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Assessment of the 2014 national reform programme and stability programme for IRELAND

Accompanying the document

Recommendation for a COUNCIL RECOMMENDATION

on Ireland's 2014 national reform programme and delivering a Council opinion on Ireland's 2014 stability programme

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EXECUTIVE SUMMARY

Ireland is emerging from the crisis and returning to a path of balanced growth. Rebalancing between the tradable and non-tradable sectors has been significant over the past few years, associated with regained competitiveness and the emergence of a large current account surplus. As per the Commission 2014 spring forecast, real GDP is expected to grow by 1.7 % in 2014, with rising momentum from investment and private consumption as business and consumer confidence improve. The continued recovery in key trading partners should help boost exports of goods and services. Employment is expected to continue rising by 2.4% in 2014. However, due to migration trends and rising participation rates, unemployment is projected to decline more moderately to 11.4% in 2014. Wage and price pressures should remain subdued, further boosting competitiveness.

Ireland successfully completed its EU-IMF financial assistance programme in December 2013. Given that the programme was still on-going, Ireland had only one country-specific recommendation in 2013, namely to meet the terms of the Memorandum of Understanding. Under the three-year programme, the government launched a fiscal consolidation plan that reduced the general government deficit from 10.6 % of GDP in 2010 (excluding bank support measures) to 7.2% in 2013, and significantly improved fiscal rules and institutions. Banks embarked on an impressive deleveraging process with loan-to-deposit ratios falling by 90 pps. between 2008 and 2013. Bank capital adequacy ratios rose thanks to further capital injections by the government following stress tests. The supervisory and regulatory role of the Central Bank of Ireland was strengthened through numerous reforms. The authorities undertook labour market reforms, including a reshaping of activation policies. The unemployment rate fell from a high of 14.9 % in early 2012 to 11.6 % at end-2013 while labour costs declined. Private households increased their saving rates to cut their indebtedness, while house prices, after falling by more than 50 % from their peak in 2007 peak, have started to recover, especially in Dublin. As a result, real GDP posted low but positive growth in 2011-13.

Despite these achievements, there are still important challenges to be addressed, especially in the areas of fiscal consolidation, and financial and structural reforms. These challenges are at the core of the policy plans submitted by Ireland, and the national reform programme rightly proposes to build on the reform momentum gained under the EU-IMF programme of financial assistance.

- **Public finances:** Government debt remains high at 123.7 % of GDP in 2013 and significantly above the 60 % threshold. The level of debt reflects the impact of the banking crisis, among other things. Under the Excessive Deficit Procedure, the government is expected to reduce the budget deficit to below 3.0 % of GDP by 2015. The continued provision of quality health services poses a challenge to fiscal sustainability. Pensions and other costs associated with an ageing population are also a challenge for the long-term debt sustainability of public finances.

- **Financial sector:** High private-sector debt remains a risk to financial stability. Bank lending continues to fall, the level of non-performing loans remains high and the banking sector is still not profitable. The latter is due in part to the large amount of tracker mortgages (low-yielding legacy assets) on banks' balance sheets. The restructuring of all banks concerned has not yet been finalised. It is still difficult for SME to access finance, reflecting a combination of sluggish credit demand and supply constraints. Restoring credit channels is nevertheless crucial for the growth outlook, while government-backed SME financing facilities have had a low uptake.

- **Labour market and education:** Long-term and youth unemployment, the high prevalence of low work intensity, skills mismatches and inactivity traps for some

groups are key challenges facing Ireland. They have led to deterioration in social indicators and generated significant distress. Although overall unemployment has fallen recently, these challenges remain to be addressed fully.

- **Business environment:** Overall, Ireland has a positive business climate, but the cost of legal services remains high and raises the cost of doing business, particularly for SMEs.

1. INTRODUCTION

In May 2013, the Commission proposed only one country-specific recommendation (CSR) for economic and structural reforms in Ireland. This was to implement its commitment under the EU-IMF financial assistance programme. On the basis of this recommendation, the Council of the European Union adopted this CSR in the form of a Council Recommendation. Ireland successfully completed its three-year EU-IMF-supported programme in December 2013 (box 1).[1] The programme focused on fiscal consolidation, banking sector restructuring and structural reforms. The authorities' strong ownership of the programme was key to its success and programme implementation was strong overall. However, there are still challenges, as highlighted in the Commission's in-depth review (IDR) of Ireland. Public debt remains high at 123.7 % of GDP in 2013, fiscal consolidation is incomplete, the private sector still suffers from a debt overhang, banks remain affected by the high level of non-performing loans and low profitability, and credit channels are not fully restored. This staff working document identifies current policy challenges.

Box 1: Implementation of the EU/IMF financial assistance programme in Ireland

Performance under the EU/IMF-supported programme was strong and underpinned by the authorities' ownership of the arrangement. The programme was based on the government's National Recovery Plan. It was approved by the European Commission and the IMF in December 2010, and expired three years later. The centrepiece of the programme was to regain financial stability, and it also focused on fiscal policy and structural reforms. The programme also attempted to protect growth and to an extent, this was achieved, as Ireland's average growth during 2011-13 was 0.7 %, higher than that of the euro area.

Regulatory and supervisory reforms along with a recapitalisation of the banking system safeguarded financial stability. Stress tests in 2011 led to a further EUR 24 billion (15 % of GDP) recapitalisation and fundamental reorganisation of the banking system. Legislation gave new resolution powers to the Central Bank of Ireland and created a credit institutions resolution fund. It also reformed the bankruptcy and personal insolvency regimes; enhanced the supervision and enforcement powers of the Central Bank of Ireland; strengthened the regulatory framework for credit unions; and provided for the establishment of a statutory credit register. Supervision was reinforced through enhanced provisioning and disclosure guidelines for banks and a new risk-based supervisory system. Financial soundness indicators improved as the three main domestic banks' core tier one risk based capital ratio was 14.1 % in June 2013, and provisions rose by 7.9 % from end-2010 to mid-2013. Large bank balance sheets shrunk as loan-to-deposit ratios fell from 170 % at end-2010 to 120 % by September 2013. Domestic deposits stabilised and grew by 7.5 % between end-2010 and end-2013, while deposit rates declined. Irish banks' reliance on funding from the Eurosystem fell by 73 % from its peak in November 2010, to below pre-programme levels.

Fiscal consolidation was underpinned by improvements in the fiscal framework. Work on comprehensive reform of the medium-term budgetary framework progressed. *The Fiscal Responsibility Act (2012)* introduced the national budgetary rules and implemented an Irish Fiscal Advisory Council. The Council assesses the official economic and budgetary forecasts, compliance with budgetary rules and the government's fiscal stance. Ministerial expenditure ceilings for three years on a rolling basis were also introduced. Fiscal data provision, quality and transparency improved with the quarterly publication of general

[1] Quarterly reviews under the programme are available at http://ec.europa.eu/economy_finance/assistance_eu_ms/ireland/index_en.htm

government finance statistics. From 2010, the structural budget deficit fell by 2.5 percentage points of GDP to 6.4 % of GDP in 2013 and most of the adjustment was expenditure based.

Structural reforms focused on the labour market to raise employment and on measures to raise competitiveness. An activation system was established and there are reforms to improve training for the unemployed, increase capacity to deliver activation support and improve incentives to work. Reforms were adopted to enable wage-setting in certain sectors to be more responsive to economic conditions. The programme included measures to open up sheltered sectors to competition, with a focus on the legal and medical professions. A major reform of the water sector was undertaken to improve efficiency and ensure financial sustainability. Real unit labour costs fell 9.9 % between 2009 and 2013, while the unemployment rate (age group 20-64) fell from a high of 14.9 % in the first quarter of 2012 to 11.6 % in the fourth quarter of 2013.

This staff working document also assesses policy measures against the background of the Commission's Annual Growth Survey 2014 (AGS)[2] and the third annual Alert Mechanism Report (AMR)[3], which were published in November 2013, as well as the IDR published in March 2014. The 2014 Annual Growth Survey sets out the Commission's proposals for building the necessary common understanding about the priorities for action at national and EU level in 2014. It identifies five priorities to guide Member States to renewed growth: pursuing differentiated, growth-friendly fiscal consolidation; restoring normal lending to the economy; promoting growth and competitiveness; tackling unemployment and the social consequences of the crisis; and modernising public administration. The 2013 Alert Mechanism Report served as an initial screening device to ascertain whether macroeconomic imbalances exist or risk emerging in Member States. In the report, the Commission briefly discussed the case of Ireland and stated that the country's situation in the context of the Macroeconomic Imbalance Procedure would be assessed after the end of the EU-IMF financial assistance programme. Following the end of the programme in February 2014, the Council considered that Ireland should be fully integrated in the European Semester framework, including the Macroeconomic Imbalance Procedure, and invited the Commission to prepare an IDR for Ireland. Thus Ireland, along with 16 other Member States, was selected for a review of developments in the accumulation and unwinding of imbalances. These in-depth reviews were published on 5 March 2014 along with a Commission communication. The 2014 IDR highlighted remaining macroeconomic imbalances in Ireland that require specific monitoring and decisive policy action. The Commission put in motion specific monitoring of policy implementation, and will regularly report to the Council and the Euro Group. This monitoring will rely on post-programme surveillance.

Against this background, Ireland sent its national reform programme (NRP) on 17 April 2014 and its stability programme on 29 April 2014. The programmes provide details of plans for the future, and consistency between the two documents has been ensured. These programmes were submitted to an inclusive consultation process involving the Parliament, local authorities and social partners prior to approval by the Government. The macroeconomic forecasts contained in the stability programme were endorsed by the Irish Fiscal Advisory Council on 7 April 2014. The national reform programme confirms Ireland's commitment to addressing shortcomings in the areas identified by the 2014 Annual Growth Survey and the 2014 IDR.

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[2] COM(2013) 800 final.

[3] COM(2013) 790 final.

2. ECONOMIC SITUATION AND OUTLOOK

Economic situation

Flat growth in 2013 obscures an underlying recovery in the domestic economy. In the year as a whole real GDP shrank by 0.3 %, driven largely by falling output in the foreign-owned pharmaceutical sector. GNP growth was more robust, at 2.9 %, and is a reflection of the relative health of the domestic economy. This recovery was evident in a surge in investment in machinery and a smaller increase in construction, even as private consumption remained muted.

The labour market, on which there was a significant impact during the crisis, marked a turning point in 2013, with improvements across all labour market indicators. Employment gains seen earlier in 2013 mainly in the part-time and casual sectors of the labour force have since been matched by further gains in full-time employment. The unemployment rate fell from 13.7 % in January 2013 to 11.9 % a year later. Employment gains have been recorded across all sectors, and participation rates are also rising steadily. Net migration, though still negative, has risen from a trough of -34 400 in 2012 to an estimated -4 200 in 2014, and is expected to turn positive by 2015.

The housing market appears to have stabilised, but the credit conditions faced by households remain tight. Although the number of new mortgages continued to contract throughout 2013, property prices have stabilised nationally, rising at a rate of 8.1% in the year to February 2014. The national figure disguises the emergence of a two-tiered property market, driven by growth in the Dublin market, where prices rose 13.3% over the same period.

Economic outlook

The Commission 2014 spring forecast expects the Irish recovery to continue apace. GDP is projected to grow by 1.7 % in 2014, accelerating to 2.9 % in 2015. Public consumption is still affected by the ongoing need to achieve fiscal consolidation, while investment and private sector consumption are beginning to make positive contributions, as both businesses and consumers regain confidence. Recovery in key trading partners such as the United Kingdom has already given Ireland a boost, and this is set to continue into 2014, supporting in particular service exports and exports from the agri-food sector. As the recovery begins to take hold in other key trading partners, Ireland's export-oriented economy is set to benefit further in 2015.

The Irish labour market will continue to stabilise. Employment is projected to continue on its steady upwards path as employers gain confidence and the recovery spreads to more job-rich sectors of the labour market, resulting in an annualised employment growth rate of 2.4% and 2.3% for 2014 and 2015 respectively. However, a projected reversal of recent net emigration trends and a rise in participation rates will mean that the effect on unemployment may be somewhat more subdued, with rates still falling to 11.4 % in 2014 and 10.2 % in 2015. The persistence of significant slack and the very low rates of imported inflation mean that labour market growth is not expected to result in significant wage pressure. This, combined with sustained rates of inflation below the euro area average, should further improve Ireland's competitiveness.

Investment will grow against a backdrop of continued credit constraints. Also, as a result of a large contribution from aircraft purchases, investment levels are forecast to rise in both 2014 and 2015, but their contribution to growth will remain modest. For construction, the expected level of investment is seen as insufficient to meet the emerging demand for both residential and commercial property, which is projected to grow in key centres of economic activity.

The macroeconomic scenario underpinning the stability programme and national reform programme is broadly in line with Commission forecasts. However, the contributions of the demand components for 2014 and 2015 differ, with the authorities forecasting a stronger contribution from private consumption and a weaker net export performance than is estimated in the Commission 2014 spring forecast. Additionally, while overall the Commission forecasts stronger nominal growth in the short term, different assumptions on price developments lead to a lower real GDP forecast for 2014 and 2015 than is assumed in the stability programme. The authorities' medium-term forecast (from 2016 to 2018) appears based on an optimistic assessment of the recovery in net exports, while their forecast unemployment rate for the outer years is also below that of the Commission. The macroeconomic scenario set out in the stability programme does not include a quantification of the impact of structural reforms.

3. CHALLENGES AND ASSESSMENT OF POLICY AGENDA

The Medium Term Economic Strategy 2014–20 provides the umbrella for Ireland's economic policy agenda. The government published the strategy in December 2013 upon exiting the EU-IMF programme of financial assistance. It defines a high-level policy framework with which more specific strategies and plans at the Department level need to be aligned. It is based on three pillars: ensuring debt sustainability; financing growth and supporting employment and living standards. It also underpins the national reform programme, which rightly higlights the need to sustain the reform momentum achieved under the EU-IMF programme and identifies challenges that need to be addressed further.

3.1. Fiscal policy and taxation

Budgetary developments and debt dynamics

The main objectives of the budgetary strategy outlined in the medium term economic strategy and confirmed in the 2014 stability programme are to correct the excessive deficit by 2015 and reaching the medium-term budgetary objective by 2018. The government targets a fiscal deficit below the 3 % of GDP threshold in 2015 (excluding one-off financial sector measures of less than 0.1 % of GDP).[4] The deficit is expected to be further reduced to 2.2 % of GDP in 2016, 1.2 % in 2017 and to a balanced position in 2018. Based on the programme's estimates, the medium-term budgetary objective is projected to be reached in 2018. The medium-term budgetary objective is defined as a balanced position in structural terms and is consistent with the provisions of the Stability and Growth Pact. The recalculated structural balance[5] amounts to a deficit of 1.9 % of GDP in 2018 as a consequence of significantly different potential output and output gap estimates. The authorities project the closure of the output gap in 2017–18. In contrast, the recalculated positive output gap is at 3.7 % of potential GDP in 2018. The difference largely reflects the authorities' buoyant annual growth projections of 3.5 % per annum in 2007–18 and specificities in the government's method for calculating potential growth.[6] While the measurement of potential output in real-time for a small open economy like Ireland is subject to considerbale degree of

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[4] One-off deficit increasing financial sector measures are excluded from the EDP deficit ceilings for Ireland. The authorities assume one-off deficit increasing transfers to credit unions of EUR 50 million in 2014 and EUR 100 million in both 2015 and 2016 (less than 0.1% of GDP).

[5] Cyclically adjusted balance net of one-off and temporary measures, recalculated by the Commission services on the basis of the information provided in the programme, using the commonly agreed methodology.

[6] An important assumption of working age population growth from 2016 (outside the Commission forecast period) relies on the EUROPOP2013 population projections, in line with the commonly agreed methodology.

uncertainty, the budgetary targets of the programme seem to rely on optimistic growth projections.

In 2013, the fiscal deficit turned out better than expected, but the medium-term outlook has worsened as compared to the 2013 stability programme. The 2013 deficit outturn of 7.2 % of GDP is below the EDP ceiling and the estimate of last year's stability programme of 7.5 % of GDP. The improvement is mostly due to the reclassification of one-off revenues (0.2 % of GDP) and interest expenditure savings (0.3 % of GDP), more than compensating for the impact of lower economic growth on tax revenue. The government's 2014 deficit target of 4.8 % of GDP is higher than the 4.4 % of GDP presented in the last year's stability programme. This upward revision is largely linked to lower tax revenue projections in line with the weaker growth forecast. While the overall fiscal adjustment of EUR 3.1 billion (1.8 % of GDP) for 2014 is in line with the 2013 stability programme, some of the discretionary effort has been substituted by non-discretionary deficit-improving factors of EUR 0.6 billion, including revenue from the lottery licence sale and higher dividends from the Central Bank of Ireland. This implies a higher structural effort in the following year in order to ensure a timely correction of the excessive deficit. The Commission 2014 spring deficit forecast of 4.8 % of GDP is in line with the stability programme target. The risks around this forecast are balanced.

Compliance with EDP targets has been strong so far. The deficit outturns in 2011–2013 have been consistently below the annual nominal ceilings, net of financial sector measures, and the Commission services estimate the 2014 deficit at 4.8 % of GDP, again lower than the EDP ceiling of 5.1 % of GDP. In addition, the recommended structural effort is estimated to be met based on a careful analysis. Ireland has delivered the amount of fiscal measures that were originally projected to be necessary to reach the annual fiscal deficit ceilings over the period 2011–2014. The total amount of discretionary revenue measures has been slightly higher (0.5 % of GDP) than initially planned, which more than offsets expenditure slippages of some 0.2 % of GDP. Overall, discretionary consolidation measures, excluding one-offs and other temporary measures are estimated at 9.9 % of GDP over the period 2011–2014, higher than the recommended cumulative structural effort of 9½ % of GDP over the whole EDP period (2011–2015) and before the 2015 budget. However, the top-down estimate of annual average structural effort of 1.6 % of GDP by 2014 is below the recommended annual average effort of 1.9 % of GDP.

