INTERNATIONAL MONETARY FUND

IMF Country Report No. 16/256

IRELAND

July 2016

2016 ARTICLE IV CONSULTATION AND FIFTH POST-PROGRAM MONITORING—PRESS RELEASE; AND STAFF REPORT

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2016 Article IV consultation and Fifth Post-Program Monitoring with Ireland, the following documents have been released and are included in this package:

- A **Press Release** summarizing the views of the Executive Board as expressed during its July 27, 2016 consideration of the staff report that concluded the Article IV consultation Fifth Post-Program Monitoring with Ireland.
- A **Staff Supplement** updating information on recent developments.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on July 27, 2016, following discussions that ended on June 23, 2016 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 13, 2016.
- An **Informational Annex** prepared by the IMF staff.

The documents listed below have been or will be separately released.

Selected Issues

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

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July 27, 2016

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IMF Executive Board Concludes the 2016 Article IV Consultation and the Fifth Post-Program Monitoring Discussion with Ireland

On July 27, 2016, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[1] and the Fifth Post-Program Monitoring Discussion with Ireland.

The rebound of the Irish economy has been exceptional. According to the previous data release in March 2016, Ireland's real GDP was reported to have grown by 7.8 percent in 2015 on the back of strong domestic demand and solid export growth. Subsequent revisions to the national accounts in July 2016 have led to an upgrade of the 2015 GDP growth to 26.3 percent, mainly due to much larger net exports contributions, while private consumption growth was modified much more moderately from 3.5 to 4.5 percent. The GDP revisions, which represent a level shift, are largely related to relocation of multinational companies to Ireland, which had a limited impact on the underlying Irish economy, as explained in the Supplementary Information to the Staff Report.

High frequency indicators suggest that growth momentum has continued in 2016. Solid job creation has reduced the unemployment rate below 8 percent. Inflation has hovered around zero as low commodity and food prices more than offset rising cost of services, particularly housing rents. Owing to buoyant revenues, the general government deficit narrowed to 2.3 percent of GDP (pre-revision national accounts) in 2015, thus allowing Ireland to exit the Excessive Deficit Procedure. The deficit is projected to fall below one percent this year, despite some spending overruns, mainly in the health sector.

The positive economic performance is expected to continue, but the UK vote to leave the EU amplifies downward risks. Over the medium term, Ireland's economy is likely to be affected by the spillovers. The severity of the impact is, however, difficult to gauge at this stage, and will crucially depend on the future relationship between the UK and the EU, especially regarding trade, financial flows, and movement of labor.

[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.

Taking into account negative spillovers, real GDP growth is projected to decline to just below 5 percent in 2016 and converge to its estimated potential (about 3 percent a year) over the medium-term on the back of more moderate export growth and investment activity. As a result, the output gap is expected to virtually close and the current account surplus to moderate by the end of the forecasting period. Against this backdrop, staff estimate that the government's objective of reaching the medium-term objective of a structural deficit of ½ percent of GDP remains broadly within reach.

Since the crisis, Ireland's financial regulatory and supervisory frameworks have been significantly upgraded and the financial soundness of the banking sector has improved, yet challenges from crisis legacies persist. This progress was evaluated by the IMF's Financial Sector Assessment Program, the findings of which are summarized in the accompanying Financial System Stability Assessment.

Executive Board Assessment[2]

Executive Directors welcomed Ireland's remarkable economic rebound, improving public finances, and positive outlook. At the same time, they noted that the recovery is incomplete and crisis legacies persist in an environment of increased uncertainty, including following the U.K. vote to leave the EU. They urged the authorities to continue to strengthen the foundations for sustainable and inclusive long-term growth. They recommended locking in recent gains, tackling lingering crisis legacies, rebuilding policy buffers, and bolstering the economy's resilience through structural reform.

Directors commended the authorities' solid track record of fiscal prudence, which has allowed Ireland to exit the EU's Excessive Deficit Procedure. They supported continued public debt reduction to lessen the Irish economy's vulnerability to shocks and rebuild room for countercyclical fiscal policy. They noted that the authorities' plan to create a "rainy day" fund over the medium term could be an important buffer in case of need. Directors agreed that fiscal policy could better support job-rich growth by rebalancing the tax mix away from direct taxes; widening the tax base and reducing the burden on middle-income households; increasing spending efficiency, particularly in health; and better targeting social transfers to improve intergenerational fairness. Directors noted that higher and prioritized capital expenditure would help buttress Ireland's competitiveness.

Directors welcomed the improvement in banks' financial soundness. They stressed, however, that persistent banking vulnerabilities, together with potential adverse spillovers from the U.K. vote, point to the importance of continued supervisory vigilance and careful risk

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[2] At the conclusion of the discussion, the Deputy Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

management. While there has been significant progress in reducing nonperforming loans, Directors underscored the need for continued efforts, and supported the authorities' plans in this area, including providing access to financial and legal advice to distressed mortgage borrowers.

Directors supported the authorities' intention to maintain macroprudential measures on mortgage lending, and the central bank's plan to periodically assess the effectiveness of these measures. They underscored the importance of policies to alleviate housing supply shortage, and encouraged monitoring of the commercial real estate market and the asset management sector.

Directors highlighted the importance of policies to support a robust and inclusive medium-term growth and job creation. Priorities could include broadening financing options for small and medium enterprises, supporting innovation, enhancing labor activation policies and technical and vocational programs to reduce skills mismatches, and strengthening female labor force participation.

Noting the recent revision of Ireland's national accounts, Directors supported the authorities' work underway to develop additional metrics that better reflect Ireland's underlying economic activity.

Ireland: Selected Economic Indicators, 2011–17 1/

(Annual percentage change unless indicated otherwise)

						Projections	
	2011	2012	2013	2014	2015	2016	2017
National accounts (constant prices)							
Real GDP	2.6	0.2	1.4	5.2	7.8	4.9	3.2
Final domestic demand	-0.1	1.0	-1.5	5.2	8.6	5.3	3.8
Private consumption	-0.7	-0.8	-0.3	2.0	3.5	3.1	2.2
Public consumption	-2.0	-2.2	1.4	4.6	-0.8	4.4	2.7
Gross fixed investment	3.2	8.6	-6.6	14.3	28.2	10.2	7.3
Net exports 2/	3.6	-0.3	2.6	0.1	0.1	0.9	0.2
Exports of goods and services	2.1	2.1	2.5	12.1	13.8	6.8	5.2
Imports of goods and services	-1.5	2.9	0.0	14.7	16.4	7.0	5.8
Real GNP	-0.8	1.6	4.6	6.9	5.7	4.5	2.8
Gross national saving (in percent of GDP)	16.0	17.6	20.7	22.9	26.5	26.8	27.6
Private	22.3	23.6	24.6	24.6	26.9	25.9	26.4
Public 3/	-6.2	-6.0	-3.8	-1.7	-0.5	0.9	1.1
Gross investment (in percent of GDP)	17.2	19.1	17.7	19.3	22.0	23.0	24.0
Private	14.8	17.1	15.8	17.2	20.2	21.2	22.3
Public	2.4	2.0	1.8	2.1	1.8	1.8	1.7
Prices, wages and employment (annual average)							
Harmonized index of consumer prices	1.2	1.9	0.5	0.3	0.0	0.3	1.2
Average wage, whole economy	-0.6	0.5	-0.7	-0.2	1.8	3.2	2.6
Employment	-1.8	-0.6	2.4	1.7	2.6	2.0	1.7
Unemployment rate (in percent)	14.7	14.7	13.1	11.3	9.5	8.3	7.7
Money and credit (end-period)							
Irish resident private sector credit	-2.9	-4.0	-4.9	-4.4	-4.4	...	...
Financial and asset markets (end-period)							
Three-month interbank rate	1.4	0.2	0.3	0.1	-0.1	...	...
Government bond yield (in percent, 10-year)	8.5	4.5	3.5	1.2	1.2	...	...
Annual change in ISEQ index (in percent)	5.2	16.3	30.3	15.1	33.5	...	...
House prices	-16.7	-4.5	6.4	16.3	6.6	...	...
Public finance (in percent of GDP)							
Net lending/borrowing	-12.6	-8.0	-5.7	-3.8	-2.3	-0.9	-0.6
Net lending/borrowing (excl. one-off items)	-8.7	-8.0	-6.1	-3.9	-1.3	-0.9	-0.6
Primary balance (excl. bank support)	-5.2	-3.9	-1.4	0.2	0.8	1.8	2.0
General government gross debt	109.1	120.2	120.0	107.5	93.8	89.0	86.6
General government net debt	77.3	86.7	89.6	88.1	75.5	72.1	70.5
External trade and balance of payments (percent of GDP)							
Balance of goods and services	18.0	17.2	19.3	18.3	20.9	21.9	21.7
Balance of income and current transfers	-19.2	-18.7	-16.2	-14.7	-16.4	-18.1	-18.2
Current account	-1.2	-1.5	3.1	3.6	4.4	3.8	3.5
Effective exchange rates (1999:Q1=100, average)							
Nominal	108.5	104.1	107.3	107.7	100.1	...	...
Real (CPI based)	110.1	105.1	106.8	106.0	97.9	...	...
Memorandum items:							
Population (in millions)	4.6	4.6	4.6	4.6	4.6	4.7	4.7
GDP per capita (in euros)	38,021	38,131	39,069	41,011	46,301	49,505	51,436
GDP (in billions of euros)	173.9	174.8	179.4	189.0	214.6	231.4	242.5
National accounts released in July 2016:							
Nominal GDP (in billions of euros)	173.1	175.8	180.2	193.2	255.8	...	...
GDP per capita (in euros)	37,830	38,329	39,235	41,904	55,187	...	...
Real GDP growth (in percent)	0.0	-1.1	1.1	8.5	26.3	...	...

Sources: Bloomberg; Central Bank of Ireland; Department of Finance; International Financial Statistics; and IMF staff projections.

1/ The data reported in this table refer to those available at the time of the mission.

2/ Contribution to growth.

3/ Excludes bank restructuring costs.

IRELAND

July 21, 2016

STAFF REPORT FOR THE 2016 ARTICLE IV CONSULTATION AND FIFTH POST-PROGRAM MONITORING DISCUSSIONS—SUPPLEMENTARY INFORMATION

Prepared by The European Department

The purpose of this supplement is to inform the Board about the recent revisions of Ireland's national accounts and the latest economic developments. The GDP growth for 2014-15 was significantly revised upwards largely due to operations of multinational companies. As this reflects a level shift and the underlying economic developments appear unchanged, these revisions do not alter the thrust of the staff appraisal. Nonetheless, additional metrics better reflecting the underlying developments of the Irish economy should be developed to support policymaking and communications to the public.

1. **On July 12, Ireland's Central Statistics Office (CSO) released the new national accounts for 2015 and prior years.** The annual benchmarking exercise of national income and expenditure resulted in a large upward level shift of nominal and real GDP, largely on the back of higher net exports (Table). The already impressive growth rate in 2015 was upgraded from 7.8 percent to 26.3 percent,[1] and the real GNP growth rate from 5.7 percent to 18.7 percent. Reflecting the large revision of net exports, the trade and current account surpluses were revised upward from 30.1 percent of GDP to 43.2 percent of GDP and from 4.4 percent of GDP to 10.2 percent of GDP, respectively. The recording of new large direct and portfolio investment led to a marked deterioration of Ireland's negative net international investment position (NIIP) from 69.6 percent of GDP to 207.7 percent of GDP. In addition, the upward revision of nominal GDP mechanically improved the fiscal metrics, with the general government budget deficit narrowing from 2.3 percent of GDP to 1.9 percent of GDP and gross debt declining from 93.8 percent of GDP to 78.7 percent of GDP in staff's calculations.

[1] The growth rate in 2014 was also lifted up from 5.2 percent to 8.5 percent.

2. These revisions, which are in line with *ESA2010* and *BPM6* methodology, are explained by a number of factors, largely related to operations of multinational companies. Corporate restructuring through the relocation to Ireland of companies' entire balance sheets, the shifting of assets to Irish subsidiaries, and the takeover of foreign companies by Irish entities, have led to a dramatic increase in the level of capital assets in Ireland. The mirror image of this has been a substantial negative revision of Ireland's NIIP due to higher liabilities to nonresidents. The relocation of companies has also been associated with an increase in "contract manufacturing", which boosts Ireland's exports and GDP.[2] The significant upward adjustment of net exports has more than offset the now more-negative net factor income from abroad, thereby leading to an upward revision of Ireland's GNP as well. The increase in the number of new aircraft imports into Ireland for international leasing activities is an additional factor driving the revision of national accounts and balance of payments statistics.

3. Although these revisions make the assessment of the Irish economy more complex, a number of indicators confirms its strong underlying rebound. For example, private consumption and retail sales grew strongly in 2015 (4.5 percent and 8.2 percent, respectively) on the back of rising employment (2.6 percent). Public finances have continued to improve and government's debt-to-GDP ratio has declined rapidly, irrespective of the recent revision of the nominal GDP. However, owing to the open and globalized nature of the Irish economy, the revised headline metrics, such as GDP and GNP, are somewhat delinked from the underlying economic developments. A thorough analysis of the revised data would require more detailed information on the activity of the multinational corporations, which is unavailable for confidentiality reasons.

4. Staff and the authorities agree that the underlying economic developments, which formed the basis of the Article IV consultation discussions, remain valid, despite the revision of the national accounts. If staff were to include the revised national accounts figures into the macroeconomic framework, it would distort the true representation of underlying economic developments and the headline ratios to GDP. This could lead to incorrect analysis and policy conclusions. For example, while this would mechanically reduce the debt-to-GDP ratio, it would not represent a true improvement in Ireland's ability to service debt or the capacity to repay the Fund. ***Consequently, these statistical revisions do not alter staff's analysis and policy recommendations.***

5. Staff now recommend that the authorities develop additional metrics that better reflect Ireland's underlying economic activity, to support policymaking and communications to the public, but this process will likely require some time. Staff, therefore, welcome the CSO's initiative to convene a high-level cross-sector consultative group to examine how best to provide

[2] "Contract manufacturing" refers to a special form of outsourcing, where an Irish company engages a company abroad to manufacture products on its behalf but retains the economic ownership of the inputs used in this production process. When the product is sold to a customer abroad, a change in economic ownership takes place and the export of this good is then recorded in the Irish national accounts and balance of payments, even though it was never produced in Ireland.

insight and understanding of all aspects of the Irish economy, including the potential to develop additional indicators.

6. The authorities noted that they will prepare full macroeconomic projections in advance of Budget 2017 in October. This will include updated forecasts of economic growth, public finances, and fiscal space, taking account of developments up to that time, including the latest CSO numbers, and the UK decision to leave the EU. The authorities have indicated that the 26.3 percent GDP growth in 2015 will not affect policymaking, and have outlined that policies will be based on more moderate growth rates. Specifically, in relation to fiscal policy, the revenue projections for 2017 will be based on the estimated tax revenue outturn for 2016, and the projected nominal GDP growth rate for 2017 of about 5 percent.

7. The thrust of the staff appraisal remains unchanged, with the exception of the recommendation above to develop additional metrics that better reflect the underlying economic activity, to support policymaking and communications to the public.

Update of recent developments

8. Several recent data releases by the CSO confirm that the Irish economy is recovering at a solid pace. These indicators do not change the outlook for 2016 at this stage.

- **Output.** On the basis of the new national accounts, output in Q1 2016 was 2.3 percent higher than a year ago. While investment and net exports declined, personal consumption rose by 5 percent. This reflects the continued mending of the labor market (the unemployment rate declined to 7.8 percent in June), earnings growth, and high level of consumer confidence.

- **Inflation**. Headline inflation came in at 0.1 percent year-on year in June 2016, mostly reflecting still weak commodity and fuel prices. Core inflation remained at around 1 percent.

- **Public finances.** In Q1 2016, the general government deficit was reported at €1,471 million, well below that recorded a year ago (€2,331 million). This was mainly due to strong tax revenues, while government expenditure experienced a small decline, due to lower net capital investment. This performance bodes well for achieving the annual deficit target. The general government gross debt marginally rose to €206.8 billion from €201.3 billion in Q4 2015, reflecting a net increase in the issuance of debt securities in the period considered.

- **External sector.** The current account balance recorded a surplus of €8,955 million in Q1 2016 compared to €4,519 million in Q1 2015 reflecting mainly lower investment income payable to foreign investors, lower merchandise imports, and higher computer service exports. Total gross external debt declined to €2,169 million in Q1 2016 from €2,227 million in Q4 2015.

Ireland: New and Old National Accounts

		2010	2011	2012	2013	2014	2015
		(percentage changes)					
Real GDP	New	2.0	0.0	-1.1	1.1	8.5	26.3
	Old	0.4	2.6	0.2	1.4	5.2	7.8
Private consumption	New	0.7	-1.0	-1.0	-0.8	1.7	4.5
	Old	*0.8*	*-0.7*	*-0.8*	*-0.3*	*2.0*	*3.5*
Public consumption	New	-6.5	-0.9	-4.1	0.1	5.4	1.1
	Old	*-7.1*	*-2.0*	*-2.2*	*1.4*	*4.6*	*-0.8*
Gross fixed capital formation	New	-14.9	3.4	11.7	-5.4	18.2	32.7
	Old	*-15.5*	*3.2*	*8.6*	*-6.6*	*14.3*	*28.2*
Exports of goods	New	2.5	-1.1	-1.8	-0.3	16.2	55.4
	Old	*5.0*	*-2.2*	*-2.8*	*-1.8*	*16.1*	*17.2*
Exports of services	New	10.7	8.3	7.6	7.0	12.6	11.5
	Old	*8.5*	*8.3*	*8.5*	*7.4*	*7.9*	*10.0*
Imports of goods	New	-4.8	3.4	5.8	2.6	8.6	13.6
	Old	*1.1*	*-3.8*	*-2.7*	*0.8*	*11.3*	*8.4*
Imports of services	New	5.1	2.1	5.1	0.0	20.2	27.1
	Old	*5.6*	*0.3*	*7.0*	*-0.5*	*17.0*	*21.5*
Real GNP	New	3.8	-4.0	-0.4	4.7	9.2	18.7
	Old	*2.2*	*-0.8*	*1.6*	*4.6*	*6.9*	*5.7*

Sources: Central Statistics Office and IMF staff calculations.

INTERNATIONAL MONETARY FUND

July 13, 2016

IRELAND

STAFF REPORT FOR THE 2016 ARTICLE IV CONSULTATION AND FIFTH POST-PROGRAM MONITORING DISCUSSIONS

KEY ISSUES

Ireland's growth has been exceptional, but the recovery is incomplete, and is now subject to appreciable downside risks. GDP growth reached 7.8 percent in 2015, supported by robust domestic demand and exports, and unemployment is receding. Yet the recovery remains to be completed, with employment and consumption below their pre-crisis levels. Vulnerabilities are still elevated due to high public and private debts, and a large stock of nonperforming loans (NPLs). The economic outlook continues to appear broadly positive, but the heightened uncertainty resulting from the UK vote to leave the EU and the ensuing negative spillovers are a cause for concern. More than many other EU economies, Ireland's medium-to long-term outlook will be affected by the nature of the future relationship between the UK and the EU, especially regarding trade, financial flows, and labor movement.

Policy priorities include tackling the remaining crisis legacies, buttressing foundations for sustainable and inclusive long-term growth, and monitoring and mitigating the fall-out of the UK vote to leave the EU.

- **Attain sustainable public finances and continue public debt reduction.** Improve spending efficiency and rebalance the tax mix to boost employment and growth.
- **Improve private sector's balance sheets.** Household debt remains high and corporate sector vulnerabilities are also elevated, particularly among domestic SMEs. Recovery in the banking system is progressing, and, as noted in the Financial System Stability Assessment, continued intensified efforts are needed to further reduce NPLs and boost the private sector's resilience and ability to support durable growth.
- **Mitigate boom-bust cycles.** Maintain macroprudential limits on mortgages as a permanent feature of the mortgage market and periodically assess their impact and effectiveness. Monitor commercial real estate markets and stand ready to activate policy tools if risks to financial stability emerge. Help boost housing supply.
- **Address structural weaknesses to support robust and inclusive medium-term growth and job creation.** Broaden the options for SME financing and promote innovation. Strengthen incentives for female labor force participation, enhance labor activation policies, and expand technical and vocational training.
- **In the meantime, closely monitor and mitigate spillovers from the UK vote to leave the EU.** Policymakers will need to monitor closely the response of the economy and the financial system and stand ready to take remedial actions—such as a countercyclical fiscal policy together with central banks' commitment to backstop liquidity in euros and other currencies—if and when needed.

Approved By
Jörg Decressin (EUR) and Alfred Kammer (SPR)

Discussions took place in Dublin, during June 13-23. The staff team comprised Zuzana Murgasova (head), Nir Klein and Alessandro Giustiniani (all EUR), Alexandre Chailloux and Aleksandra Zdzienicka (both SPR), and Christopher Wilson (MCM). Ann-Margret Westin, the FSAP deputy mission chief (MCM), and Michael McGrath (Alternate ED) also joined the discussions. The team was supported from headquarters by Zsofia Arvai (MCM); as well as Vizhdan Boranova and Nomelie Veluz (both EUR).

CONTENTS

ANNEXES

Acronyms

AIB	Allied Irish Banks
BEPS	Base Erosion and Profit Shifting
BOI	Bank of Ireland
CA	Current Account
CBI	Central Bank of Ireland
CCR	Central Credit Register
CIT	Corporate Income Tax
CRE	Commercial Real Estate
DSA	Debt Sustainability Analysis
DTI	Debt-to-income
EBA	External Balance Assessment
EBITDA	Earnings before Interest, Taxes, Depreciation and Amortization
EC	European Commission
ECB	European Central Bank
ES	External Sustainability
EU	European Union
FDI	Foreign Direct Investment
FSSA	Financial System Stability Assessment
FSAP	Financial Sector Assessment Program
FTB	First Time Buyers
GFN	Gross Financing Needs
HICP	Harmonized CPI
ICR	Interest Cover Ratio
ICT	Information and Communications Technology
IFAC	Irish Fiscal Advisory Council
IFSC	International Financial Services Center
IIP	International Investment Position
JSTs	Joint Supervisory Teams
LLF	Loan-loss-forecasting Model
LTI	Loan-to-income
LTV	Loan-to-value
MMFs	Money Market Funds
MNE	Multinational Enterprise
MTO	Medium-term Objective
NAMA	National Asset Management Agency
NFC	Nonfinancial Corporate
NIIP	Net International Investment Position
NPL	Nonperforming Loan
NTMA	National Treasury Management Agency
OECD	The Organization for Economic Co-operation and Development
OLS	Ordinary Least Squares
OMT	Outright Monetary Transactions
PCAR	Prudential Capital Assessment Review
PDH	Primary Dwelling Houses

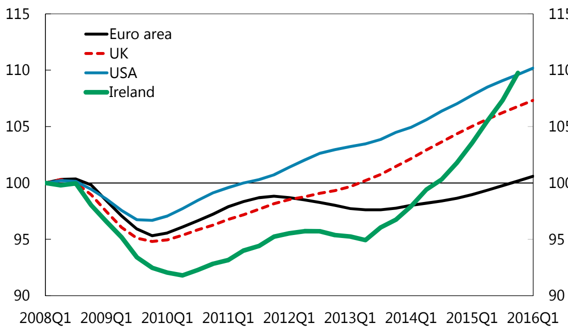
PD	Probability of Default
PIAAC	Programme for the International Assessment of Adult Competencies
PISA	Programme for International Student Assessment
PIT	Personal Income Tax
PTSB	Permanent TSP
QE	Quantitative Easing
R&D	Research and Development
RAM	Risk Assessment Matrix
REER	Real Effective Exchange Rate
RRE	Residential Real Estate
SDR	Standard Drawing Rights
SGP	Stability and Growth Pact
SIP	Selected Issues Paper
SMEs	Small-and Medium-sized Enterprises
SRF	Single Resolution Fund
SRM	Single Resolution Mechanism
SSM	Single Supervisory Mechanism
SVR	Standard Variable Rate
TFP	Total Factor Productivity
UK	United Kingdom
ULC	Unit Labor Cost
USC	Universal Social Charge
VAT	Value Added Tax
VECM	Vector Error Correction Model
WEO	World Economic Outlook

CONTEXT

1. Ireland's economy has rebounded exceptionally, but the recovery is incomplete and crisis legacies still pose challenges. Ireland's growth outperformed that of its peers during 2014-15, bringing real GDP at end-2015 ten percent above its pre-crisis level. The robust economic growth was supported by favorable external conditions, and was accompanied by improved balance sheets, a strengthening banking sector, steady job creation, and rising incomes and asset prices. Policy implementation has been strong (Annex I). Nevertheless, the recovery is unfinished and has yet to benefit parts of the population. Moreover, elevated public and private sector debts and a large stock of banks' distressed loans leave the economy susceptible to shocks.

Real GDP

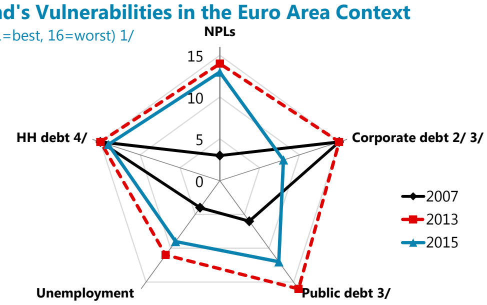
(Index, 2008Q1=100, seasonally adjusted)



Sources: Haver Analytics; and IMF staff calculations.

Ireland's Vulnerabilities in the Euro Area Context

(Rank, 1=best, 16=worst) 1/



Sources: BIS; Haver Analytics; WBDI; National authorities; and IMF staff calculations.
1/ Based on the relative ranking of EA countries excl. the Baltics.
2/ Ireland data excludes MNEs debt.
3/ In percent of GDP.
4/ In percent of gross disposable income.

2. The newly-elected government needs to maintain the economic policy course and tackle crisis legacies to achieve durable and inclusive long-term growth. The minority coalition that was formed in May 2016 following the February general election consists of the former incumbent party, Fine Gael, and independents. The importance of preserving economic recovery and safeguarding public finances is widely shared, and the broad policy course is likely to be continued. Nevertheless, the increased political fragmentation and reform fatigue may complicate policymaking and the fallout from the UK vote to leave the EU could do so too.

EXCEPTIONAL GROWTH BUT ELEVATED VULNERABILITIES

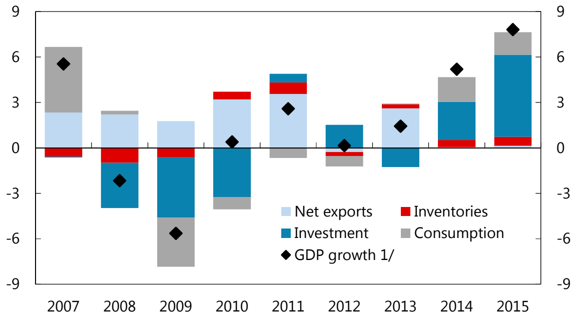
A remarkable growth performance is supported by favorable external conditions

3. The Irish economy has performed beyond expectations (Figure 1). Real GDP posted 7.8 percent growth in 2015 on the back of strong domestic demand and solid export growth. Gross fixed capital formation was mainly driven by investment in intellectual property by multinationals (MNEs) (Box 1), and a rise in machinery and construction investment.[1] Private consumption

[1] Multinationals account for 57 percent of the business sector's gross value added and 20 percent of employment. Financial linkages with domestic banks are limited.

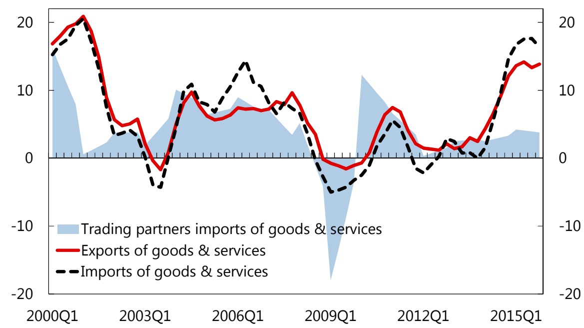
expanded strongly as consumer sentiment surged, the drag from deleveraging moderated, wages and employment improved, and low inflation supported real incomes. Double-digit export growth benefited from favorable external conditions: a real effective depreciation of the euro reflecting continued monetary easing by the ECB and strong trading-partner demand. Yet the contribution of net exports to growth was only marginal as imports rebounded together with exports and investment.[2] The recovery has been broad based, though the information and communications technology (ICT) and manufacturing (including pharmaceuticals) sectors have been particularly buoyant. High-frequency indicators suggest that the growth momentum has continued in 2016.

Contributions to Real GDP Growth
(Percent y/y)



Sources: Central Statistics Office; and IMF staff calculations.
1/ GDP growth accounts for statistical discrepancy as well.

Trade in Goods and Services
(Percent change y/y, real terms)



Sources: Central Statistics Office; and IMF staff calculations.

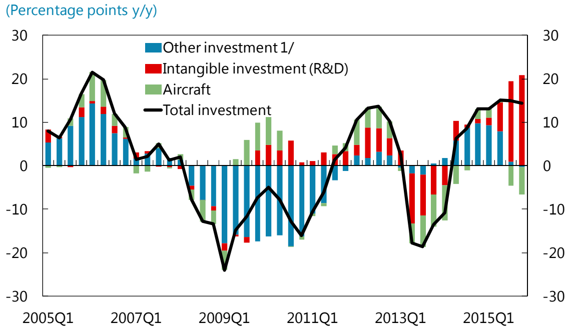
[2] When aircraft purchases by leasing companies and intangibles are excluded from both investment and imports, the core demand expansion is more subdued and net exports contribute positively to GDP growth (Box 1).

Box 1. Onshoring of Intangible Assets to Ireland

Partly in response to increasing multilateral efforts to combat aggressive tax planning and avoidance, including the OECD's Base Erosion and Profit Shifting (BEPS) Action Plan, some MNEs have chosen to restructure their businesses and relocate their intangible assets, such as patents and copyrights, to countries with supportive business environment.

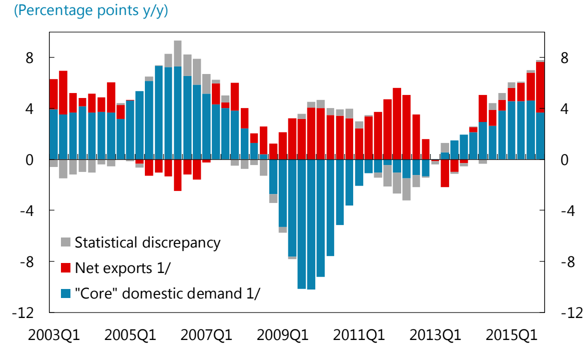
Consequently, Ireland, which maintains a competitive taxation environment, including for intellectual property-related activities (Knowledge Box), experienced a sharp increase in intangibles investment to 9½ percent of GDP in 2015 from about 5 percent of GDP in 2014. To the extent that investment in intangibles is related to patent onshoring, it is matched by imports, and thus is GDP neutral during the year of the transaction. Nevertheless, this investment adds to Ireland's capital stock, and in the future, ceteris paribus, will contribute positively to net export growth (mainly due to lower royalty payments abroad).

Contributions to Fixed Investment Growth
(Percentage points y/y)



Source: Central Statistics Office.
1/ Includes machinery & equipment, construction & other residential investment.

Contributions to GDP Growth
(Percentage points y/y)



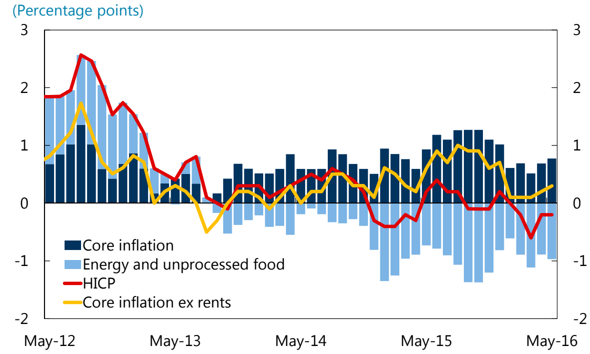
Sources: Central Statistics Office; and IMF staff calculations.
1/ Excludes aircraft and intangibles.

4. **Labor markets continued to improve without inflationary pressures**. The solid employment growth in 2015 helped reduce the unemployment rate to 7.8 percent in May 2016, and was reflected in a moderate increase in private sector's real wages, though labor force participation has not recovered so far. Inflation hovered around zero owing to lower commodity and food prices, which more than offset the rising cost of services, particularly housing rents.

Employment and Unemployment Rate
(Thousands of persons) (Percent)

Source: Central Statistics Office.

Contribution to Annual HICP Inflation
(Percentage points)



Sources: Central Statistics Office; Eurostat; and IMF staff calculations.

5. Public finances delivered a sizeable outperformance in 2015. Revenues significantly exceeded the initial budget profile, largely reflecting strong corporate income tax (CIT) receipts.[3] Expenditures rose more moderately over the budget profile (but slightly below the supplementary budget envelope), as a lower-than-planned interest bill partly offset higher current primary spending. The general government deficit fell to 2.3 percent of GDP—well below the initial budget target of 2.7 percent of GDP and the Stability and Growth Pact (SGP) 3 percent of GDP threshold. As a result, Ireland exited the Excessive Deficit Procedure (EDP). The overperformance would have been even more sizeable (yielding an underlying deficit of 1.3 percent of GDP), if conversion of government's remaining AIB preference shares to ordinary shares (equivalent to 1 percent of GDP), had been excluded from capital transfers.

