgeting framework would be highly desirable.** Such a framework becomes all the more important during a period of unusually buoyant growth to maintain fiscal discipline and preserve medium-term fiscal sustainability. It could also help guide private sector expectations by signaling the government's priorities as between debt reduction and tax and spending initiatives, and on how revenue windfalls will be handled. In the staff's view, the current framework, as encompassed in the Stability Program, the PPF and the NDP, does not provide sufficient clarity in this regard.

48. **Ireland's participation in the FSAP pilot project is welcome. The sustained rapid growth in private sector lending calls for extreme vigilance, and supervisors should use all the tools at their disposal to ensure that the financial system remains sound.** The growing complexity of the financial sector will pose increasing regulatory and supervisory challenges in coming years. Early resolution of the issue of a single supervisor would be desirable, and developments in this regard should not be allowed to disrupt the effectiveness of financial sector oversight.

49. **Recent moves to promote better balance in the property market are timely, as international experience suggests that the economic costs of allowing an unsustainable property boom to develop can be very large.** While the focus on alleviating supply-side constraints is appropriate, however, it is unclear whether the latest measures on the demand side go far enough in reducing expectations-driven demand.

50. **The rise in services price inflation highlights the importance of pushing ahead with efforts to foster greater competition.** Recent signs of more rapid progress are welcome, and every effort should be made to further accelerate the pace of deregulation and privatization.

51. **The authorities' support for trade liberalization on a multilateral basis under the WTO process is welcome.** The government should strive to raise official development assistance from the current 0.3 percent of GDP to the U.N. target of 0.7 percent.

52. **Ireland is making ongoing efforts to improve the coverage and timeliness of its macroeconomic data.** The new quarterly balance of payments series is a welcome advance. However, delays in publishing key indicators such as the national income accounts, wages and industrial production, and gaps in other areas still need to be addressed to permit more effective monitoring of economic developments.

53. It is proposed that the next Article IV consultation take place on the standard 12-month cycle.

Table 1. Ireland: Selected Economic Indicators

	1995	1996	1997	1998	1999 Prel.	2000 Proj.	2001 Proj.
(Percent change from preceding year, unless otherwise noted)							
National accounts (constant prices) 1/							
GNP	8.0	7.2	9.0	8.1	8.9	7.8	6.2
Net foreign balance 2/	1.6	-0.3	-0.2	-1.4	-1.0	-0.8	-1.6
GDP	9.5	7.7	10.7	8.9	9.9	8.7	6.9
Domestic demand	7.0	7.8	9.5	9.4	8.9	8.4	7.6
Private consumption	3.7	6.5	7.3	7.4	8.5	9.0	7.5
Public consumption	2.9	2.8	4.8	5.9	4.3	4.5	4.0
Gross fixed investment	13.5	16.2	17.4	16.8	15.0	12.5	11.0
Exports of goods and services	19.6	11.8	17.0	20.5	15.0	15.4	12.0
Imports of goods and services	16.1	12.0	16.1	23.2	15.6	16.0	13.3
Prices, wages and employment							
Consumer prices (annual average)	2.5	1.6	1.5	2.4	1.6	4.9	3.7
Consumer prices (end of period)	...	...	...	1.7	3.4	5.2 3/	...
Harmonized Index of Consumer Prices (annual average)	...	2.1	1.2	2.2	2.5	...	...
Average hourly earnings	2.2	2.8	2.9	5.3	6.0 4/	...	...
Output, manufacturing	20.1	8.2	16.6	16.7	6.8 4/	...	...
Unit wage costs (manufacturing)	-9.9	-1.4	-6.4	-8.2	-5.2 5/	...	...
Employment	5.0	3.7	3.8	6.2	6.3	...	...
Unemployment rate (in percent)	12.1	11.5	9.8	7.4	5.6	4.5	4.0
Money and credit (end-period)							
M3E 6/	11.6	15.7	19.1	18.1	...	...	...
Private sector credit 7/	16.9	16.7	29.6	22.6	33.5	28.6	...
Public finances (in percent of GDP)							
General Government Balance 8/	-2.6	-0.6	0.8	2.1	3.7	3.7	3.1
Primary balance 8/	1.7	3.4	4.4	5.5	6.1	5.7	4.9
Structural balance 8/	-1.5	0.2	0.3	1.1	2.0	1.6	0.9
Structural primary balance 8/	2.8	4.2	3.9	4.5	4.3	3.5	2.7
General government debt	83.6	74.1	65.3	55.6	50.3	42.1	36.2
External trade and balance of payments							
Merchandise export volume	21.4	11.5	17.6	22.0	15.0	15.4	12.0
Merchandise import volume	15.0	11.0	15.0	23.0	13.0	13.0	11.0
Terms of trade	-2.4	0.6	0.6	0.3	-2.4	...	...
Balance of goods and services (percent of GDP) 9/	10.9	11.0	12.2	11.8	12.8	12.9	12.2
Current account (percent of GDP) 9/	2.6	2.8	2.5	2.0	0.3	-0.6	-0.9
Official reserves (in billions of SDRs, end of period.)	5.9	5.8	4.9	6.8	3.9	...	...
Effective exchange rates (1995=100)							
Nominal	100.0	102.1	102.4	97.1	94.2	90.4 10/	...
Real (CPI based)	100.0	101.9	101.6	97.0	94.1	90.7 10/	...

Sources: The Irish authorities, International Financial Statistics, and staff estimates.

1/ Based on National Income and Expenditure, compiled in accordance with the new European System of National Accounts (ESA 95). Data for 1999 are staff estimates.

2/ Contribution of net exports and net factor incomes to GNP growth.