Going forward, the consolidation effort is concentrated on correcting the excessive deficit by 2015, but details are still to be revealed. The headline fiscal deficit is targeted to be reduced by 2.4 pp of GDP in 2014 and 1.8 pp in 2015. This is consistent with the budgeted measures for 2014 and the authorities' estimate of EUR 2 billion (1.1 % of GDP) in revenue and expenditure measures in 2015 to reduce the deficit below 3% of GDP. However, details of the 2015 adjustment are not yet specified, with around one-third of the adjustment assumed to be on the revenue side and two-thirds on expenditure. Ireland submitted data as per the additional reporting requirements defined under Article 10 of Regulation (EU) No 473/2013,[7] but without further specifying the details of 2015 adjustment measures. The revenue-to-GDP ratio is projected to remain largely unchanged (+0.1pp of GDP) as tax revenue increases offset decline in other revenue. Most of the adjustment is expected in the primary expenditure to GDP ratio (1.8 pp of GDP), with reductions in social transfers (1.1 pp) and compensation of employees (0.6 pp). The improving unemployment situation is estimated to reduce unemployment benefits by 0.1 % of GDP in 2015. The Commission 2014 spring forecast projects a deficit of 4.2 % of GDP, based on a no-policy change assumption, which means that measures to be announced in October 2014 as part of the draft budget for 2015 are not

[7] Supplemented by Commission Delegated Regulation (EU) No 877/2013.

taken into account. This forecast suggests a necessary fiscal effort of some 1½ % of GDP in 2015 in order to reduce the deficit below 3 % of GDP.

Fiscal restraint is planned to continue until reaching the MTO in 2018. The headline fiscal deficit is targeted to be reduced by around 1 pp of GDP annually in 2016–18. The adjustment is planned mostly on the expenditure side by limiting expenditure growth in nominal terms. Core primary expenditure targeted under the national expenditure ceilings (set to ensure compliance with the EU expenditure benchmark at national level) is targeted to increase by 0.1 % annually in nominal terms. This represents a tightening of 0.2% of GDP per annum from 2016 compared to the 2013 stability programme and the 2014 budget. No further details are provided on adjustment, but expenditure restraints seem to be higher than the underlying expenditure pressures related to the increasing and gradually ageing population. However, the track record so far of adherence to the national medium-term expenditure ceilings is relatively weak. Upward revisions in annual budget decisions, especially when unplanned revenue or savings are available, represents a risk to the effective implementation of the expenditure plans. The total expenditure to GDP ratio is projected to decline by 4.3 pp with the largest reduction in social transfers (2.2 pp of GDP) and compensation of employees (1.3 pp) between 2015 and 2018. The revenue-to-GDP ratio is projected to decline by 1.3 pp of GDP, including an increase in the direct tax revenue ratio (0.4 pp) and drops in the indirect tax revenue (0.5 pp) and other revenue ratios (1 pp). The decline in the tax intensity of GDP on a no policy change basis is consistent with the expected export-led growth in the medium term. However, direct tax revenue projections seem to rely on optimistic wage growth trend considering very limited increases in the public sector wage bill, the still high unemployment rate and the flexibility of inward migration given high income level in Ireland.

Box 2: Main budgetary measures

The main measures presented in the stabilty programme and in the additional EDP reporting requirements are consistent with the 2014 budget. Revenue measures include both new measures and the full-year effect of measures announced in 2013. Expenditure measures include paybill savings in line with the 2013 public sector pay agreement and social and health expenditure cuts. Measures for 2015 and the following years are not yet specified.

Main budgetary measures in 2014

Revenue	**Expenditure**
• Deposit Interest Retention Tax and exit tax on life insurance policies and investment funds set at 41% (0.1 % of GDP) • New levy on financial institutions (0.1 % of GDP) • Increased levy on pension fund assets (0.1 % of GDP) • Increased excise on tobacco and alcohol (0.1 % of GDP) • Full year effec of the new Local Property Tax (0.2 % of GDP)	• Pay bill savings (-0.3 % of GDP) • Social benefit cuts and control measures (-0.2 % of GDP) • Drug cost savings, increased income collection, co-payments and control measures in heath sector (-0.2 % of GDP)

Note: the budgetary impact in the table is the impact reported in the stability programme and other budgetary documents by the national authorities. A positive sign implies that revenue / expenditure increases as a consequence of this measure.

Box 3: Excessive deficit procedure for Ireland

Ireland is currently subject to the corrective arm of the Stability and Growth Pact. The Council recommended to Ireland in December 2010 to bring the general government deficit below 3 % of GDP by 2015 and specified annual nominal deficit ceilings of 10.6 % of GDP in 2011, 8.6 % in 2012, 7.5 % in 2013, 5.1 % in 2014 and 2.9% in 2015, as well as a cumulative improvement in the structural balance of 9.5 percentage points of GDP in 2011-2015. In addition, the recommendation called on Ireland to establish a budgetary advisory council and introduce a fiscal responsibility law introducing a medium-term expenditure framework with binding multi-annual ceilings on expenditure in each area, and pursuing further pension reforms.

The year after the correction of the excessive deficit, Ireland will be subject to the preventive arm of the Pact and will have to ensure sufficient progress towards its medium-term objective, which the stability programme sets at 0 % of GDP in both nominal and structural terms. As the debt ratio in 2015 is projected at 120 % of GDP, exceeding the 60 % reference value, Ireland will also be subject to the transitional arrangements as regards compliance with the debt criterion during the three years following the correction of the excessive deficit, and it will have to ensure sufficient progress towards compliance.

An overview of the current state of excessive deficit procedures is available on: http://ec.europa.eu/economy_finance/economic_governance/sgp/deficit/index_en.htm.

General government debt peaked at 123.7 % of GDP at the end of 2013 and is expected to decline over the stability programme period to 107 % of GDP in 2018. This reduction assumes achieving high primary surpluses of 4.8% of GDP by 2018, strong nominal GDP growth and the use of cash balances and financial assets for financing needs. The upward revision of the debt path relative to the previous stability programme is related to revisions to GDP level and growth and coinciding changes in budgetary plans. The main risks to the debt path are related to potential negative growth shocks and deviations from the fiscal adjustment path. Interest rate risks are assessed to be low due to low future refinancing needs.

Long-term sustainability

There are significant risks to the sustainability of public finances. The medium-term sustainability gap indicator,[8] showing the adjustment effort up to 2020 required to bring the public debt ratio to 60 % of GDP by 2030, is at 5.2 % of GDP, primarily reflecting the currently still high deficit-to-GDP ratio and underscoring the need to continue the path of fiscal consolidation. This places Ireland in the category of 'high fiscal sustainability risk' as per the medium-term indicator. The long-term sustainability gap indicator,[9] showing the

[8] See table V. The medium-term sustainability gap (S1) indicator shows the upfront adjustment effort required, in terms of a steady improvement in the structural primary balance to be introduced until 2020, and then sustained for a decade, to bring debt ratios back to 60 % of GDP in 2030, including financing for any additional expenditure until the target date, arising from an ageing population. The following thresholds were used to assess the scale of the sustainability challenge: (i) if the S1 value is less than zero, the country is assigned low risk; (ii) if a structural adjustment in the primary balance of up to 0.5 p.p. of GDP per year until 2020 after the last year covered by the autumn 2013 forecast (year 2015) is required(indicating an cumulated adjustment of 2.5 pp.), it is assigned medium risk; and, (iii) if it is greater than 2.5 (meaning a structural adjustment of more than 0.5 p.p. of GDP per year is necessary), it is assigned high risk.

[9] See table V. The long-term sustainability gap (S2) indicator shows the immediate and permanent adjustment required to satisfy an inter-temporal budgetary constraint, including the costs of ageing. The S2 indicator has two components: i) the initial budgetary position (IBP) which gives the gap to the debt stabilising primary balance; and ii) the additional adjustment required due to the costs of ageing. The main assumption used in the derivation of S2 is that in an infinite horizon, the growth in the debt ratio is bounded by the interest rate differential (i.e. the difference between the nominal interest and the real growth rates); thereby not necessarily implying that the debt

adjustment effort needed to ensure a stable debt-to-GDP ratio over time, is at 3.2 % of GDP, including a contribution from the projected costs of an ageing population of 2.7 pp of GDP. This places Ireland in the category of 'medium fiscal sustainability risk' as per the long-term indicator.

The continued provision of quality health services poses a challenge to fiscal sustainability, unless fundamental reform is undertaken. Even though Ireland has a relatively young population, public healthcare expenditure was the third highest in the EU-28 in 2012 at 8.7 % of GNI, significantly above the EU average of 7.3 %. Given the current difficulties in managing the health budget, expected demographic pressures due to an ageing population imply that current service levels can only be maintained if value-for-money gains are achieved over the medium to long term. The rise in health-related expenditure to 2060 due to demographic pressures is projected at 1.2 pp of GDP.

Challenges to the health sector are multifaceted. Financial management and accounting systems and processes are fragmented across healthcare providers. This fragmentation causes substantial delays and hurdles in collecting and processing information. It hinders the monitoring of health expenditure and efforts to achieve value-for-money, as timely and reliable financial information is critical to identify waste and potential efficiency gains. Streamlining financial management system is also a prerequisite to ensuring an appropriate allocation of resources under the 'Money Follows the Patient' funding model. The high level of pharmaceutical expenditure is another critical challenge. When adjustments are made for the age profile of the population, expenditure on outpatient drugs in Ireland is higher than in all countries against which it benchmarks its pharmaceutical prices.[10] A number of important reforms have begun under the *Future Health* strategy and under the EU-IMF financial assistance programme to address these issues (box 4).

Costs associated with an ageing population represent a challenge to Ireland's debt sustainability, but the impact of recent reforms still needs to be assessed fully. The 2012 Ageing Report concludes that coping with the projected increase in ageing-related expenditure will be challenging. Pension reforms[11] have been implemented since then, however, and the long-term sustainability analysis will be updated accordingly in the 2015 Ageing Report. As per the 2012 report, the cumulative increase in total ageing-related public expenditure, including the provision of long-term care, is projected at 5.4 percentage points of GDP between 2014 and 2060, compared with 2.9 percentage points for the EU. This largely reflects a projected strong increase in gross public expenditure on pensions, only partly offset by an improvement in the labour market and a significant fall in unemployment in the second half of the current decade.

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ratio will fall below the EU Treaty 60% debt threshold. The following thresholds for the S2 indicator were used: (i) if the value of S2 is lower than 2, the country is assigned low risk; (ii) if it is between 2 and 6, it is assigned medium risk; and, (iii) if it is greater than 6, it is assigned high risk.

[10] A comparison of annual spending on outpatient pharmaceuticals adjusted for the age composition of the population, using Spain as the reference point (index = 100), shows Ireland at an index value of 194. This compares with an index value of 129 for the United Kingdom and about 150 for Germany and the Netherlands. These countries are all part of the reference basket Ireland uses to set pharmaceutical prices.

[11] As a result of the pension reforms announced in 2010, the state pension age will increase to 67 in 2021 and 68 in 2028. A single pension scheme for all new entrants to the public service was introduced in 2012. Under the single scheme, the minimum pension age was increased to 66 initially and to the state pension age subsequently, and pensions are calculated based on career average earnings rather than final salary. In addition, the 2013 public service wage agreement included pension cuts for annual pension above EUR 32 500 for new retirees from 31 August 2014.

Box 4: Healthcare reforms

The Irish government is committed to moving from the current two-tier health system to a single-tier health service financed by Universal Health Insurance, guaranteeing a basic level of primary and hospital care services for all residents. This political objective is supported by structural reforms under the *Future Health* strategy, and a number of steps have already been taken under the EU-IMF programme of financial assistance.

Key enabling steps towards healthcare reforms include financial management reforms and the introduction of individual health identifiers:

- Work has started to establish an integrated financial management system. When completed, the reform should enable better control of health expenditures, which have registered repeated overruns in recent budgets. A key challenge of the reform in 2014 will be the full implementation of a common chart of accounts across all care providers, including those in the voluntary sector.
- Individual health identifiers for patients and healthcare professionals are a cornerstone of the *eHealth* strategy. Individual health identifiers reduce the risk of duplication and medical errors and therefore improve operating efficiencies. They are also essential for the roll-out of a full system of ePrescription (i.e. electronic prescribing and dispensing of pharmaceuticals) and the use of electronic patient records.

Major steps are being taken to improve value for money in the delivery of healthcare, in the context of a move away from the current model of hospital care provision towards greater reliance on the primary care system:

- 'Money Follows the Patient' funding is being rolled out on a pilot basis. This funding model will replace the current system of block funding and operate by reimbursing providers on the basis of diagnosis-related groups. When fully operational, it should incentivise more efficient use of resources to achieve the same or better treatment outcomes at lower costs. Implementation of 'Money Follows the Patient' funding will depend on improving financial management systems and putting in place individual health identifiers, further underlining the need for the eHealth reforms.
- Universal primary care is expected to be rolled out in 2016. The move to free general practitioner care may produce savings in the acute hospital sector over time, but there is also a risk of cost increases, as the number of publicly-covered general practitioner visits goes up. This risk can be managed through phased implementation and careful costing based on robust analysis of available data on current medical card patients.
- The cost of pharmaceuticals has been reduced gradually. However, the planned mid-term review of the 2012 agreement with the association of manufacturers of patented drugs (IPHA) has considerable potential to unlock further savings in this market segment, given that patented medicines account for over 70 % of outpatient expenditure. For generics, reference pricing is being rolled out for interchangeable medicines covering 80 % of the off-patent market, with expected savings of EUR 50 million in 2014. Under the programme, the authorities also made a commitment to introducing guidelines in 2014 to make it compulsory to prescribe by international non-proprietary name. The effectiveness of this measure in increasing the use of generics will depend on how rigorously it is enforced and on how much discretion is given to prescribers to include brand names with a 'do not substitute' condition on the prescription. In the longer term, continuing to promote sound prescribing practices, for instance on antibiotics, is likely to improve overall cost-effectiveness as well as patient outcomes.

Current pension payments are adequate to prevent poverty, but the future adequacy of pensions is at risk. The current at-risk-of-poverty rate for the elderly (65 and over) is relatively low (11 % in 2011), but the aggregate income replacement ratio is only 0.43, among the lowest in the EU, partly due to the limited coverage of voluntary private pensions. The future adequacy of pensions is at risk because more than 50% of workers do not contribute to private pension schemes. To address this, the authorities plan to introduce auto-enrolment in private pension schemes, combined with a mandatory employers' contribution and tax incentives. They are also considering options to improve the regulatory framework for occupational schemes, including to protect entitlements in cases of underfunding of schemes or insolvency of sponsoring employers. The OECD stated in a recent review of the Irish pension system commissioned by the authorities that auto-enrolment is a second-best option in comparison to compulsory enrolment, which is less costly and more effective to increase pension coverage.[12]

Public service pension have been reformed for new entrants. The reformed public service pension scheme, introduced in 2012, applies only to new employees, leaving out the majority of public-sector workers. Under the new scheme, pensions are calculated based on average career earnings instead of final salary for existing public employees. This implies that cost-savings will accrue over the long term. Most public-service pensions are funded on a pay-as-you-go basis, and annual pension contributions actually paid are lower than the actuarial value of the pension entitlements (1.5 % of GDP in 2012).

The state pension (contributory) regime has a weak link between contribution and benefits. The current system of calculating entitlements leads to inequitable treatment of people who may have contributed for the same duration. In addition, the difference between the full-rate state pension (contributory) and the state pension (non-contributory) is small, blurring the difference between the two schemes, even though the latter is means tested and the contributory regime is not. The authorities have announced plans to replace the current average contributions test for the state pension (contributory) with a total contributions approach from 2020 onwards. This reform also envisages incentives for people reaching pension age to go on working, but details are still to be decided.

Solvency issues affect some defined-benefit pension schemes and pose a potential risk to their members and to public finances. Defined-benefit pension schemes accounted for 64 % of total occupational pension schemes by assets, but are on a steady decline, with defined-contribution schemes becoming more prevalent. Due to the poor performance of pension fund assets during the financial crisis, defined-benefit pension schemes are underfunded (20 % of liabilities in 2009). In 2013, the authorities changed the regulation of defined-benefit schemes providing a backup option of state funding in the event of double insolvency (employer and pension scheme), as well as reducing the previous 100 % priority for existing pensioners if the pension scheme is wound up.

Fiscal framework

There have been significant steps to improve the Irish fiscal framework and the quality and timeliness of data provision. The main areas of progress concern the passage of the Fiscal Responsibility Act, the establishment of the Irish Fiscal Advisory Council, the introduction of a medium-term expenditure framework and better reporting and fiscal statistics. The Irish Fiscal Advisory Council's financial and functional independence is ensured by provisions in primary legislation. It has fully assumed its role of assessing and endorsing the macroeconomic forecasts underpinning annual budgets and stability programmes, in addition to assessing budgetary forecasts, the appropriateness of the fiscal

[12] Review of the Irish Pensions System, OECD, 2013.

stance and compliance with fiscal rules. New fiscal reports are coming on stream that cover the general government sector and complement the existing fragmented reports by individual government entities.