Fiscal Performance

(Percent of GDP)

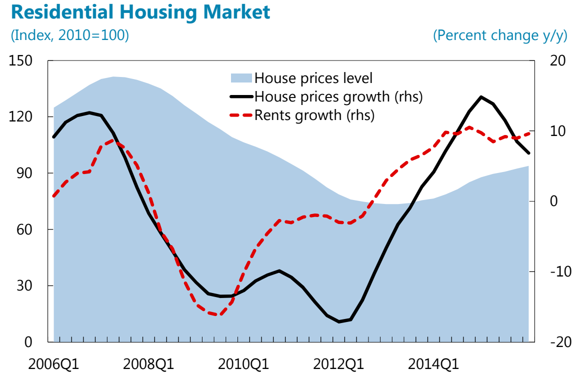
	2012	2013	2014	2015
Revenue	33.8	34.0	34.8	32.8
Taxes	23.4	23.7	24.6	23.6
Social contributions	5.5	5.7	5.8	5.3
Other revenue	4.9	4.6	4.4	3.9
Expenditure	41.8	39.7	38.6	35.1
Current primary	34.9	33.1	31.9	28.5
Interest payment	4.1	4.3	4.0	3.1
Capital expenditure	2.8	2.3	2.7	3.5
Net lending/borrowing 1/	-8.0	-5.7	-3.8	-2.3
Net lending/borrowing (exl. one-offs)	-8.0	-6.1	-3.9	-1.3

Sources: Department of Finance; Eurostat; and IMF staff calulcations.
1/ In 2015, it includes the increase in capital transfers due to the conversion of the remaining AIB preference shares to ordinary shares (Eurostat decision).

6. Rising demand, partially fueled by global search for yield, and supply-side bottlenecks have stimulated property prices (Figure 2).

- ***Residential real estate (RRE)*** prices and rents continued to increase. Nevertheless, following the abolishment of tax exemptions on capital gains in December 2014 and the introduction of new macroprudential loan-to-value (LTV) and loan-to-income (LTI) limits in February 2015 (see 2015 Article IV Staff Report), the market somewhat cooled off: RRE price growth decelerated in late 2015 and the number of mortgage approvals temporarily declined (Figure 3).

Residential Housing Market



Sources: Daft.ie; OECD; and IMF staff calculations.

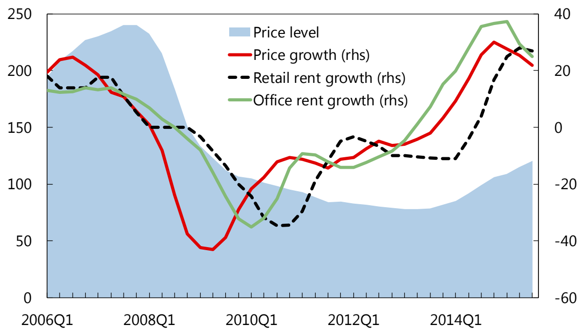
- ***Commercial real estate (CRE)*** prices rose even more rapidly. Total returns of the Irish CRE sector outstripped those of other European countries, reflecting the confluence of strong equity

[3] Yet only one half of the 2015 CIT overperformance can be explained by corporate profitability (Central Bank of Ireland's Quarterly Bulletin), and BEPS-related changes could have incentivized corporate restructuring in Ireland with a favorable impact on CIT revenues.

investment largely financed by foreigners in search for high yield, and still limited new construction.

Commercial Real Estate Market

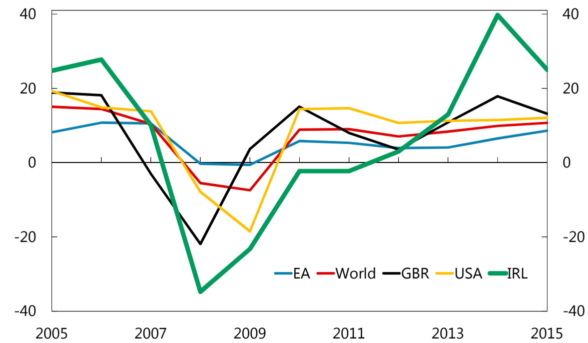
(Index, 2010=100) (Percent change y/y)



Sources: CBRE (Ireland); CSO; MSCI (IPD); and IMF staff calculations.

Commercial Real Estate Total Returns

(Percent)

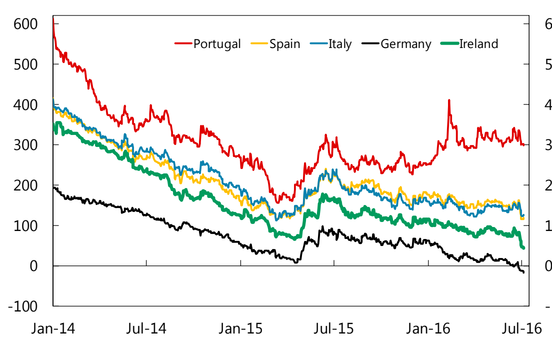


Source: MSCI/Invetsment Property Databank.

7. Financial conditions have been broadly supportive. As elsewhere, the UK vote to leave the EU has led to stock market losses but the sovereign bond market has been well behaved**.** The ECB's quantitative easing (QE), together with Ireland's favorable growth prospects, have kept the 10-year Irish sovereign yields very low, even if the spreads slightly widened temporarily following the UK vote to leave the EU. In line with other European countries, the Irish equity market partly reversed its last year's gains and declined by about 17 percent in 2016H1. Reflecting the strong GDP growth, improved balance sheets and prudent fiscal policy, Moody's upgraded Ireland's sovereign rating to A3 (May 2016), following Fitch's and S&P's upgrades to A (February 2016) and A+ (June 2015), respectively. The recent issuance of a 100-year sovereign bond is an additional sign of market confidence.

Ten-Year Sovereign Bond Yields

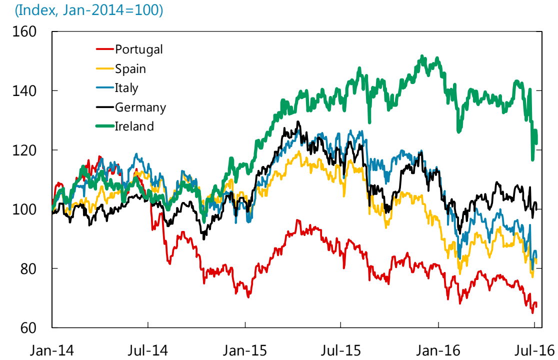
(Basis points)



Source: Bloomberg.

Stock Markets

(Index, Jan-2014=100)



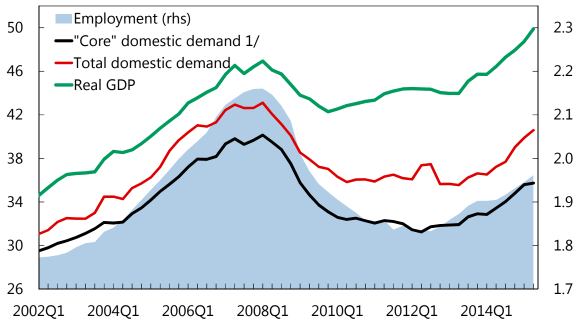
Source: Bloomberg.

Yet the recovery is still incomplete

8. Domestic demand and employment have yet to return to their pre-crisis levels. Private consumption, albeit recovering, is held back by the ongoing deleveraging process and the prevalence of households with low or negative equity. Disposable income is still some 5 percent below its peak, partly due to the higher tax burden. Investment in residential properties is lagging behind demand. With a still elevated jobless rate and sluggish labor participation, labor market slack persists and employment growth has been uneven across regions.

Real GDP Components and Employment

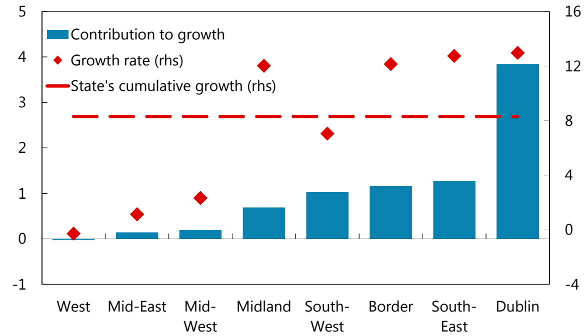
(Billions of euros, 2-quarter average, seasonally adjusted) (Millions)



Sources: Central Statistics Office; Haver Analytics; and IMF staff calculations.
1/ Excluding aircraft and intangibles.

Regional Employment Growth, 2012Q1-2016Q1

(Percentage points) (Percentage change y/y)

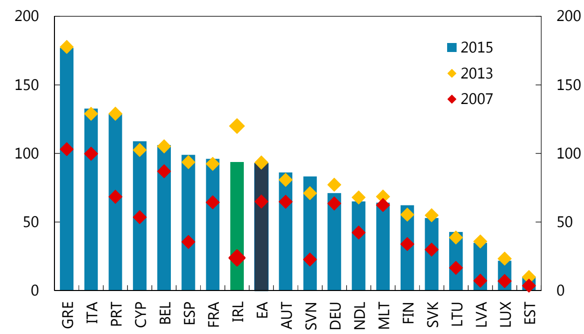


Sources: Central Statistics Office; and IMF staff calculations.

9. **High public and private debt burdens leave the economy vulnerable to shocks.** Public debt has declined to about 94 percent of GDP at end-2015 from a peak of 120 percent of GDP in 2013, but remains well above the pre-crisis levels. Despite falling debt, many households are susceptible to a drop in income or an interest rate increase. Nonfinancial corporates' (NFC) profitability has improved significantly and deleveraging has continued in recent years. Nevertheless, many small firms are financially weak and vulnerable to shocks.

Gross Public Debt

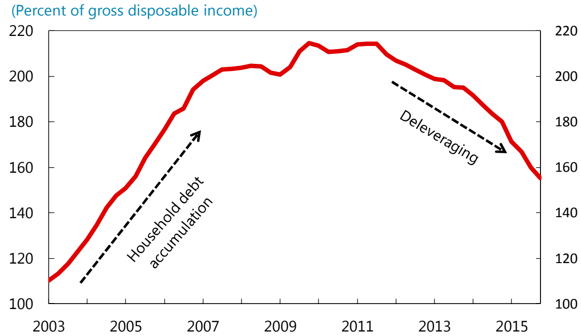
(Percent of GDP)



Source: IMF World Economic Outlook.

Household Debt Burden 1/

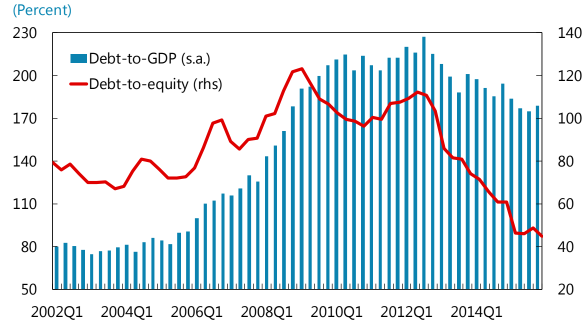
(Percent of gross disposable income)



Sources: Central Bank of Ireland; Haver Analytics; and IMF staff calculations.
1/ Total household loans in percent of 4 quarter gross disposable income.

Debt of Nonfinancial Corporations 1/

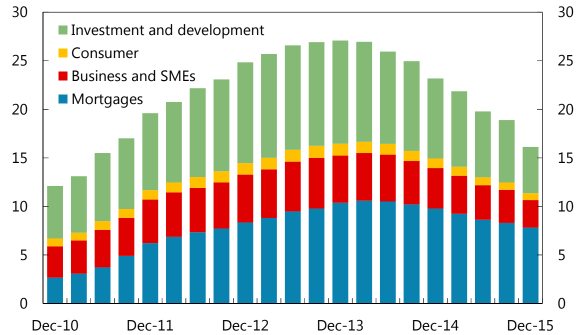
(Percent)



Sources: Central Bank of Ireland; and IMF staff calculations.
1/ Debt is equal to securities other than shares, loans, and financial derivatives and employee stock options.

10. The banking system repair continues, but challenges remain. The recent Financial Sector Assessment Program (FSAP) observed that liquidity indicators have improved as banks reduced their wholesale funding. Capitalization is also stronger, though deferred tax assets add substantially to the total. The banking sector as a whole returned to profitability in 2014-15 reflecting higher net interest income, better asset quality, and a reduction in operating cost, but also provisioning reversals as collateral values increased and loan restructuring continued. Yet, the underlying bank profitability remains subdued, bank balance sheets are still contracting despite a gradual pick up in new lending, and the high share of impaired loans poses fragilities, particularly given the increasing portion of mortgages in deep arrears (above 720 days) in the total stock of mortgage arrears (Figure 4). Provision coverage ratio remained broadly stable, and stood at about 52 percent of total nonperforming loans (NPLs) at end-2015.

Non-Performing Loans
(Percent of total loans, domestic banks)

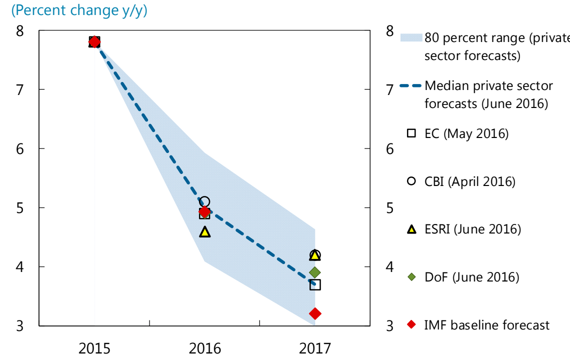


Source: Central Bank of Ireland.

The outlook is positive but risks are skewed to the downside

11. The positive economic performance is expected to continue, despite the fallout from the UK referendum result. GDP growth is projected just below 5 percent in 2016 on account of less vigorous domestic demand, mainly due to investment. Private consumption is expected to keep growing at a dynamic pace reflecting higher employment, lower household indebtedness, and positive wealth effect from rising property prices. Over the medium term, the Irish economy is likely to be affected by the consequences of the UK vote to leave the EU. The severity of the impact is however difficult to gauge at this stage. It will crucially depend on the future relationship between the UK and the EU, especially regarding trade, financial flows, and movement of labor. Taking into account some ensuing negative spillovers consistent with model-based calculations in the "limited" scenario outlined in the UK 2016 Article IV report and the accompanying Selected Issues paper, Ireland's real GDP growth has been revised downward in 2017-18.[4] Over the medium term, growth is projected to decelerate and converge to its estimated potential (about 3 percent a year) on the back of more moderate export

Real GDP Growth Projections
(Percent change y/y)



Sources: Bloomberg; CBI, ESRI; EC; MoF; and IMF staff estimates.

[4] The Economic and Social Research Institute estimates that a 1 percent reduction in UK GDP translates into a 0.3 percent decline of Ireland's GDP over the medium term.

growth and investment activity. As a result, the output gap is expected to virtually close and the current account surplus to moderate by the end of the forecasting period.

Ireland: Macroeconomic Projections, 2015–21
(Percentage change unless indicated otherwise)

		Projections					
	2015	2016	2017	2018	2019	2020	2021
Real GDP	7.8	4.9	3.2	3.1	2.8	2.8	2.8
Final domestic demand	8.6	5.3	3.8	3.1	3.0	3.0	2.9
Private consumption	3.5	3.1	2.2	2.2	2.0	1.9	1.9
Public consumption	-0.8	4.4	2.7	2.5	2.4	2.4	2.4
Fixed investment	28.2	10.2	7.3	5.1	5.1	5.1	5.0
Change in stocks (contribution to growth)	0.6	0.0	0.0	0.0	0.0	0.0	0.0
Net exports (contribution to growth)	0.1	0.9	0.2	0.6	0.4	0.4	0.4
Exports	13.8	6.8	5.2	4.4	4.2	4.2	4.2
Imports	16.4	7.0	5.8	4.5	4.5	4.5	4.5
Current account (percent of GDP)	4.4	3.8	3.5	3.3	3.2	3.1	3.0
Unemployment rate (percent)	9.5	8.3	7.7	7.2	6.8	6.7	6.7
Output gap 1/	-0.5	0.6	0.9	0.9	0.6	0.3	0.1
Consumer Prices (HICP)	0.0	0.3	1.2	1.4	1.8	2.0	2.0

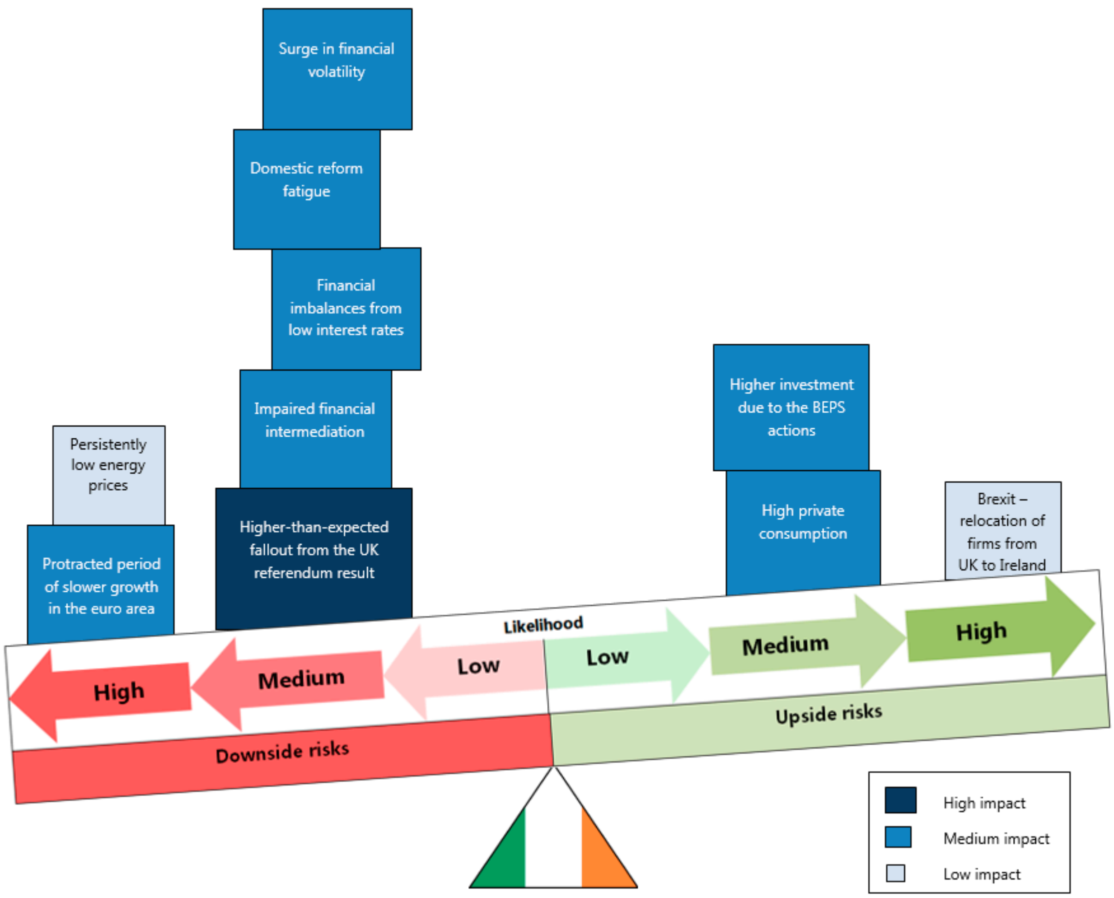
Source: Central Statistics Office; and IMF staff projections.
1/ Excluding multinational enterprises, see 2015 Article IV Selected Issues Paper.

12. Risks are tilted to the downside (Annex II):

- ***External risks have worsened since the UK referendum result and now prevail***. The recent UK vote to leave the EU, if accompanied by prolonged uncertainty over UK's new relationship with the EU, larger-than-expected slowdown in the UK and in the rest of Europe, and higher financial market volatility, would have a significant adverse effect on Ireland. In these circumstances, a countercyclical fiscal policy together with the central banks' commitment to provide additional liquidity, would help lessen the impact. Over the medium term, a possible relocation of EU-oriented firms from the UK to Ireland could partly mitigate some of these effects (Annex III). On the upside, the ongoing restructuring of operations by multinationals could reinforce Ireland's attractiveness as a destination for FDI and increase the capital stock. A surge in financial market volatility in response to other shocks and disruptive re-allocation of assets as investors reassess global growth prospects or as geopolitical tensions intensify could further undermine confidence, with possible adverse effects on investment. At the same time, the ECB's QE, the government's limited financing needs, and sizeable cash buffers (3½ percent of GDP as of end-June 2016) would mitigate the impact on sovereign spreads. An extended period of low euro area growth could also hurt confidence, investment, and FDI. Finally, while Ireland benefitted from net immigration of highly–skilled European workers in the past, inflows of refugees are expected to be small, with a limited fiscal impact.

- ***Domestic risks seem moderate.*** Rising incomes and lower deleveraging could lift private consumption and investment growth above the baseline, but continued rapid property price growth could generate new vulnerabilities. Reform fatigue combined with strong growth are fueling expectations of a recovery dividend among the Irish public, which together with political fragmentation could lead to some policy reversals. The impaired credit channel remains a medium-term risk if future demand for bank lending is not met with adequate supply.

Ireland: Balance of Risks



13. Ireland's external position is broadly in line with fundamentals and the economy remains competitive (Figure 5). The External Balance Assessment (EBA) methodologies suggest that the external position is broadly in line with fundamentals and desirable policy settings (Annex IV). The EBA Current Account approach indicates a slight undervaluation of the currency, but the current account gap can be—to a large extent—explained by undistributed profits of foreign companies that established their headquarters in Ireland. The External Sustainability and the Real Effective Exchange Rate approaches suggest minor overvaluation. Competitiveness continues to be strong in the services sector, and goods exports have also resumed robust growth, particularly in the pharmaceutical sector that appears to be less cyclical than global trade. In addition, Ireland's traditional exports have performed strongly, benefiting from the depreciation of the euro. However, some trade losses could be expected following a depreciation of sterling and a reduction of UK demand (Annex III).

Authorities' views

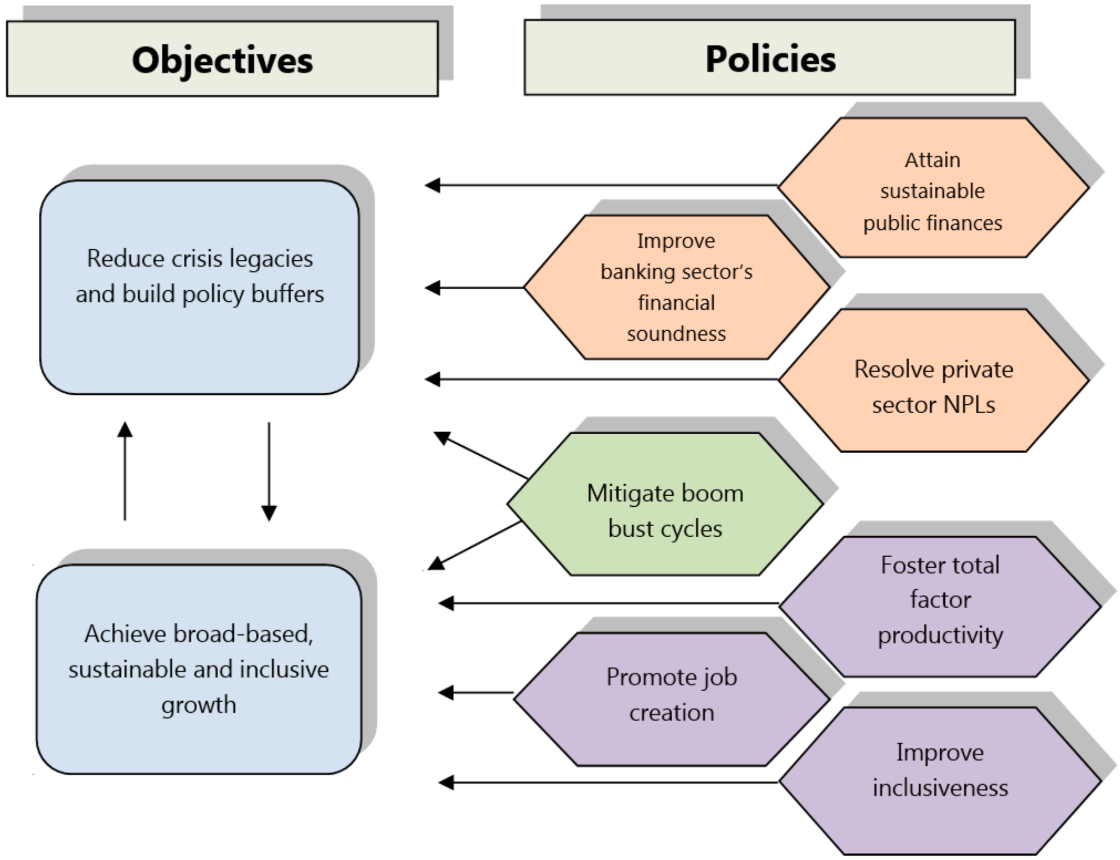
14. The authorities broadly shared staff's assessment regarding Ireland's economic outlook and risks. They saw prospects for robust real GDP growth, while somewhat decelerating over the medium term. Continuous progress in resolution of financial crisis legacies alongside increased market confidence should continue to support domestic demand, thus further reducing the unemployment rate. They concurred with the external sector assessment and predominant downside external risks reflecting the high degree of openness of the Irish economy. These include a significant slowdown in major trading partners and the ensuing adverse changes in the terms of trade, and heightened uncertainty regarding the prospects for many emerging market economies. However, this is mitigated somewhat by the fact that its exports are concentrated in sectors, such as pharmaceuticals, which are more resilient to external demand swings. Domestic factors, including tight housing markets and its adverse effect on labor mobility and competitiveness, as well as potential sectoral wage pressures could also pose downside risks. In addition, increased political fragmentation could complicate policy making. However, better-than-expected domestic demand and additional patent on-shoring represent potential upside.

15. The UK vote to leave the EU has added further uncertainty to the outlook and will adversely affect growth. The authorities' initial estimate, based on the assessment in the government's Summer Economic Statement (SES), is that growth in 2017 will be about ½ percent lower than previously expected, though the fiscal space for next year is largely fixed at this stage. The authorities will prepare a full macroeconomic projection in advance of Budget 2017 in October, and this will include updated estimates of economic growth, the public finances and the fiscal space, taking account of actual and prospective developments up to that time, including the estimated economic impact of the UK vote. The authorities have already published their contingency plans to deal with financial market volatility, potential effects on export industries, and FDI flows.

REBUILDING RESILIENCE AND SUPPORTING SUSTAINABLE AND INCLUSIVE GROWTH

Ireland's strong growth performance provides an opportunity to tackle the remaining crisis legacies, rebuild policy buffers, and increase the resilience of the economy to risks. Policies should focus on further reducing public debt while enhancing spending efficiency, lessening private sector vulnerabilities, improving bank balance sheets, and mitigating boom-bust cycles. Addressing structural weaknesses would support robust and inclusive medium-term growth and job creation.

Ireland: Medium-Term Policy Priorities



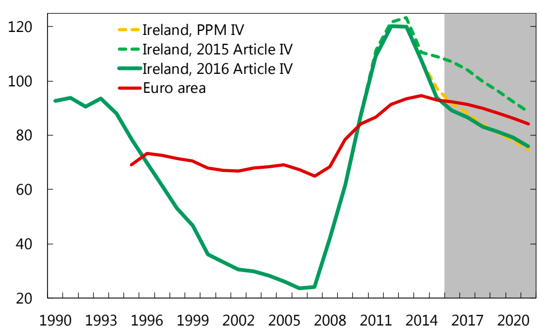
A. Fiscal Policy

Continue rebuilding fiscal buffers, increase expenditure efficiency, and rebalance the tax mix

16. Ireland is on track to further improve its fiscal position on the back of strong growth (Figure 6). Some spending overruns, mainly in the health sector, are estimated to be more than offset by higher-than-expected tax revenues due to their solid performance in the first months of 2016. As a result, staff project the fiscal deficit to narrow to 0.9 percent of GDP in 2016 and the public debt to fall below 90 percent of GDP. Given that the global push for international taxation reform and greater transparency make durability of exceptional CIT performance uncertain, staff advocated saving any near-term unanticipated revenues and using them for debt reduction.

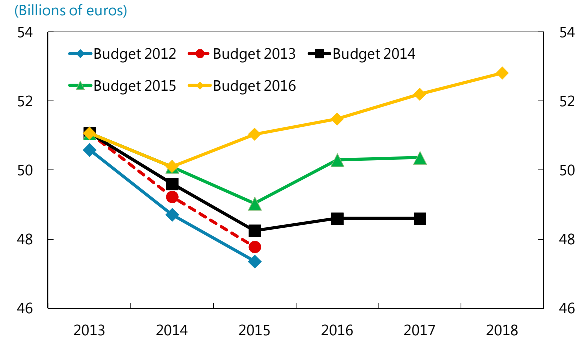
17. Fiscal policy should aim to rebuild buffers. The high degree of openness of Ireland's economy increases its susceptibility to external shocks and the volatility of the business cycles (Annex V). Against this backdrop and in the absence of monetary policy independence, staff emphasized the need for continued reduction in public debt, thereby rebuilding room for countercyclical fiscal policy.[5] To this end, staff argued that in the case of Ireland, mere compliance with the SGP rules might not be sufficiently prudent. Staff estimate that maintaining the medium-term objective (MTO) of a structural budget deficit of 0.5 percent of GDP, once achieved, would imply an unwarranted pro-cyclical fiscal policy given the positive output gaps estimated through 2021. Staff, therefore, advocated that the authorities overachieve the MTO, with primary balance surpluses, over the medium term. However, the inherent difficulties in correctly estimating Ireland's cyclical position warrant extra caution.[6] Avoiding periodic upward revisions of the three-year expenditure ceilings (thus compensating for possible overruns with other expenditure cuts) and saving potential tax windfall gains would also crucially help to rebuild fiscal buffers.

Gross Government Debt
(Percent of GDP)



Source: IMF staff calculations.

Successive Revisions to Triennial Departmental Expenditure Ceilings 1/
(Billions of euros)



Sources: Department of Finance; and IMF staff calculations.
1/ Based on comprehensive expenditure reports and budgets.

18. In line with staff's recommendations, the government plans to address social needs while ensuring sound public finances and durable debt reduction. In the Summer Economic Statement (SES) released on June 21, the government expressed the intention to achieve a structural budget deficit of 0.5 percent of GDP (MTO) by 2018. To this end, it allocates the fiscal room available under the SGP rules 2:1 toward expenditure increases and tax reductions during 2017-21. While the specific policies remain to be detailed, the fiscal plans include room to accommodate pent up spending needs, including those arising from demographic pressures. After 2018, as advocated by staff, the government intends to follow a countercyclical fiscal policy and save a portion of the fiscal space.[7] On the basis of the outlined plans, staff estimate that the government's objective of achieving the MTO by 2018 remains broadly within reach even under staff's scenario of mild spillovers from the UK vote to leave the EU, which results in a more conservative growth outlook than that of the authorities which was published in April. Public debt is projected to remain on a downward trend reaching around 76 percent of GDP by 2021. In the event of a larger-than-expected fallout from the UK vote to leave the EU, the authorities should stand

[5] An OECD study "Prudent debt targets and fiscal frameworks" estimates Ireland's prudent debt target at 35 percent of GDP.

[6] See the 2015 Article IV Staff Report. The modalities of calculating Ireland's cyclical position under the EU methodology, which differs from that used by Fund staff, may result in somewhat pro-cyclical policies.

[7] To this end, the authorities plan to establish a rainy day fund.

ready to take remedial actions, such as a countercyclical fiscal policy together with central banks' commitment to backstop liquidity in euros and other currencies—if and when needed.

Ireland: General Government Statement of Operations, 2015-21

(Percent of GDP)

		Projections					
	2015	2016	2017	2018	2019	2020	2021
Revenue	32.8	31.4	30.8	30.5	30.1	29.8	29.4
Taxes	23.6	22.9	22.8	22.7	22.5	22.2	22.0
Social contributions	5.3	5.2	5.2	5.1	5.1	5.1	5.1
Other revenue	3.9	3.2	2.8	2.6	2.6	2.5	2.3
Expenditure	35.1	32.2	31.4	30.8	30.3	29.6	29.0
Current primary	30.2	1.8	1.7	2.0	2.2	2.2	2.2
Interest payment	3.1	2.7	2.6	2.5	2.3	2.1	2.0
Gross fixed capital formation	1.8	1.8	1.7	2.0	2.2	2.2	2.2
Net lending/borrowing	-2.3	-0.9	-0.6	-0.3	-0.2	0.1	0.4
Net lending/borrowing (excl. one-offs)	-1.3	-0.9	-0.6	-0.3	-0.2	0.1	0.4
Structural balance 1/	-1.0	-0.9	-0.8	-0.6	-0.3	0.1	0.4
Primary structural balance 1/	2.1	1.8	1.8	1.9	2.0	2.2	2.4
Gross debt	93.8	89.0	86.6	83.1	81.2	79.1	75.8

Sources: Department of Finance; and IMF staff projections.
1/ In percent of nominal potential GDP. Excludes one-off items.

19. Fiscal policy can be more supportive of job-rich growth. Priority should be given to rebalancing the tax mix and broadening the tax base, while improving spending efficiency and addressing infrastructure needs.