3/ Year-on-year change in May 2000.

4/ Estimates based on available data--first six months of 1999.

5/ Estimates based on available data—first three months of 1999.

6/ M3E was discontinued in December 1998. The methodology for calculation of Ireland's contribution to the euro area money supply was amended in January 2000.

7/ Headline change, which includes the effects of transactions between credit institutions and non-bank international financial companies. For 2000 it is the 12-month change in April.

8/ Estimated prior to allocations for financing of future pension liabilities and one-off expenditures.

9/ Owing to methodological changes, a break in series occurred between 1997 and 1998.

10/ Effective rates are the first quarter averages.

Table 2. Ireland: General Government Finances
(In percent of GDP)

	1995	1996	1997	1998	1999	2000 proj.
Current surplus	-0.1	1.2	2.5	3.9	5.9	6.0
Current revenue, of which	35.0	35.2	34.6	33.8	33.1	32.1
Tax revenue	28.4	28.6	28.4	27.9	27.2	26.5
Social security receipts	4.8	4.4	4.2	4.1	4.2	4.0
Miscellaneous	1.9	2.1	2.0	1.9	1.7	1.6
Current expenditure, of which	35.1	34.0	32.1	29.9	27.2	26.1
Interest payments	5.0	4.7	4.3	3.5	2.5	2.0
Goods and services	4.0	3.7	3.7	3.6	3.8	3.7
Compensation of employees	9.7	9.3	9.3	8.6	7.9	7.6
Transfers	15.8	15.5	14.0	13.5	12.4	12.2
Other	0.5	0.8	0.8	0.7	0.7	0.6
Current expenditure, excluding interest and transfers	14.3	13.8	13.8	12.9	12.3	11.9
Capital deficit	2.5	1.8	1.7	1.8	4.0	4.3
Gross capital formation	2.3	2.3	2.5	2.7	3.0	3.3
Net capital transfers 1/	0.2	-0.5	-0.8	-0.9	1.0	1.0
General government balance 2/	-2.6	-0.6	0.8	2.1	1.9	1.7
Prefunding and once off costs	...	...	...	...	1.8	2.0
General government balance adjusted for prefunding and once off costs	-2.6	-0.6	0.8	2.1	3.7	3.7
Net interest	-5.0	-4.7	-4.2	-3.5	-2.5	-2.0
Primary balance	2.4	4.1	5.0	5.6	4.4	3.7
Primary balance adjusted for prefunding and once off costs	2.4	4.1	5.0	5.6	6.2	5.7
Memorandum items:						
Cyclically adjusted (as a percent of potential GDP) 3/						
Revenue	35.1	35.3	34.5	33.7	33.0	32.1
Expenditure, of which	36.6	35.1	34.3	32.6	31.1	30.5
unemployment benefits	2.2	2.1	2.0	1.6	1.6	1.6
Government balance	-1.5	0.2	0.3	1.1	2.0	1.6
Primary balance	2.8	4.2	3.9	4.5	4.3	3.5

Sources: Department of Finance and staff estimates.

1/ Net capital transfers were affected by the repayment of government's pensions liabilities with respect to An Post and Telecom Eireann of 1.8 percent of GDP in 1999, and by the budgeted set-aside for future public service pension liabilities of 2.0 percent of GDP in 2000.

2/ Estimated prior to allocations for financing of future pensions liabilities and one-off expenditures.

3/ Estimates based on general government balance adjusted for prefunding and one-off costs.

Table 3. Ireland: Stability Program
(As a percent of GDP)

	1999	1999 1/ outcome	2000	2001	2002
Current surplus:	5.2	5.9	5.8	6.4	7.3
Current revenue	34.1	33.1	33.7	32.8	32.6
of which:					
Tax revenue	28.0	27.2	27.8	27.2	27.1
Social Security Receipts	4.2	4.2	4.2	4.0	4.0
Miscellaneous	1.9	1.7	1.7	1.6	1.5
Current expenditure	28.9	27.3	27.9	26.4	25.3
of which:					
Interest payments	2.8	2.5	2.5	2.0	1.7
Goods and services	13.0	11.7	12.7	12.2	11.8
Other transfers	13.1	13.1	12.7	12.2	11.8
Capital deficit	-2.0	-2.2	-2.5	-2.6	-2.7
Government investment	-3.4	-3.0	-3.8	-3.9	-3.7
Capital resources	1.4	0.8	1.3	1.3	1.0
Contingency	...	...	...	-0.9	-1.7
General government surplus after contingency	3.2	3.7	3.3	2.8	2.9
of which primary surplus	6.0	6.2	5.8	4.8	4.6
General government debt	52.0	50.3	46.0	40.0	36.0
Memorandum Items					
GDP	8.4	9.9	7.4	6.5	5.7
GNP	7.4	8.9	6.3	5.7	5.0
Current account 2/	0.4	0.7	-0.9	-1.6	-2.2
Consumer prices	1.6	1.6	3.0	2.3	2.0
Employment	4.8	6.3	3.3	2.4	2.0
Unemployment rate	5.5	5.6	4.8	4.6	4.5

Source: Department of Finance.

1/ Prior to allocations for financing of future pension liabilities and one-off expenditures (see Table 2).
2/ As a percent of GNP.