However, medium-term budgetary plans are not supported by well specified adjustment measures and are subject to revisions at the time of annual budget decisions. The programme presents fiscal deficit targets and underlying estimates until 2018, but no details of budgetary measures are provided, except for confirming the 2014 budget measures. Departmental expenditure plans are to some extent anchored by the ministerial expenditure ceilings until 2016, but unspecified expenditure savings are to be allocated across government departments and revenue measures are to be announced at budget time. Moreover, the credibility of the medium-term budgetary plans is undermined by discretionary changes to government expenditure ceilings. In the 2014 budget, government expenditure ceilings were changed without following the pre-defined circumstances for adjustments specified in Circular 15/13 on the medium-term expenditure framework, both in substance and in presentation. The circular does not in practice restrain the government from discretionary changes to the ceilings, and transparency could be improved by justifying in more detail the rationale behind adjustments. This could still allow for flexibility within the binding overarching constraint of the expenditure benchmark, considering for instance changes to the projections underlying the budgetary targets. The current set-up therefore falls somewhat short of the recommendations expressed at EU level (as laid out in the EPC policy advice provided in the context of the peer review of national fiscal frameworks[13]), which called for binding multi-annual expenditure ceilings.

Tax system

The overall tax burden was the sixth lowest in the EU in 2012 at 28.7 % of GDP compared with an EU average of 39.4 %. As a percentage of GDP, direct taxes are 10th highest in the EU, with personal income tax seventh highest. The personal income tax system is very progressive and the tax wedge on low wage earners (those earning 67 % of national average wage) was among the lowest in the EU in 2013, at 21.1%. Social contributions are the second lowest in the EU, largely due to the small employers' contribution, which represent less than half the EU average. Indirect tax revenues as a percentage of GDP are the third lowest in the EU, with VAT revenue well below the EU average.

Tax reforms have been implemented in the context of the EU-IMF programme of financial assistance and have contributed to the fiscal adjustment. As agreed under the Memorandum of Understanding, property taxation has been shifted from a transaction tax to a recurrent tax based on residential property values. However, the base remains relatively narrow as it excludes all non-residential property, such as farmland, development land and derelict sites. Commercial buildings are nevertheless subject to taxes by local authorities, and some of them are considering taxation of unused development land in cities to incentivise construction in areas that face housing property shortages. Environment taxation has been increased and the personal income tax base broadened without reducing progressivity, which has helped achieve the necessary fiscal consolidation and contributed to the social acceptance of the overall adjustment.

There is further scope to improve the efficiency and growth-friendliness of the tax system. Labour taxation is fragmented and complex, with multiple rates and classes of income tax and social contributions. Also, numerous tax expenditures (tax credits and exemptions) remain in labour taxation narrowing the tax base in spite of other interventions to cut back tax reliefs. In terms of indirect taxation, revenue yield is negatively affected by

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[13] For more details, see ECFIN Occasional Papers no. 91, no. 113 and no. 168.

reduced rates and measures that narrow the tax base on consumption, property and environment taxes that are more growth-friendly. Zero and reduced VAT rates result in a VAT efficiency below the EU average. Reduced VAT rates are widely used to achieve redistribution objectives even though they are not an efficient and well-targeted policy tool to protect vulnerable groups. Recently, Ireland has retained the reduced rate of VAT on tourism-related services. Although reviews of direct taxation have been conducted recently, there is no evidence that narrowing the tax base has achieved the desired objectives in a cost-effective way.

Ireland has increased the excise duty on energy products and specific carbon taxes. The exemption on the taxing of peat as a fuel has been removed for most purposes. This is a step in the right direction, given the demanding Europe 2020 environmental targets and the high contribution of peat to greenhouse gas emissions. Peat used for electricity generation (subject to the emission trading system) is shielded from the carbon tax, but peat extraction remains heavily subsidised.[14] In proportion to the quantity of electricity generated, this subsidy scheme is almost five times as large as the support scheme for renewables. There is also still scope to improve the effectiveness and growth-friendliness of tax instruments, as the carbon tax does not apply equally to all fuel types, which creates distortions and environmentally harmful subsidies. Ireland applies a reduced VAT rate of 13.5 % to heating fuel. Although this type of tax expenditure is intended to address social and competitiveness concerns, it is not the most suitable instrument for pursuing such policy objectives as it does not target those most vulnerable and distorts incentives. Moreover, the excise duties favour electricity, as they are among the lowest in the EU both for domestic and commercial users, in contrast to excise duty rates on gas oil and diesel for transport use, which are slightly above the EU-28 average.

Incidences of corporate tax avoidance have given rise to public concern. Measures are being implemented to avert corporate tax avoidance as Ireland amended its company residence rules in the latest Finance Act to avoid Irish-registered companies taking advantage of mismatches in international tax rules to be ‘stateless’ in terms of tax residence. In addition, the Irish authorities are involved in international efforts addressing the issues of base erosion and profit shifting at the international level.

3.2. Financial sector

Despite banking sector reforms undertaken under the recently completed EU-IMF programme of financial assistance, there are still significant challenges. These challenges were analysed in detail in the Commission 2014 in-depth review of Ireland in the context of the Macroeconomic Imbalance Procedure.[15] Since end-2010, two banks have been merged and two others resolved. The government also recapitalised the three systemic Irish banks and bank liquidity and funding have improved, while the regulatory and supervisory framework has been strengthened. Legislation providing for the establishment of a central credit registry was enacted in late 2013. The registry is important to improve banks’ risk management practices and prudential supervision. However, the registry is not yet operational and some uncertainty remains concerning its implementation due to unresolved issues with the use of the personal public service number as unique borrower identifier. It has nevertheless been decided already that the establishment and operation of the registry will be procured to a private partner.

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[14] A EUR 70 million subsidy is foreseen for the period from October 2013 to September 2014, against a EUR 50 million subsidy for renewable electricity (Commission for Energy Regulation). In contrast, renewables account for almost 20 % of final electricity consumption, while peat accounts for only 6 %.

[15] http://ec.europa.eu/economy_finance/publications/occasional_paper/2014/op181_en.htm.

There has been major balance sheet deleveraging with loan-to-deposit ratios converging to the euro area average. The point-in-time balance sheet assessment conducted at the end of 2013 did not identify additional capital needs for Irish banks, though it did find that additional provisions are appropriate for some loans and that adjustments to banks' stocks of risk-weighted assets would be warranted. Nonetheless, the non-performing loans ratio remains high[16] and the banking sector has yet to regain profitability.

Private sector indebtedness is still the second highest in the EU, though it is gradually declining. However**,** the large amount of multi-national firms' debt which is foreign funded inflates private debt levels in Ireland.[17] Smaller domestic firms and SMEs have faced tight credit conditions and have been deleveraging to reduce their debt overhang. Irish households have also been deleveraging by raising their saving rate to repay debt, though they remain among the most indebted in Europe.

The Central Bank of Ireland has put in place mortgage arrears resolution targets to support the resolution of non-performing loans. Actions are aimed at intensifying engagement between borrowers and creditors in order to reach viable, sustainable solutions for borrowers in arrears. The current target (end-June 2014) for restructuring proposals for loans in arrears by more than 90 days is 75 % of customers and 35 % for concluded solutions. By the end of this year, there will be more evidence as to the durability and sustainability of the proposed strategies. Recent data confirms that mortgage arrears have begun to decline, though very long-term arrears continue to grow.[18] A similar framework is being applied to SME loan arrears in the two largest domestically-owned banks that dominate SME lending, which have been assigned non-public restructuring targets. These measures are also important for the repair of banks' balance sheets in preparation for the ECB's comprehensive assessment in 2014 and will also aid the deleveraging of households and SMEs.

The personal bankruptcy and insolvency regimes have undergone significant reforms. Previously, liquidation (the sale of debtor's assets and their division among creditors) was the only formal option to settle debts of natural persons. Currently, three new resolution mechanisms allow for a discount on debt repayment, provided that the debtor makes some repayments – and in some cases, a full discharge (box 5).

The profitability of domestic banks is seriously hampered by the large amount of tracker mortgages on their balance sheets. These mortgages mostly generate losses since their interest rates are set at a low fixed margin above the ECB's policy rate (which is likely to remain very low over a protracted period), and below the banks' funding costs. To improve their profitability, banks are reducing their costs and raising interest rates on new lending. However, this puts constraints on the supply of new credit.

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[16] The average non-performing loan ratio for the main three domestic banks is almost 27% of total loans as of June 2013, and about half of the non-performing loans relate to residential mortgages while 25% is SME-related.

[17] See the 2014 in-depth review report for more discussion of the role of multinationals debt in overall private debt.

[18] According to the Central Bank of Ireland, principal dwelling houses mortgage accounts in arrears of over 90 days at end-December 2013 decreased by 2.3 % over the quarter to 16.9 %, the first decline since the series began in September 2009. Very long-term mortgage arrears refers to cases with no payment for over 720 days.

Box 5: The reformed personal insolvency regime in Ireland

Under the economic adjustment programme, Ireland thoroughly reformed its regulatory framework for insolvent debtors with the Personal Insolvency Act (late 2012). This complements the arrears resolution strategies that banks are implementing. Alongside changes in bankruptcy regulations,[19] new non-judicial based modalities were introduced in order to enable creditors – or a qualified majority of creditors within a group of creditors – to recover debts owed to them by insolvent individuals to the extent that this was reasonably possible. The new debt resolution mechanisms are:

- Debt Relief Notices, which apply to generally unsecured debts of value up to EUR 20 000 (permit for full write-off), subject to a three-year supervision period.
- Debt Settlement Arrangements, which apply to generally unsecured debts of greater than EUR 20 000, normally over a period of five years.
- Personal Insolvency Arrangements, which apply to both secured debt up to EUR 3 million and unsecured debt with no limits, normally over six years.

After the agreed periods, the debtor will be discharged from debt.[20]

The new regulation envisioned the set-up of the Insolvency Service of Ireland, established in March 2013. This body is in charge of all personal insolvency matters, including the authorisation of approved intermediaries and personal insolvency practitioners to make proposals on behalf of the debtor.[21] This process started in August 2013. There are 121 personal insolvency practitioners and 30 money advice and budgeting services authorized as approved intermediaries.[22] Once the debtor has made an application, a protective certificate is issued, giving them 70 days to make arrangements with creditors.

The first results of the reformed personal insolvency regime in Ireland will be seen in 2014. To date, there has been little take-up of the system as it is still being set up. The first protective certificate for a personal insolvency arrangement was issued in November 2013 by the Circuit Courts and only in February 2014 by the High Court. Numbers have yet to be announced.

Complaints have been voiced about the costs and the complexity of the procedure. Insolvency Service of Ireland fees range from EUR 100 to EUR 500, while personal insolvency practitioners charge an average of EUR 2000, but in some cases, twice or three times as much, as set in the scenarios provided by the Insolvency Service of Ireland. Complexity concerns will be addressed by two new protocols planned for 2014, on debt settlement arrangements and personal insolvency arrangements respectively. In February, the creation of a Debt Solutions Protocol Steering Group was also announced.

The new protocols will aim to ensure a streamlined process, similar to that of the United Kingdom. Rules of engagement between banks and personal insolvency practitioners will be developed. A template for insolvency arrangements is being prepared to simplify the procedure, and the financial statement will also be made less burdensome in terms of the information that debtors need to provide. These further regulatory improvements aim to raise the take-up numbers for non-judicial debt resolution and the modified bankruptcy regime.

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[19] The period of discharge was lowered from 12 years (in some cases 20 years) to 3 years.

[20] The only exception is under PIA, when the secured debt portion will not be discharged in full, but only up to the amount stated in the PIA.

[21] Applications for a DRN, DSA or PIA need to be submitted through an Approved Intermediary (for a DRN) or a Personal Insolvency Practitioner (for a DSA or PIA).

[22] The numbers refer to February 2014 and are from the Insolvency Service of Ireland.

The European Commission is still assessing two of the three main domestic banks' restructuring plans. Following the agreed revised restructuring plan for the Bank of Ireland in 2013, the Directorate-General for Competition has yet to finalise and approve restructuring plans for Allied Irish Bank and Permanent TSB. These plans set out the paths to long-term viability which are necessary for the banks' return to private ownership and improved profitability. The resolution of their legacy issues will enable them to take up their role of lender to households and enterprises adequately in a context of economic recovery.

Both bank and SME balance sheet repair are critical to restore credit channels. Access to finance is a key challenge for SMEs, with issues on both the demand and supply sides. The government has put in place initiatives to support credit to SMEs (see section 3.4), and there are programmes to build the capacity of SMEs to use more complex funding schemes. Since banks have also partly lost the skills to assess loan applications properly on the basis of the potential viability of the business, they are starting to rebuild capacity in this area. Credit channels are unlikely to be fully restored, however, until the balance sheet of banks and SMEs have been adequately repaired, including through debt restructurings. The main banks recently signed an agreement that enables SMEs with loans from multiple banks to ask for a liaison group to be set up to facilitate a joint consideration of their financial problems. This is an encouraging development.

3.3. Labour market[23], education and social policies

Unemployment has been declining for over a year, but there are still significant labour market and social challenges. The consistent increase in private-sector employment in 2013 with the associated fall in unemployment rates and slight up-tick in participation rates are encouraging signs that the reforms put in place over the past few years are starting to pay off. However, at close to 12 %, the unemployment rate is still more than double the pre-crisis level, despite lower participation rates, and the youth unemployment and not in employment, education or training (NEET) rates remain above the EU average. Also, skills mismatches have still to be fully addressed, and significant improvements in social indicators will be difficult to achieve unless further progress is made in providing job opportunities to the unemployed.

Labour market

Cutting long-term and youth unemployment, eliminating inactivity traps, and reducing the prevalence of low work intensity situations are critical challenges facing Ireland. The collapse of the property market and the broad-based economic crisis of the past few years led to a sharp deterioration in labour market indicators, with unemployment surging from 4.1 % on average in 2000–07 to a peak of 14.9 % in early 2012. The boom and bust cycle has generated structural labour market challenges related to the necessary sectoral rebalancing of the economy and the associated shift in resource allocation. Ireland has put in place a number of policies to address the situation over the past few years, including specific commitments on labour market and education reforms under the EU-IMF programme of financial assistance. In recent quarters, labour market indicators have improved steadily, with renewed job creation in the private sector, modest rises in participation and a fall in the unemployment rate to 11.6 % in the final quarter of 2013 (age group 20-64).

Long-term unemployment remains a serious challenge. Long-term unemployment has fallen gradually with the strengthening of the labour market, but it remains high and is still rising as a proportion of overall unemployment, representing over 61 % of the total at the end of 2013. In part, this reflects the specificity of many construction-sector skills and the

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[23] For further details, see the 2014 Joint Employment Report, COM(2013)801, which includes a scoreboard of key employment and social indicators.

difficulty that people who work in this sector have in transferring to other types of employment. The high prevalence of long-term and very long-term unemployment generates high risks of losses of tangible and intangible skills for the workers affected and could durably affect their ability to regain employment.

Ireland has made substantial progress in tackling the unemployment challenge recently. Labour market reforms were a major focus of the EU-IMF programme of financial assistance, with a focus on active labour market policies, job creation and entitlements reforms. In parallel, reforms improving the further education and training system sought to facilitate the re-skilling and up-skilling of the labour force.

Activation policies have been reformed but the capacity to deliver support services remains insufficient. The *Pathways to Work* strategy seeks to put in place a modern activation system through the establishment of *Intreo* offices. These deliver one-stop-shop services to jobseekers, with a focus on regular engagement, better training opportunities, stronger incentives to take up job opportunities and clearer rights and obligations. At present, these reforms are underachieving due to a lack of staff in the employment service, particularly to address the needs of the long-term unemployed. However, the number of trained case-workers assigned to handle jobseekers has been increased recently. Still, projected capacity at *Intreo* remains insufficient to deal with the entire pool of unemployed. The authorities have decided to address the issue by contracting out the provision of support services for around 100 000 jobseekers, all long-term unemployed, to private providers. These are expected to be operational by end-2014.

The *Action Plan for Jobs* coordinates efforts to foster job creation. The first *Action Plan for Jobs* was launched in 2012 to coordinate job-creation initiatives across all government Departments. It has become an annual process that increasingly involves stakeholders in the preparatory and monitoring phases. Around 1 000 individual measures, some big and some small with a direct impact that is at times difficult to evaluate, have been identified as part of the plans so far. They are subject to quarterly monitoring and have been implemented on schedule in the vast majority of cases. Recently, the authorities have also stated their intention to monitor the impact of the *Action Plan for Jobs* more regularly and in depth.[24]

Youth unemployment is severe. The crisis has taken a particular toll on young people, who have faced difficulties in integrating into the job market. The unemployment rate among the 15-24 age group peaked above 30 % in late 2012 and early 2013, and difficulties in getting a job quickly upon completing education also generate significant risks of losses of human capital. There are also risks due to the rising percentage of young people not in employment, education or training (NEET), which went up by 8 percentage points between 2007 and 2012 to 18.7 % before ebbing to 16.1 % in 2013, but still the eighth highest rate in the EU. The unemployment rate among young people is particularly severe for those with relatively low education (levels 0-2 on the ISCED scale[25]), but graduates of tertiary education have also been affected by the crisis.

Ireland has submitted a comprehensive plan to implement the Youth Guarantee and intends to roll it out by 2015. The plan rightly focuses on young long-term unemployed in the first place and second on all newly unemployed young people. It builds on *Intreo* services and on existing training and employment support schemes. Newly registered unemployed

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[24] The OECD published a preliminary review of the *Action Plan for Jobs* in April 2014, at the request of the Irish authorities.