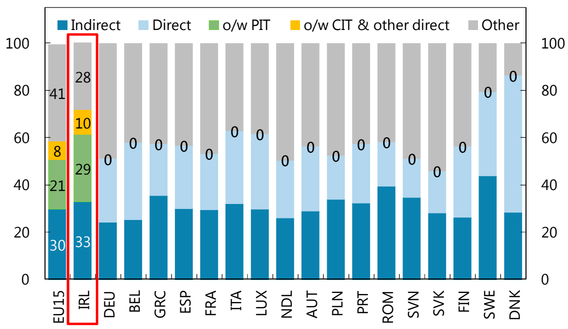
- *Rebalancing the tax mix would boost sustainable revenues and support job creation.* Compared to EU peers, Ireland's tax system has a higher reliance on more distortionary direct taxes, less on property and wealth taxes, while indirect taxes are about the EU average (Figure 7). In particular, personal income taxation (PIT and Universal Social Charge-USC) has a relatively narrow base (about 30 percent of households are exempted) and a relatively rapid progressivity (the top marginal rates are among the highest in the OECD).[8] This places a large tax burden on middle-income households, undermines female labor force participation, creates welfare traps for low-skilled worker, and discourages high-skilled worker migration to Ireland.[9] Consideration could thus be given to merging the USC into a more comprehensive PIT, with lower rates below the median wage and a broader base. Potential revenue losses could be compensated by decreasing the number of products with reduced and zero VAT rates and by faster scaling up the property

[8] While recent budgets have reduced the top marginal rate (now below 50 percent for middle-income households earning up to €70,044), the tax base has been narrowed by increasing the USC threshold and thus the proportion of exempt households from 27 to 30 percent.

[9] Central Bank of Ireland Technical Paper 01RT16.

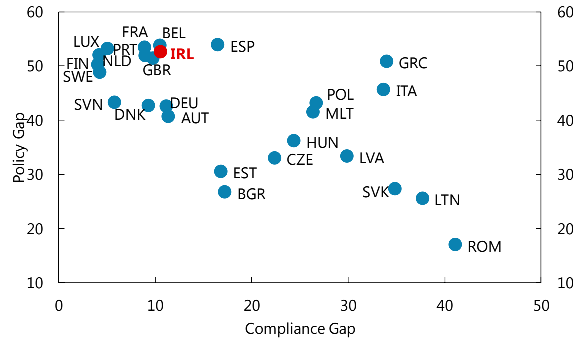
tax.[10] Income distribution concerns could be mitigated by means-tested allowances for low-income households.[11]

Direct, Indirect and Other Taxes in EU-15, 2014
(Share of total tax revenue)



Sources: AMECO; and IMF staff calculations.

VAT Compliance and Policy Gap, 2013 1/
(Percent)



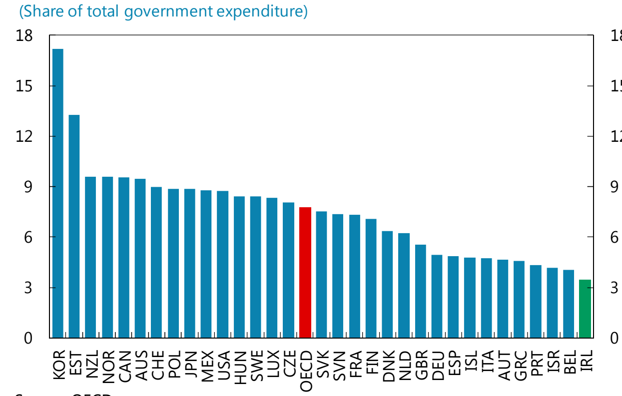
Source: EC "Study to quantify and analyse the VAT Gap in the EU Member States," 2015.

1/ The VAT compliance gap is defined as the difference between the amount of actually collected VAT and the amount of VAT that is theoretically collectable based on the VAT legislation and ancillary regulation (VTTL). The policy gap is defined as the ratio between VTTL and the amount of VAT that would be collected by applying a standard rate to final consumption.

- *Enhancing spending efficiency would improve delivery of public services*. By most metrics, Ireland is a low spending country (see Selected Issues on Public Expenditure Efficiency in Ireland). Moreover, expenditure is deemed to be generally efficient, especially for social spending where the impact on income inequality reduction is the highest in the EU (Figure 8). Nonetheless, there is scope for efficiency gains in the health sector. This would help generate resources needed to mitigate aging-related spending pressures. To this end, it is critical that ongoing reforms (strengthening of primary care, reform of hospital budgeting, lower expenditure due to greater generic drug use) progress as planned.[12] Furthermore, improved targeting of social transfers would contribute to enhanced inter-generational fairness for the young.

- *Increasing capital expenditure would buttress Ireland's competitiveness and support the population's well-being*. Ireland ranks last in the OECD for public investment as a share of government expenditure (see Selected Issues on Public Expenditure Efficiency in Ireland). Although the infrastructure quality remains above the EU average, it lags behind the "best in

Government Investment, 2014
(Share of total government expenditure)



Source: OECD.

[10] For example, the authorities' calculations suggest that replacing the reduced VAT rate for the hospitality sector with the 13.5 percent standard rate would generate about €0.7 billion in extra revenues.

[11] An OECD study suggests that means-tested support to low-income households, or the provision of state-subsidized social housing as an alternative to home ownership, could mitigate the regressivity of real estate taxation.

[12] See 8th review of the EFF Staff Report "Box 1. Public Health Spending Over-Run: Sources and Policy Options".

class" countries with which Ireland competes for high value-added exports. Technology infrastructure (broadband) and core infrastructure (power distribution and ports) need an upgrade, and maintenance of the existing insfrastructure stock is not fully met.[13] Public capital expenditure should thus be scaled up and prioritized, thereby strengthening Ireland's leading edge in the global export markets. Strengthening the evaluation framework for public investment would help maximize the growth impact.

Authorities' views

20. The government reiterated its broad objective to build a social economy based upon sound public finances. The authorities were in broad agreement with the staff's analysis and agreed that Ireland's high degree of economic volatility calls for adequate fiscal buffers to deal with potential negative shocks. They also stressed the importance of avoiding procyclical fiscal policy, hence the intention of establishing a rainy day fund. While the recovery is cementing, the authorities observed that new challenges are emerging, in particular regarding the growing demand for housing and the supply of critical infrastructure. The authorities indicated that the main gaps in public transportation across regions, as well as in large cities, need to be addressed in order to achieve a more regionally balanced economic growth. One of the key objectives of the government is indeed to create additional 200,000 jobs by the end of this decade, mostly outside Dublin. The authorities were mindful that demand pressures for healthcare ought to be addressed in an efficient way. Value-for-money considerations and the continued focus on reform of public services remain a key priority in the government's policy agenda.

21. The authorities affirmed their intention to achieve a stable tax mix and entrench the progress made in recent years to broaden the tax base. Within this context, the authorities expressed their intention to reform the income tax system—including a phasing out of the USC—with a view to expanding the base while reducing the burden for lower and middle income earners. This reform is seen as a key element in promoting employment growth. On corporate taxation, the authorities recognized the wide uncertainty as to the transitory or more durable nature of the recent CIT upswing. They agreed with staff that future short-term revenue windfalls should be saved, but stressed that a better understanding of, inter alia, the structural drivers of corporate profitability was a pre-requisite to effective medium-term tax forecasting. While agreeing on the possibility of removing some VAT exemptions, the authorities highlighted the need to address them within a European context. As for the current house price valuation freeze for property tax, they emphasized the objective to maintain stable property tax revenues in the current upswing in the property market.

B. Macro-Financial Policies

22. Crisis legacies and property market swings need to be contained to enhance the resilience of the private sector. The FSAP concluded that the banking sector is tightly connected

[13] European Commission – Commission Staff Working Document, Country Report Ireland 2016.

with Ireland's real economy, but not with rest of the other financial sector.[14] The FSAP also noted that the financial soundness of banks, households, and corporates has improved in recent years, but legacy issues amplify vulnerabilities to shocks. Solvency and liquidity stress tests under an adverse macroeconomic scenario indicate that the Irish banking system would be significantly impacted, with capital and leverage of several banks falling below certain hurdle rates (Annex VI).[15] Policies should, therefore, focus on strengthening the banking sector's resilience and its ability to sustainably support growth. Furthermore, the real estate market rebound raises concerns of potential emerging imbalances.

23. The recent UK vote to leave the EU could affect Ireland's banking system through various channels. Given the large uncertainties involved, it is difficult to quantify the direct and indirect spillovers at this stage. However, there are a number of channels through which the banking system could be affected. The profitability of Irish subsidiaries in the UK could be adversely affected by the slowdown in the UK economy and the depreciation of the pound against the euro. Furthermore, the downturn may lead to deterioration in banks' asset quality, reflecting in part a fall in UK property prices (particularly housing). In addition, Irish corporates that export to the UK may face lower demand and profitability, which in turn could hamper their debt repayment capacity. More broadly, slower economic activity in Ireland accompanied by higher unemployment could affect lending volumes, NPLs, and bank profitability, and slow the repair of private sector balance sheets. Heightened uncertainty and market volatility could increase bank funding costs, though the heavy reliance on deposits lessens this risk. Liquidity risks are mitigated by central banks' commitment to backstop liquidity in euros and other currencies to deal with the market volatility following the referendum result.

Tackling crisis legacies

[14] There are also close bank-sovereign financial linkages through banks' holdings of government bonds and the government's holdings of bank equity. Meanwhile, the linkages between the banking system and the funds industry, insurance companies, or pension funds are very limited.

[15] The FSAP's adverse macroeconomic scenario is more severe than the mild spillovers from the UK vote to leave the EU assumed in staff's projections.

24. Raising banks' profitability in a durable manner remains a key challenge. Despite progress, pre-provision profits continue to be modest. Prospects for further improvement are clouded by a number of factors, including low credit demand and ongoing system-wide deleveraging, limited scope for lower funding costs, prevalence of low-yield tracker mortgages, continued headwinds from unresolved distressed loans, and the need to upgrade technology infrastructure. More recently, the UK vote to leave the EU could further undermine profitability. Given these pressures, banks could lean toward riskier activities in an effort to boost earnings. While this could lead to higher internal capital generation, staff underlined the need to ensure that banks appropriately balance profit seeking and risk management. Staff encouraged conservative collateral valuations, and stressed the need for continued adequate provisioning.

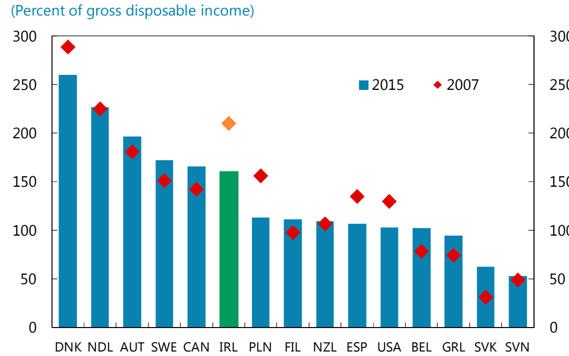
Irish Banks: Key Financial Indicators 1/
(Percent)

	2011	2012	2013	2014	2015
Credit growth 2/	-4.1	-10.2	-10.8	-4.3	-1.1
Return on assets	-1.2	-2.0	-0.8	0.6	0.7
Pre-provision profits 3/	0.6	-0.2	0.4	0.5	0.9
Net interest margin	0.9	0.8	1.2	1.6	1.8
Cost-to-income ratio	31.8	166.0	72.7	64.1	62.5
NPL ratio	19.6	24.8	27.1	23.2	16.1
Coverage ratio 4/	49.8	48.5	51.4	51.7	51.8
Texas ratio 5/	93.0	115.0	120.0	106.0	93.4
CT1 ratio	16.4	14.7	13.3	15.5	14.5
Loan to deposit 6/	146.0	124.0	111.0	108.0	106.0
Net stable funding ratio	69.0	82.3	96.1	110.5	111.5
Liquidity coverage ratio	71.0	92.3	107.7	109.9	117.7

Source: Central Bank of Ireland; and IMF staff calculations.
1/ Indicators cover the three main domestic banks: Allied Irish Banks, Bank of Ireland, and Permanent TSB. Figures are based on Q4 data.
2/ Annual percent change in end period gross loans and advances.
3/ Based on quarterly data and excluding nonrecurrent items, as a share of average total assets.
4/ Provision stock to NPLs.
5/ NPLs to sum of provision stock and CT1 capital.
6/ Net loans to customer deposits, in percent.

25. Households' balance sheets remain susceptible to shocks. Irish household indebtedness continues to be high by international standards, and about one-tenth of mortgage holders were in negative equity at end-2015. The FSAP's analysis indicates that some mortgage holders are highly vulnerable, even those with loans that are currently performing. Specifically, households with high LTV ratios are more likely to default; and in an adverse scenario young borrowers and first-time buyers with variable-rate mortgages are particularly vulnerable (Annex VII).

Households' Debt
(Percent of gross disposable income)

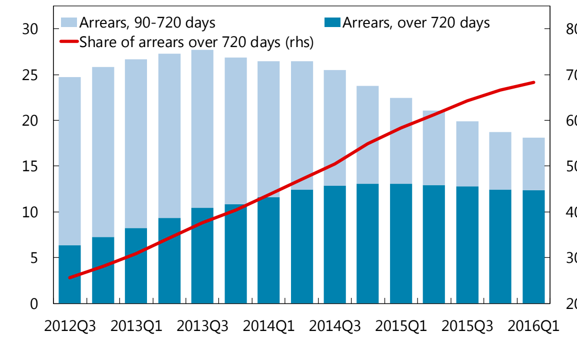


Source: BIS; Haver Analytics; National authorities; and IMF staff calculations.

- **Reducing household NPLs would help improve banks' balance sheets and reduce the drag on domestic demand.** The share of distressed mortgages has moderated, but deep arrears (over 720 days) have remained stubbornly high on the back of limited borrower-lender cooperation and lengthy legal proceedings. In line with the FSAP's recommendations, staff emphasized that continued efforts are needed to advance resolution of distressed mortgages with a particular focus on deep arrears. Staff, in this regard, underlined that further progress on loan restructuring—where feasible—should be complemented with efforts to ensure that the legal process supports timely enforcement of contracts and collateral.

Mortgages in Arrears

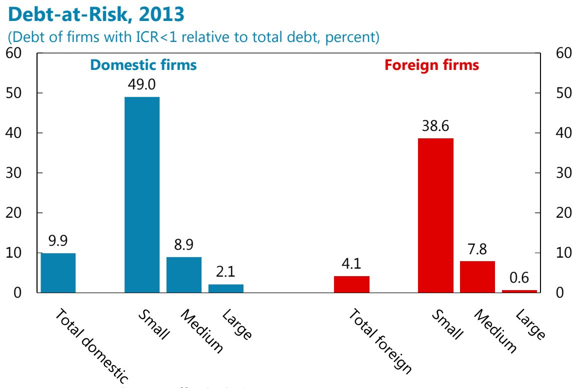
(Billions of euros) (Percent of total)



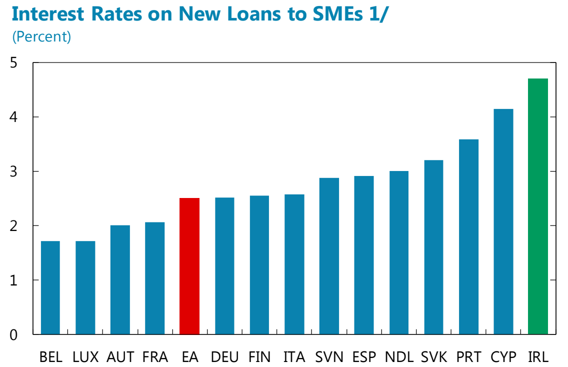
Source: Central Bank of Ireland.

- **Households' repayment capacity must be safeguarded through prudent mortgage lending.** Banks are increasingly extending fixed-rate mortgages, though the vast majority of the outstanding mortgages (90 percent of stock as of March 2016) is still at a variable rates. Staff welcomed these developments noting that fixed-rate products will reduce households' vulnerability to interest rate shocks, and stressed the need to ensure that banks adequately price borrowers' capacity to repay by using conservative assumptions on future interest rates and incomes, while taking into account the difficulties in enforcing collateral, the ongoing deleveraging process, and the legacy burden.

26. Corporate sector vulnerabilities need to be addressed to enhance the economy's resilience to shocks. Favorable demand conditions are supporting recovery in the nonfinancial corporate sector. However, with high NPLs (13 percent of corporate loans in 2016Q1) and tight credit conditions for SMEs, corporate vulnerabilities remain elevated. Furthermore, the ongoing deleveraging reflects demand side factors as well as supply side constraints faced by Irish SMEs, including higher borrowing costs and—albeit declining—elevated loan-application rejection rates compared to their European peers. The FSAP's analysis suggests that small firms have a higher share of risky debt than larger enterprises, and that a decline in profitability and an increase in interest rates would likely push many firms into a vulnerable state and increase new defaults (Annex VII). Staff therefore called for continued pace of corporate NPL resolution, including through loan restructuring for the most vulnerable, yet viable, firms. This would enhance the corporate sector's resilience to shocks and ability to support a durable expansion of economic activity. Staff also underlined that closing data gaps on firm-level balance sheets would help the Central Bank of Ireland detect and mitigate a buildup of new vulnerabilities at an early stage.



Sources: BvD; and IMF staff calculations.



Sources: ECB; and Haver Analytics.
1/ Amounts less or equal to €1 million. Data is as of April 2016.

27. The disposal of the state's shareholding in the banking system should continue. The two state-owned banks—AIB and PTSB—made progress toward privatization in 2015. Following successful equity issuance, PTSB reduced the government's stakes to 75 percent from 99 percent in April 2015, and covered the capital shortfall identified in the ECB's 2014 comprehensive assessment. AIB redeemed €1.4 billion of government's preference shares and converted the remainder (€2.1 billion) to ordinary shares in December 2015, thus clearing the way for additional equity sale. The government announced plans to reduce its stakes in AIB to 75 percent, and further lower its holdings in PTSB, but a specific timeline has yet to be set. Staff stressed that disposal should continue to further reduce public debt and contain contingent liabilities, but acknowledged that market conditions, including those resulting from the UK vote to leave the EU, could affect the process.

28. Further strengthening of banking supervision would help maximize the benefits of the Single Supervisory Mechanism (SSM). The FSAP observed that the financial regulatory framework has been significantly strengthened since the crisis and the Central Bank of Ireland has increased its resources and deployed them in a more proactive manner than in the past. The SSM, in which the ECB is responsible for direct supervision of the significant instititions that make up the bulk of the Irish banking system, is working well: the Joint Supervisory Teams (JSTs) for Irish banks operate effectively, and SSM methodologies, processes, and procedures are fully operational. In line with the FSAP's recommendations, staff underlined that the recent supervisory gains need to be preserved, particularly in light of the possible changes to the banking industry landscape and business models. Staff encouraged supervisors to continue enhancing their already considerable stress testing capacity, which will help challenge commercial banks' risk modeling. In view of the high turnover of supervisory staff, review of personel policies would be appropriate to attract and retain experienced supervisors.

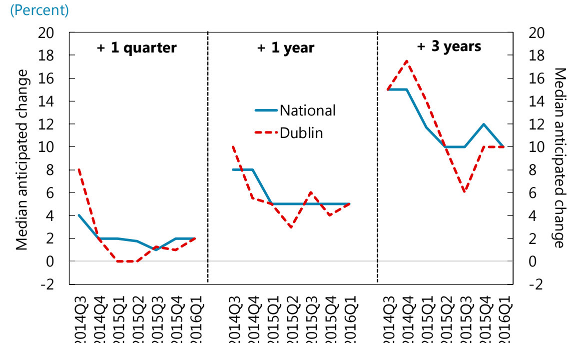
Authorities' views

29. The authorities agreed that the recovery in the banking system is ongoing, yet challenges persist. They noted that new lending is resuming and is helping to restore net interest margins. However, continued system deleveraging, the low interest rate environment, and remaining legacy issues present significant headwinds. The authorities concurred that lending rates should adequately price these factors, as well as the risks associated with the Irish economy, including the difficulties to realize collateral of distressed borrowers. The authorities pointed to the solid progress made in the workout of impaired loans across all portfolios and stressed that the resolution of the remaining NPLs is a key supervisory priority. In this regard, they indicated continued implementation of the Distress Credit Strategy, which sets out supervisory expectations for the resolution of mortgage arrears on a bank-by-bank basis while requiring banks to set quarterly resolution targets for their commercial/corporate books. Furthermore, the forthcoming introduction of a government funded scheme to allow distressed mortgage borrowers access to legal and financial advice should help increase borrower-creditor engagement. To accelerate the legal proceedings, the Programme for Government proposes to establish a special court to expeditiously handle mortgage arrears and other personal insolvency cases, with designated judges that will ensure consistent rulings. The authorities broadly agreed with the FSAP's recommendations, and noted their plans to further develop their stress testing capacity, reduce data gaps, and engage with the various stakeholders on personnel policies to retain experienced staff. Finally, disposal of state shareholding in the banks will be pursued with a view to maximizing the return to the state.

Mitigating boom-bust cycles

30. Macroprudential measures should be maintained. The measures implemented in 2015 were designed to increase the resilience of banks and households to property market swings, thus reducing the risk of future bank credit and house price spiral. In addition, it appears that the transmission channels have been working, particularly via price expectations. Staff argued—in line with the FSAP's recommendations—that the Central Bank of Ireland should retain the LTI and LTV limits as a permanent feature of the mortgage market and supported the intent to periodically assess their impact and effectiveness. Staff stressed the importance of converting the LTI limit to a debt-to-income (DTI) limit, which better captures the borrowers' repayment capacity, once the Central Credit Register (CCR) becomes fully operational.

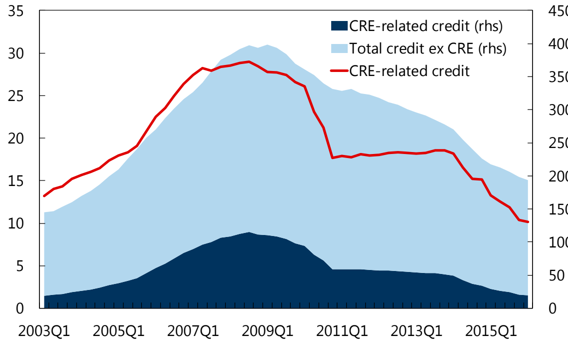
Expectations of Changes in Residential House Prices
(Percent)



Source: Central Bank of Ireland (Macro Financial Review, 2016:I).

31. A potential buildup of new imbalances in the CRE market needs to be prevented. Although CRE prices have surged since 2013, the buildup of new vulnerabilities in domestic banks appears limited to date, as demand is mostly funded by foreign investors and domestic equity, such as real estate investment trusts, compared to bank funding in the previous cycle (see Selected Issues on Commercial Real Estate and the Supervisory Response). New CRE lending is increasing from low levels, but the credit stock continues to decline. FSAP's analysis of CRE prices provides inconclusive results, ranging between an overvaluation of 10 percent to an undervaluation of 8 percent, depending on the methodology and the choice of sample period (Annex VIII). In line with the FSAP's recommendations, staff urged the authorities to closely monitor CRE market developments, address data gaps, ensure proper underwriting standards and property valuation both sector wide and in specific banks, and activate policy tools if early signals suggest a buildup of new imbalances. In this regard, staff welcomed the authorities' recent initiative to establish a new comprehensive CRE market database.

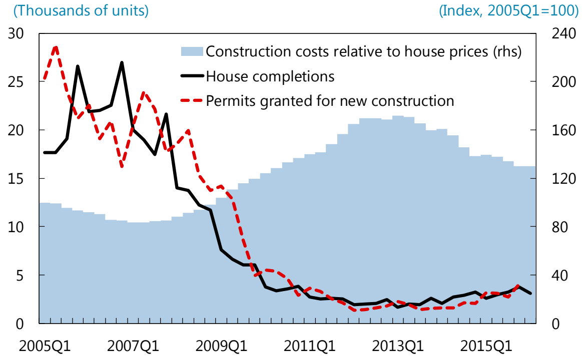
Irish Private Sector Credit and CRE-related Credit



Source: Central Bank of Ireland.

32. Boosting the housing supply would help mitigate property price and rent pressures. The sluggish construction activity in recent years reflects the sector's downsizing after the bursting of the property market bubble in 2008-09 and the ensuing limited access to finance for companies. High construction costs due to strict planning requirements have also been a factor. In response to mounting pressures in the housing market, the government introduced a package of measures in November 2015, including rebates for housing construction schemes that meet certain criteria, and new planning guidelines, which seek to reduce the building costs.[16] Additionally, the National Asset Management Agency (NAMA), within its mandate, is to fund the delivery of 20,000 residential units by 2020. Staff stressed that additional policy actions should help expedite new construction, and welcomed the authorities' intent to publish an Action Plan for Housing over the summer.

Housing Market Indicators



Source: Haver Analytics.

Authorities' view

33. The authorities confirmed their commitment to reduce the risk of a boom-bust cycle. The Central Bank of Ireland intends to maintain the macroprudential measures in place and launched the first annual review of their impact and effectiveness, to be completed by November 2016. The authorities concurred that transitioning from LTI to DTI limit would serve as a better instrument, but noted that the recalibration and implementation would require careful assessment of the data submitted to the CCR once it becomes operational. With regard to the CRE market, the

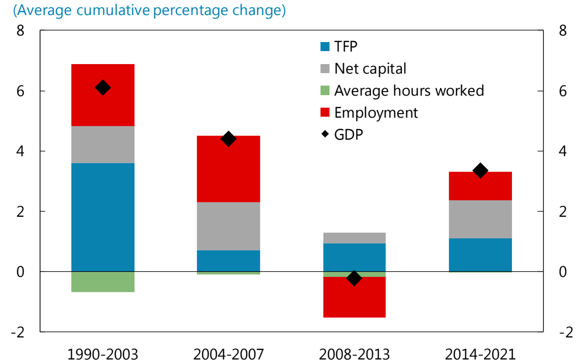
[16] Estimates by the Department of Environment suggests that the updated planning guidelines will lead to a cost reduction of about €20,000 per unit or more on top of other cost savings that have been delivered through reductions in local authority development charges.

authorities noted that the continued reduction in banks' exposures to this segment limits the potential risks to the domestic economy. Furthermore, construction activity, which has responded to improving fundamentals, suggests that a large supply is in the pipeline, which will mitigate market pressures going forward. The authorities are working to reduce data gaps and closely monitor CRE developments. They stressed that resolving the housing shortage is of high priority. In particular, the forthcoming Action Plan for Housing aims at delivering 25,000 new houses per year by the end of this decade to better align demand and supply. In this context, they noted their intent to establish an infrastructure fund for local authorities to help develop the supply of new housing, and shorten the application process for new building permits. Additionally, the government has recently introduced a vacant site levy that will become effective by 2018 to deter land hoarding.

C. Achieving Sustainable Growth and Increasing Inclusiveness

34. Strong and sustainable economic growth is needed to reduce vulnerabilities. Staff project potential GDP growth to gradually stabilize at nearly 3 percent over the medium term, mainly due to the partly-cyclical rise in labor participation and capital accumulation largely driven by the multinationals' activity. Total factor productivity (TFP) growth, however, is projected to remain modest just around one percent under current policies, falling short of the robust increases observed in the late 1990s and early 2000s.

Growth Accounting
(Average cumulative percentage change)



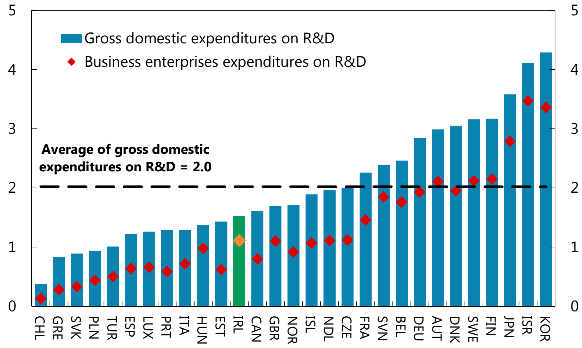
Sources: Central Statistics Office; Eurostat; Haver Analytics; and IMF staff calculations.

35. Addressing impediments to TFP growth would boost Ireland's economic potential. Many advanced economies experienced TFP moderation, possibly due to spillovers from the US productivity slowdown and a resource shift toward lower-productivity sectors.[17] Staff analysis of Ireland (see Selected Issues on Firm-Level Productivity and its Determinants: The Irish Case) indicates that, in recent years, TFP growth of SMEs has lagged behind that of large firms, and that medium and large-sized foreign-owned firms outperformed their domestic peers. Moreover, the analysis suggests that domestic firm-level factors, including limited access to finance, weak financial soundness, and low research and development (R&D) activity, may have also contributed to the slowdown in TFP growth. Staff encouraged the authorities to alleviate these potential impediments by broadening financing options for SMEs and advancing NPL resolution. As gross domestic expenditure on R&D is mainly financed by large enterprises and is below the OECD average, staff also stressed the need to encourage higher innovation activities among domestic SMEs, including

[17] Chapter 3, 2015 April WEO.

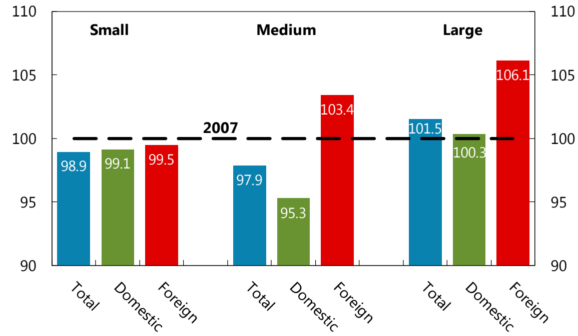
through greater direct public sector's support and by enhancing the partnerships of SMEs with education institutions.[18, 19]

Expenditures on Research & Development, 2014
(Percent of GDP)



Source: OECD.

TFP by Firm Size and Ownership, 2014
(Median, 2007=100)



Sources: BvD; and IMF staff calculations.

36. **Job-rich growth would foster inclusion.** Despite the robust recovery, some parts of the population have yet to feel its benefits. While the labor force is well educated, skill mismatches are relatively high in some segments, and youth and long-term unemployment rates remain elevated, the latter particularly among adults with lower educational attainment.[20] Furthermore, female labor force participation is among the lowest in the EU. Staff therefore advocated strengthening incentives for women to enter the labor market, such as providing more affordable and high-quality child care and reducing the high marginal income tax rates for second earners. To increase the overall labor supply and boost youth employment, staff suggested upgrading labor skills and reducing skill mismatches by strengthening labor activation policies and expanding technical and vocational programs (see also Selected Issues on Public Expenditure Efficiency in Ireland).

Authorities' view

37. **The authorities agreed with the need to enhance productivity and job creation in order to support sustainable and inclusive growth.** They noted the recently-introduced policy initiatives to alleviate difficulties in SMEs' access to finance, including the establishment of the Strategic Banking Corporation of Ireland in 2015, which provides low cost funding for SMEs. Furthermore, the expected implementation of the CCR would reduce firms' informational asymmetry and hence the risk premia charged by banks. They acknowledged that higher public spending on R&D would enhance the business sector's competitiveness and innovation capacity. They remain committed to increase Ireland's R&D intensity, improve SMEs' access to finance for innovation, develop research collaboration between enterprises and the public sector, and tailor support to meet enterprise

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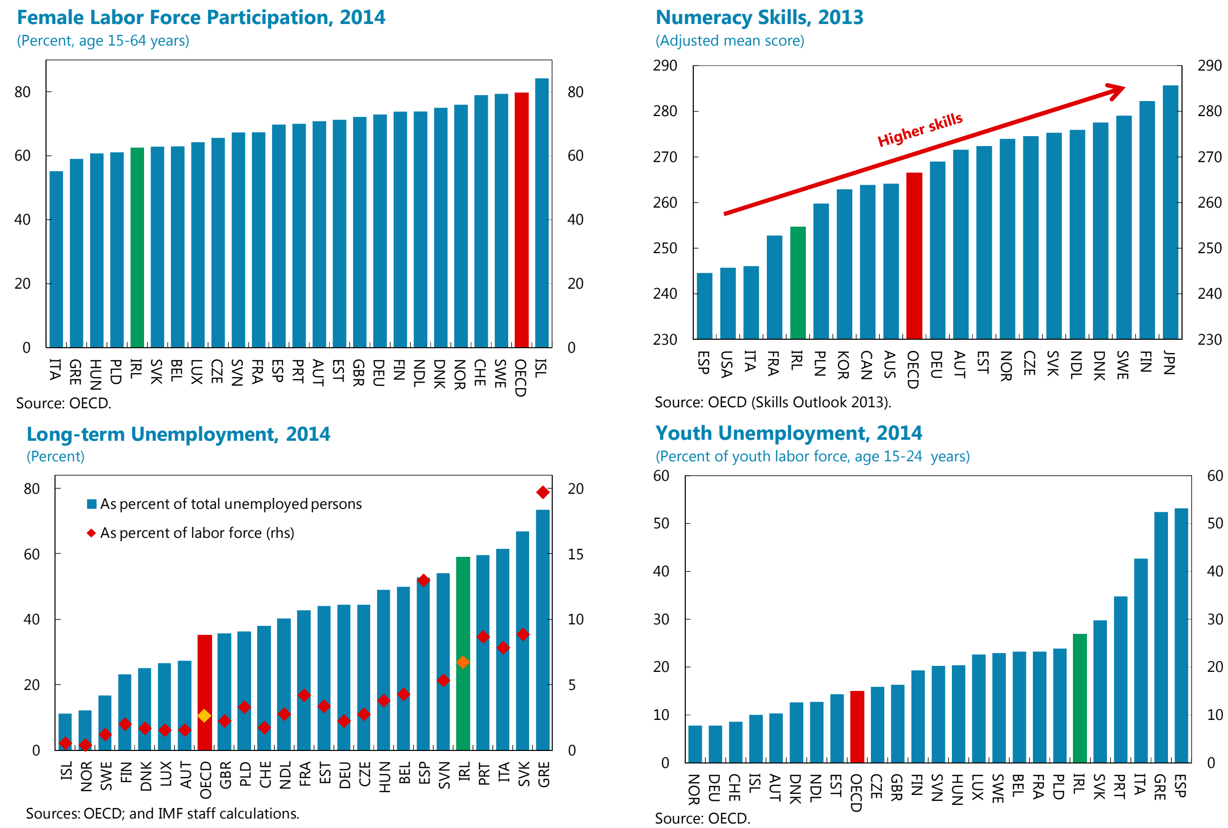
[18] The share of budget funding in gross domestic expenditures on R&D declined to 26 percent in 2014 from about 34 percent in 2008, while government's R&D expenditures per capita fell by 26 percent in nominal terms at the same time.