Table 4. Ireland: Indicators of External and Financial Vulnerability
(In percent of GDP, unless otherwise indicated)

	1995	1996	1997	1998	1999	2000	
						Latest estimate	Date
External Indicators							
Exports (annual percent change, in U.S. dollars)	23.5	10.9	18.9	24.8	13.6	...	
Imports (annual percent change, in U.S. dollars)	18.9	8.5	15.8	20.6	7.8	...	
Terms of trade (annual percent change)	-2.4	0.6	0.6	0.3	-2.4	...	
Current account balance 1/	2.6	2.8	2.5	2.0	0.3	...	
Capital and financial account balance, 1/	-2.3	-2.6	-7.3	2.5	0.8	...	
Of which:							
Inward portfolio investment	...	...	...	50.8	72.1	...	
Inward foreign direct investment	...	...	...	10.1	19.5	...	
Other investment liabilities (net)	...	...	...	9.9	-0.8	...	
Official reserves (in U.S. dollars, billions)	8.8	7.9	7.0	9.2	5.7	5.4	April
Broad money to reserves ratio 2/	5.5	7.0	9.1	7.7	17.0	17.9	April
Central bank foreign liabilities (in billions of U.S. dollars) 3/	...	...	...	...	1.5	1.4	April
Foreign assets of the financial sector (in billions of U.S. dollars)	47.3	68.0	109.0	137.9	177.4	180.8	April
Foreign liabilities of the financial sector (in billions of U.S. dollars)	54.5	73.3	113.8	148.0	187.3	193.7	April
Official reserves in months of imports	3.7	4.4	4.6	4.6	7.5	...	
Total external debt 4/	26.6	19.3	16.0	12.4	2.9	...	
Of which:							
External debt to exports ratio	39.4	28.4	22.7	16.2	5.1	...	
External interest payments to exports (in percent)	2.50	1.90	1.30	1.00	0.90	...	
Irish pound against U.S. dollar (period average)	1.60	1.60	1.52	1.43	1.35	1.25	Q1
Financial Market Indicators							
General government debt	83.6	74.1	65.3	55.6	50.3	...	
Government bond yield (10 years to maturity, end-period)	7.34	6.58	5.48	3.99	5.60	5.52	April
Government bond yield (real, 10 years to maturity)	4.84	4.98	3.98	1.59	4.00	0.62	April
Change in stock market index (percent, end of period) 2/	20.6	22.1	48.7	23.2	0.4	7.3	April
Spread of government bond yield with Germany	1.41	0.90	0.21	0.18	0.25	0.25	April
Financial Sector Risk Indicators							
Personal lending as a share of total loans (excluding financial intermediation)							
House mortgage finance	41.6	41.7	41.8	40.7	39.7	...	
Other housing finance	0.9	0.6	1.0	1.0	0.9	...	
Other personal lending	12.7	12.3	13.1	12.4	13.0	...	
Residential mortgage lending to total assets (in percent)	14.0	12.7	10.7	9.8	8.1	...	
Commercial property lending as a percent of total loans (excluding financial intermediation) 5/	6.4	6.7	7.1	8.8	9.7	...	
Off-balance sheet business (as a percent of total assets)							
Irish residents	...	...	...	81.7	55.3	...	
Non-residents	...	...	...	327.4	377.7	...	
Non-performing loans/loans to private sector (in percent) 6/	...	...	2.75	2.54	...	...	
Total capital/Risk-weighted assets (in percent)	14.61	13.6	13.00	14.01	...	...	

Sources: Data provided by the authorities, *International Financial Statistics*, and staff estimates.

1/ Owing to methodological changes, a break in the series occurred between 1997 and 1998.
2/ Break in the series; from 1999 onward data present Irish contribution to euro-area money supply.
3/ Liabilities to non-euro area residents in euro and a foreign currency.
4/ Represents a non-Irish pound debt in 1995-98, and a non-euro debt of the government sector in 1999.
5/ Includes lending for building, construction, hotels, catering and other property.
6/ Owing to differences in classification, international comparisons of non-performing loans are indicative only.

The National Development Plan, 2000-2006

A key element of the government's strategy to promote future sustainable growth is the National Development Plan (NDP), which was launched in late 1999 and envisages a major increase in public investment to address Ireland's development needs. The NDP emphasizes measures to relieve bottlenecks, improve competitiveness, foster balanced regional development, and promote social inclusion. Total spending over the period 2000-06 is estimated at IR£ 40.6 billion, or IR£ 5.3 billion per annum (about 9 percent of GNP in 1999 prices). Roughly three-quarters of the NDP is to be publicly financed. Private funding through Public Private Partnerships would contribute about 16 percent, while EU transfers would finance about 8 percent.

Distribution of Planned Investment by Category

Investment category	2000-06 In billions of Irish pounds	2000-06 In percent of total
Economic and social infrastructure	17.6	43.4
Employment and human resources	9.9	24.4
Productive sector	4.5	11.1
Regional Programs	5.1	12.5
CAP Rural Development Plan	3.4	8.4
Total	40.6	100.0

Sources: The National Development Plan and staff estimates.

The largest component of the NDP—*economic and social infrastructure*—aims to address Ireland's infrastructure deficit through an expansion of investment in social housing (34 percent of the total), roads (27 percent), water and waste treatment (14 percent), and public transport (13 percent). The *employment and human resources* component emphasizes entry-level education and training, and measures targeted at reintegrating the unemployed into the workforce. The *productive sector* component envisages a major expansion of spending on research and development, as well as a continuation of existing support schemes for indigenous industries and spending on attracting FDI inflows. The *regional programs* seek to address urban congestion and bottlenecks in developed areas, and to promote growth in less developed areas. The *Rural Development Plan* focuses on support for natural resource industries and development of rural infrastructure.