[25] The United Nations Educational, Scientific and Cultural Organisation (UNESCO) developed the International Standard Classification of Education (ISCED) for cross-country comparison purposes. Levels 0-2 correspond to education up to lower secondary level. Levels 3-4 correspond to education up to post-secondary non-tertiary level. Levels 5-6 correspond to first and second stage tertiary education.

young people with a low '*probability of exit score*' as per *Intreo*'s profiling tools will rightly receive the most immediate attention and resources, while those with a medium or high probability of exit score will receive special assistance after nine months in unemployment. The Youth Guarantee implementation plan appears feasible and tailored to national needs, but it raises some challenges (box 6).

Box 6: The delivery of a Youth Guarantee in Ireland[26]

The remaining challenges to deliver a Youth Guarantee (YG)[27] in Ireland are to:

- Reduce the time span within which the offer to young people is to be made in order to avoid scarring effects. Currently a 9-month period applies for unemployed young people (18-25) assessed to have a medium-to-high probability of exiting unemployment;
- Develop a comprehensive strategy to reach out to non-registereted NEETs;
- Better address the issue of the quality of offers.

Education

Skills mismatches have emerged with the rebalancing of the economy, making re-skilling and up-skilling a challenge for the education and training system. Structural changes in the Irish economy prior to the crisis and as a result of it have diminished employment opportunities for low-skilled workers. In parallel, the crisis triggered net migration outflows, especially of highly-skilled people.[28] For over a decade, the demand for and supply of skilled workers rose in parallel as the economy was transformed and educational achievement rose. In 2001, the level of employment of people with education level 5-6 on the ISCED scale was slightly below that of those with education level 0-2. Over the next decade, employment at level 0-2 halved, while employment at level 5-6 doubled. By late 2013, employment at level 5-6 was three times that at level 0-2. Given the growing importance of ICT to services exports and employment, addressing skills deficits in the sector is particularly vital for Ireland, where information and communications professionals as a percentage of total employment is among the highest in the EU.

Although it has one of the highest tertiary education attainment level in the EU, Ireland still has a large number of low-skilled workers. Tertiary education rates among those aged 30-34 doubled between 2000 and 2012 to almost 50 %, while the proportion of those with at most level 2 education fell to only 13.5 %. Demographic trends are such, however, that the labour force with limited educational attainment remains significant, and those in this bracket are far more numerous than the jobs currently offered at that level. In addition, participation in lifelong learning is lower than the EU average (7.3 % vs. 10.7 % in 2013) and the Survey of Adult Skills[29] stresses that there are some weaknesses in numeracy. While a significant proportion of the population with a low education level is among the older cohorts, they will remain on the labour market and in need of employment for years to come. Job creation at the low end of the skill range, re-skilling and up-skilling is therefore critical to ensure that this segment of the population, a significant proportion of the long-term unemployed do not become permanently excluded from work.

[26] Ireland presented a Youth Guarantee Implementation Plan in January 2014.

[27] Pursuant to the Council Recommendation of 22 April 2013 on establishing a Youth Guarantee (2013/C 120/01): "ensure that all young people under the age of 25 years receive a good-quality offer of employment, continued education, an apprenticeship or a traineeship within a period of four months of becoming unemployed or leaving formal education".

[28] Glyn et al. (2013). Irish Emigration in an Age of Austerity.

[29] OECD, Programme for the International Assessment of Adult Competencies (PIAAC).

Skills mismatches are likely to become more apparent as the labour market recovers further. Total labour supply remains significantly higher than demand at this stage, but the degree of slack differs widely across skills levels. While the slack ratio[30] is around 30 % for education levels 0-2, it is about 20 % for education levels 3-4 and down to 8 % for education levels 5-6. So there is relatively little excess capacity in the high-skill segment of the labour market, and skills shortages could set in relatively rapidly if the recovery on the labour market is sustained. The relatively low slack ratio at education level 5-6 also highlights a potential risk if past trends in employment growth continue, that is rising employment at the high-end of the skills spectrum: there may be a growing number of vacancies without a corresponding rise in employment. This would leave the unemployment rate stuck at a structurally high level. Ireland's ability to generate job creation at the intermediate skill level and its capacity to offer re-skilling and up-skilling opportunities to its (long-term) unemployed population will be critical to avoid this scenario.

Reforms to the further education and training system are ongoing. The government and various stakeholders have recognised the need to restructure the further education and training system and the delivery and offer of re-skilling and up-skilling opportunities to meet the needs of the economy.[31] The new further education and training authority, *An tSeirbhís Oideachais Leanúnaigh Agus Scileanna* (SOLAS), was established in October 2013 with the mandate to develop, fund and oversee the sector. At the end of March 2014, it submitted for ministerial approval a draft strategy that sets out key strategic actions to be backed up by a more detailed operational plan at a later stage. The new system will revolve around the 16 Education and Training Boards established in July 2013, which will consolidate a wider range of vocational educational and training centres.

The new institutional framework is still being established and the impact of the reform will take some time to materialise. Its success will hinge upon SOLAS' ability to put in place a credible strategy and make use of its powers to allocate funds among Education and Training Boards so as to ensure the efficiency and relevance of programmes, link the provision of training to labour market demands and put the long-term unemployed back to work. In parallel, a review of apprenticeship training published in January 2014 provides a number of recommendations to make schemes wider, more flexible, more in step with the needs of the labour market and more focused on work-based learning with more participation from employers. Until now, apprenticeship schemes have been limited to a narrow set of occupations, mostly related to construction, where current and prospective demand is limited. An implementation plan to act upon the review's recommendation is to be finalised by mid-2014. Concerns also exist over funding and maintaining standards at third level institutions. With two exceptions, these institutions have fallen down in world university rankings.

Social policies

The high proportion of people living in households with low work intensity[32] generates serious social challenges. The proportion is currently the highest in the EU and was already higher than the EU average prior to the crisis. It surged from 14.3% in 2007 to 24.2 % in 2011, almost 9 percentage points higher than in Croatia, which had the next highest rate. Low

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[30] The slack ratio is measured as the number of jobseekers (active population minus employed population) divided by the number of employed people at a given level of skills.

[31] The Further Education and Training system covers education and training that occurs after second level schooling but is not part of the third level system. It includes vocational education and training.

[32] The work intensity of a household is the ratio of the total number of months that all working-age household members have worked during the income reference year and the total number of months the same household members theoretically could have worked in the same period. A household is in low work intensity when the ratio is below 0.20.

work intensity is particularly severe among single adult households with children, and the percentage of children living in low-work-intensity households is nearly three times the EU average. This raises the risk of social exclusion of children, particularly those in single-parent households, with the overall at-risk of poverty rate for children rising from 26.2 % in 2007 to 34.1 % in 2011.[33] The affordability of childcare appears to be a significant barrier to single parents getting into employment.[34] The Early Childhood Care and Education and the Subsidised After-school Childcare schemes seek to address the problem, but no evaluation of their effectiveness is currently available.

Social transfers have sheltered the most vulnerable, but employment growth for those with lower skills-levels is needed to improve social indicators. Transfers have been effective in reducing poverty rates[35] and have mitigated the effects of the crisis on severe material deprivation. The proportion of people in severe material deprivation nevertheless increased from 4.5 % in 2007 to 7.8 % in 2011, which remains below the EU average in spite of the crisis.[36] Severe material deprivation affects people not in employment much more seriously than those in employment. However, the proportion of people in employment in severe material deprivation increased recently, including as a result of the higher prevalence of involuntary part-time employment. Ireland also ranks unfavourably in terms of the proportion of people at risk of poverty or social exclusion. This is mainly driven by the high proportion of people living in households with very low work intensity, which is itself the result of the unusually high proportion of jobless single-adult households with children. The high rate of joblessness at the household level, in particular for single parents, is a critical social concern that needs to be addressed by renewed job creation at the low-end of the skills range together with increased re-skilling and up-skilling opportunities, among others.

The structure of benefits and other factors create pockets of unemployment traps. Unemployment benefits are paid under a dual system of jobseeker's benefit (JB), which are provided to eligible workers for up to nine months without means testing, and jobseeker's allowance (JA), which is means tested but not time-bound. The flat structure of unemployment benefits under the JB and JA system, the unlimited duration of JA and the availability of supplementary payments (in particular rent supplement and medical cards) mean that replacement rates (benefits compared to income earned) are relatively high for some categories of workers.[37] As a result, although Ireland's overall benefits scheme and personal income taxation do not create disincentives to work in general, they do generate unemployment traps for the long-term unemployed with low income potential and other categories of workers depending on family circumstances (box 7).[38] There are other factors that may negatively affect incentives to take up employment in certain circumstances,

[33] The at-risk-of-poverty or social exclusion rate for single-parent households was 63.3 % in 2011, significantly higher than the EU average.

[34] Indecon (2013). Indecon Report on Support for Childcare for Working Families and Implications for Employment.

[35] The poverty reducing effect of social transfers (defined as the difference between poverty rates before and after social transfers) was second the highest in the EU in the period 2007-11. Watson and Maître (2013) provide further evidence of the effectiveness of social transfers in reducing poverty in Ireland.

[36] Eurostat data on severe material deprivation rates for 2012 were not available as of 20 May. However, data from the Central Statistics Office indicate that the proportion of people experiencing three of more types of deprivation increased from 15.4 % in 2011 to 17.6 % in 2012. A similar trend can therefore be expected for the severe material deprivation index.

[37] Standardised data on replacement rates are compiled by the OECD Directorate for Employment, Labour and Social Affairs.

[38] DG ECFIN (2013), *Tax Reforms in EU Member States 2013*, table 3.7.

especially access to childcare and its cost, a barrier to female labour participation.[39] The employment rate for women was 60.3 % in 2013, compared to 70.9 % for men and 62.5 % for the EU average for women.

Entitlements have been partly reformed, but not sufficiently to remove unemployment and inactivity traps. The Advisory Group on Tax and Social Welfare was established in 2011 to suggest ways to improve work incentives while achieving social objectives. Recently, the entitlement period for JB has been reduced by three months and JA or JB can now be suspended for up to nine weeks or reduced under certain circumstances, including refusal to take up a suitable job offer or to participate in the activation process. Rent supplement was reformed in 2014 to raise the recipient's contribution to housing costs, but it is still discontinued upon re-entering employment, thereby increasing the effective tax rate upon a transition back to employment and creating pockets of unemployment traps.

Box 7: Unemployment traps

The welfare system expanded considerably during the 1990s and 2000s, leading to a relatively complex web of benefits. Some rationalisation has taken place recently with the closing for new applicants of schemes like the Back to Work Allowance, Mortgage Interest Supplement or Telephone Allowance. However, welfare recipients may be eligible for a range of benefits on top of the jobseeker's allowance (JA). The key ones include: (1) Rent Supplement or Housing Assistance Payment; (2) Medical Cards; (3) Fuel Allowance; and (4) Back to School Clothing and Footwear Allowance. The multiplicity of supplementary payments with varying eligibility conditions complicates the evaluation of replacement rates.

Net replacement rate at 67 % of average wage, 2011	**Ireland**	**OECD median**
Initial phase:		
No children: single – one earner couple – two earner couple (No children: single – one earner couple – two earner couple)	50 – 81 – 75 (73 – 106 –75)	65 – 65 – 84 (68 – 73 – 84)
Two children: single – one earner couple – two earner couple (Two children: single – one earner couple – two earner couple)	64 – 75 – 81 (65 – 92 – 81)	73 – 71 – 85 (77 – 77 – 85)
Long-term:		
No children: single – one earner couple – two earner couple (No children: single – one earner couple – two earner couple)	51 – 81 – 53 (74 – 106 – 53)	0 – 0 – 53 (47 – 60 – 53)
Two children: single – one earner couple – two earner couple (Two children: single – one earner couple – two earner couple)	65 – 75 – 72 (66 – 92 – 72)	21 – 12 – 59 (64 – 69 – 62)
Note: figures in brackets indicate payments including cash housing assistance and top-ups if available. Source: OECD		

Payments under jobseeker's benefits (JB) and JA are capped at EUR 188 per week, with additional payments for adult or child dependents. Unemployment benefits are low for average or above-average income earners compared to OECD countries, but high for below-average income earners. This is particularly so for people in long-term unemployment as JA does not taper off with time, contrary to the majority of OECD countries. Including housing assistance, which concerns only a sub-set of the unemployed, further increases replacement rates. Accounting for the impact of other benefits is more complicated but further reduces the incentives to re-enter employment.

The loss of Rent Supplement and, in some instances, the Medical Card[40] upon return to

[39] See for example OECD (2013), *Economic Policy Reforms: Going for Growth*, and Crilly, Pentecost and Tol (2012).

[40] An unemployed person returning to work is entitled to keep the Medical Card for three years provided that he/she has been receiving JA or JB payments for 12 months or more. It was also announced as part of Budget 2014 that the Medical Card would be replaced with a less generous General Practitioner Card in future for people returning to work, but this measures has not been implemented yet.

employment can act as a disincentive to work for low-income earners. The high cost of childcare is also a disincentive to taking up work, especially for single-parents (mostly women) and second earners. OECD data from 2012 highlights that the net cost of childcare in Ireland is far above the EU average. Net childcare costs for single parents at 100% of average earning represent 40.4 % of income, against the EU average of 12 %. The limited availability of childcare benefits means that parents bear almost the entire cost directly, unlike most other EU countries, where childcare benefits are significant.

The structure of welfare benefits, while not dis-incentivising the take up of work in general, has created pockets of unemployment traps. These affect those with the most difficulties gaining employment in the first place, i.e. the long-term unemployed with relatively low skills and earning potential and single parents. The structure of some benefits risks consolidating the situation of a disenfranchised group with few prospects for upward social mobility.

3.4. Structural measures promoting sustainable growth and competitiveness

Ireland has regained significant competitiveness over the past few years but remains heavily reliant on developments in sectors dominated by foreign investors. As highlighted in the in-depth review of Ireland, the economy has rebalanced with a reallocation of resources from the non-tradable to the tradable sector, a contraction in domestic demand and regained international competitiveness (box 8). Productivity has increased significantly, which, together with stable average private-sector wages in nominal terms, contributed to falling unit labour costs. As a result, the current account balance has swung into a large surplus and direct investment by multinational companies has regained momentum. The outlook for export-oriented firms – mostly multinational companies – has improved, but the situation of the SME sector remains difficult. Most enterprises are very small, have relatively low productivity, cater exclusively for the domestic market and have limited growth potential.

Box 8: Conclusions from the March 2014 in-depth review on Ireland

The first in-depth review on Ireland under the Macroeconomic Imbalance Procedure was published on 5 March 2014.[41] On the basis of this review, the Commission concluded that while the recently completed macroeconomic adjustment programme was instrumental in managing economic risks and reducing imbalances, remaining macroeconomic imbalances required specific monitoring and decisive policy action. Key outstanding issues highlighted in the in-depth review are that:

- Private-sector debt is about three times GDP, though the ratio has started to fall recently. The significant level of private-sector indebtedness is related in part to Ireland's large multinational corporation sector. Smaller domestic firms' debt and household debt levels are also comparatively high but have fallen since late 2008.
- The government debt-to-GDP ratio peaked at around 122 % in 2013. This high level of debt reflects, among other factors, sizeable government banking support measures and the impact of the collapse of the property market on revenue.
- The financial sector remains vulnerable. Non-performing loans are high at nearly 27 % of total loans for the three main domestic banks as of mid-2013. The profitability of banks is also challenged due to the structure of their assets, which is linked to their large holdings of tracker mortgages (low-yielding legacy assets).
- Ireland has a large negative net international investment position. The negative net position is largely linked to the government bailout of the banks and the debt inflows

[41] http://ec.europa.eu/economy_finance/economic_governance/macroeconomic_imbalance_procedure/index_en.htm

under the EU-IMF financial assistance programme.

- Long-term unemployment is high at more than 60 % of total unemployment and youth unemployment is also high. This reflects the contraction of the construction sector and the difficulty of transferring related skills to other types of jobs.

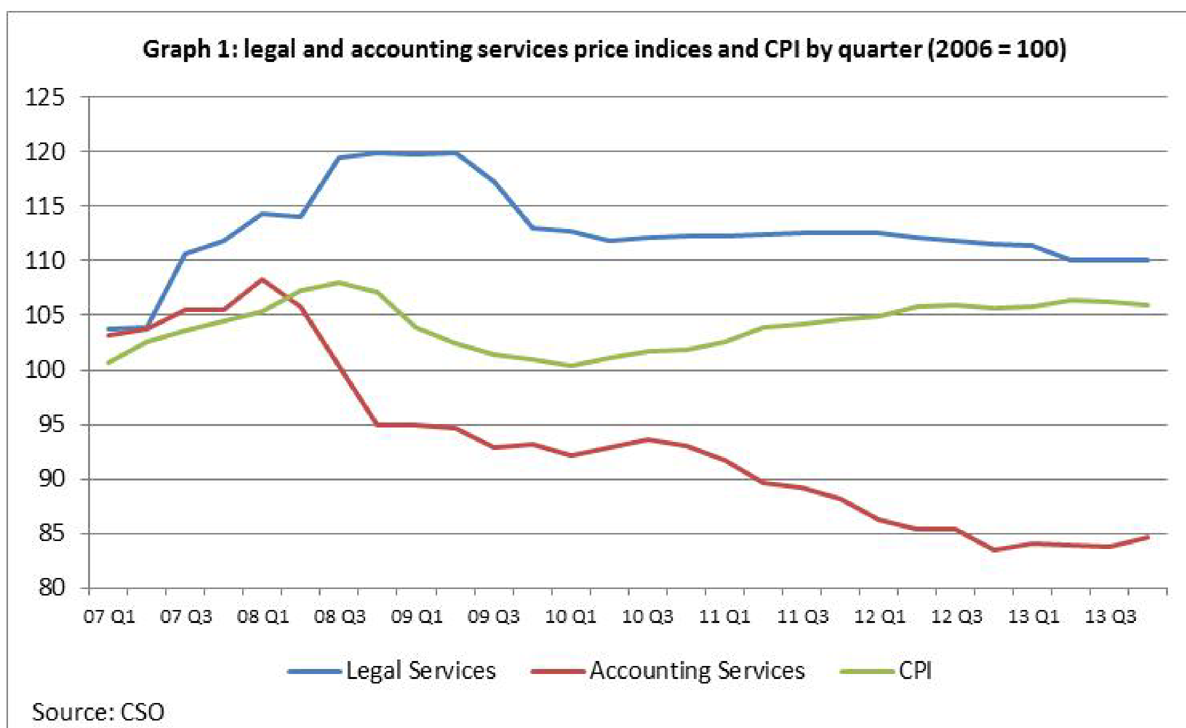
The IDR also discusses the policy challenges stemming from these imbalances and possible ways of achieving balanced growth. Further correcting imbalances would require continuing the adjustment process started under EU-IMF financial assistance programme.