[19] Public support for Irish firms' R&D is mainly through tax credits, but young firms lacking upfront funds to start innovative projects may not benefit from it.

[20] The OECD survey 2015 Survey of Adult Skills (PIAAC) suggests that, despite improvements in recent years, adults in Ireland have lower skills than other OECD countries, especially regarding numeracy and literacy.

needs, as outlined in the recently published Innovation 2020 strategy report. The authorities stressed their intent to foster reforms to improve the affordability and quality of child care. As outlined in their Action Plan for Jobs for 2016, efforts are being made to step up the skill supply by helping qualified workers to come to Ireland, and by establishing regional skills fora as a mechanism for enterprises and providers of education and training to work together in building the supply of skills for their regions.

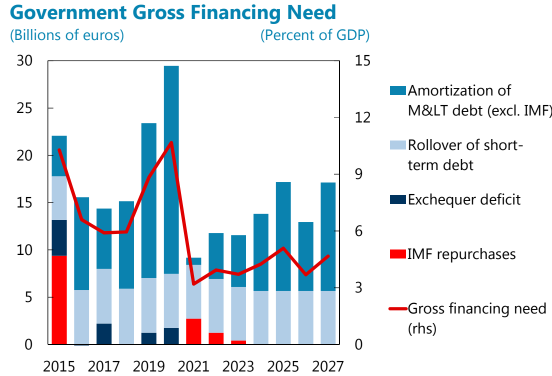
Ireland: Labor Market Conditions



D. Post-program Monitoring and Capacity to Repay the Fund

38. **Ireland's capacity to repay the Fund has strengthened further on the back of strong economic and fiscal performance, as well as favorable market funding conditions.** Ireland has raised €13.4 billion in long-term bonds in 2015 and a further €6 billion in the first half of 2016. Revenue over-performance helped increase the government's cash balance to about €8 billion as of end-June, 2016—almost twice the outstanding stock of Fund credit. The ECB's QE is proceeding as planned at secondary market

Government Gross Financing Need



Source: IMF staff calculations and projections.

purchases of about €1.1 billion a month, which is broadly equivalent to staff estimates of average monthly gross financing needs in 2016-17.

39. Medium-term financing needs appear manageable, and the falling public debt burden reduces risks going forward. Strong growth and fiscal performance have dramatically lowered the baseline public debt path, where further reduction is predicated on the authorities' continued commitment to fiscal prudence. Gross public debt fell to about 94 percent of GDP by end-2015, and is expected to decline below 90 percent by end-2016—five years earlier than anticipated at the time of the 2015 Article IV consultation. Ireland's funding strategy has significantly smoothed medium-term gross financing requirements, and it is likely that the projected hump in 2020 will be dealt with well in advance through debt management operations. Finally, the 2021–23 period—when the remaining liabilities to the IMF fall due—has relatively modest gross financing needs, further lowering risks to the Fund.

STAFF APPRAISAL

40. Ireland's economic rebound has been exceptional, but the recovery is incomplete. Robust domestic demand, particularly investment, and solid exports have supported the broad-based expansion. Unemployment has been steadily declining, and inflation has been subdued. Public finances are strengthening and the government's debt-to-GDP ratio continues on a downward trend. Yet the recovery remains incomplete. Employment and consumption are still below their pre-crisis levels. Crisis legacies, such as elevated public and private debt burdens and a high stock of banks' nonperforming loans, leave the economy vulnerable to shocks. The outlook remains favorable, but risks—mainly external—are tilted to the downside, especially after the UK vote to leave the EU.

41. Policies should strengthen further the foundations for sustainable and inclusive long-term growth. There is a need to lock in recent gains and build upon them while tackling the lingering crisis legacies, rebuilding policy buffers, and bolstering the resilience of the economy to shocks. At the same time, a recurrence of another boom-bust economic cycle needs to be avoided to allow strong, durable, and broad-based growth that will benefit all Irish people.

42. Continued steady reduction in public debt would increase the policy buffers in the event of potential negative shocks. Ireland has established a solid track record of fiscal rectitude and exited the Excessive Deficit Procedure. Building on this progress, and in light of Ireland's high degree of economic volatility, adequate fiscal room for maneuver needs to be created to deal with possible adverse shocks. In absence of major economic repercussions from the UK vote to leave the EU, the policies outlined in the recent Summer Economic Statement appear broadly consistent with the attainment of the MTO of a structural deficit of 0.5 percent of GDP by 2018, and further improvement thereafter. This would prevent additional fiscal stimulus when economic activity is projected to remain above potential and allow general government debt to decline significantly. Should the repercussions from the UK vote to leave the EU be larger than anticipated, the authorities should stand ready to take remedial actions, such as a countercyclical fiscal policy together with central banks' commitment to backstop liquidity in euros and other currencies—if and when needed.

43. **Fiscal policy can be more supportive of job-rich growth.** A rebalancing of the tax mix away from distortionary direct taxes, including by merging the universal social charge into a broader income tax with lower rates for below-median wage earners, would help reduce the tax burden on middle-income households, foster female labor force participation, and reduce welfare-traps for low-skilled workers. Implementation of a uniform VAT rate and faster scaling up of the property tax would compensate for lower revenues from direct taxes. Regressivity arising from these changes could be assuaged by means-tested transfers to low-income households. Enhancing spending efficiency, particularly in the health sector, would improve delivery of public services, while a better targeting of social transfers would improve inter-generational fairness. Capital expenditure, particularly in infrastructure and R&D, should be increased to safeguard Ireland's competitiveness.

44. **Recovery in the banking system is progressing, but challenges persist.** Although banks' financial soundness has improved in recent years, sensitivity analyses under the FSAP's adverse macroeconomic scenario point to vulnerabilities amplified by crisis legacies. Furthermore, the fallout from the UK vote to leave the EU could undermine banks' profitability and balance sheet repair. In the current low-interest environment, supervisors need to be even more vigilant to ensure that banks' profit seeking is supported by appropriate risk management. Mortgage lending rates should adequately reflect market conditions, legacy burden, and credit risk, including difficulties in realizing collateral. Disposal of the government's stakes in the banking system should continue. This would further reduce public debt.

45. **The resilience of the nonfinancial private sector to shocks needs to be bolstered further.** Intensified supervisory efforts should continue to resolve nonperforming loans, supported by the legal process to incentivize cooperation between borrowers and lenders. Further restructuring of distressed loans to the most vulnerable, but viable, firms would support a durable expansion of economic activity and reduce the corporate sector's vulnerabilities. Closing data gaps on firm level balance sheets would enable detection and mitigation of a buildup of new vulnerabilities. Continued care is needed to ensure that provisions remain adequate.

46. **A potential buildup of new imbalances in the property market should be prevented**. Macroprudential limits on mortgage lending should be maintained as a permanent feature of the mortgage market to safeguard the resilience of banks and households against shocks. The Central Bank of Ireland intent to periodically assess the impact and effectiveness of these measures is welcome. Once the Central Credit Register becomes operational, the loan-to-income limit should be replaced with a debt-to-income limit, which better captures borrowers' repayment capacity. As housing supply remains constrained, additional policy actions should help expedite new construction. Demand pressures in the commercial real estate market need to be closely monitored and policy tools activated if risks to financial stability emerge.

47. **Residual structural weaknesses should be addressed to support a robust and inclusive medium-term growth and job creation.** Policies should encourage broadening of the financing

options available to SMEs and increasing direct public sector support of their innovation activities, including through closer partnerships with education institutions. Furthermore, enhancing labor activation policies and expanding technical and vocational programs would help retool skills and increase the likelihood of finding employment. Policies to address the high cost of child care and its variable quality, and reduce high marginal income tax rates on second earners would strengthen incentives for women to enter the labor market.

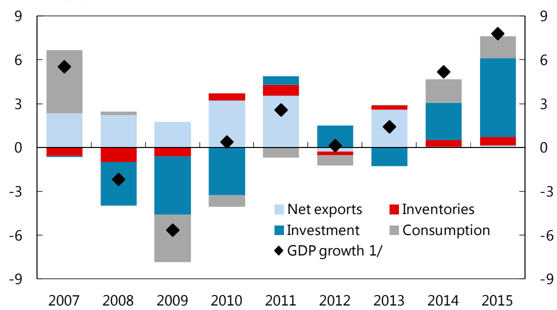
48. It is recommended that the next Article IV consultation with Ireland be held on the standard 12-month cycle.

Figure 1. Ireland: Real Sector and Inflation Indicators, 2006–16

GDP grew by 7.8 percent in 2015 driven by a robust recovery of domestic demand, particularly investment.

Contributions to Real GDP Growth

(Percent y/y)

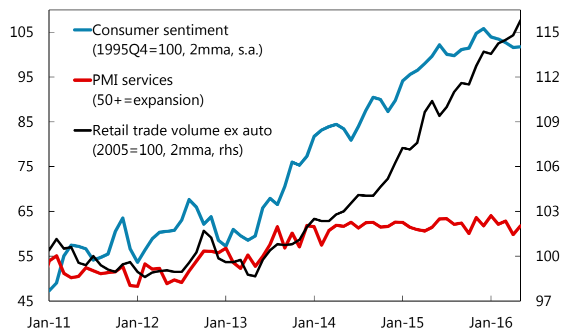


Sources: Central Statistics Office; and IMF staff calculations.

1/ GDP growth accounts for statistical discrepancy as well.

Strong consumer confidence has supported the rapidly rising retail sales.

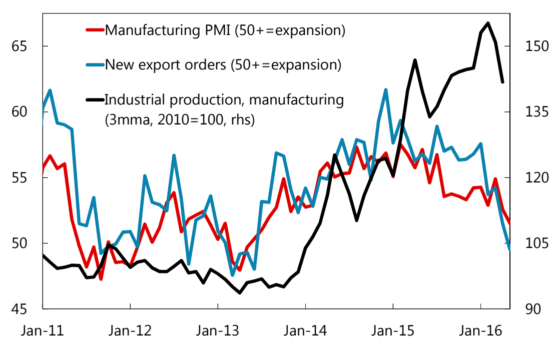
Retail Trade and Sentiment Indicators



Sources: Central Statistics Office; ESRI; Haver Analytics; and NCB Stockbrokers/Markit.

The sharp expansion of industrial production, export orders, and manufacturing have slowed down.

Manufacturing Indicators

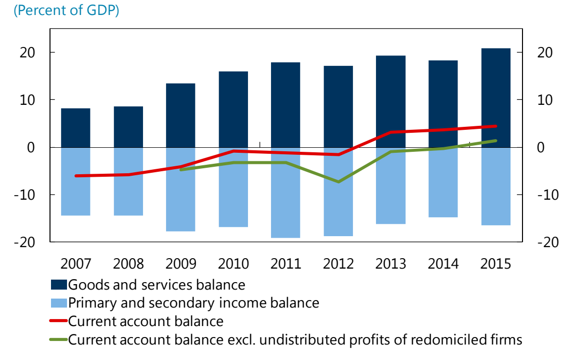


Sources: Central Statistics Office; NCB Stockbrokers/Markit; and Haver Analytics.

The current account excluding estimated profits of re-domiciled firms was in a modest surplus in 2015.

Current Account Balance Composition

(Percent of GDP)

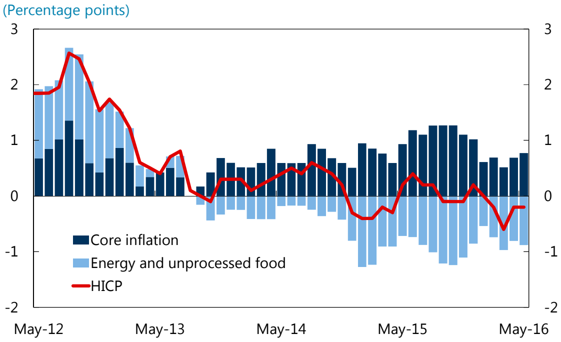


Sources: Central Statistics Office; Haver Analytics; and IMF staff estimates.

Inflation was tempered by energy and food prices.

Contribution to Annual HICP Inflation

(Percentage points)

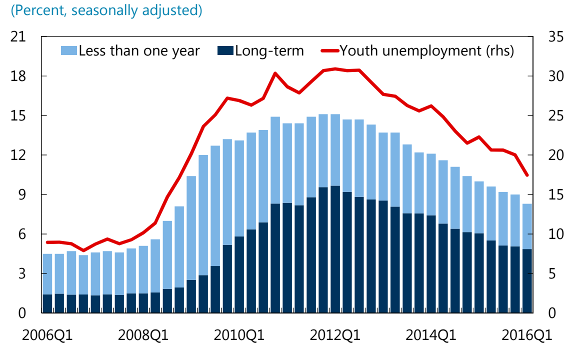


Sources: Central Statistics Office; Eurostat; and IMF staff calculations.

Unemployment continued to decline.

Unemployment Rates

(Percent, seasonally adjusted)

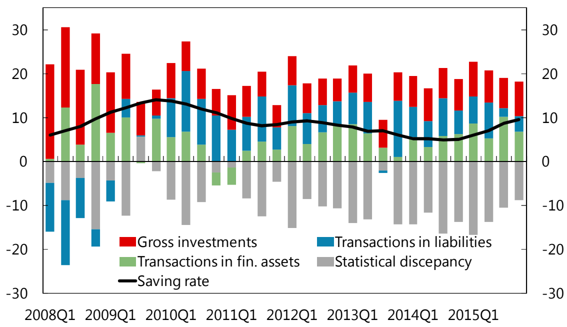


Sources: Central Statistics Office; Haver Analytics; and IMF staff calculations.

Figure 2. Ireland: Household Finance and Property Market Developments, 1995–2016

Household savings somewhat increased on the back of higher disposable income.

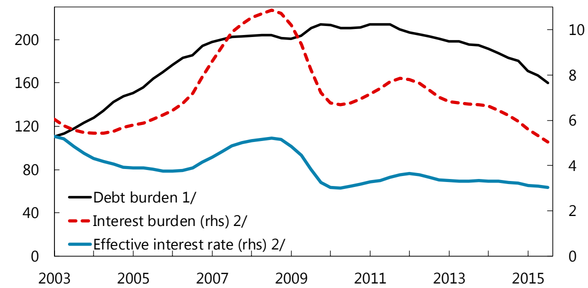
Decomposition of Household Savings
(Percent of gross disposable income)



Sources: Central Bank of Ireland; Central Statistics Office; and IMF staff calculations.

Debt burden and interest payments continue to fall.

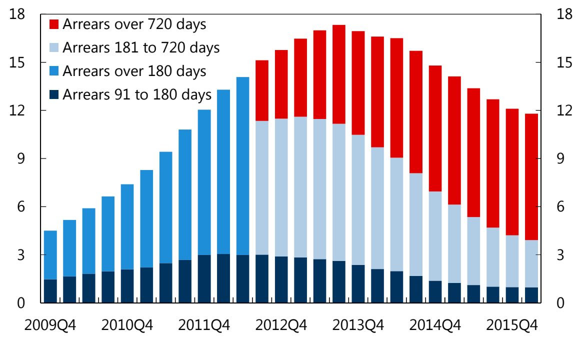
Household Debt and Interest Payments
(Percent of gross disposable income)



Sources: Central Bank of Ireland; Haver Analytics; and IMF staff calculations.
1/ Total household loans in percent of 4 quarter gross disposable income.
2/ 4 quarter interest payments (excl. FISIM adjustment) in percent of 4-quarter gross disposable income or previous quarter's total household loans, respectively.

The share of mortgages for primary dwellings in arrears continues to decline, except for arrears over 720 days.

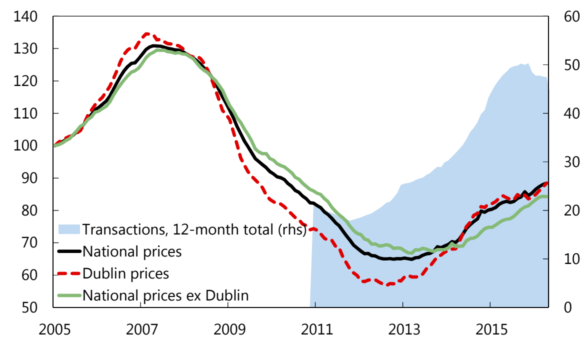
Mortgages in Arrears on Primary Dwellings
(Percent of total mortgage value)



Source: Central Bank of Ireland.

The residential property market is reviving, particularly in Dublin.

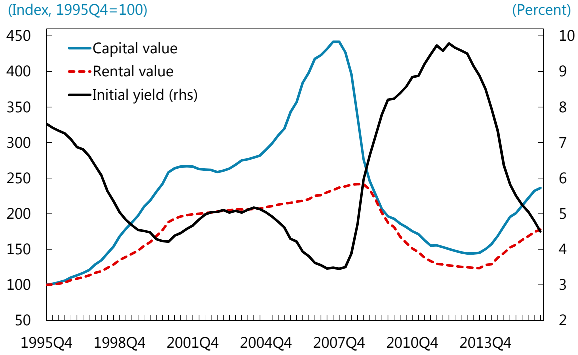
Residential Property Prices and Transactions
(2005M1=100, s.a.) (Thousands)



Sources: CSO; Property Services Regulatory Authority; and IMF staff calculations.

Commercial property prices and rents rose sharply from a low base, but remained well below the pre-crisis peaks...

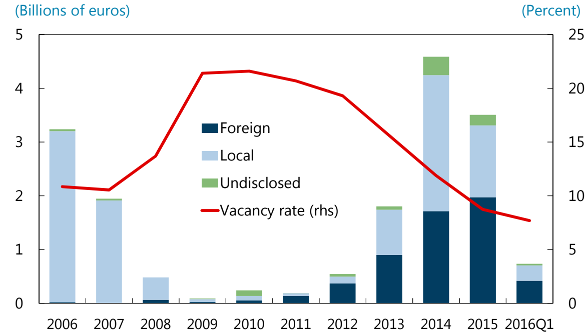
Commercial Real Estate Value Indices and Initial Yield
(Index, 1995Q4=100) (Percent)



Source: MSCI/Investment Property Databank.

...and the vacancy rate has declined further in 2015, with more than half of the transactions made by non-residents.

Commercial Property Transactions and Vacancies 1/
(Billions of euros) (Percent)

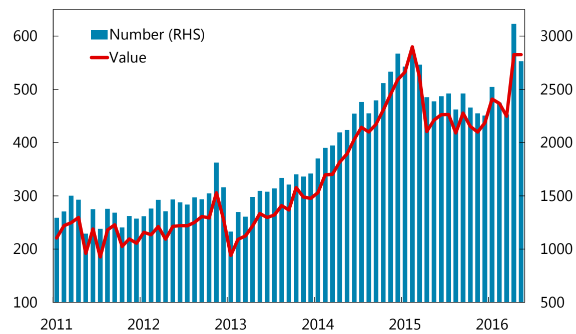


Source: CBRE Ireland Research Ireland.
1/ Relates to individual transactions worth of at least €1 mln.

Figure 3. Ireland: Housing Developments, 1990–2016

Mortgage approvals temporarily moderated with the introduction of the new macroprudential measures…

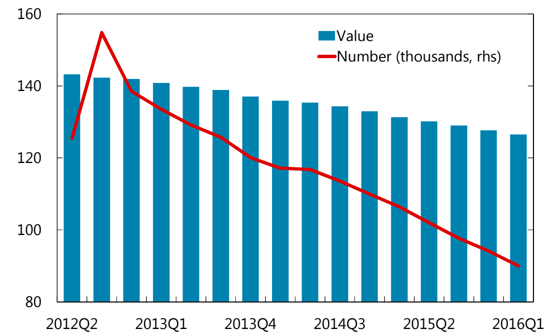
Mortgage Approvals
(Millions of euros)



Sources: Banking & Payments Federation Ireland; and Haver Analytics.

…and the stock of mortgage loans continues to fall.

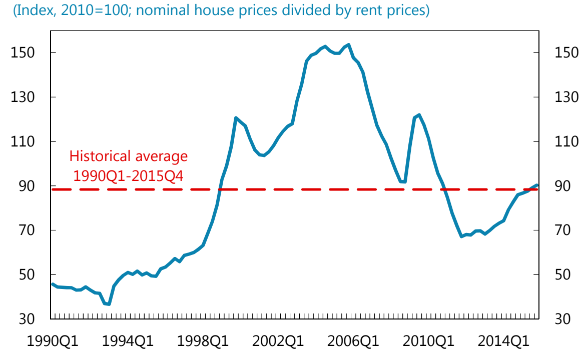
Number and Value of Residential Mortgage Loans
(Billions of euros)



Sources: Central Bank of Ireland; and Haver Analytics.

Price-to-rent ratio is at its historical average…

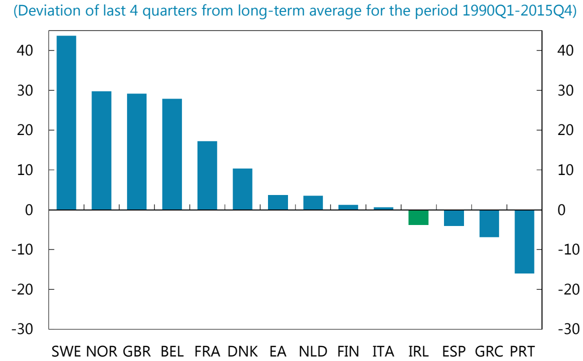
Price-to-Rent Ratio
(Index, 2010=100; nominal house prices divided by rent prices)



Source: OECD; and IMF staff calculations.

…and so is price-to-income ratio.

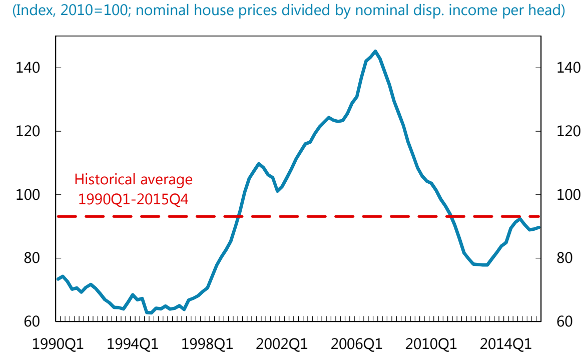
Price-to-Income Ratio
(Deviation of last 4 quarters from long-term average for the period 1990Q1-2015Q4)



Sources: OECD; and IMF staff calculations.

House prices have risen faster than income recently…

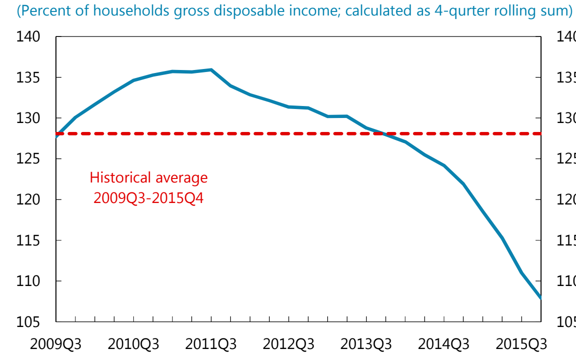
Price-to-Income Ratio
(Index, 2010=100; nominal house prices divided by nominal disp. income per head)



Source: OECD; and IMF staff calculations.

…though affordability continues to improve.

Mortgage Value (PDH)
(Percent of households gross disposable income; calculated as 4-qurter rolling sum)



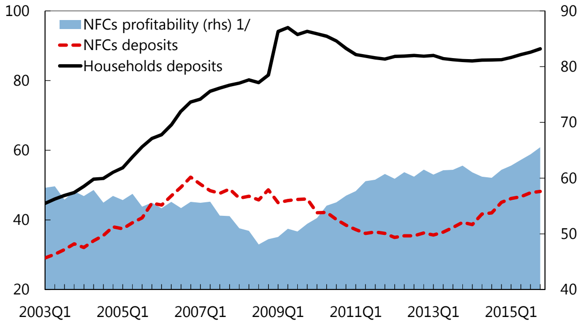
Sources: Central Bank of Ireland; Central Statistics Office; and Haver Analytics.

Figure 4. Ireland: Credit and Deposit Developments, 2003–16

While household deposits remained stable, enterprise deposits are up following strong corporate profitability …

Irish Private Residents Deposits and NFCs Profitability

(Billions of euros) (Percent)

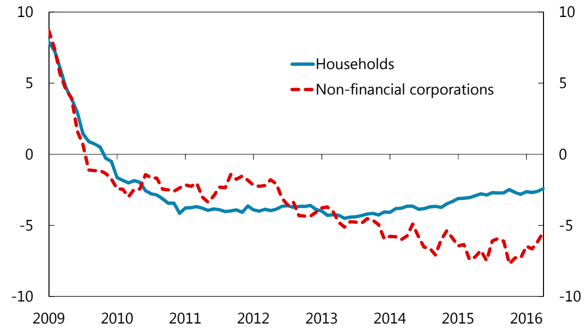


Sources: Central Bank of Ireland; and Central Statistics Office.
1/ NFCs' gross operating surplus to gross value added (National Accounts).

…which supported further deleveraging of corporations and resulted in a continued credit contraction.

Loans Outstanding to Irish Residents

(Percent change y/y)

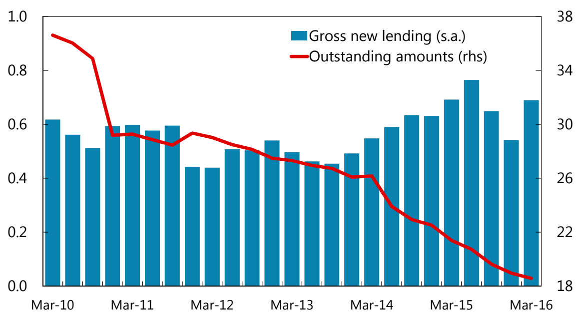


Source: Central Bank of Ireland.

Deleveraging is evident in the SME sector, where redemptions continue to exceed new credit.

Outstanding SME Credit 1/

(Billions of euros)

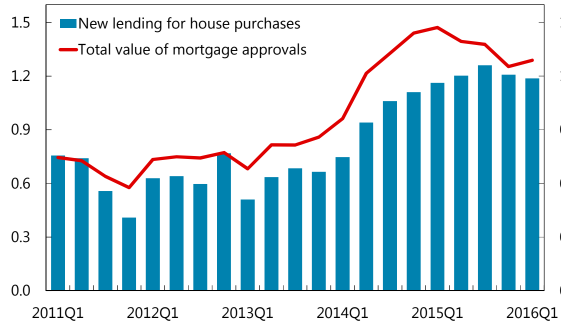


Source: Central Bank of Ireland.
1/ All resident credit institutions, excluding real estate and financial intermediation.

New mortgage lending has moderated following the introduction of macroprudential measures in 2015Q1.

Housing Loans and Mortgage Approvals

(Billions of euros, seasonally adjusted)

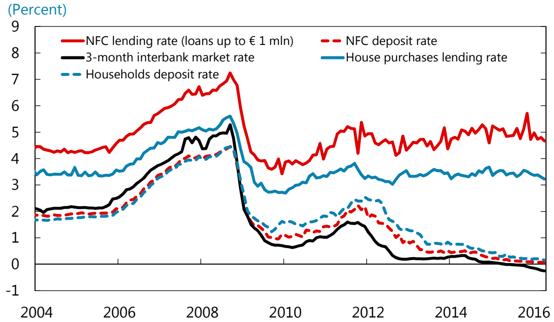


Source: Banking & Payments Federation Ireland; and IMF staff calculations.

Low deposit rates and broadly stable lending rates…

Median Lending and Deposit Rates, New Business 1/

(Percent)

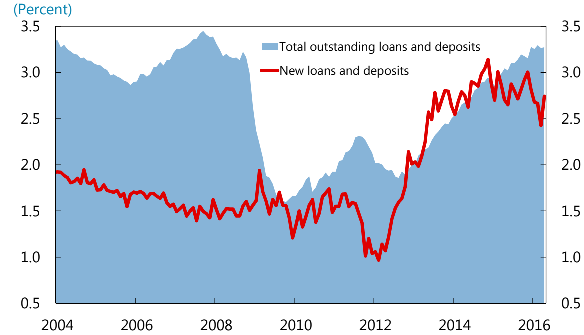


Source: Central Bank of Ireland.
1/ Data relate to new business conducted through resident offices of a sample of banks and include IBRC. Last observation Jan-2016.

…continue to boost banks' interest margins.

Interest Rate Margins Between Loans and Deposits 1/

(Percent)

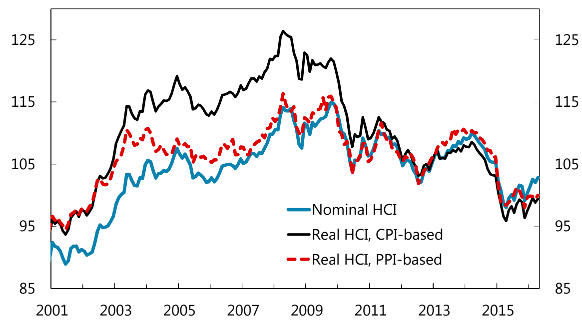


Source: Central Bank of Ireland.
1/ Weighted average loan rate minus weighted average deposit rate.

Figure 5. Ireland: Competitiveness Indicators, 1999–2016

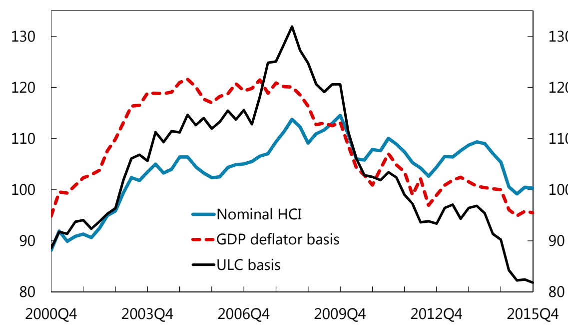
Competitiveness indicators over the last year have improved broadly in line with the euro exchange rate depreciation.

Harmonized Competitiveness Indicators (Monthly)
(1999Q1=100)



Sources: Central Bank of Ireland; and Haver Analytics.

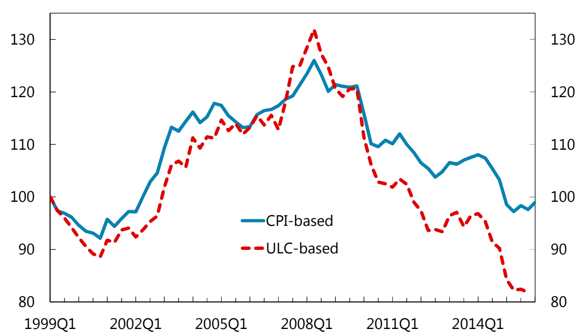
Harmonized Competitiveness Indicators (Quarterly)
(1999Q1=100)



Sources: Central Bank of Ireland; and Haver Analytics.

Part of the earlier improvement in competitiveness reflected a shift to higher value-added sectors.

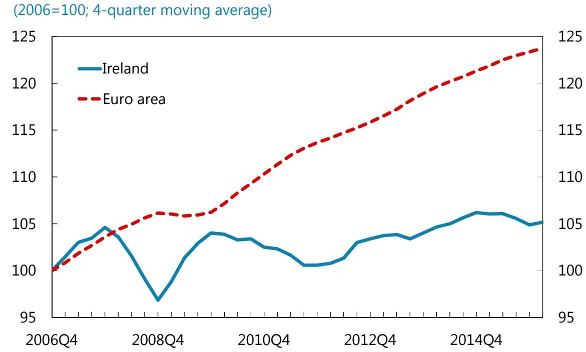
Real Effective Exchange Rates
(Index, 1999Q1=100)



Sources: Central Bank of Ireland; and Haver Analytics.

Wages in the manufacturing sector have increased at a slower pace than in the euro area.

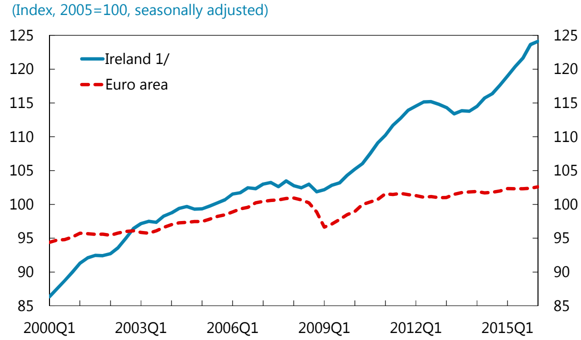
Hourly Labor Costs in Manufacturing
(2006=100; 4-quarter moving average)



Sources: Central Statistics Office; Eurostat; Haver Analytics; and IMF staff calculations.

Labor productivity continues to outpace that of the euro area.

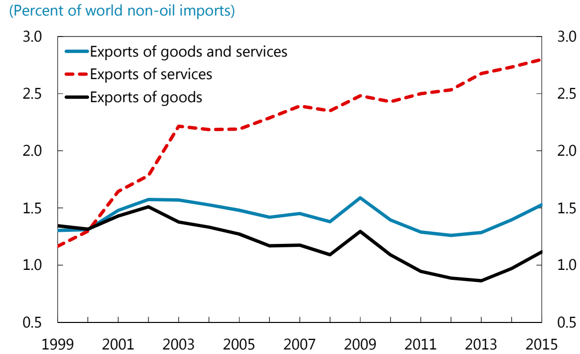
Real Labor Productivity
(Index, 2005=100, seasonally adjusted)



Source: Central Statistics Office; ECB; Haver Analytics; and IMF staff calculations.
1/ Calculated as real output per person employed.