An initial evaluation of the NDP was carried out by the Community Support Framework (CSF) Evaluation Unit—an independent entity established by the Department of Finance and the European Commission. [1] This evaluation broadly endorsed the investment balance as appropriate for the needs of the economy, and offering the prospect of significantly enhancing the long-term potential of the economy. However, it also noted that:

[1] See "Ex Ante Evaluation of the National Development Plan, 2000-2006" CSF Evaluation Unit (November 1999).

- Achievement of the planned increase in investment on infrastructure would hinge on the government's ability to overcome constraints in the construction sector and in the planning process;

- the objectives of the Plan in education and training were not clearly formulated, and may not take sufficient account of the projected decline in the school-age population and the fall in unemployment;

- the planned spending on the productive sector did not seem fully warranted, given the improved economic climate. Also, deficiencies in the delivery, targeting and cost-effectiveness of many aid schemes needed to be addressed, particularly given the planned major increase in investment on R&D.

Ireland—Alternative Medium Term Scenarios

This annex describes a macroeconomic scenario generated by MULTIMOD that illustrates some of the possible implications for Ireland of a harder landing for the United States economy than was envisaged in the Winter 2000 WEO baseline forecast.

As discussed in the main text, the staff's baseline forecast is for growth to remain strong in 2000. This outlook reflects a continuation of the recent buoyancy in domestic demand and favorable external environment. The latter is consistent with the latest WEO projections for partner country growth and exchange rates, which imply a strengthening of global demand and further depreciation of Ireland's average nominal effective exchange rate in 2000. Inflation would average about 5 percent in 2000, reflecting both one-time factors and a rise in underlying inflation. The contribution from net exports would decline and the current account balance would move from a surplus to a deficit of about ½ percent of GDP.

Over the medium term, real GDP growth is expected to moderate gradually to 4½-5 percent as further progress in reducing the unemployment rate below current levels is more limited, and as the rate of labor force growth slows compared with recent years (see Table 1; top panel). Government efforts under the NDP to relieve capacity constraints could imply some upside potential to the staff's sustainable medium-term growth estimates. Inflation is expected to remain above the euro area average but would moderate gradually based on the WEO assumptions for traded goods prices and exchange rates. However, the nontraded component of inflation would remain significantly higher than the headline rate as a result of the positive output gap, which the staff assumes would close only gradually over the period. This would imply a weakening of external competitiveness from current levels. The current account deficit would reach about 1 ½ percent of GDP in 2002 before narrowing as domestic demand growth moderates.

An alternative scenario presented in the Winter WEO considered the implications of a stronger world upturn in 2000 followed by slower growth in 2001 centered on a sharp U.S. slowdown. While the WEO explored the possible implications of such a scenario for the euro area as a whole, Ireland may be affected differently because of its position in the business cycle and relatively large trade and financial linkages with the United States and the United Kingdom. To assess the potential implications for Ireland, a small open economy block of MULTIMOD was added, with behavioral parameters estimated from Irish data.

The simulation results are presented in the bottom panel of Table 1. In 2000, output growth and inflation in Ireland would be moderately higher than in the baseline. In 2001, however, growth would slow sharply reflecting weaker external demand, a large real exchange rate appreciation (it is assumed that the euro appreciates by roughly the same magnitude against both the U.S. dollar and sterling), and negative spillover effects on domestic demand. The latter effects are difficult to fully capture in the model but most likely would include adverse effects on confidence and activity of lower foreign direct investment inflows and a possible downturn in the Irish property market. Inflation would fall sharply in 2001, and the current account balance would move back into a fairly large surplus.

Beyond 2001, growth would rebound fairly quickly, though in **level terms** domestic demand and output would remain significantly below the baseline throughout the projection period (note that the deviations from the baseline are expressed in terms of levels unless indicated). This rebound partly reflects the external environment implicit in the WEO scenario, which includes an early reversal of the rise in the euro, an easing of the euro area monetary stance, and a fairly rapid recovery in global growth. To the extent that these assumptions prove to be overly optimistic—for example, if the euro were to remain strong in subsequent years, or if the ECB did not ease monetary policy in response to the initial shock—the adjustment for Ireland could be more problematic than this simulation suggests. It is also possible that the impact of the shock on household wealth and consumer and business confidence could be longer-lived than assumed in the alternative scenario.

Table 1: Baseline Projection

	2000	2001	2002	2003	2004
Real GDP	8.7	6.9	5.4	4.9	4.6
Real GNP	7.8	6.2	4.8	6.4	3.8
Domestic demand	8.4	7.6	7.1	6.4	6.0
Exports	15.4	12.0	9.0	8.0	7.5
Imports	16.0	13.3	11.0	9.6	9.0
Potential GDP	7.7	6.8	6.4	6.2	6.1
Output gap	5.4	5.6	4.6	3.4	2.0
CPI inflation	4.9	3.7	3.4	2.9	2.7
Short-term interest rate	4.3	5.1	5.1	5.2	5.2
Real effective exchange rate (cpi based)	-1.7	2.7	2.6	2.8	3.0
Nominal effective exchange rate	-4.1	0.9	0.6	0.6	0.6
Current account (% of GDP)	-0.6	-0.9	-1.5	-1.5	-1.0
Government debt (% of GDP)	42.1	36.2	31.4	28.0	24.8