- The sustainability of government debt largely depends on a further reduction of the persistently high fiscal deficit.
- Financial sector repair needs to progress further to restore credit channels, reduce the private debt overhang and sustain economic growth. Further pursuing mortgage arrears restructuring targets would reduce the high stock of non-performing loans and improve the profitability of banks.
- Further labour market reforms are needed to reduce long-term unemployment. Measures include stepping up the delivery of activation services and improving retraining opportunities. To alleviate the highly negative net international investment position, recent competitiveness gains need to be built upon and public finances further adjusted.

Competitiveness and the business environment

Ireland has a generally favourable business environment and its cost competitiveness has improved. As illustrated by the World Bank's Doing Business and other soft indicators on the business climate, Ireland offers a generally strong business climate to investors, which has enabled it to attract significant investment by multinational companies. Rising nominal wages and unit labour costs during much of the 2000s nevertheless led to a strong appreciation of the real effective exchange rate and competitiveness losses, which have been reversed over the past few years. Increases in productivity, cuts in nominal wages in the public service and stable average nominal wages in the private sector have been the main driver of gains in international competitiveness, but price adjustments in key business support services have also contributed to reducing the cost of doing business in Ireland. A notable exception to this adjustment are legal services costs, however, whose cost did not fall significantly during the crisis.

Legal services costs remain high and affect the cost structure of all business, including SMEs. The cost of enforcing contracts, as measured by the World Bank's *Doing Business 2014* indicator, represented 26.9 % of the claim, more than 5 percentage points above the EU average and 12pp higher than top performers such as Germany. Lawyer fees represent the majority of these costs, at 18.8 %. The authorities made a commitment to introducing reforms in the sector as part of the EU-IMF programme of financial assistance. The Legal Services Regulation Bill aims to establish an independent Legal Services Regulatory Authority to replace the mostly self-regulated model, to foster competition (including the introduction of multi-disciplinary practices that should provide 'one-stop shops' bringing together barristers, solicitors and accountants), to improve the complaints system and provide increased oversight on legal cost adjudication.



Progress in advancing reforms under the Legal Services Regulation Bill has been slow, but is now gathering momentum. Although the Bill was published in October 2011, it only cleared Committee stage in the Dáil in February 2014. The Bill is now expected to be enacted this Autumn. A significant number of welcome amendments have been tabled since the Bill was published, for instance to strengthen the independence of the Authority and to allow the establishment of multi-disciplinary practices. The members of the Authority will be appointed by the government based on nominations from various institutions (including the Competition Authority and the Consumers' Association of Ireland) and from bodies representing the legal profession, following a resolution approving such appointments by the Dáil and the Seanad. A majority of the members of the Authority must be lay persons. The Commission has initiated infringement procedures in relation to legal services in the context of the Services Directive.

The Legal Services Regulation Bill offers the potential to reduce legal costs, but the precise impact is difficult to predict. The Bill should enable a higher degree of competition in legal services. The biggest potential for cost reductions probably lies in multi-disciplinary practices and the reformed system of legal cost adjudication probably offering the biggest potential for cost reductions. However, the extent to which the new framework will reduce costs will depend significantly on the work of the Authority. It will have to put in place regulations and guidelines on a range of issues, including multi-disciplinary practices, advertising and complaints in respect of legal practitioners. The Authority is expected to be established by end-2014. This means that important provisions of the new law with an impact on costs will not be effective until well into 2015. A number of other measures to increase competition in the legal profession and reduce legal services costs were included in recommendations by the Competition Authority in 2006 and could be picked up by the Authority through the use of its regulatory powers. Such measures include, the solicitor's lien, which enables a solicitor to withhold the transfer of a client's file to another solicitor when payment is outstanding or disputed and is a major impediment to competition. Reducing overall costs also hinges on other factors relating to the effectiveness of the justice system (see section 3.5).

Box 9: Potential impact of structural reforms on growth – a benchmarking exercise

Structural reforms are crucial for boosting growth. It is therefore important to know the potential benefits of these reforms. Benefits of structural reforms can be assessed with the help of economic models. The Commission uses its QUEST model to determine how structural reforms in a given Member State would affect growth if the Member State narrowed its gap vis-à-vis the average of the three best EU performers on key indicators such as labour market participation. Improvements on these indicators could raise Ireland's GDP by about 4% in a 10-year period. Some reforms could have an effect even within a relatively short time horizon. The model simulations corroborate the analysis of Section 3.3, according to which the largest gains would stem measures related to labour market integration and education. While a higher female employment rate could yield benefits already in the short run, skill enhancing reforms could have an effect of 4½% over a 50-year horizon (see note). In addition, the simulations support the priority placed by the authorities on reforming active labour market policies and social welfare payments.

Table 1: Structural indicators, targets and potential GDP effects[42]

Reform areas		IE	Average 3 best EU performers	GDP % relative to baseline	
				5 years	10 years
Market competition	Final goods sector markups (price-cost margin)	0.12	0.13	0.0	0.0
Market regulation	Entry costs	0.40	0.13	0.0	0.0
Tax reform	Implicit consumption tax rate	22.1	28.6	0.1	0.1
Skill enhancing reforms*	Share of high-skilled	9.2	10.7	0.0	0.0
	Share of low-skilled	25.4	7.5	0.0	0.1
Labour market reforms	Female non-participation rate (25-54ys):			0.8	1.7
	- low-skilled	55.0	26.4		
	- medium-skilled	31.2	10.5		
	- high-skilled	15.7	4.3		
	Low-skilled male non-participation rate (25-54ys)	21.1	7.7	0.1	0.2
	Elderly non-participation rate (55-64ys):			0.2	0.4
	- low-skilled	18.6	13.4		
	- medium-skilled	6.3	4.8		
	- high-skilled	4.1	3.3		
	ALMP (% of GDP over unemployment share)	10.7	37.4	0.4	0.4
	Benefit replacement rate**	73.9	52.6	0.6	0.7
Total				2.2	3.7

Source: Commission services. Note: Simulations assume that all Member States undertake reforms which close their structural gaps by half. The table shows the contribution of each reform to total GDP after five and ten years. If the country is above the benchmark for a given indicator, we do not simulate the impact of reform measures in that area; however, the Member State in question can still benefit from measures taken by other Member States.[43] * The long-run effect of increasing the share of high-skilled population would be 0.9% of GDP and of decreasing the share of low-skilled would be 3.5% ** EU average is set as the benchmark.

A broad range of other measures aim to improve Ireland's competitiveness and business climate. Ireland relies on investment by multi-national companies to generate growth, exports and job creation more than most other EU countries. This makes it more vulnerable to shifting

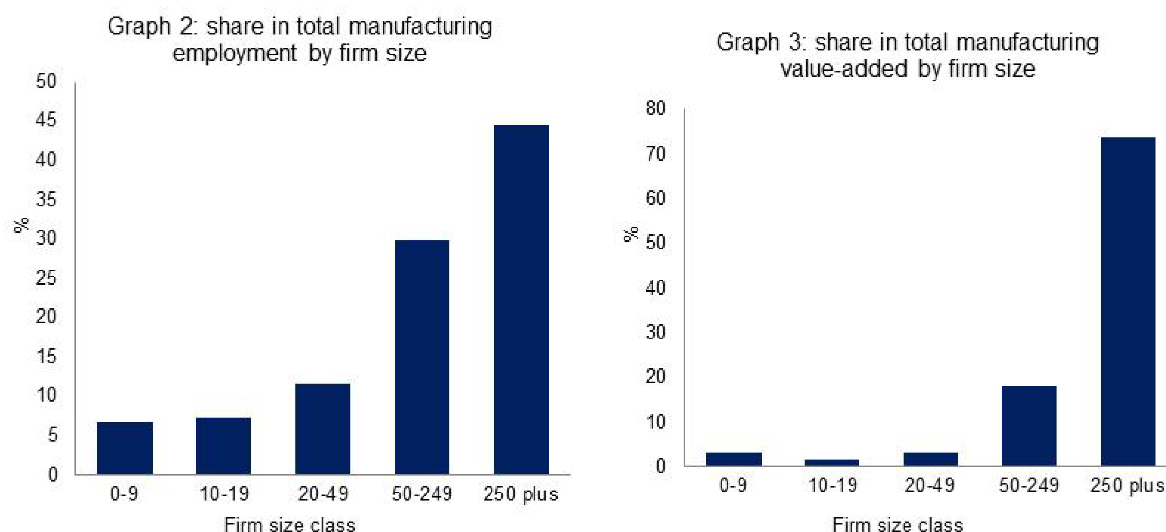
[42] Final goods sector mark-ups is the difference between the selling price of a good/service and its cost. Entry cost refers to the cost of starting a business in the intermediate sector. The implicit consumption tax rate is a proxy for shifting taxation away from labour to indirect taxes. The benefit replacement rate is the % of a worker's pre-unemployment income that is paid out by the unemployment scheme. For a detailed explanation of indicators see Annex.

[43] For a detailed explanation of the transmission mechanisms of the reform scenarios see: European Commission (2013), "The growth impact of structural reforms", Chapter 2 in QREA No. 4 December 2013. Brussels; http://ec.europa.eu/economy_finance/publications/qr_euro_area/2013/pdf/qrea4_section_2_en.pdf

patterns of global production and losses in competitiveness. As part of the annual *Action Plan for Jobs* exercise, the authorities have coordinated measures to reduce the regulatory burden on businesses, promote research and development, align skills development with enterprise needs, attract foreign investors and identify sheltered areas of the economy where competition is restricted. On competition, there has been progress with regards to the legal services profession and the retail sector, both of which were addressed as part of the commitments under the EU-IMF programme of financial assistance, even though reforms remain incomplete or in need of impact evaluation. The Competition Authority published a study on the ports sector and reviews of competition in the pharmacy and bus services sectors are planned but have yet to be conducted. In addition, the Competition and Consumer Protection Bill 2014 was published in March 2014. It provides for the amalgamation of the Competition Authority and the National Consumer Agency and aims to establish a stronger competition watchdog. This should provide an opportunity to further strengthen the effectiveness of competition enforcement, particularly in sheltered sectors of the economy.

SME development, access to finance, R&D and innovation

The SME sector is yet to fully recover from the crisis but is critical to Ireland's growth outlook. The vast majority of SMEs focus on the domestic market and they have been badly hit by the contraction of domestic demand while at the same time seeking to address their severe over-leveraging. They are not only little internationalised, but also significantly less productive than larger firms, most of which are affiliates of multinational companies.[44] In manufacturing, firms with fewer than 250 employees accounted for only 26.2 % of value-added in 2011, but for 55.4 % of employment. Goods and services exports, in turn, are largely generated by affiliates of multinational companies, though the composition of exports has changed significantly over the past decades.[45]



Source: European Commission, based on Eurostat

SMEs account for only a small part of the activity in knowledge-intensive services. Although Ireland ranks highly on the Commission's indicator of innovation output, this is mainly due to the R&D activity of foreign multinationals. There have been only limited

[44] See for example Lawless et al. (2012) SMEs in Ireland: Sylised facts from the real economy and credit market. Central Bank of Ireland Quarterly Bulletin, April 2012.

[45] Exports of chemicals (phamaceuticals) and machinery and transport equipment, which are overwhelmingly produced by affiliates of multinational companies, represented 70% of goods exports in 2013. Similarly, the surge in exports of services in recent years has been led by affiliates of multinational companies, with particularly sharp increases in computer and business services.

spillovers on the SME sector or in terms of fostering the emergence of an effective national research and innovation ecosystem. The degree of industry-academia collaboration is low and the level of innovation activities in indigenous SMEs has been declining slightly. However, reforms to promote effective R&D and innovation systems are ongoing. Recent initiatives include prioritising public research in 14 areas, a new intellectual property protocol to facilitate collaboration between industry and academia and ease access to intellectual property arising from publicly funded reseach, and a series of schemes to fund innovation by SMEs. Delivering on these initiatives would help Ireland make progress in addressing these challenges.

SME access to finance remains a challenge but is important for future growth. Lending to SMEs remains weak, reflecting a combination of subdued credit demand and supply constraints. SMEs continue to be affected by excess leveraging and weak domestic demand, and banks need to make further progress in achieving sustainable resolutions in their SME non-performing loans book (see section 3.2). The latest Red C survey[46] indicates that 40 % of SMEs requested bank credit during the period October 2012 to March 2013, of which 19 % were declined a loan. In the same period, 12 % of SMEs made non-bank financing inquiries, mostly seeking loans/equity from family or friends (5 %) and government financial support (4 %). Surveys of SMEs indicate that reliance on bank financing was significantly higher in Ireland than in a wide sample of EU countries prior to the crisis, and that a larger proportion of firms continued to use bank facilities after the crisis (2012–13) than elsewhere.[47] In addition, non-bank sources of finances for SMEs are relatively undeveloped, though some alternatives, including loan funds, are currently being examined. As the recovery gathers momentum, however, and as domestic demand recovers, supply constraints are likely to increase unless credit channels are adequately repaired.

Dedicated funds have been put in place recently to improve access to finance for SMEs. The Credit Guarantee Scheme provides a government guarantee to the lender of 75 % on individual loans to viable businesses. The Microenterprise Loan Fund Scheme provides loans of up to EUR 25 000 to businesses and sole traders employing up to 10 people who have been refused credit by banks. In addition, three SME funds[48] were put in place in June 2013, mobilising resources from the National Pensions Reserve Fund. These funds were set up in association with private investors to provide credit and take equity participation in SMEs, making a total of up to EUR 900 million of financing available to SMEs. Legislation has also been published to transform the National Pensions Reserve Fund into the Ireland Strategic Investment Fund, whose mandate will be to invest up to EUR 6.4 billion of assets in the Irish economy on a commercial basis.

The take-up for SME support funds has been low so far. The subdued demand for credit probably played a role in the low take-up,[49] but other important factors are also at play. An external review of the Credit Guarantee Scheme was commissioned and submitted to the Minister in Q3 2013. The authorities are also committed to reviewing the Microenterprise

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[46] Red C (2013). SME Credit and Demand Survey, October 2012 – March 2013.

[47] Lawless, McCann and O'Toole (2013). The 2005 Business Environment and Enterprise Perfomance Survey of 2005 shows that 79.4 % of SMEs funding for investment originated from banks, compared with 60.4 % for other EU countries in the sample. The ECB/EC SAFE survey of 2012–13 shows that 59.7 % of Irish firms used bank overdrafts in the prior six months, compared with 37.4 % on average for other EU countries in the sample.

[48] BlueBay Ireland Corporate Credit Fund, Carlyle Cardinal Ireland SME Equity Fund and Better Capital Ireland SME Turnaround Fund

[49] Take-up of the Microenterprise fund amounts to about EUR 4 million to date (out of EUR 90 million), while take-up of the three SME funds amounts to EUR 41.5 (out of EUR 900 million), but with a stronger pipeline of possible transactions.

Loan Fund by July 2014, with a view to identifying factors that hamper their take-up and putting in place corrective measures if needed. Limited awareness of the existence of these funds is a problem. In addition, the lack of capacity in domestic banks to assess SME funding requests, giving due consideration to sector-specific factors, is a limiting factor in credit extension. Weak financial capabilities in SMEs also affect their ability to file sufficiently solid funding requests based on well-developed business plans. The authorities are also exploring initiatives to improve access to trade finance, including to SMEs, through a range of financial products and services to support exporters.

Other policy initiatives aim to support SME development. The Credit Review Office was established at the end of 2009 to mediate disputes between lenders and prospective SME borrowers who have been refused credit, dealing with credit facilities from EUR 1 000 to EUR 3 000 000. As of Q3 2013, 55 % of appeals ruled in favour of borrowers. The Credit Review Office reported that this had resulted in EUR 18.5 million worth of credit being made available to SMEs, helping to protect over 1 500 jobs. Although positive, the impact of the Credit Review Office appears to remain rather limited so far, partly because the number of appeals has been rather small.[50] Until end-2013, gross lending targets had also been imposed on the Bank of Ireland and Allied Irish Bank (see section 3.2). In addition, the system of support to micro-enterprises is being substantially reformed as County and City Enterprise Boards are to be dissolved and replaced by Local Enterprise Offices. Local Enterprise Offices will be coordinated and supported by a unit responsible for micro-enterprises and small businesses within Enterprise Ireland, which had so far focused on larger enterprises with export potential. The impact of the reform cannot be assessed yet, but achieving synergies and improving support services while ensuring that channels of financial and in-kind assistance are not disrupted during the reform process will be important to sustain micro and small enterprises at a time when growth is gaining some momentum.