Ireland's overall export market share rose in 2015.

Export Shares
(Percent of world non-oil imports)



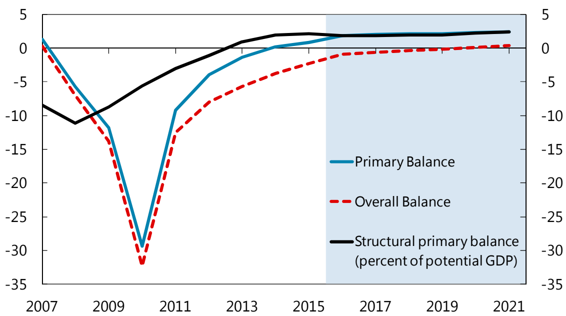
Source: IMF staff calculations.

Figure 6. Ireland: General Government Finances, 2007–21

The headline balance is projected to improve over the medium term.

Headline and Structural Balances 1/

(Percent of GDP, unless otherwise indicated)

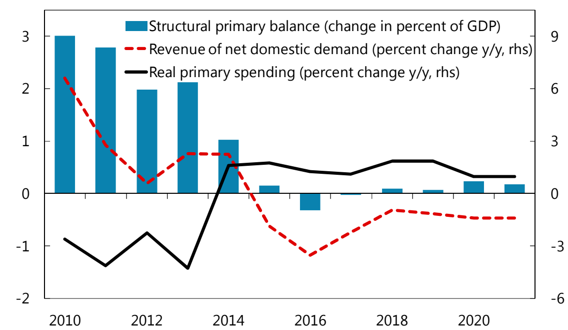


Sources: Department of Finance; and IMF staff projections.

1/ Excl. bank support costs. Structural primary balance also excludes one-off revenue and expenditure items.

After strong fiscal adjustment in 2009–14, reflecting real spending cuts and revenue-enhancing measures, adjustment has moderated.

Fiscal Adjustment: Pace and Sources

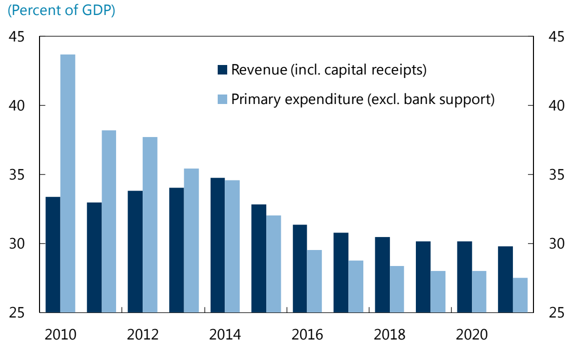


Sources: Department of Finance; and IMF staff projections.

The primary surplus is projected to increase marginally driven by further declines in spending to GDP.

Revenue and Primary Expenditure

(Percent of GDP)

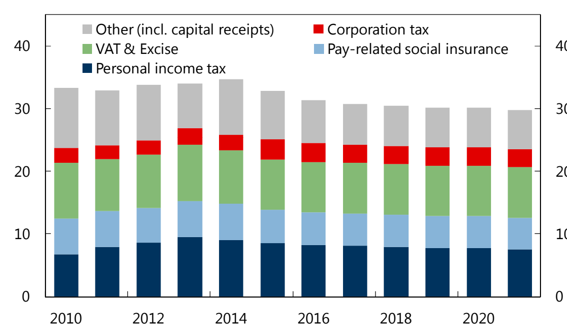


Sources: Department of Finance; and IMF staff projections.

With domestic demand increasing less than GDP, revenues are projected to decline by about 3½ percentage points of GDP from 2015 to 2021.

Revenue Composition

(Percent of GDP)

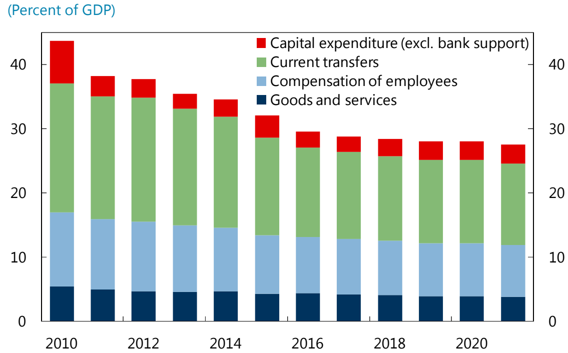


Sources: Department of Finance; and IMF staff projections.

Primary expenditures are projected to fall by 5 percentage points of GDP from 2015 to 2021.

Primary Expenditure Components

(Percent of GDP)

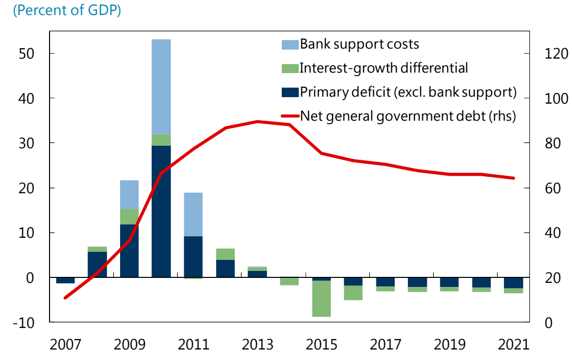


Sources: Department of Finance; and IMF staff projections.

The strong 2015 growth-interest differential will contribute less to debt reduction going forward.

Sources of Increase in Net Debt-to-GDP Ratio

(Percent of GDP)

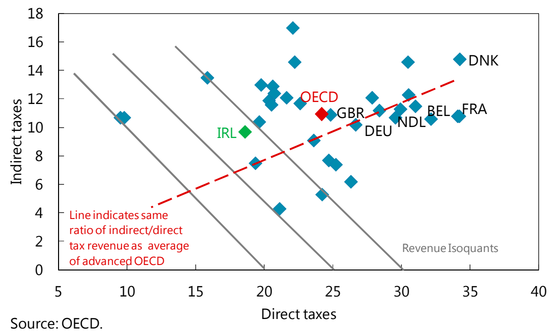


Sources: Department of Finance; and IMF staff projections.

Figure 7. Ireland: Key Features of the Tax System

Ireland ranks among the "least taxing" OECD countries.

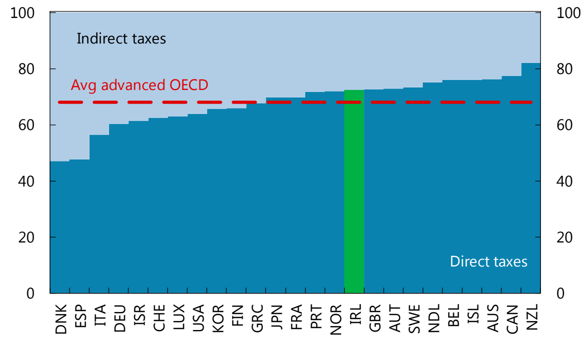
Direct and Indirect Taxes, 2013
(Percent of GDP) 1/



Source: OECD.
1/ Includes employer contributions to private pension schemes.

Direct taxation is the dominant source of revenues.

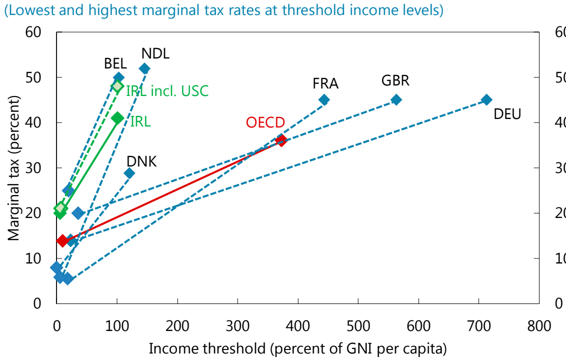
Direct and Indirect Taxes, 2013
(Percent of tax revenue)



Sources: OECD; and IMF staff calculations.

Personal income taxes are very progressive with high top marginal tax rates at low income levels.

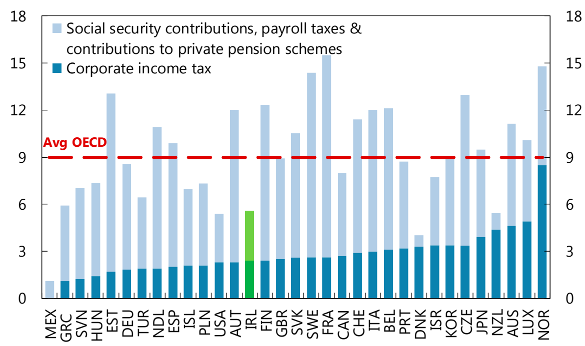
Income Tax Progressivity, 2013
(Lowest and highest marginal tax rates at threshold income levels)



Source: OECD.

Corporate taxation is low against most OECD peers

Taxation of Corporations, 2013
(Percent of GDP)



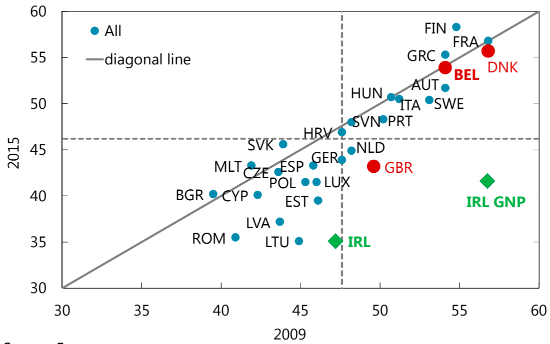
Source: OECD.

Figure 8. Ireland: Public Expenditure Efficiency

After years of fiscal consolidation, Ireland is a low spender compared to EU peers with comparable income levels.

Total Spending, 2009 vs 2015

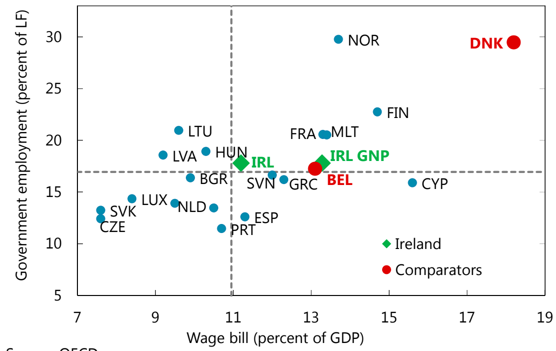
(Percent of GDP)



Source: Eurostat.

Successful efforts in controlling the public sector wage bill have helped make public spending more efficient.

General Government Wages and Employment, 2014

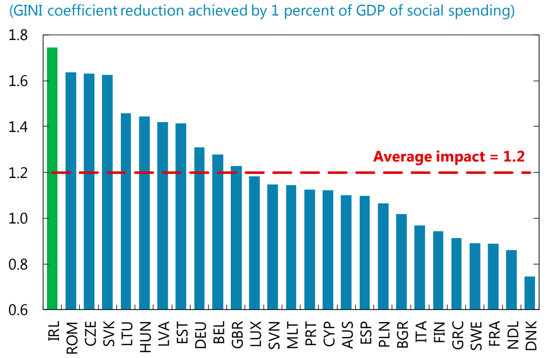


Source: OECD.

Social spending is highly efficient: while low as a share of GDP, it achieves substantial reduction in inequalities…

"Bang for the Buck" of Social Spending, 2013

(GINI coefficient reduction achieved by 1 percent of GDP of social spending)

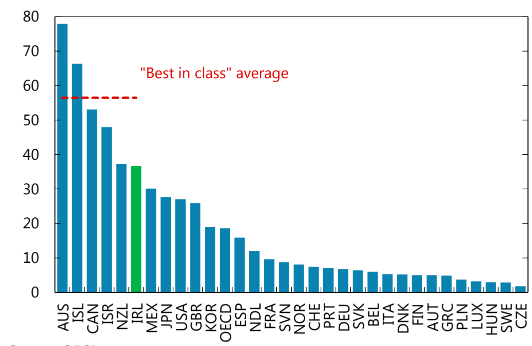


Source: OECD.

….yet better targeting of transfers could help improve further social outcomes and inter-generational fairness.

Spending on Means or Income-tested Cash Benefits, 2012

(Percent of cash public social expenditure)

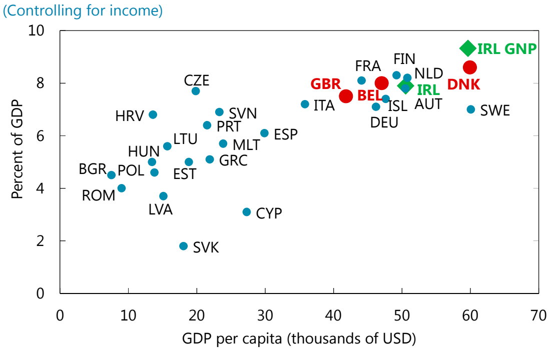


Source: OECD.

More efficiency is needed in the health sector to deal with future demographic challenges.

Health Expenditure, 2013

(Controlling for income)

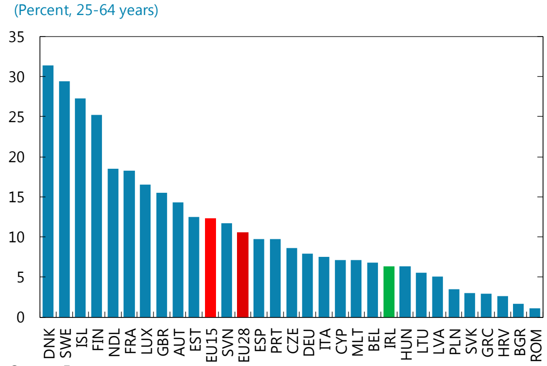


Sources: Eurostat (General Government Statistics).

Education should match better the needs of an increasingly sophisticated economy.

Participation Rate in Education and Training, 2015

(Percent, 25-64 years)



Source: Eurostat.

Table 1. Ireland: Selected Economic Indicators, 2011–17
(Annual percentage change unless indicated otherwise)

	2011	2012	2013	2014	2015	Projections 2016	Projections 2017
National accounts (constant prices)							
Real GDP	2.6	0.2	1.4	5.2	7.8	4.9	3.2
Final domestic demand	-0.1	1.0	-1.5	5.2	8.6	5.3	3.8
Private consumption	-0.7	-0.8	-0.3	2.0	3.5	3.1	2.2
Public consumption	-2.0	-2.2	1.4	4.6	-0.8	4.4	2.7
Gross fixed investment	3.2	8.6	-6.6	14.3	28.2	10.2	7.3
Net exports 1/	3.6	-0.3	2.6	0.1	0.1	0.9	0.2
Exports of goods and services	2.1	2.1	2.5	12.1	13.8	6.8	5.2
Imports of goods and services	-1.5	2.9	0.0	14.7	16.4	7.0	5.8
Real GNP	-0.8	1.6	4.6	6.9	5.7	4.5	2.8
Gross national saving (in percent of GDP)	16.0	17.6	20.7	22.9	26.5	26.8	27.6
Private	22.3	23.6	24.6	24.6	26.9	25.9	26.4
Public 2/	-6.2	-6.0	-3.8	-1.7	-0.5	0.9	1.1
Gross investment (in percent of GDP)	17.2	19.1	17.7	19.3	22.0	23.0	24.0
Private	14.8	17.1	15.8	17.2	20.2	21.2	22.3
Public	2.4	2.0	1.8	2.1	1.8	1.8	1.7
Prices, wages and employment (annual average)							
Harmonized index of consumer prices	1.2	1.9	0.5	0.3	0.0	0.3	1.2
Average wage, whole economy	-0.6	0.5	-0.7	-0.2	1.8	3.2	2.6
Employment	-1.8	-0.6	2.4	1.7	2.6	2.0	1.7
Unemployment rate (in percent)	14.7	14.7	13.1	11.3	9.5	8.3	7.7
Money and credit (end-period)							
Irish resident private sector credit	-2.9	-4.0	-4.9	-4.4	-4.4	...	...
Financial and asset markets (end-period)							
Three-month interbank rate	1.4	0.2	0.3	0.1	-0.1	...	...
Government bond yield (in percent, 10-year)	8.5	4.5	3.5	1.2	1.2	...	...
Annual change in ISEQ index (in percent)	5.2	16.3	30.3	15.1	33.5	...	...
House prices	-16.7	-4.5	6.4	16.3	6.6	...	...
Public finance (in percent of GDP)							
Net lending/borrowing	-12.6	-8.0	-5.7	-3.8	-2.3	-0.9	-0.6
Net lending/borrowing (excl. one-off items)	-8.7	-8.0	-6.1	-3.9	-1.3	-0.9	-0.6
Primary balance (excl. bank support)	-5.2	-3.9	-1.4	0.2	0.8	1.8	2.0
General government gross debt	109.1	120.2	120.0	107.5	93.8	89.0	86.6
General government net debt	77.3	86.7	89.6	88.1	75.5	72.1	70.5
External trade and balance of payments (percent of GDP)							
Balance of goods and services	18.0	17.2	19.3	18.3	20.9	21.9	21.7
Balance of income and current transfers	-19.2	-18.7	-16.2	-14.7	-16.4	-18.1	-18.2
Current account	-1.2	-1.5	3.1	3.6	4.4	3.8	3.5
Effective exchange rates (1999:Q1=100, average)							
Nominal	108.5	104.1	107.3	107.7	100.1	...	...
Real (CPI based)	110.1	105.1	106.8	106.0	97.9	...	...
Memorandum items:							
Population (in millions)	4.6	4.6	4.6	4.6	4.6	4.7	4.7
GDP per capita (in euros)	38,021	38,131	39,069	41,011	46,301	49,505	51,436
GDP (in billions of euros)	173.9	174.8	179.4	189.0	214.6	231.4	242.5

Sources: Bloomberg; Central Bank of Ireland; Department of Finance; International Financial Statistics; and IMF staff projections.
1/ Contribution to growth.
2/ Excludes bank restructuring costs.

Table 2. Ireland: Medium-Term Scenario, 2011–21

(Annual percentage change, unless indicated otherwise)

						Projections					
	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Real GDP	2.6	0.2	1.4	5.2	7.8	4.9	3.2	3.1	2.8	2.8	2.8
Domestic demand	0.8	0.7	-1.2	5.7	9.3	5.2	3.7	3.1	3.0	2.9	2.9
Final domestic demand	-0.1	1.0	-1.5	5.2	8.6	5.3	3.8	3.1	3.0	3.0	2.9
Private consumption	-0.7	-0.8	-0.3	2.0	3.5	3.1	2.2	2.2	2.0	1.9	1.9
Public consumption	-2.0	-2.2	1.4	4.6	-0.8	4.4	2.7	2.5	2.4	2.4	2.4
Gross fixed investment	3.2	8.6	-6.6	14.3	28.2	10.2	7.3	5.1	5.1	5.1	5.0
Change in stocks 1/	0.8	-0.3	0.3	0.5	0.6	0.0	0.0	0.0	0.0	0.0	0.0
Net exports 1/	3.6	-0.3	2.6	0.1	0.1	0.9	0.2	0.6	0.4	0.4	0.4
Exports of goods and services	2.1	2.1	2.5	12.1	13.8	6.8	5.2	4.4	4.2	4.2	4.2
Imports of goods and services	-1.5	2.9	0.0	14.7	16.4	7.0	5.8	4.5	4.5	4.5	4.5
Real GNP	-0.8	1.6	4.6	6.9	5.7	4.5	2.8	3.0	2.6	2.5	2.5
Current account 2/	-1.2	-1.5	3.1	3.6	4.4	3.8	3.5	3.3	3.2	3.1	3.0
Gross national saving 2/	16.0	17.6	20.7	22.9	26.5	26.8	27.6	27.9	28.5	29.1	29.6
Private	22.3	23.6	24.6	24.6	26.9	25.9	26.4	26.3	26.5	26.8	27.0
Public	-6.2	-6.0	-3.8	-1.7	-0.5	0.9	1.1	1.6	2.0	2.3	2.6
Gross investment 2/	17.2	19.1	17.7	19.3	22.0	23.0	24.0	24.6	25.3	26.0	26.6
Private	14.8	17.1	15.8	17.2	20.2	21.2	22.3	22.7	23.1	23.8	24.4
Public	2.4	2.0	1.8	2.1	1.8	1.8	1.7	2.0	2.2	2.2	2.2
Prices											
Harmonized index of consumer prices	1.2	1.9	0.5	0.3	0.0	0.3	1.2	1.4	1.8	2.0	2.0
GDP deflator	2.0	0.4	1.2	0.1	5.3	2.8	1.5	1.6	1.6	1.7	1.7
Average wage, whole economy	-0.6	0.5	-0.7	-0.2	1.8	3.2	2.6	2.4	2.8	3.0	3.0
Labor market											
Employment	-1.8	-0.6	2.4	1.7	2.6	2.0	1.7	1.5	1.4	1.3	1.3
Unemployment rate (in percent)	14.7	14.7	13.1	11.3	9.5	8.3	7.7	7.2	6.8	6.7	6.7
Public finance											
General government balance 2/	-12.6	-8.0	-5.7	-3.8	-2.3	-0.9	-0.6	-0.3	-0.2	0.1	0.4
General government balance 2/ 3/	-8.6	-8.0	-6.1	-3.9	-1.3	-0.9	-0.6	-0.3	-0.2	0.1	0.4
General government gross debt 2/	109.1	120.2	120.0	107.5	93.8	89.0	86.6	83.1	81.2	79.1	75.8
General government net debt 2/	77.3	86.7	89.6	88.1	75.5	72.1	70.5	67.7	66.0	64.2	61.3
Output gap	-4.0	-5.1	-6.0	-4.0	-0.5	0.6	0.9	0.9	0.6	0.3	0.1
Nominal GDP (in billions of euros)	173.9	174.8	179.4	189.0	214.6	231.4	242.5	253.9	265.3	277.4	290.0

Sources: Central Statistics Office; Department of Finance; and IMF staff projections.

1/ Contributions to growth.

2/ In percent of GDP.

3/ Excluding one-offs. For 2013, includes exchequer outlays for payments under the ELG scheme in the context of IBRC's liquidation.

Table 3. Ireland: General Government Statement of Operations, 2011–21

(Consistent with GFSM 2001; billions of euros)

						Projections					
	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	57.3	59.1	61.0	65.7	70.5	72.6	74.6	77.3	80.0	82.6	85.3
Taxes	38.9	40.9	42.5	46.4	50.7	53.1	55.3	57.6	59.6	61.6	63.8
Personal income tax	13.8	15.2	17.2	17.2	18.4	19.1	19.7	20.2	20.6	20.9	21.3
Corporate income tax	3.8	4.0	4.6	4.6	6.9	7.0	7.0	7.3	7.6	8.0	8.3
Value-added tax	9.7	10.2	11.2	11.2	11.9	12.7	13.4	14.0	14.6	15.3	16.0
Excise tax	4.7	4.7	5.0	5.0	5.3	5.9	6.2	6.5	6.8	7.1	7.4
Other taxes 1/	6.9	6.9	4.6	8.5	8.3	8.4	9.1	9.6	10.0	10.4	10.9
Social contributions 2/	10.0	9.7	10.3	10.9	11.4	12.0	12.6	13.1	13.6	14.1	14.7
Other revenue 3/	8.5	8.5	8.2	8.3	8.3	7.4	6.8	6.7	6.8	6.8	6.7
Expenditure (excl. fin. sector support) 4/	72.3	73.1	71.2	72.9	75.4	74.6	76.1	78.2	80.5	82.2	84.1
Expense	68.2	69.5	67.9	68.9	71.5	70.4	71.9	73.2	74.7	76.1	77.7
Compensation of employees	19.2	18.9	18.7	18.8	19.5	20.3	21.0	21.5	22.0	22.4	22.8
Use of goods and services	8.6	8.2	8.2	8.8	9.3	10.1	10.1	10.4	10.4	10.6	10.7
Interest	5.9	7.2	7.7	7.5	6.7	6.3	6.3	6.2	6.1	5.9	5.8
Subsidies	1.7	1.9	1.8	1.9	1.8	1.7	1.7	1.8	1.8	1.8	1.9
Social benefits	28.8	29.4	28.5	28.1	28.0	27.7	28.2	28.7	29.4	30.1	30.9
Other expense (excl. fin. sector support)	4.0	3.9	3.1	3.8	6.1	4.4	4.5	4.7	5.0	5.3	5.6
Other current transfers	2.6	2.5	2.2	2.7	2.6	2.9	2.9	3.0	3.2	3.3	3.4
Capital transfers (excl. fin. sector support)	1.4	1.4	0.9	1.1	3.5	1.5	1.6	1.6	1.8	2.0	2.2
Gross fixed capital formation	4.1	3.6	3.3	4.0	3.9	4.2	4.2	5.0	5.8	6.1	6.5
Financial sector support costs	6.8	0.0	0.0	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
One-off revenue and expenditure items 5/	6.7	0.0	-0.7	-0.2	2.1	0.0	0.0	0.0	0.0	0.0	0.0
Net lending/borrowing (excl. fin. sector support)	-15.0	-14.0	-10.2	-7.1	-4.9	-2.1	-1.5	-0.9	-0.5	0.4	1.1
Net lending/borrowing (excl. one-off items)	-15.1	-14.0	-10.9	-7.4	-2.8	-2.1	-1.5	-0.9	-0.5	0.4	1.1
Net lending/borrowing	-21.8	-14.0	-10.2	-7.2	-4.9	-2.1	-1.5	-0.9	-0.5	0.4	1.1
Primary balance (excl. one-off items)	-9.2	-6.9	-3.2	0.1	3.9	4.2	4.8	5.3	5.6	6.3	6.9
Net financial worth, transactions	-21.8	-14.0	-10.2	-7.2	-4.9	-2.1	-1.5	-0.9	-0.5	0.4	1.1
Net acquisition of financial assets	3.7	6.1	-5.5	-19.0	2.4	-0.5	0.0	0.0	1.0	1.0	1.0
Net incurrence of liabilities	25.5	20.1	4.7	-11.8	7.3	1.6	1.5	0.9	1.5	0.6	-0.1
Memorandum items (in percent of GDP, unless indicated other		-8.0	-5.7	-3.8	-2.3						
Revenue	33.0	33.8	34.0	34.8	32.8	31.4	30.8	30.5	30.1	29.8	29.4
Taxes and social contributions	28.1	28.9	29.4	30.4	29.0	28.1	28.0	27.8	27.6	27.3	27.1
Other revenue	4.9	4.9	4.6	4.4	3.9	3.2	2.8	2.6	2.6	2.5	2.3
Expenditure (excl. fin. sector support)	41.6	41.8	39.7	38.5	35.1	32.2	31.4	30.8	30.3	29.6	29.0
Current primary	35.8	35.7	33.6	32.5	30.2	27.7	27.0	26.4	25.8	25.3	24.8
Interest	3.4	4.1	4.3	4.0	3.1	2.7	2.6	2.5	2.3	2.1	2.0
Gross fixed capital formation	2.4	2.0	1.8	2.1	1.8	1.8	1.7	2.0	2.2	2.2	2.2
Net lending/borrowing (excl. one-off items)	-8.7	-8.0	-6.1	-3.9	-1.3	-0.9	-0.6	-0.3	-0.2	0.1	0.4
Net lending/borrowing	-12.6	-8.0	-5.7	-3.8	-2.3	-0.9	-0.6	-0.3	-0.2	0.1	0.4
Primary balance (excl. one-off items)	-5.3	-3.9	-1.8	0.0	1.8	1.8	2.0	2.1	2.1	2.3	2.4
Net financial worth, transactions	-12.6	-8.0	-5.7	-3.8	-2.3	-0.9	-0.6	-0.3	-0.2	0.1	0.4
Net acquisition of financial assets	2.1	3.5	-3.1	-10.1	1.1	-0.2	0.0	0.0	0.4	0.4	0.3
Net incurrence of liabilities	14.7	11.5	2.6	-6.2	3.4	0.7	0.6	0.3	0.6	0.2	0.0
Statistical discrepancy	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Structural balance 6/	-6.3	-5.0	-3.1	-1.9	-1.0	-0.9	-0.8	-0.6	-0.3	0.1	0.4
Structural primary balance 6/	-3.0	-1.1	0.9	1.9	2.1	1.8	1.8	1.9	2.0	2.2	2.4
General government gross debt	109.1	120.2	120.0	107.5	93.8	89.0	86.6	83.1	81.2	79.1	75.8
General government net debt	77.3	86.7	89.6	88.1	75.5	72.1	70.5	67.7	66.0	64.2	61.3
Output gap (percent of potential GDP)	-4.0	-5.1	-6.0	-4.0	-0.5	0.6	0.9	0.9	0.6	0.3	0.1
Nominal GDP (billions of euros)	173.9	174.8	179.4	189.0	214.6	231.4	242.5	253.9	265.3	277.4	290.0

Sources: Department of Finance; and IMF staff projections.

1/ Includes stamp duty, capital taxes, property tax and other taxes.

2/ Includes imputed social insurance contributions. The 2011 downward jump in the series reflects the integration of health levy receipts into the universal social charge (now part of income tax).

3/ Includes property income, sales of goods and services, current transfer revenue and capital transfer revenue.

4/ Projections take into account the expenditure profile set out in the Summer Economic Statement, June 2016.

5/ Includes financial sector support costs, license sales, and other non-recurrent revenue and expenditure items, such as the conversion of government's remaining AIB preference shares to ordinary shares in 2015, that do not affect underlying fiscal position.

6/ In percent of nominal potential GDP. Excludes one-off items.

Table 4. Ireland: Indicators of External and Financial Vulnerabilities, 2011–2015

	2011	2012	2013	2014	2015
External indicators					
Exports (annual percent change, value in euros)	2.8	6.4	2.1	12.3	21.2
Imports (annual percent change, value in euros)	0.0	8.7	-0.4	15.0	19.7
Terms of trade (goods, annual percent change)	-0.9	-1.5	0.1	-0.1	3.6
Current account balance (in percent of GDP)	-1.2	-1.5	3.1	3.6	4.4
Capital and financial account balance (in percent of GDP)	-7.7	-1.5	4.4	3.8	6.4
Inward portfolio investment	17.0	40.5	29.3	91.5	99.3
Inward foreign direct investment	14.5	20.1	18.8	12.4	42.2
Other investment liabilities	-28.0	-57.8	-12.8	36.8	-24.8
U.S. dollar per euro (period average)	1.40	1.29	1.33	1.32	1.10
U.K. pound per euro (period average)	0.87	0.81	0.85	0.80	0.72
Financial markets indicators					
General government debt (in percent of GDP)	109.1	120.2	120.0	107.5	93.8
Government bond yield (in percent, 10-year, end-period)	8.5	4.5	3.5	1.2	1.2
Spread of government bond yield with Germany (in percent, end of period)	6.5	3.2	1.4	0.6	0.5
Real government bond yield (in percent, 10-year, period average, based on HICP)	8.4	4.1	3.3	2.0	1.1
Annual change in ISEQ index (in percent, end of period)	5.2	16.3	30.3	15.1	33.5
Personal lending interest rate (in percent)	12.9	13.3	13.9	8.2	11.2
Standard variable mortgage interest rate (in percent)	3.1	3.6	3.4	3.8	3.4
Financial sector risk indicators					
Annual credit growth rates (to Irish resident private sector, in percent) 1/	-2.9	-4.0	-4.9	-4.4	-4.4
Personal lending as a share of total Irish resident credit (in percent) 2/	34.1	36.8	38.7	42.7	46.0
Loans for house purchase	24.8	28.1	29.9	34.5	38.5
Consumer credit	5.1	4.7	4.6	5.1	5.6
Other loans	4.1	3.9	4.1	3.1	1.9
Irish resident household mortgage debt annual growth rates (in percent) 3/	-19.3	5.7	-1.9	-6.0	-1.7
Foreign-currency denominated assets (in percent of total assets)	29.4	28.4	27.5	27.2	28.2
Foreign-currency denominated liabilities (in percent of total liabilities)	26.3	25.4	25.3	26.2	27.1
Non-performing loans (in percent of total loans) 4/	16.1	25.0	25.7	20.6	14.9
Total provisions for loan losses (in percent of total loans) 5/	7.2	11.9	13.0	9.9	6.0
Regulatory Tier 1 capital to risk-weighted assets of domestic banks (in percent) 5/	16.6	16.7	17.3	20.6	22.1
Bank return on assets (percent) 5/	-0.9	-0.8	-0.4	0.4	1.0
Bank return on equity (percent) 5/	-10.8	-7.8	-6.8	5.3	5.7
Deposits to M3 ratio 6/	1.2	1.3	1.3	1.1	1.1
Loan-to-deposit ratio vis-à-vis Irish residents 7/	2.1	1.9	1.6	1.5	1.2
Loan-to-deposit ratio vis-à-vis total	2.1	1.9	1.7	1.4	1.2
Concentration ratios in the banking sector					
No. of banks accounting for 25 percent of total assets	2.0	2.0	2.0	2.0	2.0
No. of banks accounting for 75 percent of total assets	14.0	14.0	13.0	13.0	12.0

Sources: Bloomberg; Central Bank of Ireland; International Financial Statistics; IMF staff calculations and projections.
1/ Adjusted growth rate of credit to households and non-financial corporations.
2/ Data is based on Table A.1 published by Central Bank of Ireland.
3/ Data is based on Table A.6 published by Central Bank of Ireland; includes securitizations.
4/ Includes lending for construction and real estate activities.
5/ Based on IMF's Financial Soundness Indicators data.
6/ Credit equivalent values. Deposits vis-à-vis Irish and nonresidents.The M3 compiliation methodology has been amended in line with Eurosystem requirements.
7/ Nongovernment credit/nongovernment deposits ratio.