Alternative Scenario

Percentage deviation from baseline unless specified otherwise

	2000	2001	2002	2003	2004
Real GDP	0.9	-5.2	-5.3	-3.9	-1.8
Real GNP	0.9	-5.3	-5.3	-3.7	-1.5
Domestic demand	1.5	-3.6	-5.7	-5.4	-4.3
Exports	3.7	-4.8	-4.0	-2.5	-1.0
Imports	4.8	-3.2	-4.2	-3.8	-3.2
Potential GDP	0.1	-0.2	-0.7	-1.1	-1.2
Output gap	0.8	-5.2	-4.8	-3.0	-0.6
CPI inflation	0.7	-2.2	-2.8	-2.5	-1.3
Short-term interest rate	0.8	-0.6	-1.1	-1.4	-1.5
Real effective exchange rate (cpi based)	0.1	11.0	6.3	1.9	-1.3
Nominal effective exchange rate	-0.3	13.1	10.5	7.8	5.4
Current account (% of GDP)	-0.4	4.3	3.9	2.9	2.2
Government debt (% of GDP)	-1.2	4.0	6.5	7.6	7.1

Ireland: Basic Data

Demographic and other data:

Area:	70.3 thousand square kilometers
Population (in million)	3.7
Natural rate of increase (percent change)	0.6 percent
Infant mortality	0.62 percent
Population per physician	633
GDP per capita (SDR)	19,831

Composition of GDP in 1999 at current prices	In millions of Irish pounds	Distribution in percent
Private consumption	34,562	49.7
Public consumption	8,783	12.6
Total investment (including stockbuilding)	17,339	24.9
Total domestic demand	60,684	87.2
Exports of goods and services	59,958	86.2
Imports of goods and services	51,083	73.4
GDP at market prices (expenditure estimate)	69,559	100.0

Selected economic data	1997	1998	1999
	(Annual percentage change)		
Output and unemployment:			
Real GDP (expenditure estimate)	10.7	8.9	9.9
Manufacturing production	16.6	16.7	...
Average unemployment (in percent)	9.8	7.4	5.6
Earnings and prices:			
Average earnings in manufacturing	2.9	5.3	6.0
Consumer price index	1.5	2.4	
Money and interest rates (end period)			
M3E	19.1	18.1	...
3-month Interbank rate	6.1	3.2	2.5
10-year government bond yield	5.5	4.0	4.6
Fiscal accounts:	(In millions of Irish pounds)		
General government receipts	17,914	20,154	23,046
General government expenditure	17,508	18,887	20,466
Balance of payments			
Current account balance	1,283	1,173	233
in percent of GDP	2.5	2.0	0.3
Trade balance	11,071	14,140	17,778
Exports	36,515	43,532	49,470
Imports	-25,444	-29,392	-31,692
Services, incomes and transfers (net)	-9,789	-12,967	-17,545
Capital and financial account	-3,767	1,466	539
Gross reserves			
(billions of SDR, end of period)	4.9	6.8	7.3

Sources: National Income and Expenditure; Balance of International Payments; and staff estimates.

Ireland: Fund Relations

(As of May 31, 2000)

I. **Membership Status**: Joined 8/08/57; Article VIII

II.	**General Resources Account:**	**SDR Million**	**% Quota**
	Quota	838.40	100.0
	Fund holdings of currency	576.14	68.7
	Reserve position in Fund	262.28	31.3
	Operational budget transfers (net)	-10.00	

III.	**SDR Department:**	**SDR Million**	**% Allocation**
	Net cumulative allocation	87.26	100.0
	Holdings	33.17	38.0

IV. **Outstanding Purchases and Loans:** None

V. **Financial Arrangements:** None

VI. **Projected Obligations to Fund :** None

VII. **Exchange Arrangement**

As of January 1, 1999, the euro became the currency of Ireland; the irrevocably fixed conversion rate between the euro and the Irish pound is 0.787564.

VIII. **Article IV Consultations**

The discussions for the last Article IV consultation were conducted in Dublin during May 7-17, 1999. The staff report (SM/99/176) was considered by the Executive Board on August 4, 1999 (SUR/99/95). Article IV consultations with Ireland are currently on the standard 12-month cycle.

IX. **Technical Assistance:** None

X. **Resident Representative:** None

Statistical Issues

Ireland is subject to the statistical requirements, timeliness, and reporting standards of Eurostat and the European System of Central Banks (ESCB). Ireland has cooperated with the IMF in providing monetary, international reserves, and other financial statistics related to its membership in the European Economic and Monetary Union (EMU). These data are considered reliable and well documented. The frequency and timeliness of the publication of the core statistical indicators are summarized in the attached table.

1. Ireland has subscribed to the Fund's Special Data Dissemination Standards (SDDS). The Irish authorities adopted the 1993 System of National Accounts (SNA) in 1999, and launched the publication of quarterly national accounts in September 1999. However, a reduction in the lags with which the data are currently published (nine months for the quarterly data and more than six months for the annual data) would allow more effective monitoring and analysis of economic developments. The authorities plan to gradually reduce these lags, which are related in part to the revisions to the industrial survey (see below).

2. The introduction of new methodology for the compilation of the balance of payments statistics has broadened the coverage of investment flows and financial services, and made the data fully consistent with the fifth edition of the Balance of Payments Manual. At present, there are no plans to bring the historical data into line with the new methodology, however, which may limit their usefulness for analytical purposes until a longer time series has been established using the new methodology.

3. Several key economic indicators are published with long delays or are not currently produced at all. For instance, earnings data are typically published with lags of 5 to 8 months, depending on the sector. More recently, there has been a longer lag in the case of manufacturing earnings data as the Central Statistics Office (CSO) temporarily discontinued publication of this and several other real sector indicators (e.g., industrial production and turnover) pending an extensive revision of the industrial survey. In early July 2000, the CSO recommenced publication of an updated industrial production index with a 1995 base year and the NACE Rev.1 classification of activities. The most recent labor cost survey covers the period through 1996 and the most recent household budget survey is for 1994/95. Data on household and corporate balance sheets are not currently compiled.