Network industries, resource efficiency and climate

Major reforms are ongoing in the water sector, but water and wastewater infrastructure remains below par. Ireland made a commitment under the EU-IMF programme of financial assistance to introduce water charges for domestic users and embarked on a reform of the sector in 2012. Legislative steps have been taken to transfer the responsibility for the sector from local authorities to a newly established utility, Irish Water. As part of the reform, Ireland is installing water meters on a large scale. This will enable the introduction of metered water charges for households as of Q4 2014.[51] The Commission for Energy Regulation has been granted regulatory oversight of the water sector and is responsible for several rounds of public consultations on the funding model for Irish Water and the level and structure of charges. The introduction of the national utility model and metered charges should enable the sector to become adequately financed in the medium term with limited financial support from the Exchequer, bringing it closer to the full cost coverage requirement of the Water Framework Directive. It should also help improve the infrastructure, which is in great need of modernisation, and generate more efficient use of a valuable resource. However, the establishment of service level agreements between local authorities and Irish Water for an extended period is likely to lead to significant reductions in the efficiency gains that are expected from moving to a national utility model, partly because it will be more difficult to achieve economies of scale.

The authorities have identified other infrastructure areas in need of investment, including as part of the *Action Plan for Jobs 2014*. This includes broadband, particularly

[50] 406 appeals were made to the CRO as of Q3 2013, of which 272 reached final conclusion.

[51] Assessed charges will apply to a large number of households at first, as the installation of meters will continue into 2016.

important, as it is an essential input for innovative and high-growth sectors and given that exports of services, including ICT services, have overtaken merchandise exports. Legislative steps to enable the use of the electricity distribution network to provide broadband telecommunication services are progressing and could contribute to increasing competition and deploying broadband infrastructure more widely. In addition, structural reforms in the port sector have been implemented in recent years, opening up market access and ensuring that ports are managed and operated on a commercial basis. The Competition Authority nevertheless made six key recommendations in a report issued in November 2013 to further increase competition in port services.[52]

Ireland is not on course to meet the greenhouse gas emission target in non-emission trading system sectors. Agriculture and transport are the biggest contributors to greenhouse gas emissions in the non-emissions trading system sectors. Both are expected to register an increase in emissions between 2005 and 2020, in sharp contrast with the overall reduction target of 20 %. The proportion of renewable energy rose to 7.2 % in 2012, compared with a target of 16% for 2020. Although Ireland has adopted a number of strategies or action plans related to energy efficiency and climate action, little progress has been made on specific actions that would lead it to meet its climate and environmental targets under Europe 2020. Improved waste management would also be needed to achieve Europe 2020 targets, and better application of the waste hierarchy has the potential to develop new economic activities and create jobs.

Flood prevention is becoming an increasingly important challenge. Ireland has not been spared the consequences of climate change. There is now an the increased risk of coastal flooding and related significant economic losses and public health problems. Between 2002 and 2013, total damage for the 16 floods recorded is estimated at EUR 1.5 billion.[53] Green infrastructure projects have the potential to deliver significant environmental benefits as well as cost savings, provided there is a long-term approach and they are designed to minimise capital costs and maintenance.

3.5. Modernisation of public administration

Public administration supports a positive business environment overall. Ireland's ranking in the World Bank's Government Effectiveness scoreboard has improved in recent years and in 2012 was higher (92.3) than before the onset of the crisis (90.7 in 2007). The 2012 ranking is well above the EU average (81.8), and just ahead of that of the United Kingdom (91.8). The quality of Ireland's public administration is perceived to be good, but some specific areas such as local government and the health and justice sectors could benefit from improvements. In terms of business facilitation, Ireland's Point of Single Contact remains under-developed. It is essentially only an information portal that does not provide e-services or enable online applications and completion of procedures. The ability to complete procedures and formalities through points of single contact is nevertheless a requirement under the EU Services Directive,[54] and the absence of this capability negatively affects the free circulation of services.

Significant efforts have been made to streamline public procurement procedures, but there are concerns that this has led to difficulties for smaller bidders. This is due to the

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[52] Competition Authority (2013). Competition in the Irish Ports Sector.

[53] RPA (2014). Study on Economic and Social Benefits of Environmental Protection and Resource Efficiency related to the European Semester.

http://ec.europa.eu/environment/integration/green_semester/pdf/RPA%20Final%20Report-main%20report.pdf

[54] Directive 2006/123/EC of the European Parliament and the Council of 12 December 2006 on services in the internal market.

increased use of framework contracts that are only accessible to SMEs if they form consortia. The new Office of Government Procurement system was established in January 2014 and is tasked with the centralisation of procurement arrangements for goods and services common across government departments. The Office is making efforts to streamline procedures and facilitate access for SMEs, including the creation of a single procurement portal. However, it remains to be seen whether the changes will improve SMEs' access to public contracts.

The new public sector reform programme has been launched. This plan includes a specific focus on local government reform. Local Government reform under the plan has already been given legislative effect by the Local Government Reform Act 2014. A key element of the Act is the consolidation of town councils into county councils, and a commensurate reduction in the number of councillors. In addition, plans to give local authorities discretion in the setting Local Property Tax rates should enhance their autonomy. Another focus of the Public Sector Reform Plan is on health. This builds on the 2012 Future Health strategy and also on commitments made under the successfully completed EU-IMF programme of financial assistance. It covers areas such as financial management reform, the delivery of universal health insurance and eHealth. The programme also outlines reforms to the civil service. However, some key elements still appear to be lacking, such as reform of the Performance Management Development System to link the payment of increments more meaningfully to verifiable performance outcomes for public servants.

Outstanding issues in the justice system may be impeding the business environment, but a full analysis is frustrated by poor data collection. A welcome change was introduced recently in company law enabling SMEs to apply for receivership in the Circuit Court, as opposed to the more costly High Court. Beyond this, the Law Reform Commission provided a number of recommendations to improve the effectiveness of the justice system. Among these, the full integration of properties currently covered by the Registry of Deeds system into the more modern Land Registry is ongoing and should facilitate a complete e-Conveyancing system and reduce delays.[55] Recommendations on important issues such as case management and case progression are still under consideration and may require additional legislative action. However, judicial and court administrative resources to implement active pre-trial case management are very limited, which may be contributing to delays.[56] In addition, as evidenced in the EU Justice Scoreboard,[57] there are significant gaps in Ireland's ability to collect data on the quality and efficiency of the justice system,[58] even though work has begun to remedy this.

4. CONCLUSIONS

Ireland's economic performance continues to be affected by high public and private-sector debt. Government debt peaked at 123.7 % of GDP in 2013, while ageing and health costs represent a challenge to debt sustainability. Domestic demand has been subdued due to deleveraging in the private sector and fiscal consolidation, and exports have been affected by some pharmaceuticals coming off patent. SMEs' access to credit also remains limited. The

[55] It is to be noted that while the proportion of land titles covered by the Land Registry is high nationally (over 90 %), it is lowest in Dublin and Cork, where property supply shortages are emerging.

[56] Ireland has the lowest number of professional judges and support staff in relation to population in the EU, with 3.2 judges and 22.4 support staff per 100 000 inhabitants, compared with an EU average of 21.5 and 68, respectively. This situation is likely to be aggravated by further staff cuts foreseen under the latest Public Sector Reform Plan and through the retirement of a number of judges in the coming years.

[57] European Commission (2014). The 2014 EU Justice Scoreboard.

[58] Some of these gaps are linked to very specific factors related to the organisational structure of the Courts and court proceedings.

financial sector remains vulnerable, with a high proportion of non-performing loans and declining credit. Despite decreases in the unemployment rate, long-term and youth unemployment are high and the prevalence of low work intensity remains one of the highest in the EU. Legal services costs remain high, negatively affecting the cost of doing business.

The analysis in this staff working document leads to the conclusion that Ireland has fully addressed its sole country-specific recommendation for 2013. This relates to the implementation of the EC-IMF financial assistance programme, which Ireland successfully completed at the end of 2013. Ireland maintained a strong track record of implementation throughout the programme. The fiscal consolidation targets under the programme were met, and Ireland improved its domestic fiscal rules and institutions. Bank deleveraging targets were met and capital adequacy ratios have improved. The supervisory and regulatory role of the central bank was strengthened. Private households have increased their saving rates to reduce their high indebtedness. The government implemented labour market and water sector reforms. House prices also stabilised and show signs of recovery.

The policy plans submitted by Ireland address current challenges, and coherence between the stability programme and national reform programme has been ensured. The stability programme indicates that Ireland remains committed to achieving the fiscal consolidation path set under the Excessive Deficit Procedure and plans to achieve its medium-term budgetary objective by 2018. The national reform programme indicates that Ireland will seek to preserve the reform momentum gained under the EU-IMF programme of financial assistance. It rightly focuses on the key challenges facing the country in its aim to return to a balance growth path and is based on a welcome whole-of-government approach.

The challenges identified under the EU-IMF programme and reiterated in the annual growth survey remain valid. One of the main challenges is the need to achieve further fiscal consolidation in line with the commitments under the Excessive Deficit Procedure and the Stability and Growth Pact, supported by health sector and pension reforms. The persistently high level of non-performing loans in domestic banks also remains a critical challenge, with implications for growth prospects and for the legal and regulatory framework governing the financial sector. The ability of the economy to resume sustainable growth will in part depend on the speed at which financial sector repair progresses, and on the extent to which credit channels are restored and the private debt overhang is reduced. Key elements in addressing the challenge of high long-term and youth unemployment, the high prevalence of low work intensity and associated problems are reforms to the labour markets, including activation policies, ongoing reforms to the further education and training system, together with efforts to foster job creation. However, these reforms have some further way to go. Overall, the business climate is favourable and competitiveness has been regained, but costs in certain sheltered sectors, especially legal services, remain high and access to finance for SMEs remains a critical issue for growth.

OVERVIEW TABLE

Europe 2020 (national targets and progress)	
Policy field target	**Progress achieved**
Employment rate target: between 69 % and 71 %	The employment rate (Eurostat definition, age group 20-64) has started to rise gradually to reach 66.6 % in Q4 2013 compared with an average of 63.7 % in 2011–12. Concurrently, the unemployment rate (Eurostat definition, age group 20-64) is on a firm declining trend, falling to 11.6 % in Q4 2013 compared with an average of 14.4 % in 2011–12.
R&D investment target: 2 % of GDP	Investment in R&D rose steadily until the financial crisis. R&D intensity increased from 1.10% in 2002 to 1.28 % in 2007 and 1.72 % in 2012. The first part reflects considerable growth in the volume of investment as this came at a time of sustained economic growth, whereas the latter growth in intensity occurred at a time of contraction in GDP. Upon taking office in 2011, the current administration has maintained public expenditure on research at 2010 nominal levels. Business expenditure on R&D which has been evolving in recent years more favourably than public expenditure has been supported indirectly by an R&D tax credit scheme, which has seen a large uptake.
Reduction of greenhouse gas (GHG) emissions in sectors that are not covered by the Emission Trading System by 20 % compared to 2005 levels	Change in non-ETS greenhouse gas emissions between 2005 and 2012: -12 %. According to the latest national projections submitted to the Commission and taking into account existing measures, the target is likely to be missed: -2 % in 2020 as compared with 2005 (i.e. a projected shortfall of 18 percentage points).
Renewable energy target: 16 % proportion of renewable energy in total gross energy consumption in 2020.	The proportion of renewable energy was 7.2 % in 2012. Although this is in line with the linear trajectory up to 2020, the existing policy, market and budget framework appears to be insufficient to enable the step-wise achievement of the 2020 objective.
Energy efficiency target	The second national Irish energy efficiency action plan aims to achieve 20 % energy savings in 2020 (as compared to 2005). The Commission's EU reference scenario projects a 1 % decrease in gross primary energy consumption

	in 2030 as compared to 2005.
Early school leaving target: 8 %	The early school leaving rate was 11.5 % in 2010, 10.8 % in 2011, 9.7% in 2012 and 8.4 % in 2013. There is a consistent positive trend recent years and Ireland performs better than the EU-28 average for the early school leaving rate (8.4 % and 11.9 % respectively in 2013) and is on track to reach the target of 8 %.
Tertiary education attainment target: 60 %	The tertiary attainment rate was 50.1 % in 2010, 49.7 % in 2011, 51.1 % in 2012 and 52.6 % in 2013. With the exception of 2011, the tertiary attainment rate has been consistently increasing and Ireland has at present the highest tertiary attainment rate in the whole of the EU. Further participation in tertiary education can be sought by improving access to students from disadvantaged backgrounds and addressing the gender imbalance (57.9 % females against 44 % males in 2012).
To reduce the number experiencing consistent poverty to 4 % by 2016 (interim target) and to 2% or less by 2020, from the 2010 baseline rate of 6.2 %, which will lift at least 200 000 people out of the risk of poverty and exclusion between 2012 and 2020 (revised target).	The number of people at risk of poverty or social exclusion increased from a pre-crisis level of 1.05 million in 2008 to 1.32 million in 2011. Achieving the national target remains ambitious.

ANNEX

Standard Tables

Table I. Macroeconomic indicators

	1996-2000	2001-2005	2006-2010	2011	2012	2013	2014	2015
Core indicators								
GDP growth rate	10.3	4.9	0.2	2.2	0.2	-0.3	1.7	3.0
Output gap [1]	2.0	0.8	0.1	-1.2	-0.6	-1.4	-1.0	0.0
HICP (annual % change)	2.7	3.4	1.1	1.2	1.9	0.5	0.6	1.1
Domestic demand (annual % change) [2]	8.8	5.1	-1.4	-1.8	-1.6	-0.1	1.7	1.5
Unemployment rate (% of labour force) [3]	7.8	4.4	8.3	14.7	14.7	13.1	11.4	10.2
Gross fixed capital formation (% of GDP)	21.4	23.6	20.6	10.6	10.7	11.2	12.4	12.9
Gross national saving (% of GDP)	23.0	22.3	17.7	13.2	14.5	17.7	19.1	21.1
General Government (% of GDP)								
Net lending (+) or net borrowing (-)	**2.1**	**0.8**	**-9.7**	**-13.1**	**-8.2**	**-7.2**	**-4.8**	**-4.2**
Gross debt	**54.5**	**30.8**	**49.8**	**104.1**	**117.4**	**123.7**	**121.0**	**120.4**
Net financial assets	**-28.7**	**-10.5**	**-17.8**	**-65.3**	**-83.4**	**n.a**	**n.a**	**n.a**
Total revenue	37.3	34.3	35.8	34.0	34.5	35.9	35.7	35.2
Total expenditure	35.2	33.6	45.5	47.2	42.7	43.1	40.5	39.4
of which: Interest	3.2	1.3	1.7	3.3	3.7	4.7	4.7	4.9
Corporations (% of GDP)								
Net lending (+) or net borrowing (-)	**n.a**	**3.5**	**9.2**	**12.6**	**6.5**	**8.8**	**9.2**	**10.0**
Net financial assets; non-financial corporations	**n.a**	**-88.0**	**-101.0**	**-136.6**	**-141.0**	**n.a**	**n.a**	**n.a**
Net financial assets; financial corporations	**n.a**	**16.2**	**-1.5**	**3.0**	**15.6**	**n.a**	**n.a**	**n.a**
Gross capital formation	n.a	9.2	7.5	5.6	5.9	6.3	7.3	7.5
Gross operating surplus	n.a	34.5	31.2	35.2	34.6	35.2	35.1	35.7
Households and NPISH (% of GDP)								
Net lending (+) or net borrowing (-)	**n.a**	**-7.3**	**-2.4**	**2.9**	**2.5**	**3.1**	**1.8**	**1.1**
Net financial assets	**n.a**	**86.8**	**59.6**	**74.4**	**85.3**	**n.a**	**n.a**	**n.a**
Gross wages and salaries	n.a	36.5	40.6	39.1	39.0	39.3	38.6	38.1
Net property income	n.a	2.1	0.8	0.8	1.3	2.9	1.7	0.6
Current transfers received	n.a	13.1	16.6	19.1	18.8	18.5	17.6	17.0
Gross saving	n.a	4.0	6.2	6.0	5.4	6.4	5.4	5.1
Rest of the world (% of GDP)								
Net lending (+) or net borrowing (-)	**2.2**	**-0.4**	**-3.4**	**1.1**	**3.2**	**6.6**	**6.8**	**7.4**
Net financial assets	**n.a**	**21.6**	**64.0**	**122.3**	**122.3**	**n.a**	**n.a**	**n.a**
Net exports of goods and services	12.7	15.0	12.5	21.6	24.2	23.4	23.6	24.7
Net primary income from the rest of the world	-11.7	-15.0	-14.3	-18.9	-18.3	-15.6	-15.5	-15.1
Net capital transactions	1.0	0.3	-0.2	-0.2	-1.3	0.0	-0.6	-1.4
Tradable sector	50.8	45.9	42.7	48.3	47.8	47.4	n.a	n.a
Non tradable sector	38.4	42.5	46.7	43.3	42.1	42.5	n.a	n.a
of which: Building and construction sector	5.8	7.5	5.8	1.5	1.4	1.5	n.a	n.a
Real effective exchange rate (index, 2000=100)	85.0	90.6	107.4	95.1	90.0	92.7	94.2	93.0
Terms of trade goods and services (index, 2000=100)	101.1	100.8	97.1	93.2	93.5	93.3	93.6	93.6
Market performance of exports (index, 2000=100)	80.6	101.8	102.9	106.6	106.9	106.2	105.8	104.6

Notes:

[1] The output gap constitutes the gap between the actual and potential gross domestic product at 2005 market prices.

[2] The indicator on domestic demand includes stocks.