Table 5. Ireland: Summary of Balance of Payments, 2011–21

	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
						Projections					
					(Billions of euros)						
Current account balance	-2.0	-2.7	5.6	6.8	9.5	8.8	8.5	8.4	8.6	8.7	8.8
Balance of goods and services	31.3	30.0	34.7	34.7	44.8	50.6	52.6	55.4	57.7	60.2	62.7
Trade balance	41.3	37.6	35.1	42.3	64.6	66.6	68.8	70.9	72.4	72.7	72.8
Exports of goods	100.6	101.9	98.7	113.2	143.8	152.2	158.9	166.0	173.3	180.3	187.4
Imports of goods	-59.3	-64.3	-63.7	-70.9	-79.2	-85.6	-90.1	-95.1	-100.9	-107.6	-114.7
Services balance	-10.0	-7.6	-0.4	-7.6	-19.8	-16.0	-16.2	-15.6	-14.7	-12.5	-10.1
Credit	75.5	85.5	92.7	101.8	116.8	130.7	142.3	152.2	162.2	173.6	185.7
Debit	-85.5	-93.1	-93.1	-109.4	-136.6	-146.8	-158.5	-167.7	-176.9	-186.1	-195.7
Primary income balance	-30.7	-30.1	-26.2	-25.1	-32.4	-38.8	-40.8	-43.3	-45.1	-47.0	-48.8
Credit	58.3	58.4	56.5	62.9	68.4	69.5	72.6	75.5	79.1	82.9	86.9
Debit	-89.0	-88.5	-82.7	-88.0	-100.7	-108.3	-113.5	-118.8	-124.2	-129.8	-135.7
Secondary income balance	-2.7	-2.6	-2.9	-2.7	-2.9	-3.1	-3.2	-3.6	-4.1	-4.5	-5.1
Capital and financial account balance	20.6	18.5	18.7	7.9	13.7	8.9	8.7	8.5	8.7	8.9	9.2
Capital account balance	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.2
Financial account	20.4	18.4	18.6	7.8	13.6	8.8	8.6	8.5	8.7	8.8	9.0
Direct investment	-17.8	-17.7	-12.0	9.0	1.0	3.6	4.5	5.4	6.2	7.1	8.0
Portfolio investment	-26.9	3.8	46.0	-20.1	-88.6	-88.6	-88.6	-88.6	-88.4	-88.4	-88.4
Other investment	65.6	32.3	-15.5	18.7	100.7	93.8	92.7	91.6	90.8	90.1	89.4
Change in reserve assets 1/	-0.3	0.0	0.0	0.1	0.6	0.0	0.0	0.0	0.0	0.0	0.0
Net errors and omissions	-12.2	-0.2	2.0	0.0	4.0	0.0	0.0	0.0	0.0	0.0	0.0
Financing gap	34.3	21.3	11.0	0.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Program financing	34.5	21.3	11.0	0.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0
IMF	12.6	6.4	3.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
EU	21.9	14.8	7.5	0.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0
					(Percent of GDP)						
Current account balance	-1.2	-1.5	3.1	3.6	4.4	3.8	3.5	3.3	3.2	3.1	3.0
Balance of goods and services	18.0	17.2	19.3	18.3	20.9	21.9	21.7	21.8	21.8	21.7	21.6
Trade balance	23.7	21.5	19.5	22.4	30.1	28.8	28.4	27.9	27.3	26.2	25.1
Services balance	-5.7	-4.4	-0.2	-4.0	-9.2	-6.9	-6.7	-6.1	-5.6	-4.5	-3.5
Income balance	-17.6	-17.2	-14.6	-13.3	-15.1	-16.8	-16.8	-17.1	-17.0	-16.9	-16.8
Current transfers (net)	-1.5	-1.5	-1.6	-1.4	-1.3	-1.3	-1.3	-1.4	-1.5	-1.6	-1.7
Capital and financial account balance	11.8	10.6	10.4	4.2	6.4	3.8	3.6	3.4	3.3	3.2	3.2
Of which:											
Direct investment	-10.2	-10.1	-6.7	4.8	0.5	1.6	1.9	2.1	2.3	2.5	2.8
Portfolio investment	-15.5	2.2	25.6	-10.6	-41.3	-38.3	-36.5	-34.9	-33.3	-31.9	-30.5
Other investment	37.7	18.5	-8.6	9.9	46.9	40.5	38.2	36.1	34.2	32.5	30.8
Change in reserve assets 1/	-0.2	0.0	0.0	0.1	0.3	0.0	0.0	0.0	0.0	0.0	0.0
Net errors and omissions	-7.0	-0.1	1.1	0.0	1.9	0.0	0.0	0.0	0.0	0.0	0.0
Financing gap	19.7	12.2	6.1	0.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Program financing	19.8	12.2	6.1	0.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0
IMF	7.2	3.7	1.9	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
EU	12.6	8.5	4.2	0.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:											
Current account balance excluding undistributed profits 2/	-4.5	-5.7	-0.8	-0.2	1.1	0.6	0.5	0.4	0.5	0.5	0.5

Sources: Central Bank of Ireland; Central Statistics Office; and IMF staff projections.

1/ Includes financing need to build reserves for bank support.

2/ Undistributed profits of redomiciled firms, as estimated by FitzGerald (2013).

Table 6. Ireland Monetary Survey, 2011–16
(Billions of euros, unless otherwise indicated; end of period)

	Dec-11	Dec-12	Dec-13	Dec-14	Dec-15	May-16
Aggregate balance sheet of domestic market credit institutions						
Assets	644	555	477	424	378	369
Claims on Central Bank of Ireland	4	2	2	3	6	8
Claims on Irish resident Other MFIs	92	53	49	47	46	43
Claims on Irish resident non MFIs	340	326	281	237	206	200
General government	42	47	21	20	18	17
Private sector	298	279	260	217	187	183
Households	110	111	108	97	92	89
Non-Financial Corporations	86	83	78	58	44	43
Non-Bank Financial Intermediaries	101	85	74	62	51	51
Claims on non-residents	155	127	105	94	84	81
Other assets	52	47	40	42	37	37
Liabilities	644	555	477	424	378	369
Liabilities to Eurosystem 1/	73	61	31	14	10	8
Liabilities to Irish resident Other MFIs	99	59	52	50	46	43
Deposits of Irish resident non MFIs	147	154	175	163	167	167
General government	2	6	14	9	4	4
Private sector	144	148	162	155	162	163
Households	91	92	91	91	95	95
Non-Financial Corporations	29	30	32	38	40	43
Non-Bank Financial Intermediaries	24	26	38	26	28	25
Deposits of non-residents	103	79	72	64	43	40
Debt securities	52	38	27	27	25	26
Capital and reserves	91	99	97	80	67	68
Other liabilities (incl. Central Bank of Ireland)	79	66	23	26	19	17
Money and credit 2/						
Net foreign assets	-39	-14	2	20	43	…
Central Bank of Ireland 3/	-101	-62	-37	-18	2	…
Commercial banks	62	48	39	38	41	42
Net domestic assets	221	194	199	155	147	…
Public sector credit	43	48	21	21	19	18
Private sector credit	324	302	278	227	200	194
Other	-145	-156	-100	-93	-72	…
Irish Resident Broad money (M3) 4/	182	180	201	175	190	191
Irish Resident Intermediate money (M2) 4/	167	168	183	172	184	185
Irish Resident Narrow money (M1)	90	92	113	116	133	136
			(Percent of GDP)			
Public sector credit 5/	27.0	29.4	12.8	12.5	11.5	10.4
Private sector credit 5/	190.2	173.6	161.9	134.9	116.7	114.0
			(Percentage change y/y)			
Broad money - Irish contribution to euro area M3 6/	0.4	-7.8	11.5	-0.6	5.1	10.6
Irish Public sector credit 6/ 7/	1.5	8.5	-57.8	-3.0	-9.3	-12.4
Irish Household and non-financial corporations credit 6/ /7	-2.9	-4.0	-4.9	-4.5	-4.6	-3.7
Memorandum items: 8/						
Credit to deposits (in percent) 9/	206.3	188.6	160.9	140.1	115.4	112.1
Deposits from Irish Private Sector (y-o-y percent change)	-8.6	2.5	8.8	-2.9	4.4	2.4
Wholesale funding (billions of euros)	237.9	161.1	135.8	126.9	105.4	101.4
Deposits from MFIs	186.0	122.9	109.0	99.5	80.2	75.3
Debt securities	51.9	38.2	26.9	27.4	25.2	26.1
Wholesale funding (y-o-y percent change) 10/	-26.7	-32.7	-12.5	-6.7	-17.7	-16.7
Wholesale funding (percent of assets) 10/	37.0	29.0	28.5	30.0	27.9	27.5

Sources: Central Bank of Ireland and staff estimates.
1/ Relating to Eurosystem monetary policy operations.
2/ Including banks in the International Financial Service Centre.
3/ Sourced from quarterly IIP statistics.
4/ Differs from the M3 (M2) Irish contribution to euro area as only liabilities vis-a-vis Irish residents are used.
5/ Refers to credit advanced by domestic market credit institutions.
6/ Includes IFSC.
7/ Growth rates adjusted for valuation, reclassification, derecognition/loan transfer to non-MFIs, and exchange rates.
8/ Excludes IFSC.
9/ Domestic market credit institutions' private sector credit to deposits.
10/ Includes resident and non-resident MFI deposits, and debt securities issued.

Table 7. Ireland: Indicators of Fund Credit, 2011–23

(Millions of SDR)

	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Fund credit													
Disbursement	11,050	5,493	2,922	-	-	-	-	-	-	-	-	-	-
Stock 1/	11,050	16,543	19,466	11,822	3,773	3,773	3,773	3,773	3,773	3,773	1,420	349	-
Obligations	109	332	456	8,292	8,234	20	40	40	40	40	2,385	1,083	351
Repurchase 2/	-	-	-	7,644	8,049	0	0	0	0	0	2,353	1,071	349
Charges	109	332	456	648	185	20	40	40	40	40	32	12	3
Stock of Fund credit													
In percent of quota 3/	879	1,315	1,548	940	300	109	109	109	109	109	41	10	-
In percent of GDP	7.2	11.3	12.4	7.1	2.2	2.0	1.9	1.8	1.8	1.7	0.6	0.1	-
In percent of exports of goods and services	7.1	10.5	11.6	6.3	1.8	1.7	1.6	1.5	1.4	1.3	0.5	0.1	-
Obligations to the Fund													
In percent of quota 3/	9	26	36	659	655	1	1	1	1	1	69	31	10
In percent of GDP	0.1	0.2	0.3	5.0	4.8	0.0	0.0	0.0	0.0	0.0	1.0	0.4	0.1
In percent of exports of goods and services	0.1	0.2	0.3	4.4	4.0	0.0	0.0	0.0	0.0	0.0	0.8	0.4	0.1

Source: IMF staff calculations and projections.

1/ End of period.

2/ Reflects early repurchases to date.

3/ Quota raised from SDR 1257.6 million to SDR 3449.9 million as of February 2016.

Table 8. Ireland: Main Domestic Banks' Aggregated Summary Financial Statements, 2014–15 1/

(Billions of euros unless otherwise indicated)

Balance Sheet	2014	2015	Y/Y change	
	€ bn.	€ bn.	€ bn.	%
Cash & due from Eurosystem	12.7	13.2	0.5	3.8
Net loans	172.9	171.2	-1.7	-1.0
Due from banks	6.4	6.8	0.4	5.5
Securities & derivatives	57.6	48.4	-9.1	-15.9
Other assets	10.4	9.2	-1.2	-11.6
Total assets	260.0	248.8	-11.2	-4.3
Total average assets (TAA)	335.8	255.9	-79.9	-23.8
Due to Eurosystem	10.2	7.8	-2.3	-23.0
Due to banks	21.6	17.0	-4.6	-21.2
Deposits	160.2	161.4	1.2	0.7
Debt & derivatives	38.6	32.1	-6.4	-16.7
Other liabilities	6.9	6.8	-0.1	-1.1
Total liabilities	237.4	225.2	-12.2	-5.2
Net equity	22.6	23.6	1.0	4.6
Total liabilities & equity	260.0	248.8	-11.2	-4.3

Profit and Loss Account	2014		2015	
	€ bn.	% of TAA	€ bn.	% of TAA
Interest income	7.9	2.3	7.3	2.9
Interest expense	-3.6	-1.1	-2.6	-1.0
Net interest margin	4.2	1.3	4.7	1.8
Net fee income	1.1	0.3	1.0	0.4
Net trading gains	-0.3	-0.1	0.0	0.0
Other nonrecurrent items	0.7	0.2	0.4	0.1
Gross operating income	5.6	1.7	6.1	2.4
Operating expenses	-3.6	-1.1	-3.8	-1.5
o/w: administration & other	-2.0	-0.6	-2.1	-0.8
o/w: staff	-1.6	-0.5	-1.8	-0.7
Preprovision profits (PPP)	2.0	0.6	2.3	0.9
Loan loss & NAMA provisions	-0.3	-0.1	0.5	0.2
Loss on derecognized assets	0.2	0.1	-0.2	-0.1
Net income before tax	2.0	0.6	2.7	1.0
Tax effects & other 3/	-0.4	-0.1	-0.8	-0.3
Net income	1.6	0.5	1.9	0.7

Memorandum items:

	2014 € bn.	2015 € bn.	Y/Y change € bn.	Y/Y change %
Gross loans 2/	196.9	186.5	-10.5	-5.3
Loan loss provisions	23.6	15.6	-8.0	-34.1
Gross NPLs	45.7	30.1	-15.6	-34.2
Gross NPLs to gross loans (%)	23.2	16.1		-30.5
Provisions to gross NPLs (%)	51.7	51.8		0.1
Net NPLs to net equity (%)	97.5	61.4		-37.1

	2014 € bn.	2014 % of TAA	2015 € bn.	2015 % of TAA
PPP net of other nonrecurrent items	1.4	0.4	1.9	0.8
Return on equity		7.1		8.0
Provisions to gross loans		-0.4		0.4
Risk weighted assets (RWA)	125.5	37.4	124.0	48.5
Core tier 1 capital (CT1) and CT1 to RWA (%)	19.5	15.5	17.9	14.4
CT1 to total assets = leverage ratio (%)		7.5		7.2

Sources: Central Bank of Ireland; and IMF staff estimates.

1/ Bank of Ireland, Allied Irish Banks, and Permanent tsb.

2/ Includes loans held for sale, classified on balance sheet as other assets.

3/ Includes profits from discontinued operations of €1.6 billion and tax credits of €1.5 billion in 2011.

Annex I. Progress against IMF Recommendations

Several policy recommendations in the 2015 Article IV consultation have been taken on board.

Key recommendations	Implemented policies
Further reduce public debt while broadening the tax base, containing the public wage bill, and improving the targeting of social programs.	Public debt ratio rapidly declined in 2015. Budget 2016 aims for further consolidation, but includes measures that erode the tax base. Additionally, the increase in social spending could have been better targeted.
Advance the resolution of distressed loans.	The government announced reforms to increase the utilization of personal insolvency arrangements (May 2015); introduced new court rules to shorten the legal proceedings (August 2015); reduced the bankruptcy discharge period to one year from three years (December 2015).
Strengthen the financial resilience of banks and borrowers.	New macro prudential measures on mortgage lending were implemented (February 2015). Countercyclical Capital Buffer was introduced (January 2016), and "Other Systemically Important Institutions" buffer will be phased in 2019-21 in line with the new EU banking regulations.
Take early actions to strengthen banks' capital.	PTSB raised equity to cover capital shortfall (April 2015) while AIB redeemed the remaining preference shares (December 2015).
Improve the construction supply response.	The government launched a policy package comprising measures to boost housing supply (November 2015).

Annex II. Ireland: Risk Assessment Matrix

Source of Risks	Relative Likelihood	Impact	Policy response
Structurally weak growth in key advanced and emerging economies.	H (euro area and Japan) M (emerging markets)	M Ireland's exports were 120 percent of GDP in 2015, with the euro area some 35 percent of the total. The export growth impact would be significant but moderated to the extent that US and UK markets remained robust. However protracted euro area weakness could undermine domestic confidence, investment, and FDI inflows.	Strengthen growth potential through reforms, including by strengthening incentives for female labor force participation, enhancing activation policies, better targeting of benefits, improving access to finance for SMEs, and removing impediments for productivity growth. ECB policy actions should help revive growth and could also aid competitiveness.
Sharp asset price decline and decompression of credit spreads.	M	M High level of private and public debt, and high degree of financial sector interconnectedness make Ireland susceptible to financial contagion. However, market developments suggest any spread widening is most likely contained by the ECB's QE. To the extent spreads widen, the impact on deficits and debt would be also limited by low financing needs, and substantial cash buffers. The impact on growth could be more significant also in the case of a reversal of inflows into commercial property.	Continue phased and steady fiscal consolidation to ensure market confidence.
Higher-than-expected fallout from the UK vote to leave the EU. The vote to leave the EU is expected to lead to a period of heightened uncertainty regarding cross-border trade, financial, and migration relationships between the UK and EU. These effects could be larger than projected in the baseline, especially if the	M	H In view of Ireland's strong trade and financial links with the UK, the recent UK vote to leave the EU, if accompanied by a sharper-than-expected slowdown in the UK and the rest of Europe and further increase in financial market volatility, would adversely affect the Irish economy. Irish banks' profitability would decline, given their direct and indirect exposures, and asset quality may deteriorate. An increase in trade	Continue close supervision to ensure that banks would be able to withstand negative shocks. Central banks should stand ready to provide liquidity support to banks if needed.

process is volatile, looks likely to result in a large increase in barriers, or has significant political repercussions.	H	barriers would reduce trade with the UK. M/L Some of these effects are likely to be mitigated by possible relocation of firms that service the EU from the UK to Ireland, resulting also in a potential increase of FDI inflows over the medium term.	Pursue counter-cyclical fiscal policy in the event of a sharp economic downturn. Continue monitoring developments and adjust contingency actions to mitigate adverse effects.
Financial imbalances from protracted period of low interest rates.	M	M Low domestic credit growth limits risks. Yet, given the continued global search for yield, further strong inflows into commercial real estate could eventually generate over-building and risks of future slump in prices.	Deploying prudential policy instruments to limit the exposure of domestic banks to potential asset price bubbles if they begin to emerge, including in commercial real estate.
Persistently low energy prices, triggered by supply factors.	H	L Lasting low energy prices would reduce production costs and increase the real income of consumers therefore supporting economic growth. However, low inflation and inflation expectations could also lead to high savings and lower investment given the slower decline in the real private debt burdens.	ECB policy actions should contribute to mitigating imported disinflation in Ireland.
Domestic reform fatigue coupled with increased political fragmentation. The new government is facing increasing public expectations to reap the fruits of the recovery.	M	M While the government is committed to maintain prudent policies, public pressure to reverse some of the measures that were implemented in recent years may slow down fiscal consolidation and increase the economy's vulnerabilities to adverse shocks.	Ensure sound public finances and a durable debt reduction to rebuild fiscal buffers, which might require outperforming the MTO over the medium term.

Note: The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relatively likelihood of risks listed is the staff's subjective assessment of the risks surrounding the baseline (with L, M, H, denote low, medium, and high, respectively). The RAM reflects staff views on the sources of risk and overall level of concern as of the time of discussions with the authorities.

Annex III. The Possible Economic Impact on Ireland of the UK Vote to Leave the EU

1. Ireland has tight economic linkages with the UK.[1] Although the nature and the size of economic consequences of Brexit on Ireland would depend on the eventual terms of the UK's withdrawal and its future relations with the EU involving a range of potential outcomes, the overall assessment is that it is likely to have an adverse impact on Ireland.[2]

2. Trade. The UK is Ireland's single largest trading partner in Europe, with annual export of goods and services of around €35 billion, or about 15 percent of Irish exports. The UK ranks second only to the US in terms of Ireland's global exports. The main export items comprise food and drink, computers, and financial and transport services. The UK is a particularly important trading partner for indigenous Irish firms, accounting for 43 percent of their exports in 2014, as opposed to 12 percent of foreign-owned companies' exports. Overall, Irish exports could be negatively impacted through several channels: (i) a potential significant depreciation of the sterling against the euro; (ii) potential introduction of tariffs, customs requirements, as well as higher transactions and compliance costs due to divergence in regulations; and (iii) a decline in the UK's and the euro area's import demand from Ireland if the impact of Brexit on the UK economy and the euro area turns out to be significantly negative.

3. Labor movement and travel. The UK and Ireland form a common travel area, without border controls between Northern Ireland and the Republic of Ireland being one of the major benefits. The UK is an important destination for labor migration of Irish nationals, especially at times of high domestic unemployment. Brexit could open up the possibility of labor movement restrictions and changes to the common travel area, potentially affecting tourism.

4. Energy. Ireland is highly connected to the UK energy market, with 90 percent of energy products coming from the UK in 2014. A potential introduction of tariffs on EU energy exports to the UK could raise energy costs there, and these costs could be passed on to Ireland, thus hurting Ireland's competitiveness. Brexit could also affect the Irish energy sector through the operation and degree of integration of the Irish electricity market with the UK market, climate change policy, security of oil and gas supplies, as well as gas storage.

5. Foreign direct investment. A potential benefit of Brexit for Ireland could arise from higher FDI flows, which could relocate from the UK to Ireland given uncertainties about access to the single market. However, a recent ESRI empirical analysis suggests that the positive impact on Ireland's attractiveness as a location for FDI would be marginal.

[1] See analysis of Brexit in the United Kingdom 2016 Article IV report and the accompanied Selected Issues.

[2] See ESRI (2015), "Scoping the Possible Economic Implications of Brexit on Ireland"; Ibec (2016), "The impact of a possible Brexit on Irish business"; Davy Research (March 31, 2016), "The economic impact of Brexit on Ireland"; and Central Bank of Ireland (2015), "Macro-Financial Review (2015:II)".

6. Financial sector. Ireland could also benefit from the relocation of some financial institutions from the UK to Ireland due to the possible loss of the EU "passport rights", which allow them to sell services across the EU. On the other hand, recent CBI analysis suggests that, given strong linkages, an exit of the UK from the EU could have a significant negative impact on Irish banks, insurance firms and non-bank financial intermediaries, if it occurred in a disorderly manner and/or had a large negative impact on the UK economy. Banking sector profitability could be negatively impacted as a result of any slowdown in the UK economy, particularly through reduced lending to exporters dependent on UK markets, and a decline in real estate markets as Irish banks have sizeable UK property-related exposures. As there is a substantial cross-border life and non-life business between Ireland and the UK, the insurance sector could also be adversely affected. Finally, for non-bank financial intermediaries, the potential loss of access to the UK client base might have a negative impact on business, although the exit of UK competitors from the market might benefit other firms.

7. Contingency plans.[3] The authorities have published contingency plans to deal with market volatility, potential adverse effects on export industries, and FDI flows. They continue to monitor developments and adjust their actions and mitigation strategies on an ongoing basis.

[3] See Irish Government Brexit Contingency Plans

Annex IV. External Balance and Competitiveness Assessment

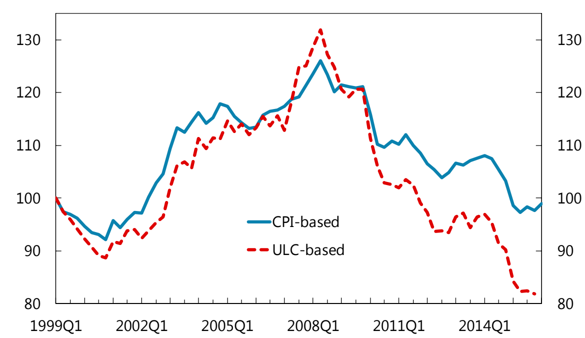
A range of External Balance Assessment (EBA) methodologies suggests that the external position is broadly in line with fundamentals and desirable policy settings. Ireland's competitiveness has further improved in recent years, manifested in strong growth of goods and services exports, particularly in pharmaceuticals and information technology (IT) services. Ireland is a booming hub for service industries, non-pharmaceutical goods exports have managed to reclaim some market share since 2012, and strong FDI inflows serve as proof of investors' continued favorable assessment of the country's business-friendly environment. Some trade losses could be expected following a depreciation of sterling and reduction of UK demand on the back of the UK vote to leave the EU (Annex III).

A. External Balance Broadly in Equilibrium

Current Account and Exchange Rates

1. **External Balance Assessment methodologies indicate that the external position is broadly in line with fundamentals and desirable policy settings.** The real exchange rate has fallen markedly in the years following the crisis—especially when measured on a unit labor cost (ULC) basis—with a further notable decline in 2015 primarily due to the depreciation of the euro. The Current Account (CA) approach suggests a small undervaluation of the currency. Policy gaps make a negligible contribution to the overall CA gap, which is dominated by the residual. The External Sustainability (ES) and the Real Effective Exchange Rate (REER) approaches suggest slight overvaluation. In case of the REER approach, health expenditures are the largest contributor to the policy gap.

Real Effective Exchange Rates
(Index, 1999Q1=100)



Sources: Central Bank of Ireland; and Haver Analytics.

Table 1. Ireland: External Balance Assessment Results

Methodology	**CA gap** Percent of GDP	**REER gap** percent
Current Account (CA) approach	3.8	-4.0
External sustainability (ES) approach	-0.6	0.6
REER approach	-	3.8

Note: A positive CA gap indicates undervaluation, a positive REER gap indicates overvaluation. Estimates are based on data available in April 2016.

2. **Redomiciled firms may explain the bulk of the estimated positive current account balance gap**. The apparent contradiction between the CA- and REER-based approaches can be reconciled by the proliferation of "redomiciled firms", enterprises which only establish their headquarters in Ireland to consolidate their profits for taxation at the Irish corporate tax rate. Having

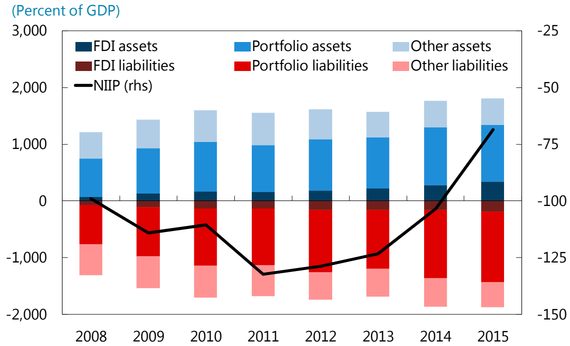
risen rapidly in the period 2009-2012, the undistributed profits of these companies seem to have reached a plateau in 2013 and 2014. FitzGerald (2014) estimates that retained earnings contributed around 3.7 percent of GDP to the current account balance in 2014, which would eliminate the estimated undervaluation.

Capital Account Flows and International Investment Position (IIP)

3. **Ireland's capital account is dominated by the International Financial Services Center (IFSC), which serves as a hub for international financial transactions.** The IFSC accounted for around 90 percent of overall portfolio flows in 2015, and IFSC inflows and outflows were closely matched. As a result the IFSC's IIP was very close to balance, with the overall net IIP dominated by the non-IFSC sector. In this respect, it should be noted that although Ireland is a large FDI recipient, its net direct investment position is in fact positive. This is due in part to large positive valuation effects associated with redomiciled firms' foreign assets.

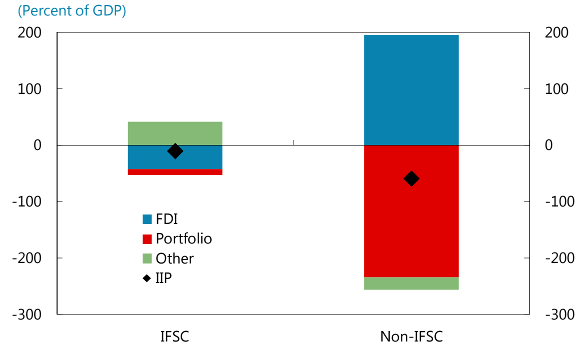
International Investment Position, 2015

Overall IIP (IFSC and non-IFSC)
(Percent of GDP)



Sources: Central Statistics Office; and IMF staff calculations.

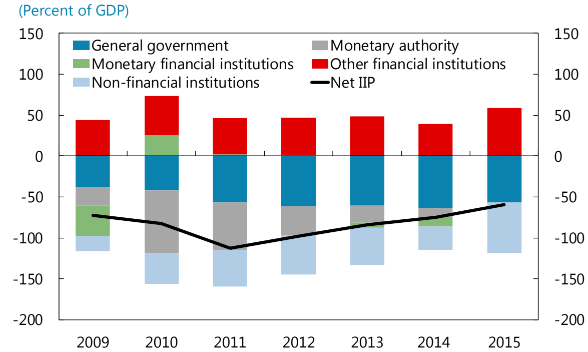
Net IIP by Financial Instrument, 2015
(Percent of GDP)



Sources: Central Statistics Office; and IMF staff calculations.

4. **The IIP of the non-IFSC sector has improved rapidly over the last few years.** From -115 percent of GDP in 2011, the IIP has risen to -60 percent of GDP by 2015. The primary contributors were banks' diminished reliance on Eurosystem funding, which therefore reduced the CBI's Target 2 liabilities, and a decline in banks' short-term debt. The general government's external liabilities have also stabilized and are projected to decline gradually as a percent of GDP. With a current account surplus projected at around 3 percent in the medium term, Ireland's NIIP-to-GDP ratio is expected to continue its gradual improvement.

Non-IFSC NIIP by Sector
(Percent of GDP)



Sources: Central Statistics Office; and IMF staff calculations.

B. Competitiveness

5. Ireland's strong export performance in 2015 was driven both by the goods and services sectors, pharmaceuticals and computer services in particular. Exports of goods relative to GDP resumed their growth since 2013 following a pause due to the "patent cliff" in 2011-2013. The patent cliff also held back Ireland's share in total global trade of its major pharmaceutical products (Figure 1). As a result, goods exports have fallen notably in relation to international goods trade, from 1.5 percent of world exports in 2002 to around 0.8 percent by 2013. Since then, they have started to recover mainly due to the recovery of pharmaceutical exports. On the other hand, exports of services, predominantly computer services, have steadily increased. This has also translated into Ireland's rapidly increasing share in world services exports.

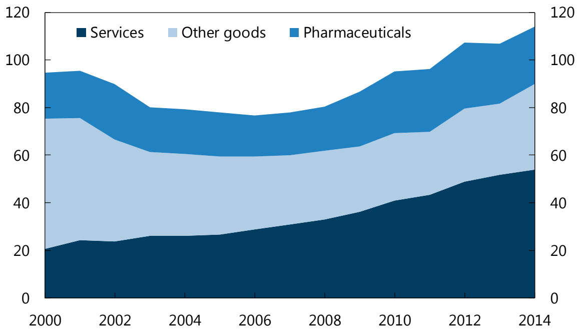
6. The assessment of developments in goods exports is complicated by "contract manufacturing" in the pharmaceutical sector. Exports of goods reported in the national accounts have been growing much faster than those recorded at the customs since 2014. The wedge between the two types of trade has increased from 11 percent in 2013 to 22 percent in 2015. This discrepancy can be traced in part to the proliferation of contract manufacturing—exports of goods manufactured abroad by companies headquartered in Ireland. Such exports are part of GDP as the goods remain in the ownership of the Irish resident company. The issue is most important in the pharmaceutical sector, particularly with the recovery of pharmaceutical export following the patent cliff.

7. Ireland's attractiveness as a destination for foreign direct investment has increased further. Following a brief period of decline between 2010 and 2013, Ireland's share in EU and world inward FDI has picked up strongly, supported by strong economic performance, improving business efficiency, and—despite relatively high skill mismatches in some segments—its educated workforce (Figure 2).

Figure 1. Ireland: Export Composition and World Market Share, 2000-14

Export growth has been dominated by services…

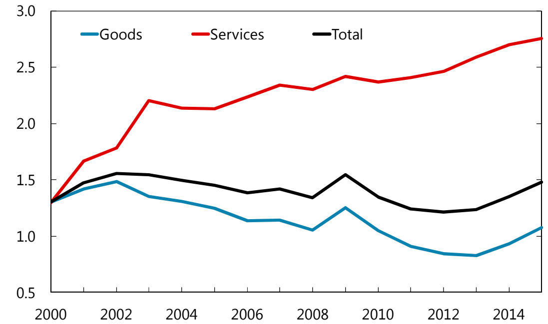
Ireland Exports
(Percent of GDP)



Sources: Central Statistics Office; UN Comtrade; and IMF staff calculations.

…but exports of goods have picked up recently as well, raising Ireland's market share.

Export Shares
(Percent of world non-oil exports)



Sources: IMF WEO; and staff calculations.

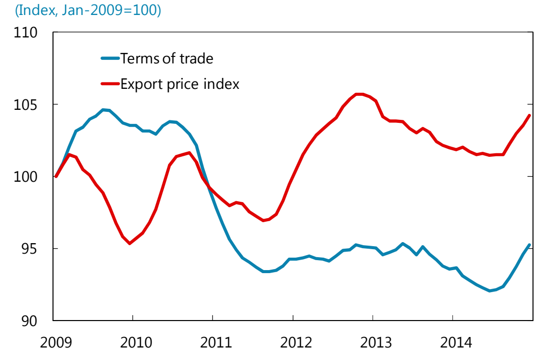
Market share of pharmaceutical products is rising again following a brief period of decline due to the patent cliff.

Ireland: Exports of the Four Largest Pharmaceutical Products
(Percent of total world exports)

Sources: UN Comtrade; and IMF staff calculations.