Ireland: Core Statistical Indicators
(As of mid-June, 2000)

	Exchange Rates	International Reserves	Central Bank Balance Sheet	Reserve/ Base Money	Broad Money	Interest Rates	Consumer Price Index	Exports/ Imports	Current Account Balance	Overall Govern-ment Balance	External (Non-euro denominatead) Debt/Debt Service	GDP/GNP
Date of Latest Observation	6/15/2000	April 2000	Apr. 2000	Apr. 2000	Apr. 2000	6/15/2000	May 2000	Feb. 2000	4th quarter 1999	May 2000	1999	3rd quarter 1999
Date Received	6/15/2000	June 2000	June 2000	June 2000	June 2000	6/15/2000	6/14/2000	May 2000	May 2000	June 2000	April 2000	May 2000
Frequency of Data	Daily	Monthly	Monthly	Monthly	Monthly	Daily	Monthly	Monthly	Quarterly	Monthly	Annual	Quarterly
Frequency of Reporting	Daily	Monthly	Monthly	Monthly	Monthly	Daily	Monthly	Monthly	Quarterly	Monthly	Annual	Quarterly
Source of Update	Commercial	Central Bank	Central Bank	Central Bank	Central Bank	Commercial	CSO	CSO	CSO	Dept. of Finance	Central Bank	CSO
Monthly Reporting	On Line	Internet	Internet	Internet	Internet	On Line	On Line/ Diskette/ Publication	On Line/ Diskette/ Publication	On Line/ Diskette/ Publication	On Line	Publication	Diskette Publication
Confidentiality	Public	Public	Public	Public	Public	Public	Public	Public	Public	Public	Public	Public
Frequency of Publication	Daily	Monthly	Monthly	Monthly	Monthly	Daily	Monthly	Monthly	Quarterly	Monthly	Quarterly	Quarterly

Statement by the IMF Staff Representative
August 2, 2000

The following information has become available since the staff report (SM/00/163) was issued. This information does not change the thrust of the staff appraisal.

1. Preliminary national income accounts data for 1999 indicate that real GNP expanded by 7.8 percent, the same increase as in 1998 and lower than the 8.9 percent estimate shown in the staff report (see attached table). The difference mainly reflects larger outflows of net factor incomes, as real GDP growth (9.8 percent) was broadly in line with the estimate in the staff report. Growth in private consumption and gross capital formation remained very buoyant, while the contribution of net exports was somewhat larger than expected, reflecting relatively sluggish growth in imports. However, there was an offsetting effect from a decline in inventories.

2. The Central Statistics Office has also released revised balance of payments data for 1998 and 1999. The changes included a downward revision in the estimated current account surplus for 1998 (from 2 percent of GDP to 0.9 percent) and an upward revision for 1999 (from 0.3 percent to 0.6 percent). The current account remained in a modest surplus in the first quarter of 2000 amid strong growth in both exports and imports (up 22 and 17 percent, respectively, in volume terms on a 12-month basis).

3. Harmonized consumer price inflation accelerated further to 5.4 percent (12 month basis) in June, up from 5.1 percent in May. On a national basis, the headline inflation rate (including mortgage interest costs) reached 5.5 percent. Services price inflation was 6 percent, and underlying services price inflation (based on the methodology used by the Central Bank of Ireland) was 7.5 percent. In a recent speech, the Minister of Finance said that he expects inflation to rise further in coming months before falling back somewhat in December, and that revised official forecasts to be released next month are likely to show average inflation for 2000 within the 4 ¾ - 5 ¼ percent range projected by most market analysts.

4. According to the Irish Permanent Index, national house price inflation averaged 20.1 percent in the first half of 2000 (12-month basis), down from 26.8 percent for the same period in 1999 but above the 18.9 percent average recorded in the second half of 1999. Over the 12 months to June, national house prices increased by 21.4 percent. Official data for the first quarter show more moderate rates of increase (12.9 percent for new houses and 13.7 percent for existing houses on a 12-month basis).[1]

[1] The official data measure average house prices based on mortgage loan approvals, whereas the Irish Permanent Index is a standardized measure that takes into account changes in the composition of house sales.

- over -

Ireland: National Accounts

	1995	1996	1997	1998	1999	
					Staff estimates SM/00/163	Preliminary outcome
	(Real growth rates in percent)					
Consumption	4.0	5.7	7.1	7.3	7.7	7.2
Private	4.3	6.3	7.4	7.8	8.5	7.7
Public	2.8	3.1	5.7	5.1	4.3	5.2
Investment	22.0	16.1	19.8	16.0	12.3	3.7
Gross domestic fixed capital formation	12.7	16.4	17.9	15.5	15.0	13.0
Stockbuilding 1/	1.3	1.3	1.8	2.0	1.3	-0.3
Total domestic demand	7.2	7.8	9.8	9.4	8.9	6.3
Exports of goods and nonfactor services	20.0	12.2	17.4	21.4	15.0	12.4
Imports of goods and nonfactor services	16.4	12.5	16.8	25.8	15.6	8.7
Net exports 1/	4.3	1.4	2.9	-0.4	1.5	5.2
Gross domestic product	9.7	7.7	10.7	8.6	9.9	9.8
Net factor income from abroad	-2.4	-1.2	-2.5	-1.7	-2.2	-3.0
Gross national product	8.2	7.4	9.3	7.8	8.9	7.8

Sources: Central Statistics Office, *National Income and Expenditure: First Results for 1999*.

1/ Contribution to GNP growth.

2/ Contribution to GDP growth.