[3] Unemployed persons are all persons who were not employed, had actively sought work and were ready to begin working immediately or within two weeks. The labour force is the total number of people employed and unemployed. The unemployment rate covers the age group 15-74.

Source:
Commission 2014 spring forecast (COM); Stability programme (SP).

Table II. Comparison of macroeconomic developments and forecasts

	2013		2014		2015		2016	2017	2018
	COM	SP	COM	SP	COM	SP	SP	SP	SP
Real GDP (% change)	-0.3	-0.3	1.7	2.1	3.0	2.7	3.0	3.5	3.5
Private consumption (% change)	-1.1	-1.1	0.4	2.0	0.8	1.6	1.2	1.2	1.2
Gross fixed capital formation (% change)	3.6	4.2	12.0	15.4	6.5	12.4	7.5	7.5	6.0
Exports of goods and services (% change)	0.2	0.2	2.8	2.1	3.7	3.2	4.2	4.4	4.4
Imports of goods and services (% change)	1.0	1.0	3.1	3.2	2.6	3.4	3.6	3.5	3.4
Contributions to real GDP growth:									
- Final domestic demand	-0.3	-0.2	1.4	2.6	1.2	2.2	1.6	1.7	1.5
- Change in inventories	0.2	0.1	-0.1	0.0	0.0	0.0	0.0	0.0	0.0
- Net exports	-0.7	-0.6	0.4	-0.5	1.8	0.5	1.4	1.8	2.0
Output gap[1]	-1.4	-1.2	-1.0	-0.6	0.0	-0.4	0.8	2.3	3.7
Employment (% change)	2.4	2.4	2.4	2.2	2.3	2.0	2.0	1.9	1.9
Unemployment rate (%)	13.1	13.0	11.4	11.5	10.2	10.5	9.7	8.9	8.0
Labour productivity (% change)	-2.6	-2.6	-0.6	-0.1	0.7	0.7	1.0	1.5	1.5
HICP inflation (%)	0.5	0.5	0.6	0.5	1.1	0.9	1.4	1.6	1.6
GDP deflator (% change)	0.4	0.4	1.1	0.5	0.9	0.9	1.2	1.2	1.2
Comp. of employees (per head, % change)	-1.7	0.5	0.4	1.1	0.5	1.5	2.0	2.2	2.2
Net lending/borrowing vis-à-vis the rest of the world (% of GDP)	6.6	6.6	6.8	5.8	7.4	5.2	5.3	5.3	5.3

Note:

[1] In percent of potential GDP, with potential GDP growth recalculated by Commission services on the basis of the programme scenario using the commonly agreed methodology.

Source :

Commission 2014 spring forecast (COM); Stability programme (SP).

Table III. Composition of the budgetary adjustment

(% of GDP)	2013	2014		2015		2016	2017	2018	Change: 2013-2018
	COM	**COM**	**SP**	**COM[1]**	**SP**	**SP**	**SP**	**SP**	**SP**
Revenue	**35.9**	**35.7**	**36.2**	**35.2**	**36.3**	**35.7**	**35.2**	**35.0**	**-0.9**
of which:									
- Taxes on production and imports	11.6	11.6	11.6	11.4	11.8	11.7	11.5	11.3	-0.3
- Current taxes on income, wealth, etc.	13.2	13.3	13.9	13.4	14.2	14.3	14.4	14.6	1.4
- Social contributions	6.2	6.2	6.0	6.1	5.9	5.9	5.8	5.7	-0.5
- Other (residual)	4.9	4.7	4.7	4.2	4.4	3.8	3.5	3.4	-1.5
Expenditure	**43.1**	**40.5**	**41.0**	**39.4**	**39.3**	**37.9**	**36.3**	**35.0**	**-8.1**
of which:									
- Primary expenditure	38.4	35.8	36.3	34.6	34.5	33.0	31.4	30.2	-8.2
of which:									
Compensation of employees	11.2	10.4	10.9	10.0	10.3	9.9	9.4	9.0	-2.2
Intermediate consumption	5.1	4.9	4.9	4.6	4.7	4.6	4.6	4.4	-0.5
Social payments	17.4	16.6	16.6	16.0	15.5	14.8	13.9	13.3	-4.1
Subsidies	0.9	0.9	0.8	0.9	0.9	0.8	0.8	0.8	-0.1
Gross fixed capital formation	1.7	1.6	1.6	1.5	1.5	1.5	1.4	1.3	-0.4
Other (residual)	2.1	1.4	1.5	1.5	1.6	1.6	1.4	1.4	-0.7
- Interest expenditure	4.7	4.7	4.7	4.9	4.8	4.9	4.9	4.8	0.1
General government balance (GGB)	**-7.2**	**-4.8**	**-4.8**	**-4.2**	**-3.0**	**-2.2**	**-1.2**	**0.0**	**7.2**
Primary balance	**-2.5**	**-0.1**	**-0.1**	**0.6**	**1.8**	**2.6**	**3.7**	**4.8**	**7.3**
One-off and other temporary measures	-0.2	0.2	0.2	-0.1	-0.1	0.0	0.0	0.0	0.2
GGB excl. one-offs	**-6.9**	**-5.0**	**-5.0**	**-4.2**	**-2.9**	**-2.2**	**-1.2**	**0.0**	**6.9**
Output gap[2]	-1.4	-1.0	-0.6	0.0	-0.4	0.8	2.3	3.7	5.1
Cyclically-adjusted balance[2]	-6.5	-4.3	-4.5	-4.2	-2.8	-2.6	-2.4	-1.9	4.6
Structural balance (SB)[3]	**-6.2**	**-4.5**	**-4.7**	**-4.2**	**-2.7**	**-2.6**	**-2.4**	**-1.9**	**4.6**
Change in SB	*1.7*	*1.7*	*1.8*	*0.4*	*2.0*	*0.1*	*0.2*	*0.5*	-
Two year average change in SB	*1.1*	*1.7*	*1.6*	*1.0*	*1.9*	*1.1*	*0.2*	*0.4*	-
Structural primary balance[3]	-1.5	0.2	0.0	0.7	2.1	2.3	2.5	2.9	4.7
Change in structural primary balance		*1.7*	*1.8*	*0.5*	*2.1*	*0.2*	*0.2*	*0.4*	-
Expenditure benchmark									
Applicable reference rate[4]	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	-
Deviation[5] (% GDP)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	-
Two-year average deviation (% GDP)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	-

Notes:

[1] On a no-policy-change basis.

[2] Output gap (in % of potential GDP) and cyclically-adjusted balance according to the programme as recalculated by Commission services on the basis of the programme scenario using the commonly agreed methodology.

[3] Structural (primary) balance = cyclically-adjusted (primary) balance excluding one-off and other temporary measures.

[4] Reference medium-term rate of potential GDP growth. The (standard) reference rate applies from year t+1, if the country has reached its MTO in year t. A lower rate applies as long as the country is adjusting towards its MTO, including in year t.The reference rates applicable to 2014 onwards have been updated in 2013.

[5] Deviation of the growth rate of public expenditure net of discretionary revenue measures and revenue increases mandated by law from the applicable reference rate. The expenditure aggregate used for the expenditure benchmark is obtained following the commonly agreed methodology. A negative sign implies that expenditure growth exceeds the applicable reference rate.

Source :

Stability programme (SP); Commission 2014 spring forecast (COM); Commission calculations.

Table IV. Debt dynamics

(% of GDP)	Average 2008-2012	2013	2014		2015		2016	2017	2018
			COM	SP	COM	SP	SP	SP	SP
Gross debt ratio[1]	**84.2**	**123.7**	**121.0**	**121.4**	**120.4**	**120.0**	**115.9**	**112.0**	**107.2**
Change in the ratio	18.5	6.3	-2.7	-2.3	-0.6	-1.4	-4.1	-3.9	-4.8
Contributions[2] *:*									
1. Primary balance	**11.9**	**2.5**	**0.1**	**0.1**	**-0.6**	**-1.8**	**-2.6**	**-3.7**	**-4.8**
2. "Snow-ball" effect	**3.6**	**4.6**	**1.1**	**1.6**	**0.3**	**0.6**	**-0.1**	**-0.3**	**-0.2**
Of which:									
Interest expenditure	2.7	4.7	4.7	4.7	4.9	4.8	4.8	4.9	4.8
Growth effect	0.5	0.4	-2.1	-2.5	-3.5	-3.2	-3.5	-3.9	-3.7
Inflation effect	0.5	-0.5	-1.5	-0.6	-1.1	-1.0	-1.5	-1.3	-1.2
3. Stock-flow adjustment	**3.0**	**-0.8**	**-3.9**	**-4.0**	**-0.2**	**-0.2**	**-1.4**	**0.1**	**0.2**
Of which:									
Cash/accruals diff.				0.2		0.4	0.0	0.3	0.3
Acc. financial assets				-4.2		-0.6	-1.4	-0.1	0.0
Privatisation									
Val. effect & residual									

	2013	2014		2015		2016	2017	2018
		COM	SP	COM	SP	SP	SP	SP
Gap to the debt benchmark[3,4]	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Structural adjustment[5]	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
To be compared to:								
Required adjustment[6]	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.

Notes:

[1]End of period.

[2]The snow-ball effect captures the impact of interest expenditure on accumulated debt, as well as the impact of real GDP growth and inflation on the debt ratio (through the denominator). The stock-flow adjustment includes differences in cash and accrual accounting, accumulation of financial assets and valuation and other residual effects.

[3]Not relevant for Member Sates that were subject to an EDP procedure in November 2011 and for a period of three years following the correction of the excessive deficit.

[4]Shows the difference between the debt-to-GDP ratio and the debt benchmark. If positive, projected gross debt-to-GDP ratio does not comply with the debt reduction benchmark.

[5]Applicable only during the transition period of three years from the correction of the excessive deficit for EDP that were ongoing in November 2011.

[6]Defines the remaining annual structural adjustment over the transition period which ensures that - if followed – Member State will comply with the debt reduction benchmark at the end of the transition period, assuming that COM (SP/CP) budgetary projections for the previous years are achieved.

Source :

Stability programme (SP); Commission 2014 spring forecast (COM); Commission calculations.

Table V. Sustainability indicators

	Ireland			European Union		
	2013 scenario	No-policy-change scenario	Stability programme scenario	2013 scenario	No-policy-change scenario	Stability programme scenario
S2*	6.4	3.2	0.9	2.4	2.4	0.7
of which:						
Initial budgetary position (IBP)	2.7	0.4	-1.2	0.5	0.4	-1.3
Long-term cost of ageing (CoA)	3.7	2.7	2.1	1.9	2.0	2.0
of which:						
pensions	3.3	3.0	2.5	0.7	0.8	0.9
healthcare	1.2	1.1	1.1	0.9	0.9	0.8
long-term care	1.3	1.2	1.2	0.6	0.6	0.6
others	-2.1	-2.6	-2.6	-0.4	-0.4	-0.3
S1**	8.9	5.2	1.0	1.5	1.7	-0.2
of which:						
Initial budgetary position (IBP)	4.0	1.0	-2.6	-0.2	-0.4	-2.0
Debt requirement (DR)	3.6	3.9	3.9	1.5	1.8	1.5
Long-term cost of ageing (CoA)	1.2	0.3	-0.4	0.2	0.3	0.3
S0 (risk for fiscal stress)***	0.28	:		:		
Debt as % of GDP (2013)	123.7			88.9		
Age-related expenditure as % of GDP (2013)	26.0			25.8		

Source *: Commission; 2014 stability programme.*

Note : The 2013 scenario depicts the sustainability gap under the assumption that the budgetary position evolves until 2013 in line with the Commission's 2014 spring forecast. The 'no-policy-change' scenario depicts the sustainability gap under the assumption that the budgetary position evolves until 2015 in line with the Commission's 2014 spring forecast. The 'stability programme' scenario depicts the sustainability gap under the assumption that the budgetary plans in the programme are fully implemented. Age-related expenditure as given in the 2012 Ageing Report.

* The long-term sustainability gap (S2) indicator shows the immediate and permanent adjustment required to satisfy an inter-temporal budgetary constraint, including the costs of ageing. The S2 indicator has two components: (i) the initial budgetary position (IBP), which gives the gap vis-à-vis the debt-stabilising primary balance and (ii) the additional adjustment required due to the costs of ageing. The main assumption used in the derivation of S2 is that, in an infinite horizon, the growth in the debt ratio is bound by the interest rate differential (i.e. the difference between the nominal interest and the real growth rates); thereby not necessarily implying that the debt ratio will fall below the EU Treaty 60 % debt threshold. The following thresholds were used for the S2 indicator: (i) if the value of S2 is lower than 2, the country is classed as low risk; (ii) if it is between 2 and 6, it is classed as medium risk; and (iii) if it is greater than 6, it is classed as high risk.

** The medium-term sustainability gap (S1) indicator shows the upfront adjustment effort required, in terms of a steady improvement in the structural primary balance in the period to 2020 and then sustained for a decade, to bring debt ratios back to 60% of GDP in 2030, including financing for any additional expenditure by the target date, arising from population ageing. The following thresholds were used to assess the scale of the sustainability challenge: (i) if the S1 value is less than zero, the country is classed as low risk; (ii) if a structural adjustment in the primary balance of up to 0.5 pp of GDP per year until 2020 after the last year covered by the 2014 spring forecast (2015) is required (indicating a cumulated adjustment of 2.5 pp), it is classed as medium risk; and (iii) if the S1 value is greater than 2.5 (i.e. a structural adjustment of more than 0.5 pp of GDP per year is necessary), it is classed as high risk.

*** The S0 indicator reflects up-to-date evidence on the role played by fiscal and financial competitiveness variables in creating potential fiscal risks. The methodology for the S0 indicator differs fundamentally from that for the S1 and S2 indicators. Unlike S1 and S2, S0 is not a quantification of the required fiscal adjustment effort, but a composite indicator which estimates the extent to which there might be a risk of fiscal stress in the short term. The critical threshold for the S0 indicator is 0.43.

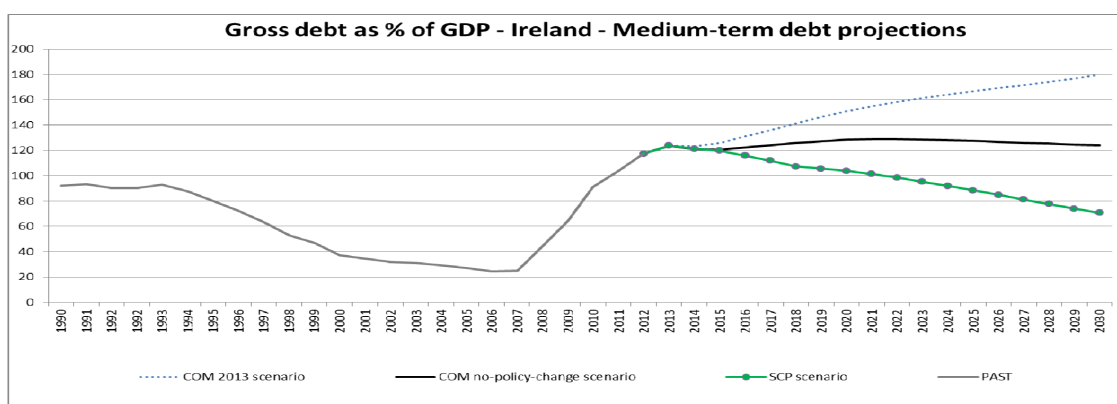

Table VI. Taxation indicators

	2002	2006	2008	2010	2011	2012
Total tax revenues (incl. actual compulsory social contributions, % of GDP)	28.3	32.1	29.5	28.0	28.2	28.7
Breakdown by economic function (% of GDP)[1]						
Consumption	11.0	11.5	10.9	10.3	9.8	10.0
of which:						
- VAT	7.0	7.7	7.3	6.4	6.0	6.2
- excise duties on tobacco and alcohol	1.6	1.2	1.2	1.3	1.2	1.2
- energy	1.3	1.2	1.2	1.4	1.4	1.3
- other (residual)	1.1	1.3	1.1	1.3	1.2	1.3
Labour employed	9.9	10.4	11.2	11.4	11.9	12.1
Labour non-employed	0.1	0.1	0.1	0.1	0.2	0.2
Capital and business income	5.6	7.1	5.2	4.3	4.1	4.3
Stocks of capital/wealth	1.7	3.1	2.2	1.9	2.2	2.2
p.m. Environmental taxes[2]	2.4	2.5	2.4	2.6	2.5	2.5
VAT efficiency[3]						
Actual VAT revenues as % of theoretical revenues at standard rate	60.3	67.9	55.9	48.8	47.2	45.6

Note:

1. Tax revenues are broken down by economic function, i.e. according to whether taxes are raised on consumption, labour or capital. See European Commission (2014), Taxation trends in the European Union, for a more detailed explanation.

2. This category comprises taxes on energy, transport and pollution, and resources included in taxes on consumption and capital.

3. The VAT efficiency is measured via the VAT revenue ratio. It is defined as the ratio between the actual VAT revenue collected and the revenue that would be raised if VAT was applied at the standard rate to all final (domestic) consumption expenditures, which is an imperfect measure of the theoretical pure VAT base. A low ratio can indicate a reduction of the tax base due to large exemptions or the application of reduced rates to a wide range of goods and services ('policy gap') or a failure to collect all tax due to e.g. fraud ('collection gap'). It should be noted that the relative size of cross-border shopping compared to domestic consumption also influences the value of the ratio, notably for smaller economies. See European Commission (2012), Tax Reforms in EU Member States and OECD (2012), Consumption tax trends for a more detailed discussion.