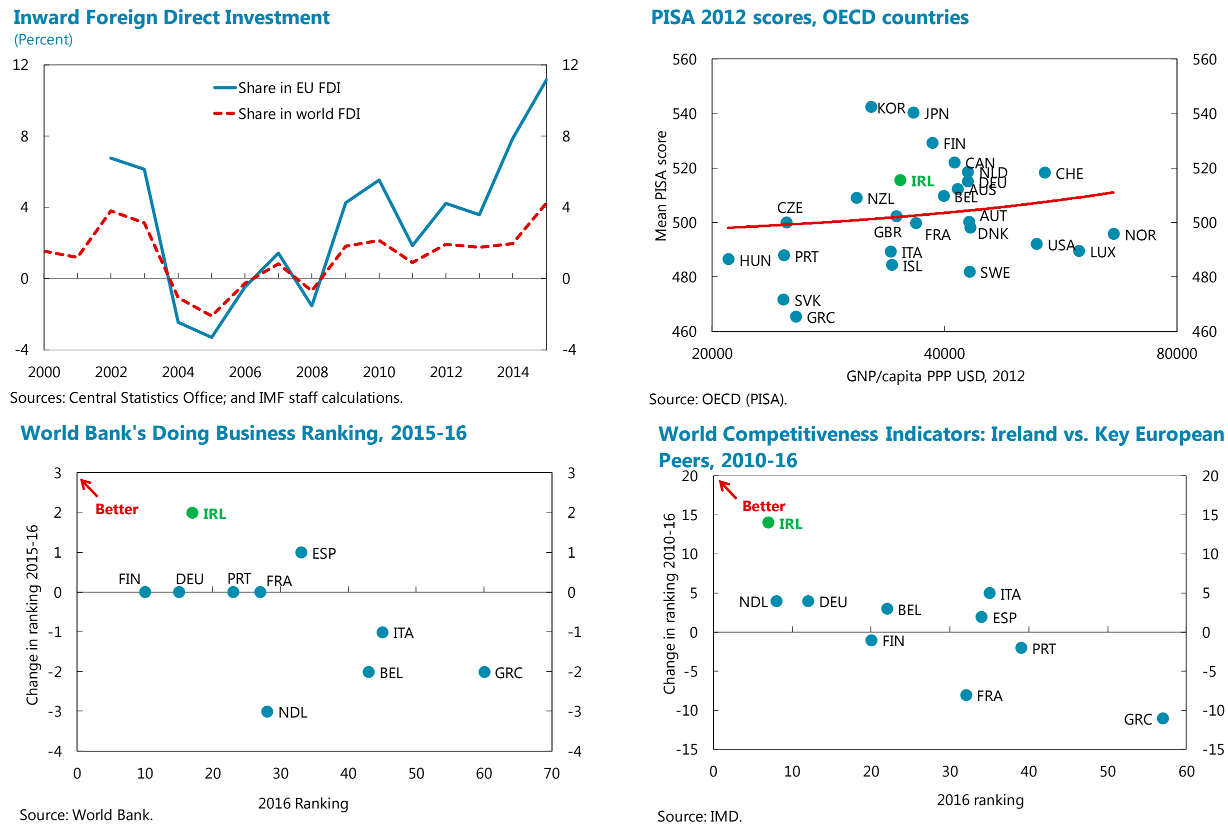
Terms of trade improved sharply in 2015.

Terms of Trade and Export Price Index
(Index, Jan-2009=100)



Source: Central Statistics Office.

Figure 2. Ireland: Share in World and EU FDI and Educational Quality



Annex V. Debt Sustainability Analysis

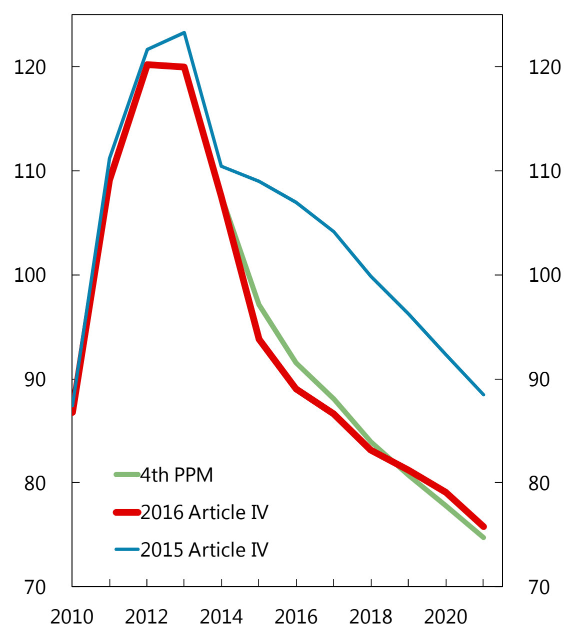
Ireland's public debt sustainability has improved substantially compared to what projected in the 2015 Article IV consultation. This improvement stems from the combination of prudent fiscal policy, strong growth, and favorable financing conditions. The debt dynamics are robust to most shocks; under the contingent liability shock, the public debt ratio deteriorates in the short run before resuming its downward trend. Gross financing needs remain moderate. Asset sales still present an upside risk to the debt trajectory. High external financing requirements and the high share of debt held by non-residents pose potential vulnerabilities. However, the former reflects intra-company and intra-group debt of large multinational corporations operating in Ireland, which is regularly rolled-over. The external debt of the non-IFSC sector, albeit still high, has declined rapidly in the last few years and it is projected to continue on a downward path over the forecast period. Moreover, non-resident holders are mainly real-money investors with long-term investment plans.

Public Debt Sustainability

1. **Rapid nominal GDP growth as well as revisions to historical GDP have lowered Irish debt stock substantially in 2015**. The upward revision of GDP series in mid-2014 (see Box 1 of the Staff Report on Fourth Post-program Monitoring Discussions) led to a decrease of end-2014 debt-to-GDP ratio to 107.5 percent from 110 percent. The lower starting point, together with a large increase in nominal GDP in 2015 (13.5 percent), resulted in a substantial decline of the debt-to-GDP ratio to 93.8 percent at end-2015—about 15 percentage points lower than projected at the time of the 2015 Article IV.

2. **The baseline debt outlook has improved substantially relative to the DSA in the 2015 Article IV report.** This improvement results essentially from a set of positive macroeconomic developments and outlook, particularly the large nominal increase in GDP arising from the robust growth, and the associated revenue buoyancy and falling fiscal deficit:

General Government Gross Debt
(Percent of GDP)



Source: IMF staff calculations and projections.

- *Better growth prospects.* The upward revision to historical GDP data and better growth prospects have improved the debt dynamics.

- *Improved financing conditions.* The ECB's quantitative easing program has been extended and broadened in 2015 and early 2016, and thus the financing conditions are likely to remain benign for most of 2016, despite some widening of Irish sovereign bond spreads following the UK vote to leave the EU. Irish long-term yields have remained below 1 percent. The NTMA has already funded the majority of its requirement for 2016, raising some €6 billion of its full-year target of €6-10 billion, thus locking in the favorable borrowing conditions. The baseline interest rate trajectory is, nonetheless, embedding conservative projections, and rates are assumed to go back to around 3½ percent by the end of the forecasting period.

3. **Despite a much lower debt ratio, the heat map and fan charts indicate that Ireland still faces high debt sustainability risks** (Figure 1). The debt burden threshold placing advanced economies into the "high risk" category is 85 percent of GDP. Although Ireland is now on track to cross this threshold in 2018, at 93.8 percent of GDP at end-2015 it is still classified as highly vulnerable under all scenarios, regardless of the extent to which a shock increases debt. The debt profile under all stress scenarios remains below 95 percent of GDP reached under the contingent liability shock. Gross Financing Needs (GFN) remain moderate under all stress test scenarios, peaking at 13.7 percent of GDP at most under the combined macro-fiscal shock, but remaining below the vulnerability threshold of 20 percent in all cases. High external financing requirements and public debt held by non-residents exceed the upper risk assessment benchmarks for these indicators, raising a high risk flag on the debt profile. However, the former reflects intra-company and intra-group debt of large multinational corporations operating in Ireland, which is regularly rolled-over. The external debt of the non-IFSC sector, albeit still high, has declined rapidly in the last few years and it is projected to continue on a downward path over the forecast period. Moreover, non-resident holders are mainly real-money investors with long-term investment plans.

4. **There is no evidence of a systematic projection bias in the baseline assumptions for key macroeconomic variables**. The median forecast errors for real GDP growth and the primary balance during 2005–13 are below 1 percent and in line with other countries (Figure 2). Individual large forecast errors for growth, primary balance, and inflation mostly arise during the crisis period, especially for the primary balance where there were very large unforeseen bank recapitalization costs.

5. **Ireland's fiscal adjustment is projected to improve its primary balance to above its debt stabilizing threshold** (Figure 3). The projected change in the cyclically-adjusted primary balance is slightly below the top quartile of fiscal adjustments observed in advanced and emerging market countries with debt greater than 60 percent of GDP. This projected adjustment, while reflecting a slowing structural adjustment effort, is also the consequence of diminishing needs for adjustment as the country is getting closer to the medium-term objective (MTO). Nonetheless, the Irish government expressed the intention to over-perform its MTO of a structural deficit of 0.5 percent over the medium term.

6. **The large growth-interest rate differential will continue to drive Ireland's debt ratio lower in the coming two years** (Figures 3 and 4). The interest rate-growth differential contributes, according to staff projections, to most of the decline in the debt ratio over 2016-2017 (about -5 percent of GDP). Thereafter, the debt ratio is projected to record more modest declines and be

driven by a combination of automatic debt dynamics, and a headline surplus. GFN are projected to peak at about 12 percent of GDP in 2020, before dropping back to about 5 percent in 2021.

7. The projected decline in public debt remains vulnerable to a number of shocks (Figure 5). Key risks include:

- **Growth shock**. If projected real GDP growth rates for 2016–17 are lowered by one half of a standard deviation, the debt-to-GDP ratio peaks at 90 percent in 2018 (compared with 83.6 percent under the baseline) before declining.[1]

- **Interest rate shock**. In the medium term, Ireland is shielded from a rise in interest rates by its still-high share of fixed-rate bonds, its EU/IMF and other official sector borrowing, and by relatively low financing needs in coming years (small rollover needs). The assumed interest rate increase on new borrowing affects the debt trajectory only marginally.

- **Macro-fiscal shock.** If slower growth in 2016–17 were accompanied by a primary balance shock[2] and by an increase in interest rates on new borrowing by 2 percentage points, the debt ratio would rise to about 90 percent of GDP in 2018 and resume its declining trajectory thereafter, reaching about 85 percent of GDP in 2021. In this scenario, gross financing needs increase by about 1.6 percentage points of GDP on average over the medium term, reaching 13.7 percent at most in 2020.

- **Contingent liability shock**. Remaining sources of financial sector contingent liabilities include: (i) risks that bank provisions are inadequate to cover losses on their large NPLs; (ii) shortfalls in the crystallized value of NAMA assets; and (iii) costs related to the restructuring of the credit union sector, although these are contained by the size of the sector, with net loans being only 1½ percent of GDP. Without estimates of the potential realization of these contingencies, a scenario assuming a 10 percent of GDP shock is used.[3] Such a shock, if combined with the above growth shock, would push gross public debt to around 94 percent of GDP in 2017 before declining to about 86 percent by 2021.

8. Despite the recent shock to bank stock valuations, asset sales still present an upside risk to debt trajectories. Current baseline assumptions do not incorporate proceeds from any further state asset disposals of stakes in the banks. Recent valuations of state holdings conclude that

---

[1] A one-half standard deviation shock, instead of a default one standard deviation shock, is applied to the growth rate to adjust for the exceptionally volatile growth rates during the recent boom-bust years.

[2] A shock equivalent to the full size of the planned fiscal adjustment over the medium term is used, which worsens primary balances by an average of 1.1 percentage points of GDP. A larger temporary shock derived from baseline primary balance minus one-half of the 10-year historical standard deviation is not yet appropriate, given the exceptionally high primary deficits (reflecting bank recap costs) during the crisis years.

[3] A 10 percent of GDP shock is used, instead of a default shock of 10 percent of banking sector assets (equivalent to around 30 percent of GDP), taking into account the 40 percent of GDP of public support to the financial sector already incurred.

the sale of all state participation would generate about 5 percent of GDP based on end-March 2016 stock prices.

External debt sustainability analysis

9. **While still high, the external debt of the non-IFSC sector has declined rapidly in the last few years, and is projected to continue its fast decline as a percent of GDP.** [4] External debt reached its peak in 2010 at around 320 percent of GDP, and fell to around 250 percent of GDP by end-2015 (Table 1). This gross debt figure includes debt of large multinational corporations, including both intra-company and intra-group debt, which is sizable in Ireland (around 50 percent of total non-IFSC external debt in 2015) because the Irish entity often acts as a group treasury that also has large financial assets. The intra-company and intra-group debt is regularly rolled over, and thus helps explain the high annual gross external financing needs to a large extent, therefore mitigating external vulnerabilities. The debt decline in recent years mostly represented a continued drop in the Target 2 liabilities of the Central Bank of Ireland as banks reduced their reliance on Eurosystem funding, as well as a significant fall in banks' short-term debt. External debt of the general government has flattened in nominal terms since the last tranches of the EU-IMF program were disbursed in late 2013/early 2014. External debt is expected to continue falling, but this is subject to some risks, as all shock scenarios would suggest more gradual reductions in public debt with the interest rate shock having the lowest impact among the historical scenarios. The external debt ratio increases to 162-169 percent of GDP under standardized shocks to the non-interest current account and growth, as well as the combined scenario (Figure 6). Including the IFSC, total external debt remains very high at 815 percent of GDP. Although IFSC debt has declined considerably in recent years, it picked up in 2015, in particular on account of direct investment debt.

[4] The discussion focuses on the non-IFSC sector, as the IFSC principally serves nonresidents.

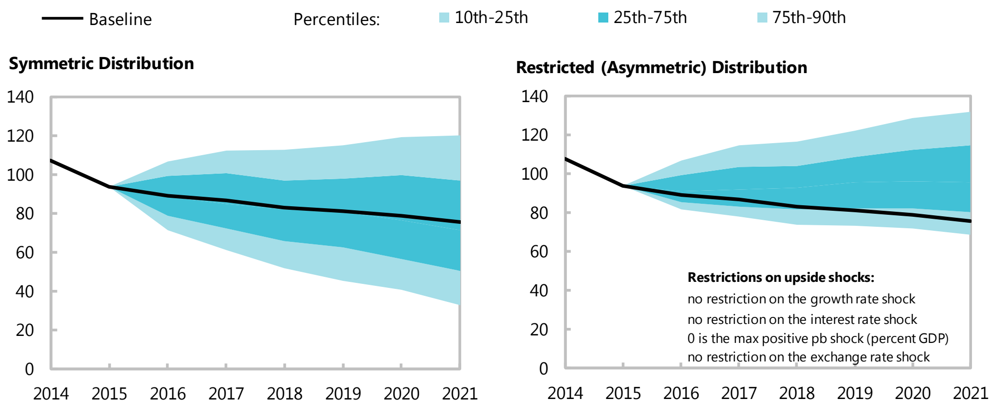
Figure 1. Ireland: Public DSA–Risk Assessment

Heat Map

Debt level 1/	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability shock
Gross financing needs 2/	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability Shock
Debt profile 3/	Market Perception	External Financing Requirements	Change in the Share of Short-Term Debt	Public Debt Held by Non-Residents	Foreign Currency Debt

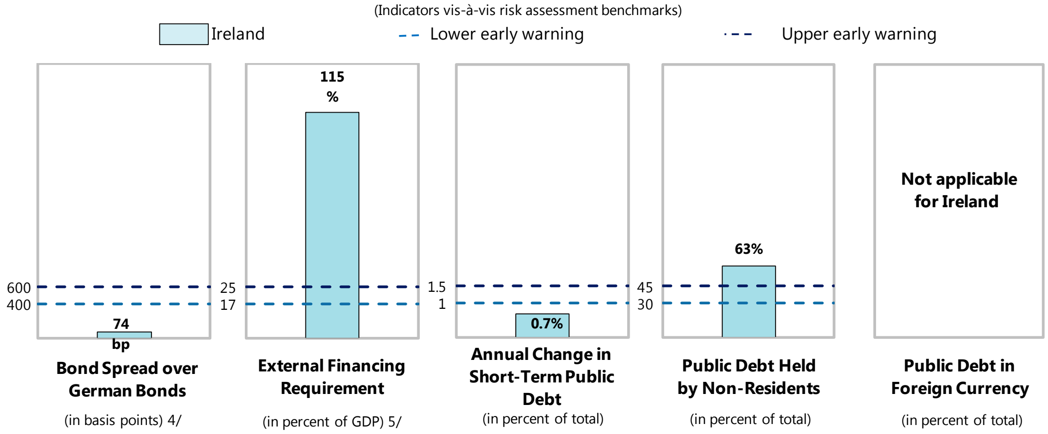
Evolution of Predictive Densities of Gross Nominal Public Debt

(in percent of GDP)



Debt Profile Vulnerabilities

(Indicators vis-à-vis risk assessment benchmarks)



Source: IMF staff.

1/ The cell is highlighted in green if debt burden benchmark of 85 percent of GDP is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

2/ The cell is highlighted in green if gross financing needs benchmark of 20 percent of GDP is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

3/ The cell is highlighted in green if country value is less than the lower risk-assessment benchmark, red if country value exceeds the upper risk-assessment benchmark, yellow if country value is between the lower and upper risk-assessment benchmarks. If data are unavailable or indicator is not relevant, cell is white.
Lower and upper risk-assessment benchmarks are:

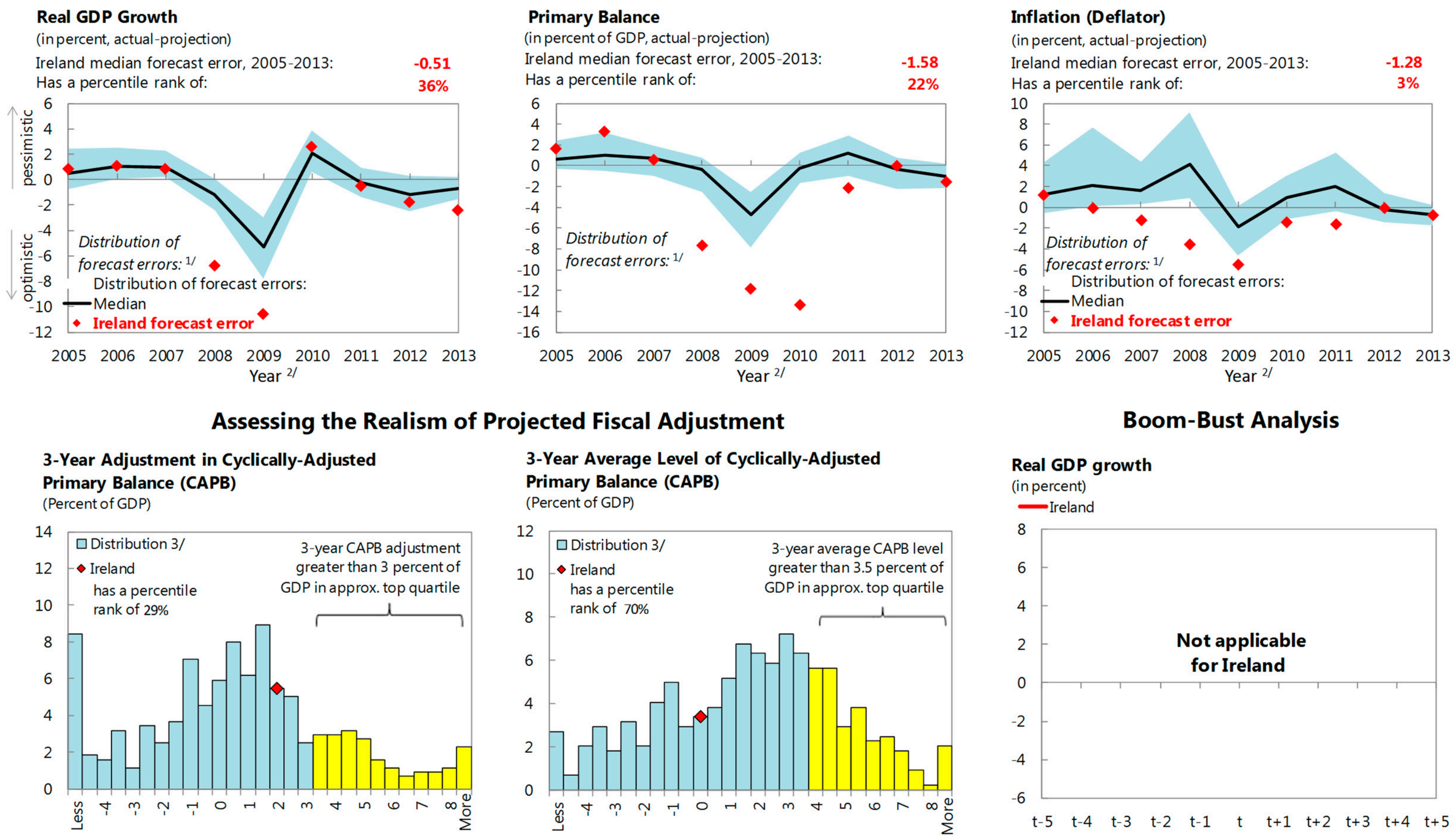
400 and 600 basis points for bond spreads; 17 and 25 percent of GDP for external financing requirement; 1 and 1.5 percent for change in the share of short-term debt; 30 and 45 percent for the public debt held by non-residents.

4/ Average over the last 3 months, 26-Dec-15 through 25-Mar-16.

5/ External financing requirement is defined as the sum of current account deficit, amortization of medium and long-term total external debt, and short-term total external debt at the end of previous period.

Figure 2. Ireland: Public DSA–Realism of Baseline Assumptions

Forecast Track Record, versus surveillance countries



Source : IMF staff.

1/ Plotted distribution includes surveillance countries, percentile rank refers to all countries.

2/ Projections made in the spring WEO vintage of the preceding year.

3/ Data cover annual obervations from 1990 to 2011 for advanced and emerging economies with debt greater than 60 percent of GDP. Percent of sample on vertical axis.

Figure 3. Ireland: Public DSA–Baseline Scenario

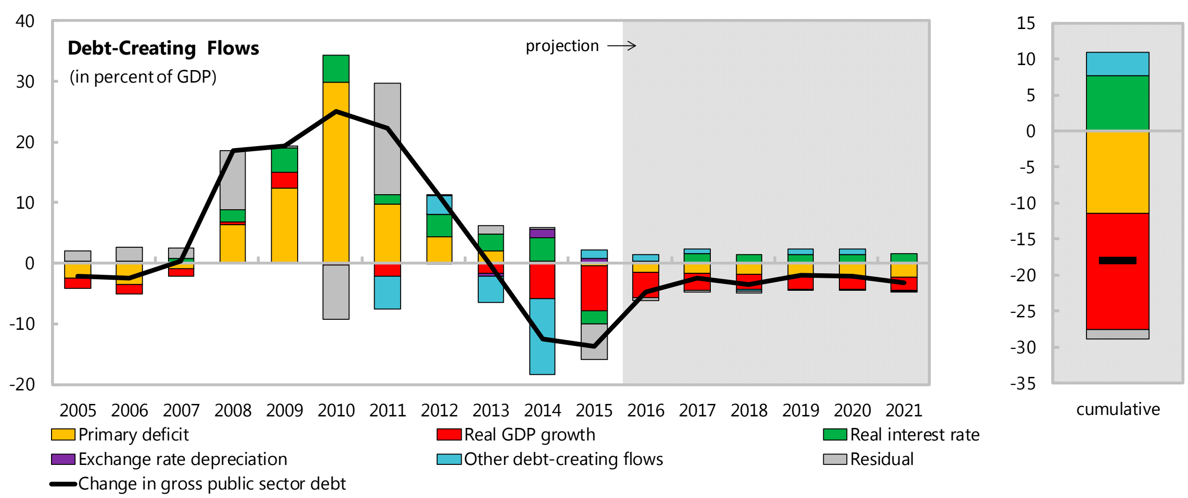
(In percent of GDP unless otherwise indicated)

Debt, Economic and Market Indicators [1/]

	Actual			Projections						As of June 30, 2016		
	2005-2013	2014	2015	2016	2017	2018	2019	2020	2021	Sovereign Spreads		
Nominal gross public debt	68.2	107.5	93.8	89.1	86.6	83.2	81.2	79.0	75.8	Spread (bp) 2/		65
Public gross financing needs	...	18.5	12.5	7.9	7.3	8.1	10.2	11.7	4.9	CDS (bp)		79
Real GDP growth (in percent)	1.7	5.2	7.8	4.9	3.2	3.1	2.8	2.8	2.8	Ratings	Foreign	Local
Inflation (GDP deflator, in percent)	0.0	0.1	5.3	2.8	1.5	1.6	1.6	1.7	1.7	Moody's	A3	A3
Nominal GDP growth (in percent)	1.7	5.3	13.5	7.8	4.8	4.7	4.5	4.5	4.5	S&Ps	A+	A+
Effective interest rate (in percent) [3/]	4.2	3.5	3.3	3.3	3.3	3.4	3.4	3.6	3.7	Fitch	A	A

Contribution to Changes in Public Debt

	Actual			Projections							
	2005-2013	2014	2015	2016	2017	2018	2019	2020	2021	cumulative	debt-stabilizing
Change in gross public sector debt	10.2	-12.4	-13.8	-4.7	-2.4	-3.5	-2.0	-2.1	-3.3	-18.0	primary
Identified debt-creating flows	7.3	-12.8	-7.9	-4.3	-2.1	-3.2	-1.9	-2.0	-3.1	-16.7	balance [7/]
Primary deficit	6.4	0.3	-0.4	-1.5	-1.7	-1.8	-2.0	-2.1	-2.3	-11.4	-0.9
Primary (noninterest) revenue and grants	34.0	34.3	32.4	31.0	30.5	30.2	30.0	29.6	29.3	180.6	
Primary (noninterest) expenditure	40.4	34.6	32.0	29.5	28.8	28.3	28.0	27.5	27.0	169.2	
Automatic debt dynamics [4/]	1.6	-0.7	-8.8	-4.0	-1.2	-1.1	-0.9	-0.8	-0.6	-8.5	
Interest rate/growth differential [5/]	1.6	-2.1	-9.7	-3.9	-1.2	-1.1	-0.8	-0.8	-0.6	-8.5	
Of which: real interest rate	2.2	3.8	-2.3	0.4	1.5	1.5	1.4	1.4	1.5	7.7	
Of which: real GDP growth	-0.6	-5.9	-7.4	-4.3	-2.7	-2.6	-2.3	-2.2	-2.1	-16.1	
Other identified debt-creating flows	-0.7	-12.4	1.3	1.1	0.8	-0.3	1.0	0.9	-0.3	3.3	
Drawdown of deposits (negative)	-0.3	-5.4	1.1	-0.2	0.0	0.0	0.4	0.4	0.3	0.9	
Other, incl. stock-flow adjustment	-0.4	-6.9	0.1	1.3	0.8	-0.3	0.6	0.6	-0.6	2.4	
Residual, incl. interest revenue [6/]	2.9	0.3	-5.8	-0.4	-0.3	-0.3	-0.1	-0.1	-0.1	-1.4	



Source: IMF staff.

1/ Public sector is defined as thegeneral government (including IBRC)

2/ Bond Spread over German Bonds.

3/ Defined as interest payments divided by debt stock (excluding guarantees) at the end of previous year.

4/ Derived as [(r - p(1+g) - g + ae(1+r)]/(1+g+p+gp)) times previous period debt ratio, with r = interest rate; p = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

5/ The real interest rate contribution is derived from the numerator in footnote 4 as r - π (1+g) and the real growth contribution as -g.

6/ Includes asset and exchange rate changes.

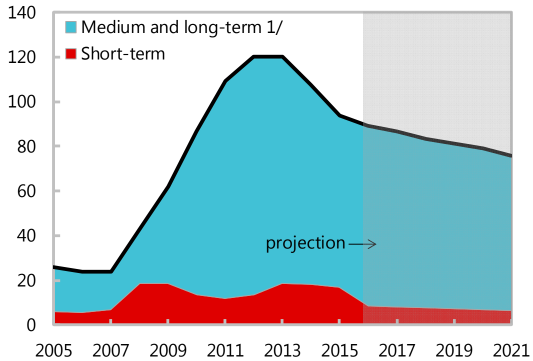
7/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Figure 4. Ireland: Public DSA–composition of Public Debt and Alternative Scenarios

Composition of Public Debt

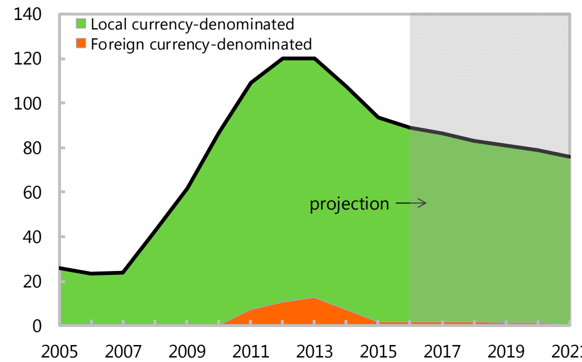
By Maturity

(in percent of GDP)



By Currency

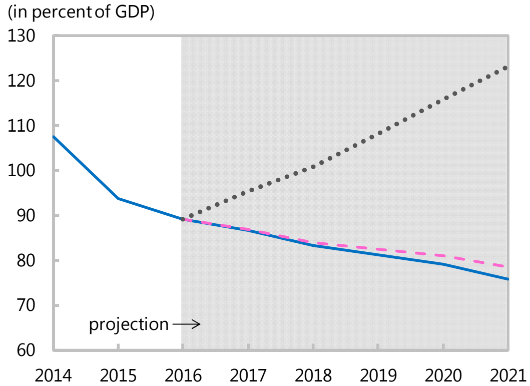
(in percent of GDP)



Alternative Scenarios

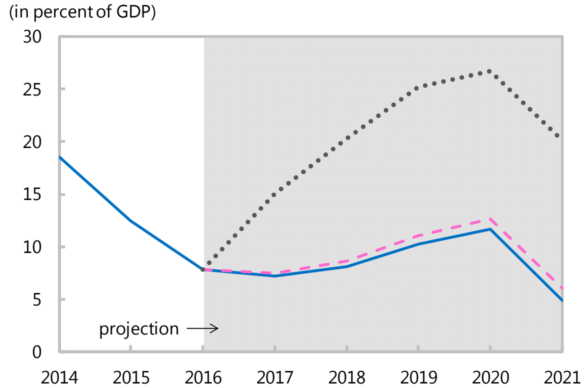
Gross Nominal Public Debt

(in percent of GDP)



Public Gross Financing Needs

(in percent of GDP)



Underlying Assumptions

(in percent)

Baseline Scenario	2016	2017	2018	2019	2020	2021
Real GDP growth	4.9	3.2	3.1	2.8	2.8	2.8
Inflation	2.8	1.5	1.6	1.6	1.7	1.7
Primary Balance	1.5	1.7	1.8	2.0	2.1	2.3
Effective interest rate	3.3	3.3	3.4	3.4	3.6	3.7
Constant Primary Balance Scenario						
Real GDP growth	4.9	3.2	3.1	2.8	2.8	2.8
Inflation	2.8	1.5	1.6	1.6	1.7	1.7
Primary Balance	1.5	1.5	1.5	1.5	1.5	1.5
Effective interest rate	3.3	3.4	3.4	3.5	3.6	3.8

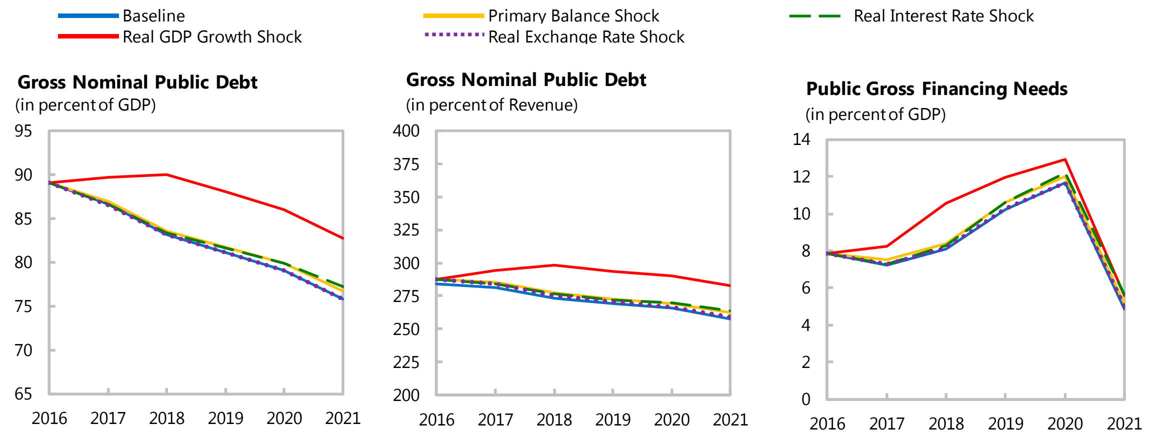
Historical Scenario	2016	2017	2018	2019	2020	2021
Real GDP growth	4.9	2.2	2.2	2.2	2.2	2.2
Inflation	2.8	1.5	1.6	1.6	1.7	1.7
Primary Balance	1.5	-6.0	-6.0	-6.0	-6.0	-6.0
Effective interest rate	3.3	3.4	3.8	4.2	4.8	5.4

Source: IMF staff.