INTERNATIONAL MONETARY FUND

Public Information Notice

EXTERNAL RELATIONS DEPARTMENT

Public Information Notice (PIN) No. 00/61
FOR IMMEDIATE RELEASE
August 10, 2000

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

IMF Concludes Article IV Consultation with Ireland

On August 2, 2000, the Executive Board concluded the Article IV consultation with Ireland.[1]

Background

Over the past six years, Ireland's economic performance has been spectacular. Real GNP has expanded at an average rate of 8 percent, raising per capita GNP to about 90 percent of the EU average. This strong growth has been accompanied by rapid increases in employment, with the unemployment rate falling to historic lows. The public finances strengthened markedly, as the general government balance moved from deficit into sizable surplus, and the public debt ratio was cut in half. The external current account balance also remained in surplus. More recently, however, strains associated with this rapid growth have become more pronounced. Inflation has accelerated sharply, labor shortages are widespread, and property prices have been rising rapidly for four consecutive years.

Economic activity remained very buoyant in 1999, with real GNP rising by almost 8 percent. Growth was driven mainly by domestic demand, as private consumption was boosted by strong gains in disposable incomes and wealth, and investment remained extremely buoyant. However, external demand also strengthened during the year, reflecting the global economic recovery. Inflation remained subdued until mid-1999 but has since risen to over 5 percent, by far the highest rate in the euro area. This increase reflects both temporary factors associated with higher fuel prices and a tax increase on tobacco, as well as a rise in underlying inflation, particularly for services. Wage pressures have also intensified as the unemployment rate dropped to 4.7 percent in the first quarter of 2000. However, at least until very recently, the adverse effects of higher wage and price inflation on competitiveness have been outweighed by

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. In this PIN, the main features of the Board's discussion are described.

Ireland's relatively strong productivity growth in the tradable goods sectors and the weakness of the euro. Monetary conditions are clearly expansionary from Ireland's point of view, contributing to robust demand growth as well as rapid increases in house prices and private sector credit. Buoyant tax revenues have enabled the government to implement sizable tax cuts and increases in real spending over the past three years, while still achieving an increase in the overall general government surplus.

Near-term prospects are for continued buoyant growth. Real GNP is projected to rise by almost 8 percent in 2000, before moderating to about 6 percent in 2001. Consumer spending growth is likely to remain strong while investment will be boosted by increased government outlays under the National Development Plan. External demand is expected to remain robust, fuelled by the ongoing pick-up in activity in European trading partners. However, limits on available capacity are likely to exert an increasing constraint on Ireland's ability to meet this demand in the short-run, and the current account balance is projected to weaken moderately in 2000. With the economy already operating above estimated potential, the strength of domestic demand is being reflected in upward pressures on domestic prices, most notably in sectors that are not fully exposed to competition. Headline inflation is projected to peak during the second half of 2000 and decline late in the year as the effects of higher fuel prices and the tobacco tax rate hike begin to fade. However, services and non-traded goods price inflation may remain high or increase further. Macroeconomic policies are generally set to be supportive of demand in 2000. While nominal interest rates have increased since late 1999, real rates remain very low in Ireland given its higher inflation rate. Also, the 2000 budget contained further sizable tax cuts and spending increases, implying a net addition to demand. The latest national wage agreement envisages sizable increases in disposable incomes over the next three years that are likely to add to demand growth going forward.

Executive Board Assessment

Executive Directors commended the authorities for the performance of Ireland's economy over the past decade. Output and employment growth have been remarkably buoyant, the public finances have strengthened considerably, and the external current account balance has remained in surplus. While many factors accounted for this performance, Directors stressed the roles played by sound and consistent macroeconomic policies, a generally flexible labor market, a favorable tax regime, and the long-standing outward orientation of Ireland's trade and industrial policies. Directors considered that the economy should be well placed to continue to perform strongly in the future, taking account of its well-established positions in several high-growth sectors.

Directors noted, however, that signs of overheating had become more pronounced since the last consultation. Headline inflation had accelerated sharply since mid-1999, and now exceeded the euro area average by a considerable margin. While this increase reflected higher fuel prices and a tobacco tax hike, underlying inflation had also picked up markedly owing to rapid price increases in the non-traded sector, particularly services. Labor shortages were widespread, physical bottlenecks had worsened, property prices continued to increase rapidly, and private sector credit was still growing at a very high rate.

Directors considered that these developments were indicative of a growing imbalance between demand and supply that posed a risk to Ireland's otherwise favorable medium-term outlook. They noted that higher inflation would place a strain on the latest three-year national wage agreement that had been ratified only a few months ago. Persistent, rapid property price inflation added to these strains. These developments gave rise to the concern that the social consensus underlying the wage agreement could erode, undermining the stability that has been central to Ireland's economic success. While competitiveness remained relatively strong at present, in part reflecting the weak euro, rising wage and price pressures could set the stage for a difficult adjustment later, if the euro were to appreciate substantially.

Directors agreed that the policy responses to address these concerns should include measures on both the demand and supply side. On the supply side, Directors welcomed the Government's plans to increase public investment outlays aimed at addressing infrastructure bottlenecks under the 2000 to 2006 National Development Plan, to pursue further tax reforms aimed at encouraging increased labor force participation, and to foster greater competition through deregulation and privatization. Directors considered that demand-side measures were also needed to contain overheating risks in the short run. Given that monetary conditions, now determined on a euro area-wide basis, were excessively accommodative for Ireland's cyclical position, Directors called for a tightening of fiscal policy to help dampen excess demand and contribute to the moderation of inflation.