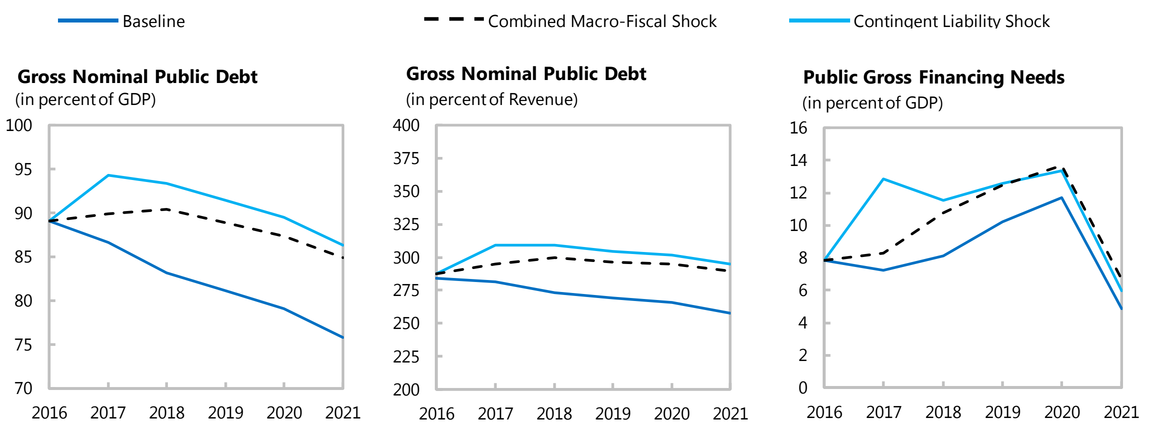
1/ Includes retail debt.

Figure 5. Ireland: Public DSA–Stress Tests

Macro-Fiscal Stress Tests



Additional Stress Tests



Underlying Assumptions

(in percent)

	2016	2017	2018	2019	2020	2021
Primary Balance Shock						
Real GDP growth	4.9	3.2	3.1	2.8	2.8	2.8
Inflation	2.8	1.5	1.6	1.6	1.7	1.7
Primary Balance	1.5	1.5	1.7	1.8	2.0	2.1
Effective interest rate	3.3	3.4	3.4	3.5	3.6	3.8
Real Interest Rate Shock						
Real GDP growth	4.9	3.2	3.1	2.8	2.8	2.8
Inflation	2.8	1.5	1.6	1.6	1.7	1.7
Primary Balance	1.5	1.7	1.8	2.0	2.1	2.3
Effective interest rate	3.3	3.4	3.6	3.8	4.1	4.5
Combined Macro-Fiscal Shock						
Real GDP growth	4.9	1.1	1.0	2.8	2.8	2.8
Inflation	2.8	1.0	1.0	1.6	1.7	1.7
Primary Balance	1.5	1.0	0.3	1.8	2.0	2.1
Effective interest rate	3.3	3.4	3.6	3.8	4.2	4.6

	2016	2017	2018	2019	2020	2021
Real GDP Growth Shock						
Real GDP growth	4.9	1.1	1.0	2.8	2.8	2.8
Inflation	2.8	1.0	1.0	1.6	1.7	1.7
Primary Balance	1.5	1.0	0.3	2.0	2.1	2.3
Effective interest rate	3.3	3.4	3.5	3.6	3.7	3.8
Real Exchange Rate Shock						
Real GDP growth	4.9	3.2	3.1	2.8	2.8	2.8
Inflation	2.8	1.9	1.6	1.6	1.7	1.7
Primary Balance	1.5	1.7	1.8	2.0	2.1	2.3
Effective interest rate	3.3	3.4	3.4	3.5	3.6	3.8
Contingent Liability Shock						
Real GDP growth	4.9	1.1	1.0	2.8	2.8	2.8
Inflation	2.8	1.0	1.0	1.6	1.7	1.7
Primary Balance	1.5	-3.6	1.8	2.0	2.1	2.3
Effective interest rate	3.3	3.4	3.6	3.7	3.8	4.0

Source: IMF Staff.

Table 1. Ireland: External Debt Sustainability Framework, 2011–2021

(In percent of GDP, unless otherwise indicated)

	Actual							Projections						
	2011	2012	2013	2014	2015			2016	2017	2018	2019	2020	2021	Debt-stabilizing non-interest current account 6/
1 **Baseline: External debt**	301.7	280.6	276.5	269.6	248.3			**223.5**	**206.7**	**190.8**	**176.2**	**162.4**	**149.5**	**-0.7**
2 Change in external debt	-16.1	-21.1	-4.1	-6.9	-21.2			-24.9	-16.8	-15.9	-14.6	-13.8	-12.9	
3 Identified external debt-creating flows (4+8+9)	-30.1	53.4	5.1	-3.9	22.8			-16.5	-11.5	-10.4	-9.1	-8.1	-7.3	
4 Current account deficit, excluding interest payments	-18.2	-13.6	-24.8	-11.9	-9.4			-13.3	-11.2	-9.8	-9.4	-9.1	-8.8	
5 Deficit in balance of goods and services	-18.2	-11.7	-13.4	-12.8	-14.8			-21.7	-21.4	-21.4	-21.2	-20.9	-20.6	
6 Exports	92.2	93.0	92.5	99.4	107.0			110.0	111.4	112.3	113.1	113.9	114.7	
7 Imports	73.9	81.3	79.1	86.6	92.1			88.3	90.0	90.9	92.0	93.0	94.1	
8 Net non-debt creating capital inflows (negative)	-2.4	24.0	19.8	9.2	5.9			0.8	1.0	1.1	1.2	1.4	1.5	
9 Automatic debt dynamics 1/	-9.5	43.0	10.2	-1.1	26.3			-4.1	-1.3	-1.8	-0.9	-0.4	0.1	
10 Contribution from nominal interest rate	19.0	19.9	26.2	12.7	11.8			7.3	5.6	4.3	4.3	4.3	4.4	
11 Contribution from real GDP growth	-7.5	-0.5	-3.8	-13.7	-22.2			-11.4	-6.8	-6.1	-5.2	-4.7	-4.3	
12 Contribution from price and exchange rate changes 2/	-21.1	23.5	-12.2	-0.2	36.7			...	...	...	...	...	...	
13 Residual, incl. change in gross foreign assets (2-3) 3/	14.0	-74.4	-9.3	-3.0	-44.0			-8.3	-5.3	-5.4	-5.5	-5.7	-5.6	
External debt-to-exports ratio (in percent)	327.2	301.6	298.9	271.1	232.1			203.2	185.5	170.0	155.7	142.5	130.3	
Gross external financing need (in billions of US dollars) 4/	108.1	60.0	296.7	268.4	247.1			202.0	199.0	195.5	192.2	189.3	186.4	
in percent of GDP	62.1	34.3	165.3	142.0	115.1	10-Year	10-Year	87.3	82.1	77.0	72.4	68.2	64.3	
Scenario with key variables at their historical averages 5/								**220.7**	**220.2**	**219.2**	**218.0**	**216.4**	**214.5**	**13.6**
Key Macroeconomic Assumptions Underlying Baseline						Historical Average	Standard Deviation							
Real GDP growth (in percent)	2.6	0.2	1.4	5.2	7.8	2.2	4.2	4.9	3.2	3.1	2.8	2.8	2.8	
GDP deflator in US dollars (change in percent)	7.1	-7.2	4.6	0.1	-12.0	0.3	2.8	4.0	2.5	1.7	2.1	2.4	1.5	
Nominal external interest rate (in percent)	6.6	6.1	9.9	4.8	4.2	6.2	3.1	3.1	2.6	2.2	2.3	2.5	2.8	
Growth of exports (US dollar terms, in percent)	2.5	1.5	2.0	13.3	22.2	7.3	6.7	10.8	6.2	5.5	5.3	5.3	5.3	
Growth of imports (US dollar terms, in percent)	-0.6	10.6	-0.2	15.4	20.8	7.1	7.5	3.3	6.9	5.7	5.7	5.8	5.8	
Current account balance, excluding interest payments	18.2	13.6	24.8	11.9	9.4	12.4	8.3	13.3	11.2	9.8	9.4	9.1	8.8	
Net non-debt creating capital inflows	2.4	-24.0	-19.8	-9.2	-5.9	-5.8	9.7	-0.8	-1.0	-1.1	-1.2	-1.4	-1.5	

1/ Derived as [r - g - r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock, with r = nominal effective interest rate on external debt; r = change in domestic GDP deflator in US dollar terms, g = real GDP growth rate, e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.

2/ The contribution from price and exchange rate changes is defined as [-r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock. r increases with an appreciating domestic currency (e > 0) and rising inflation (based on GDP deflator).

3/ For projection, line includes the impact of price and exchange rate changes.

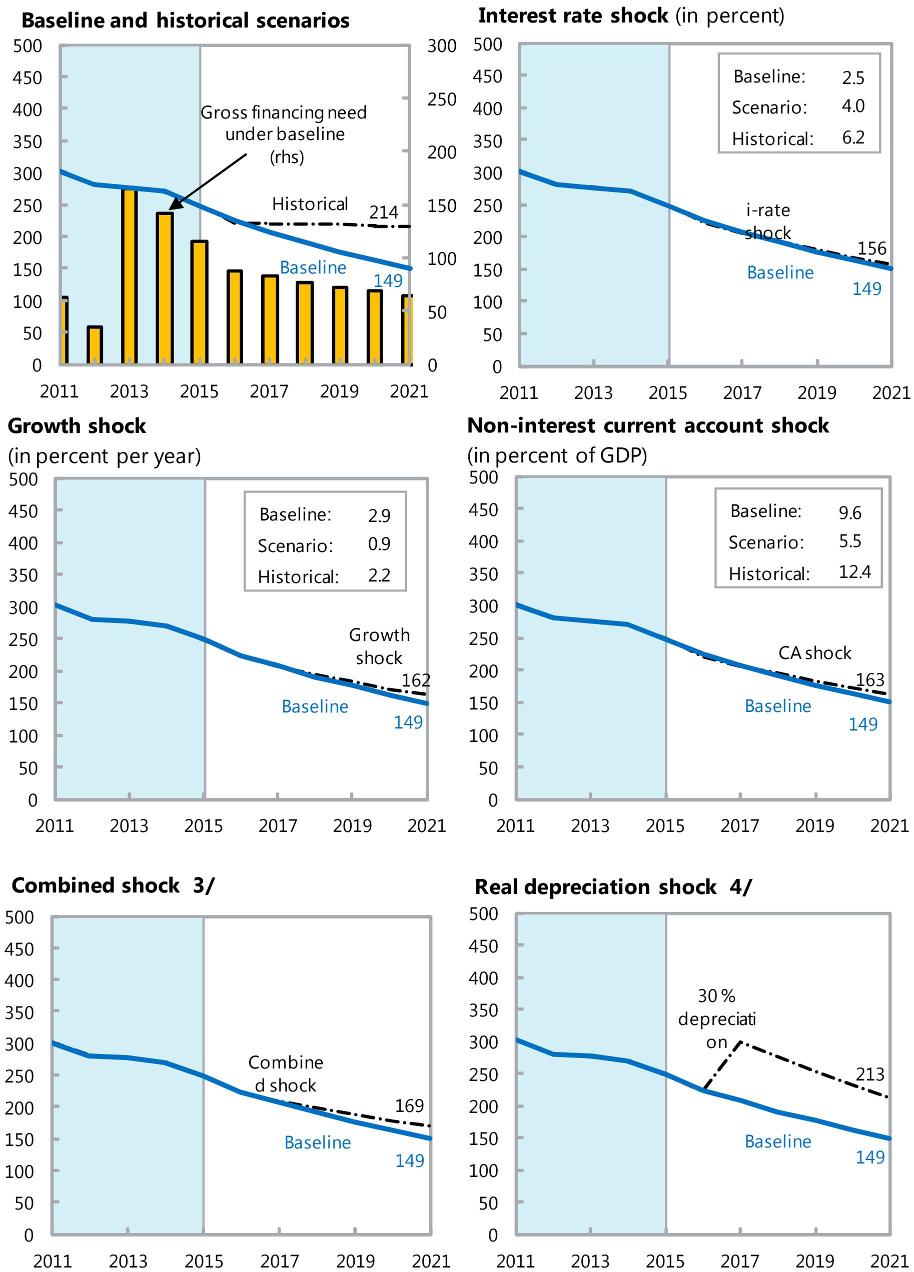
4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

5/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

6/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

Figure 6. Ireland: External Debt Sustainability: Bound Tests 1/ 2/

(External debt in percent of GDP)



Sources: International Monetary Fund; country desk data; and staff projections.
1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.
3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.
4/ One-time real depreciation of 30 percent occurs in 2010.

Annex VI. FSAP Key Conclusions and Recommendations

1. The Irish financial system has strengthened significantly since the crisis but key vulnerabilities remain. While most financial institutions, and in particular the major banks, seem to have built up buffers of capital and liquidity, the FSAP bank stability analysis identified and quantified certain vulnerabilities, notably towards the real estate sector, the sovereign, and funding in pound sterling. Among bank counterparts, pockets of weakness were identified, notably among highly leveraged households. Connections among Irish banks and from them to other financial centers—except the UK—seem to have attenuated over time. Cross-border connections predominate in the funds management industry, which is now of global scale. Still, domestic commercial banks have only limited connections with the funds industry.

2. Financial regulation and supervision have been much strengthened since the crisis, based on recognition of the need to address the vulnerabilities summarized in this report and detailed in the accompanying Financial System Stability Assessment (FSSA). Several of the areas for improvement identified through the recent assessments of observance of the main financial standards have been tackled (see IMF Country Reports 14/135, 14/137, and 15/117). Across the financial system, the authorities have updated regulations to implement relevant EU Directives and refine national legislation. More off-site analysis and on-site supervision—of individual institutions and related to cross-cutting themes such as cyber-risk and the economic consequence of the UK vote to leave the EU—is being undertaken. Staff resources has been expanded substantially, although the retention of experienced personnel is proving difficult. The increased regulatory burden and intrusiveness of supervision, and the necessary independence, demand a high degree of accountability from supervisors.

Regarding individual sectors:

- The Single Supervisory Mechanism (SSM) for banks, in which the ECB is responsible for direct oversight of the "significant institutions" that make up the bulk of the Irish banking system, seems to be working well. It is generally recognized that, as experience is gained with the SSM, further streamlining of certain supervisory processes and regulatory harmonization (such as on licensing and branch authorizations) will yield efficiency gains;
- The complex Solvency II regulations for insurers have been shepherded in. Some current priorities relate to enhancing cross-border supervisory coordination, and ensuring that insurers manage credit risk with due care;
- Securities market regulation continues to evolve quickly, for example, with regard to the capital and governance regime for securities firms, and the protection of investors' funds in winding-up cases. The authorities have undertaken a major effort to gather necessary data and perform analysis of possible systemic risks associated with the funds management industry;
- Macroprudential supervision and policy actions have been ramped up, at both a national and a European level; and

- Financial system safety nets and the resolution framework have been transformed by the recent establishment of the Single Resolution Mechanism. Effort now has to go into optimizing the operations of the revamped system and addressing some transition issues.

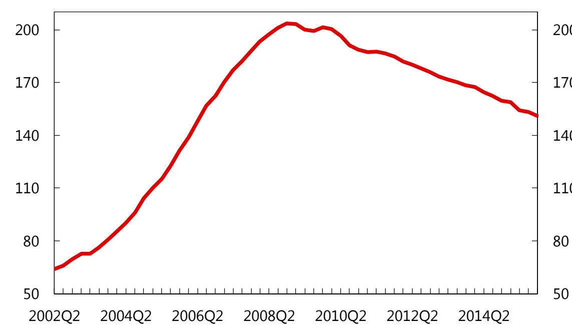
Annex VII. Vulnerabilities of Household and Corporate Sectors[1]

Household sector

1. Since the outbreak of the crisis, households have deleveraged, but are still highly indebted. Household debt-to-disposable income ratio declined to 155.1 percent in 2015Q4 (€151 billion or 74 percent of GDP), but still the Irish household indebtedness is one of the highest in Europe.

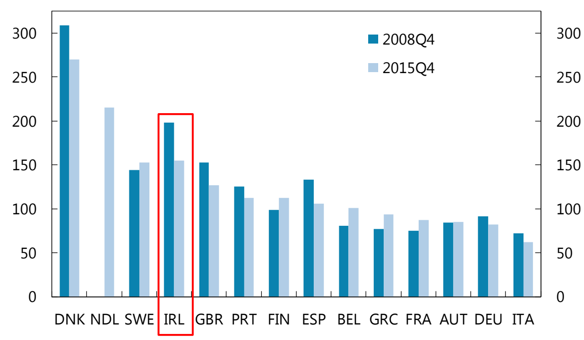
Ireland: Household Debt and Debt-to-Disposable Income Ratio

Household Debt
(Billions of euros)



Source: Central Bank of Ireland.

Household Debt-to-Disposable Income
(Percent of gross disposable income)



Sources: ECB; and Haver Analytics.

2. A sizable share of mortgage loans (23 percent) remains in negative equity, and almost all mortgages (93 percent) have variable interest rates. Negative equity is a well-documented cause of default.[2] As of 2015Q2, tracker loans (linked to ECB interest rates) and standard variable rate (SVR) loans accounted for 51 percent and 41 percent of total mortgages, respectively. Interest rates on existing tracker mortgages are currently very low, reflecting the ECB policy rate. However, if interest rates rise, interest payments will increase and some households may face difficulties servicing their debts.

3. Staff's analysis indicates that existing borrowers with high loan-to-value (LTV) ratios or standard variable rates are more vulnerable to shocks than other groups of households under the FSAP adverse scenario.[3] There is a positive relationship between LTV groups and the stressed probability of default (PD). At an LTV ratio of over 150 percent, the PD under adverse scenario exceeds 20 percent. This segment of households includes younger borrowers, first-time buyers (FTBs), and borrowers outside Dublin. Tracker mortgages have an average PD of 6 percent in

[1] Findings are based on FSAP's technical note on non-banks sector stability analysis by Heedon Kang (MCM), Nir Klein (EUR), and Fergal McCann (CBI).

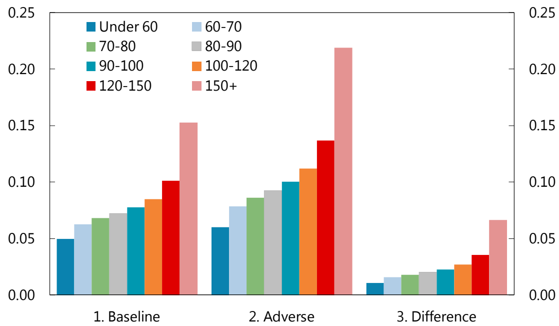
[2] See Lydon and McCarthy (2011) and Kelly and O'Malley (2016).

[3] Predicted three-year probability of default for performing loans as of December 2014 is projected under the FSAP baseline and adverse scenarios using the CBI's Loan-Loss-Forecasting (LLF) model. See Technical Note on Non-Bank Sectors. The assumptions underpinning the stress scenarios are described in the accompanying FSSA.

the adverse scenario, as opposed to a predicted rate of closer to 10 percent for SVR customers. The magnitude of predicted default probabilities suggests that key vulnerabilities persist in the Irish mortgage system, even among those not included in the high stock of defaulted loans, such as FTBs and young households, because of their high current LTV ratios.[4]

Probability of Default by LTV Buckets

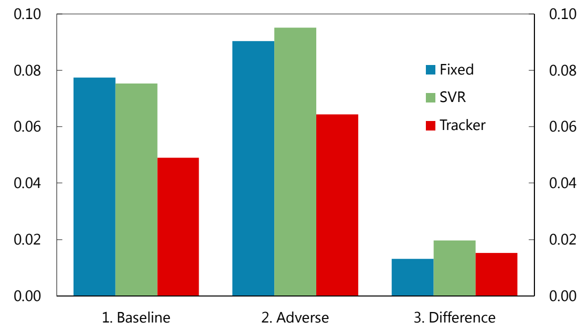
Three-year Scenario PDs for Performing Loans, end 2014
(Across LTV groups)



Source: Central Bank of Ireland.

Probability of Default by Interest Rate Types

Three-year Scenario of PDs for Performing Loans, end 2014
(Accross interest rate types)

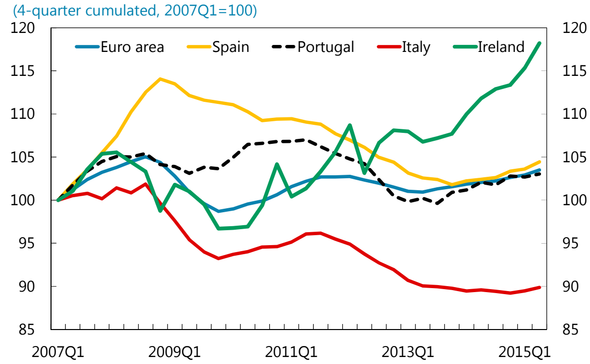


Source: Central Bank of Ireland.

Corporate sector

4. **The activity level of the corporate sector in Ireland has risen significantly recently**. Following a sharp downturn in 2008-09, the activity in the corporate sector has rebounded rapidly in recent years and has exceeded that seen in many of its euro area peers. The robust performance was accompanied with an increase in profitability, which supported the sector's strong investment activity without relying heavily on debt issuance. Accordingly, the sector continued to deleverage.

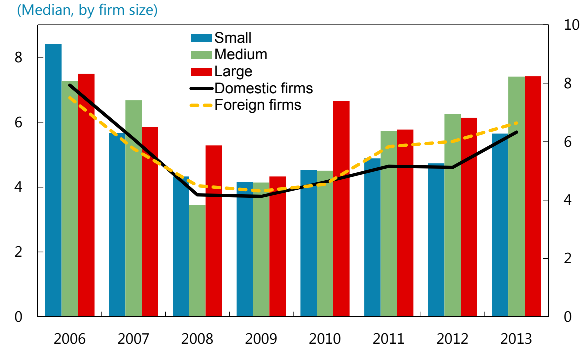
Real Gross Value Added
(4-quarter cumulated, 2007Q1=100)



Sources: Eurostat; and IMF staff calculations.

5. **The increased profitability and the persistent deleveraging reduced the corporate sector's vulnerabilities.** An analysis using Irish firm-level data shows that firms' financial health significantly improved in recent years. The interest cover ratio (ICR) of the median firm across all categories of firm size and sectors increased steadily in recent years, following a sharp decline in 2008-09. The share of firms with ICR lower than one moderated to 18 percent in 2013 from about 28 percent in 2009, reflecting lower

Interest Cover Ratio
(Median, by firm size)



Sources: BvD; and IMF staff estimates.

[4] Kelly and others (2014) have previously shown that, around originating LTV value of 85 percent, the FTB default rate is 45 percent lower than that of previous-owners.

leverage ratios and higher profitability, while the share of risky debt (i.e. owned by firms with ICR lower than one) in total debt has declined to the pre-crisis level of about 10 percent in 2013 from 15 percent in 2009.[5]

6. Still, the corporate sector's vulnerabilities remain elevated. While firms' financial health has generally improved, SMEs remain particularly vulnerable as they account for most of the firms that are under "technical default" (with ICR of less than one). Moreover, the analysis shows that the share of risky debt among small firms (with less than 50 employees) constituted nearly one half of small firms' total debt compared to 9 percent among medium-sized firms and 2 percent among large firms. The analysis also shows that the financial health of foreign subsidiaries operating in Ireland is significantly better than that of domestic firms.

7. A sensitivity analysis indicates that corporates, and especially smaller firms, remain highly vulnerable even to moderate shocks. An adverse shock, which comprises a decline in profitability and an increase in interest rates, is likely to push many firms into a vulnerable state. In particular, the share of firms with ICR lower than one would triple to 47 percent from 16½ percent in the baseline, with more than half of this related to the deterioration in the financial health of small firms. In such a scenario, the share of risky debt would increase to about 15 percent, similar to the level observed during the financial crisis.

8. The analysis suggests that further efforts are needed to strengthen the corporate sector's resilience. Continued corporate NPL resolution, including through loan restructuring for the most vulnerable, yet viable, firms would allow the remaining companies to invest and support a durable expansion of economic activity. At the same time, policies should support the exit of unproductive or unviable firms.

[5] The interest cover ratio is calculated as the ratio between the firms' earnings before interest, taxes, depreciation and amortization (EBITDA), and the firms' interest expenses.

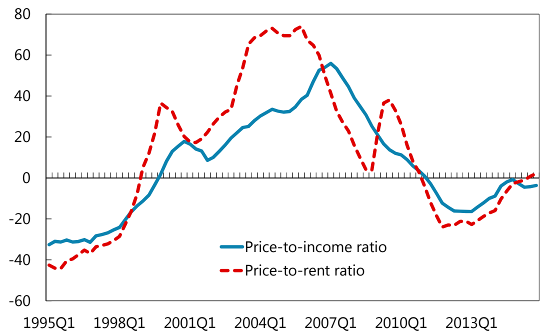
Annex VIII. Do Property Prices Diverge from Equilibrium?[1]

1. Residential and commercial real estate prices in Ireland have been increasing rapidly in recent years, raising concerns about possible overvaluation and a build-up of new imbalances. An analysis that is based on both non-parametric and parametric methods suggests that the residential property market is close to or moderately below its equilibrium level, while the CRE market shows more mixed results.

Residential Real Estate (RRE) Market

2. Non-parametric approach: The standard metrics of price-to-income and price-to-rent ratios suggest that, following a protracted period of over-valuation prior to the crisis and a correction afterwards, the market was close to its equilibrium level in 2015Q2.[2]

Price-to-Income and Price-to-Rent Ratio
(Percent, deviation from historical mean, 1990Q1-2015Q4)



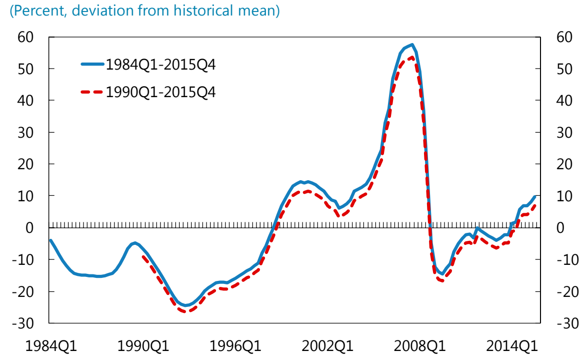
Sources: OECD; and IMF staff calculations.

3. Parametric methods: Various estimation techniques, including frequency and Hoddrick-Prescott filters, Ordinary Least Squares with a pseudo error correction, and a Vector Error Correction Model (VECM), showing an undervaluation of property prices in a range of 0-10 percent. The Markov Regime Switching Model, which identifies different periods of growth regimes, indicates that the probability of being in a "high growth" regime increased markedly in 2013-14, but dropped in the beginning of 2015 with the implementation of the new macro-prudential measures.

Commercial Real Estate (CRE) Market

4. Non-parametric approach: The CRE price-to-rent ratio suggests that following a sharp correction at the onset of the crisis, CRE prices increased above their historical averages in 2014, and, at 2015Q3, they were moderately overvalued at about 10 percent.

Commercial Real Estate Market: Price-to-Rent Ratio
(Percent, deviation from historical mean)



Sources: Central Bank of Ireland; and IMF staff calculation.

5. Parametric methods: While the frequency and HP filters show that the CRE prices have recently converged to their long-term trends, econometric models show a

[1] The findings are based on an FSAP's technical note by Heedon Kang with inputs from Chris Wilson.

[2] The required return on property has fluctuated over time. A long-term average benchmark (deviations of price-to-rent and price-to-income ratios from their historical means) is used to reflect the return over the whole cycle.

moderate undervaluation of about 5-8 percent. A Markov Regime Switching Model suggests that the CRE market entered into a high-growth regime probability since the second half of 2013.

INTERNATIONAL MONETARY FUND

IRELAND

July 13, 2016

STAFF REPORT FOR THE 2016 ARTICLE IV CONSULTATION AND FIFTH POST-PROGRAM MONITORING DISCUSSIONS—INFORMATIONAL ANNEX

Prepared By	European Department

CONTENTS

FUND RELATIONS

(As of June 30, 2016)

Membership Status: Joined August 8, 1957; Article VIII

General Resources Account:	**SDR Million**	**Percent of Quota**
Quota	3,449.90	100.00
Fund holdings of currency	6,415.96	185.98
Reserve position in Fund	806.78	23.39

SDR Department:	**SDR Million**	**Percent of Allocation**
Net cumulative allocation	775.42	100.00
Holdings	651.14	83.97

Outstanding Purchases and Loans:	**SDR Million**	**Percent of Quota**
Extended Arrangement	3,772.80	109.36

Financial Arrangements:

Type	**Approval Date**	**Expiration Date**	**Amount Approved (SDR million)**	**Amount Drawn (SDR million)**
EFF	12/16/10	12/18/13	19,465.80	19,465.80

Projected Payments to the Fund (SDR million; based on existing use of resources and present holdings of SDRs):

	2016	2017	2018	2019	2020
Principal					
Charges/Interest	19.95	39.69	39.70	39.70	39.72
Total	19.95	39.69	39.70	39.70	39.72

Exchange Rate Arrangement and Exchange Restrictions:

Ireland's currency is the euro, which floats freely and independently against other currencies. Ireland has accepted the obligations of Article VIII, Sections 2, 3, and 4, and maintains an exchange system free of restrictions on payments and transfers for current international transactions, other than restrictions notified to the Fund under Decision No. 144 (52/51).

Article IV Consultations:

The last Article IV consultation was concluded on March 25, 2015 (IMF Country Report No. 15/77). Article IV consultations with Ireland were on the 24-month cycle during the Extended Arrangement.

Resident Representative:

The resident representative office in Ireland closed in June 2014.

STATISTICAL ISSUES

A. Assessment of Data Adequacy for Surveillance
General: Data provision is broadly adequate for surveillance.
National accounts and real sector data. Quarterly national accounts are currently published within three months of its reference period. Other real sector data are relatively timely, with industrial production and retail sales data published within six weeks and employment data within 3 months of the reference period, but some non-SDDS series are published one and a half years later (e.g., household disposable income). Employment and unit labor costs, and national income and expenditure data are usually available with a three-month lag.
Wages and earnings statistics. The quarterly Earnings, Hours and Employment Costs Survey has replaced the four-yearly Labor Cost Survey, and also replaces all other existing short-term earnings surveys. The results are comparable across sectors and include more detail on components of earnings and labor costs than was available before. However, data are only available with more than a six-month lag.
Government finance statistics. The authorities publish Exchequer returns and indicative estimates of the general government balance on a monthly basis. The definitive general government balance is reported quarterly and annually. Ireland reports these data to STA through a conversion of the datasets reported to Eurostat under the "ESA Transmission Programme".
Monetary and financial statistics: The ECB reporting framework is used for monetary statistics and data are reported to the IMF through a "gateway" arrangement with the ECB. The arrangement provides an efficient transmission of monetary statistics to the IMF and for publication in the IMF's *International Financial Statistics (IFS)*.
Financial sector surveillance: Ireland reports FSIs for deposit takers, other financial corporations, and real estate markets on a regular basis for posting on the IMF's FSI website.
External sector statistics. Quarterly balance of payments (BOP) and international investment position (IIP) data are compiled by the Central Statistics Office. The authorities implemented the sixth edition of the *Balance of Payments and International Investment Position Manual (BPM6)*. The most recent BOP and IIP data reported to STA and disseminated in the *IFS* are for Q4/2015. Ireland reports data for the Coordinated Portfolio Investment Survey (CPIS), the Coordinated Direct Investment Survey (CDIS), and the Data Template on International Reserves and Foreign Currency Liquidity.

B. Data Standards and Quality	
Ireland is subject to the statistical requirements and timeliness and reporting standards of Eurostat and the European Central Bank (ECB). Ireland subscribes to the Fund's Special Data Dissemination Standard and uses SDDS flexibility options on the timeliness of wages and earnings, and central government debt data.	No data ROSC is available.

Ireland: Table of Common Indicators Required for Surveillance

(as of July 11, 2016)

	Date of Latest Observation	Date Received	Frequency of Data[7]	Frequency of Reporting[7]	Frequency of Publication[7]
Exchange Rates	July 11, 16	7/11/2016	D	D	D
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	June 2016	7/7/2016	M	M	M
Reserve/Base Money	May 2016	6/30/2016	M	M	M
Broad Money	May 2016	6/30/2016	M	M	M
Central Bank Balance Sheet	June 2016	7/8/2016	M	M	M
Consolidated Balance Sheet of the Banking System	May 2016	6/30/2016	M	M	M
Interest Rates[2]	June 2016	7/1/2016	M	M	M
Consumer Price Index	May 2016	6/09/2016	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	2015:Q4	4/20/2016	Q	A	A
Revenue, Expenditure, Balance and Composition of Financing[3]– Central Government	June 2016	7/4/2016	M	M	M
Stocks of Central Government and Central Government-Guaranteed Debt[5]	2015:Q4	5/5/2016	Q	Q	Q
External Current Account Balance	2015:Q4	3/10/2016	Q	Q	Q
Exports and Imports of Goods and Services	2015:Q4	3/10/2016	Q	Q	Q
GDP/GNP	2015:Q4	3/10/2016	Q	Q	Q
Gross External Debt	2015:Q4	3/16/2016	Q	Q	Q
International Investment Position[6]	2015:Q4	3/16/2016	Q	Q	Q

[1] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[2] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[3] Foreign, domestic bank, and domestic nonbank financing.
[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
[5] Including currency and maturity composition.
[6] Includes external gross financial asset and liability positions vis-à-vis nonresidents.
[6] Includes external gross financial asset and liability positions vis-à-vis nonresidents.
[7] Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Annually (A); Not Available (NA).