Against this background, Directors urged the authorities to save any dividend from stronger-than-expected tax receipts in 2000 and to adopt a budget for 2001 that would imply an improvement in the structural primary balance. Directors stressed that, while the commitment to further moderate tax cuts under the national wage agreement should be respected, pressures for larger tax reductions should be resisted because such reductions would add to, rather than ease, the risks of overheating in the near term. On the spending side, Directors supported the authorities' plans to increase public investment in priority areas to relieve supply constraints, but noted that the desired fiscal tightening in 2001 would imply a need for tight control over growth in other public spending.

To help keep temporary factors from feeding through into higher wage settlements, the government also had an important role to play by ensuring that the increases in public sector wages agreed under the latest multi-year national accord are strictly adhered to. Directors also encouraged the authorities to use the period of this accord to explore alternative mechanisms for public sector wage determination that would reduce the rigidities inherent in the current process. The planned benchmarking exercise offered the prospect of addressing entrenched relativities, but Directors emphasized that this should not come at the expense of overall public sector wage restraint. It would also be desirable to reduce the reliance on wage-tax trade-offs, which tend to impart a pro-cyclical bias to fiscal policy and are likely to be increasingly constrained in the future by medium-term fiscal sustainability considerations. More generally, Directors noted that maintaining discipline over public sector spending is likely to pose an increasing challenge during a period of buoyant tax revenues and sizable budget surpluses. Directors encouraged the authorities to proceed with their earlier plans to implement a multi-year budgeting framework, which could play a useful role in helping preserve fiscal discipline.

Directors welcomed Ireland's participation in the Financial Sector Assessment Program, which had been timely in view of the recent rapid credit growth and significant changes in the financial sector. They agreed that Ireland had a sound and highly developed financial system that has been very stable, even during periods of international financial turmoil. The overall framework of prudential regulation and supervision is well developed with a high degree of observance of international standards and codes. Nonetheless, risks to financial sector and macroeconomic stability could arise from rapid lending growth, in particular related to the domestic property boom. Directors, therefore, welcomed the efforts of the supervisory authorities to ensure that credit institutions follow prudent lending criteria and take adequate account of the potential impact on their portfolios of an adverse macroeconomic shock, which could include a downturn in the property market. Directors encouraged the authorities to continue to monitor the situation closely, and use the full range of prudential tools at their disposal. Directors also considered it desirable that the authorities implement expeditiously their plan to establish a single supervisory agency.

Directors expressed concern that, after several years of rapid property price increases, housing demand may increasingly be driven by expectations of further price increases—a trend that could be abruptly reversed. Given these concerns, Directors welcomed the government's latest initiatives to promote a better balance in the property market through steps to alleviate supply-side constraints and discourage speculative demand. Directors encouraged the authorities to keep the situation under review and address any remaining distortions that may be contributing to excess demand pressures in the property market.

Directors commended the authorities for their ongoing efforts to promote greater competition in the economy, particularly in those sectors that to date have been relatively insulated from competitive forces. They stressed that such policies can be expected to lead to an improved quality of services and help dampen the current strong inflationary pressures in the non-traded sector. Directors urged the authorities to continue and, where possible, accelerate their efforts in this regard.

Core macroeconomic data provided to the Fund were adequate for surveillance purposes. Directors welcomed the authorities' ongoing efforts to improve the quality of economic statistics, but stressed the need for further improvements in the coverage and timeliness of several key indicators.

Directors encouraged the authorities to make greater progress toward achieving the United Nations' target of 0.7 percent of GDP for official development assistance.

Public Information Notices (PINs) are issued, (i) at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies; and (ii) following policy discussions in the Executive Board at the decision of the Board. As part of a pilot project, the staff report for the 2000 Article IV consultation with Ireland is also available.

Ireland: Selected Economic Indicators

	1996	1997	1998	1999 1/	2000 1/
Real Economy (change in percent)					
Real GDP	7.7	10.7	8.6	9.8	8.7
Real GNP	7.4	9.3	7.8	7.8	7.8
Domestic demand	7.8	9.8	9.4	6.3	8.4
CPI	1.6	1.5	2.4	1.6	4.9
Unemployment rate (in percent)	11.5	9.8	7.4	5.6	4.5
Gross national saving 2/ 3/	22.4	24.0	24.3	23.9	25.0
Gross domestic investment 3/	19.6	21.5	23.4	23.3	25.6
Public Finances (percent of GDP)					
General government balance	-0.6	0.8	2.1	3.7	3.7
Structural balance	0.2	0.3	1.1	2.0	1.6
General government debt	74	65	56	50	42
Money and Credit (end-year, percent change)					
M3E	15.7	19.1	18.1	...	...
Private sector credit	16.7	29.6	22.6	33.5	...
Interest rates (year average)					
Three-month interbank 4/	5.9	6.1	3.2	2.5	3.8
10-year government bond yield 4/	6.6	5.5	4.0	4.6	5.6
Balance of Payments (percent of GDP)					
Trade balance	19.2	21.0	23.1	25.9	24.3
Current account	2.8	2.5	0.9	0.6	-0.6
Reserves (gold valued at SDR 35 per ounce end of period, in billions of SDRs)	5.8	4.9	6.8	3.9	...
Exchange Rate					
Exchange rate regime	Member of euro area				
Present rate (June 21, 2000)	US$ per euro 0.946				
Nominal effective rate (1995=100)	102.1	102.4	97.1	94.2	...
Real effective rate (1995=100, CPI based)	101.9	101.6	97.0	94.1	...

Sources: Central Statistics Office; Department of Finance, and IMF, International Financial Statistics.

1/ Staff projections, except where noted.

2/ Staff estimates.

3/ In percent of GDP.

4/ For 2000, average of the first four months.