Source: Commission

Table VII. Financial market indicators

	2009	2010	2011	2012	2013
Total assets of the banking sector (% of GDP)	1 006.9	965.9	807.8	713.7	619.9
Share of assets of the five largest banks (% of total assets)	58.8	56.8	53.2	56.9	-
Foreign ownership of banking system (% of total assets)	40.4	33.8	37.4	35.7	-
Financial soundness indicators:					
- non-performing loans (% of total loans)[1)]	9.8	10.9	16.1	24.6	24.6
- capital adequacy ratio (%) [1)]	12.8	14.5	18.9	19.2	21.1
- return on equity (%) [1)]	-35.8	-54.0	-10.8	-7.8	-3.1
Bank loans to the private sector (year-on-year % change)	-5.6	-12.3	-4.7	-2.6	-6.8
Lending for house purchase (year-on-year % change)	-4.1	-2.5	-0.9	6.6	-1.7
Loan to deposit ratio	162.0	140.8	133.4	128.7	113.3
CB liquidity as % of liabilities	9.0	18.3	18.4	16.6	6.9
Banks' exposure to countries receiving official financial assistance (% of GDP)[2)]	19.6	8.8	2.7	2.2	1.5
Private debt (% of GDP)	280.7	283.2	300.7	306.4	-
Gross external debt (% of GDP)					
- Public	46.5	50.8	63.6	75.7	77.6
- Private	606.7	680.1	695.6	694.2	711.9
Long term interest rates spread versus Bund (basis points)*	200.3	299.6	699.3	467.7	222.0
Credit default swap spreads for sovereign securities (5-year)*	189.8	267.2	673.9	406.0	120.4

Notes:

[1)] Latest data 2013Q3.

[2)] Covered countries are CY, EL, ES, LV, HU, IE, PT and RO.

* Measured in basis points.

Source :

Bank for International Settlements and Eurostat (exposure to macro-financially vulnerable countries), IMF (financial soundness indicators), Commission (long-term interest rates), World Bank (gross external debt) and ECB (all other indicators).

Table VIII. Labour market and social indicators

Labour market indicators	2008	2009	2010	2011	2012	2013
Employment rate (% of population aged 20-64)	72.3	66.9	64.6	63.8	63.7	65.5
Employment growth (% change from previous year)	-0.6	-7.8	-4.1	-1.8	-0.6	2.4
Employment rate of women (% of female population aged 20-64)	64.1	61.8	60.2	59.4	59.4	60.3
Employment rate of men (% of male population aged 20-64)	80.4	72.1	69.1	68.2	68.1	70.9
Employment rate of older workers (% of population aged 55-64)	53.7	51.3	50.2	50.0	49.3	51.3
Part-time employment (% of total employment, 15 years and more)	18.6	21.5	22.7	23.6	24.0	24.1
Part-time employment of women (% of women employment, 15 years and more)	32.4	34.0	34.9	35.7	35.4	35.6
Part-time employment of men (% of men employment, 15 years and more)	7.8	10.9	12.1	13.1	14.1	14.3
Fixed term employment (% of employees with a fixed term contract, 15 years and more)	8.5	8.8	9.6	10.2	10.2	10.0
Transitions from temporary to permanent employment	:	:	:	:	:	:
Unemployment rate[1] (% of labour force, age group 15-74)	6.4	12.0	13.9	14.7	14.7	13.1
Long-term unemployment rate[2] (% of labour force)	1.7	3.5	6.8	8.7	9.1	7.9
Youth unemployment rate (% of youth labour force aged 15-24)	13.3	24.0	27.6	29.1	30.4	26.8
Youth NEET rate (% of population aged 15-24)	14.9	18.6	19.2	18.8	18.7	16.1
Early leavers from education and training (% of pop. 18-24 with at most lower sec. educ. and not in further education or training)	11.3	11.7	11.5	10.8	9.7	8.4
Tertiary educational attainment (% of population 30-34 having successfully completed tertiary education)	46.1	48.9	50.1	49.7	51.1	52.6
Formal childcare (from 1 to 29 hours; % over the population less than 3 years)	16.0	15.0	21.0	10.0	:	:
Formal childcare (30 hours or over; % over the population less than 3 year)	8.0	5.0	8.0	11.0	:	:
Labour productivity per person employed (annual % change)	-1.5	1.6	3.1	4.0	0.8	-2.6
Hours worked per person employed (annual % change)	-1.1	-1.7	-0.6	0.0	0.2	0.5
Labour productivity per hour worked (annual % change; constant prices)	-0.4	3.4	3.7	4.0	0.5	-3.1
Compensation per employee (annual % change; constant prices)	8.3	2.9	-2.3	-0.8	0.1	-2.1
Nominal unit labour cost growth (annual % change)	6.8	-2.6	-6.7	-4.0	0.0	1.0
Real unit labour cost growth (annual % change)	10.0	1.3	-5.3	-4.6	-0.6	0.6

Notes:

[1] Unemployed persons are all persons who were not employed, had actively sought work and were ready to begin working immediately or within two weeks. The labour force is the total number of people employed and unemployed.

[2] Long-term unemployed are unemployed persons for at least 12 months.

Sources:
Commission (EU Labour Force Survey and European National Accounts)

Expenditure on social protection benefits (% of GDP)	2007	2008	2009	2010	2011
Sickness/Health care	6.7	7.9	9.8	11.4	12.8
Invalidity	1.0	1.1	1.3	1.3	1.2
Old age and survivors	4.7	5.5	6.4	6.6	6.6
Family/Children	2.6	3.1	3.6	3.6	3.4
Unemployment	1.4	1.8	3.0	3.5	3.3
Housing and Social exclusion n.e.c.	0.4	0.4	0.4	0.4	0.4
Total	17.1	20.3	25.1	27.3	28.3
of which: means tested benefits	4.4	5.3	6.7	7.6	7.8
Social inclusion indicators	**2008**	**2009**	**2010**	**2011**	**2012**
At-risk-of-poverty or social exclusion[1] (% of total population)	23.7	25.7	27.3	29.4	:
At-risk-of-poverty or social exclusion of children (% of people aged 0-17)	26.6	31.4	34.1	34.1	:
At-risk-of-poverty or social exclusion of elderly (% of people aged 65+)	22.5	17.9	11.3	13.8	:
At-Risk-of-Poverty rate[2] (% of total population)	15.5	15.0	15.2	15.2	:
Severe Material Deprivation[3] (% of total population)	5.5	6.1	5.7	7.8	:
Share of people living in low work intensity households[4] (% of people aged 0-59)	13.7	20.0	22.9	24.2	:
In-work at-risk-of poverty rate (% of persons employed)	6.5	5.3	5.5	5.6	:
Impact of social transfers (excluding pensions) on reducing poverty	54.4	60.0	61.9	61.6	:
Poverty thresholds, expressed in national currency at constant prices[5]	13 418	12 700	11 801	11 533	:
Gross disponsable income (households)	98 634	91 922	87 374	85 579	84 597
Relative median poverty risk gap (60% of median equivalised income, age: total)	17.7	16.2	15.5	17.5	:

Notes:

[1] People at-risk-of poverty or social exclusion (AROPE): individuals who are at-risk-of poverty (AROP) and/or suffering from severe material deprivation (SMD) and/or living in household with zero or very low work intensity (LWI).

[2] At-risk-of poverty rate (AROP): share of people with an equivalised disposable income below 60% of the national equivalised median income.

[3] Share of people who experience at least 4 out of 9 deprivations: people cannot afford to i) pay their rent or utility bills, ii) keep their home adequately warm, iii) face unexpected expenses, iv) eat meat, fish, or a protein equivalent every second day, v) enjoy a week of holiday away from home once a year, vi) have a car, vii) have a washing machine, viii) have a colour tv, or ix) have a telephone.

[4] People living in households with very low work intensity: share of people aged 0-59 living in households where the adults (excluding dependent children) work less than 20% of their total work-time potential during the previous 12 months.

[5] For EE, CY, MT, SI, SK, thresholds in nominal values in Euros; HICP - index 100 in 2006 (2007 survey refers to 2006 incomes)

Sources:
For expenditure for social protection benefits ESSPROS; for social inclusion EU-SILC.

Table IX. Product market performance and policy indicators

Performance indicators	2004-2008	2009	2010	2011	2012	2013
Labour productivity[1] total economy (annual growth in %)	3.1	-0.8	-1.2	2.3	3.4	-0.9
Labour productivity[1] in manufacturing (annual growth in %)	0.7	6.1	23.3	0.0	8.2	-6.3
Labour productivity[1] in electricity, gas, water (annual growth in %)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Labour productivity[1] in the construction sector (annual growth in %)	4.2	-16.7	-50.2	-17.2	5.2	10.5
Patent intensity in manufacturing[2] (patents of the EPO divided by gross value added of the sector)	140.3	150.1	159.7	165.5	n.a.	n.a.
Policy indicators	**2004-2008**	**2009**	**2010**	**2011**	**2012**	**2013**
Enforcing contracts[3] (days)	515.0	515	515	650	650	650
Time to start a business[3] (days)	15.0	13	13	13	10	10
R&D expenditure (% of GDP)	1.3	1.7	1.7	1.7	1.7	n.a.
Tertiary educational attainment (% of 30-34 years old population)	41.7	48.9	50.1	49.7	51.1	52.6
Total public expenditure on education (% of GDP)	4.9	6.4	6.4	6.2	n.a.	n.a.
	2008	**2009**	**2010**	**2011**	**2012**	**2013**
Product market regulation[4], Overall (Index; 0=not regulated; 6=most regulated)	1.4	n.a.	n.a.	n.a.	n.a.	1.4
Product market regulation[4], Retail (Index; 0=not regulated; 6=most regulated)	1.5	n.a.	n.a.	n.a.	n.a.	1.5
Product market regulation[4], Network Industries[5] (Index; 0=not regulated; 6=most regulated)	2.6	n.a.	n.a.	n.a.	n.a.	2.2

Notes:

[1] Labour productivity is defined as gross value added (in constant prices) divided by the number of persons employed.

[2] Patent data refer to applications to the European Patent Office (EPO). They are counted according to the year in which they were filed at the EPO. They are broken down according to the inventor's place of residence, using fractional counting if multiple inventors or IPC classes are provided to avoid double counting.

[3] The methodologies, including the assumptions, for this indicator are presented in detail on the website http://www.doingbusiness.org/methodology.

[4] The methodologies of the product market regulation indicators are presented in detail on the website http://www.oecd.org/document/1/0,3746,en_2649_34323_2367297_1_1_1_1,00.html.

[5] Aggregate ETCR.

Source :
Commission, World Bank - *Doing Business* (for enforcing contracts and time to start a business) and OECD (for the product market regulation indicators).

Table X. Green Growth

		2003-2007	2008	2009	2010	2011	2012
Green Growth performance							
Macroeconomic							
Energy intensity	kgoe / €	0.11	0.11	0.11	0.11	0.10	0.10
Carbon intensity	kg / €	0.51	0.47	0.45	0.46	0.42	n.a.
Resource intensity (reciprocal of resource productivity)	kg / €	1.55	1.03	0.89	0.85	0.72	n.a.
Waste intensity	kg / €	n.a.	0.15	n.a.	0.15	n.a.	n.a.
Energy balance of trade	% GDP	-1.8%	-3.2%	-2.4%	-3.0%	-3.5%	-3%
Energy weight in HICP	%	8	9	9	9	11	13
Difference between change energy price and inflation	%	6.56	5.6	-4.1	3.3	8.4	7.9
Environmental taxes over labour taxes	ratio	23.9%	22.2%	20.4%	22.1%	21.2%	n.a.
Environmental taxes over total taxes	ratio	8.0%	8.4%	8.5%	9.1%	8.9%	n.a.
Sectoral							
Industry energy intensity	kgoe / €	0.07	0.06	0.05	0.05	n.a.	n.a.
Share of energy-intensive industries in the economy	% GDP	14.7	14.0	16.0	n.a.	n.a.	n.a.
Electricity prices for medium-sized industrial users**	€ / kWh	n.a.	0.14	0.12	0.11	0.12	0.13
Gas prices for medium-sized industrial users***	€ / kWh	n.a.	0.04	0.03	0.03	0.04	0.04
Public R&D for energy	% GDP	n.a.	0.02%	0.02%	0.02%	0.01%	0.00%
Public R&D for the environment	% GDP	n.a.	0.01%	0.01%	0.01%	0.01%	0.01%
Recycling rate of municipal waste	ratio	30.4%	36.2%	37.3%	39.5%	40.8%	60.7%
Share of GHG emissions covered by ETS*	%	n.a.	30.1%	27.8%	28.2%	27.5%	29.1%
Transport energy intensity	kgoe / €	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Transport carbon intensity	kg / €	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Security of energy supply							
Energy import dependency	%	89.6%	90.6%	88.8%	86.5%	89.6%	84.8%
Diversification of oil import sources	HHI	n.a.	0.48	0.54	0.50	0.49	n.a.
Diversification of energy mix	HHI	0.40	0.39	0.38	0.38	0.36	0.34
Share renewable energy in energy mix	%	2.3%	3.6%	4.5%	4.4%	5.8%	5.9%

Country-specific notes:
The year 2012 is not included in the table due to lack of data.
General explanation of the table items:
Source: Eurostat unless indicated otherwise; ECFIN elaborations indicated below
All macro intensity indicators are expressed as a ratio of a physical quantity to GDP (in 2000 prices)
Energy intensity: gross inland energy consumption (in kgoe) divided by GDP (in EUR)
Carbon intensity: Greenhouse gas emissions (in kg CO2 equivalents) divided by GDP (in EUR)
Resource intensity: Domestic Material Consumption (in kg) divided by GDP (in EUR)
Waste intensity: waste (in kg) divided by GDP (in EUR)
Energy balance of trade: the balance of energy exports and imports, expressed as % of GDP
Energy weight in HICP: the share of the "energy" items in the consumption basket used in the construction of the HICP
Difference between energy price change and inflation: energy component of HICP, and total HICP inflation (annual %-change)
Environmental taxes over labour or total taxes: from DG TAXUD's database "Taxation trends in the European Union"
Industry energy intensity: final energy consumption of industry (in kgoe) divided by gross value added of industry (in 2005 EUR)
Share of energy-intensive industries in the economy: share of gross value added of the energy-intensive industries in GDP
Electricity and gas prices medium industrial users: consumption band 500 - 2000MWh and 10000 - 100000 GJ; figures excl. VAT.
Recycling rate of municipal waste: ratio of municipal waste recycled over total municipal waste
Public R&D for energy or for the environment: government spending on R&D (GBAORD) for these categories as % of GDP
Share of GHG emissions covered by ETS: based on greenhouse gas emissions as reported by Member States to EEA (excl LULUCF)
Transport energy intensity: final energy consumption of transport activity (kgoe) divided by transp industry gross value added (2005 EUR)
Transport carbon intensity: greenhouse gas emissions in transport activity divided by gross value added of the transport sector
Energy import dependency: net energy imports divided by gross inland energy consumption incl. energy consumption international bunkers
Diversification of oil import sources: Herfindahl index (HHI), calculated as the sum of the squared market shares of countries of origin
Diversification of the energy mix: Herfindahl Index over natural gas, total petrol products, nuclear heat, renewable energies and solid fuels
Share renewable energy in energy mix: %-share in gross inland energy consumption, expressed in tonne oil equivalents
* Commission and EEA.
** For 2007 average of S1 & S2 for DE, HR, LU, NL, FI, SE & UK. Other countries only have S2.
*** For 2007 average of S1 & S2 for HR, IT, NL, FI, SE & UK. Other countries only have S2.

List of indicators used in Box 9 on the potential impact on growth of structural reforms.

Final goods sector mark-ups: Price-cost margin, i.e. the difference between the selling price of a good or service and its cost. Final goods mark-ups are proxied by the mark-ups in selected services sectors (transport and storage, post and telecommunications, electricity, gas and water supply, hotels and restaurants and financial intermediation but excluding real estate and renting of machinery and equipment and other business activities[59]).
Source: Commission services estimation using the methodology of Roeger, W. (1995). "Can imperfect Competition explain the Difference between primal and dual Productivity?" *Journal of Political Economy* Vol. 103(2) pp. 316-30, based on EUKLEMS 1996-2007 data.

Entry costs: Cost of starting a business in the intermediate sector as a share of income per capita. The intermediate sector is proxied by the manufacturing sector in the model.
Source: World Bank, Doing Business Database. www.doingbusiness.org. 2012 data.

Implicit consumption tax rate: Defined as total taxes on consumption over the value of private consumption. In the simulations it is used as a proxy for shifting taxation away from labour to indirect taxes. The implicit consumption tax-rates are increased (halving the gap vis-à-vis the best performers) while labour tax-rates are reduced so that the combined impact is ex-ante budgetary neutral.
Source: European Commission, Taxation trends in the European Union, 2013 edition, Luxembourg, 2013. 2011 data.

Shares of high-skilled and low-skilled: The share of high skilled workers is increased, the share of low-skilled workers is reduced (halving the gap vis-à-vis the best performers). Low-skilled correspond to ISCED 0-2 categories; high-skilled correspond to scientists (in mathematics and computing, engineering, manufacturing and construction). The remainder is medium-skilled.
Source: EUROSTAT. 2012 data or latest available.

Female non-participation rate: Share of women of working age not in paid work and not looking for paid work in total female working-age population
Source: EUROSTAT. 2012 data or latest available.

Low-skilled male non-participation rates: Share of low-skilled men of working age not in paid work and not looking for paid work in total male working-age population
Source: EUROSTAT. 2012 data or latest available.

Elderly non-participation rates (55-64 years): Share of the population aged 55-64 years not in paid work and not looking for paid work in total population aged 55-64 years.
Source: EUROSTAT. 2012 data or latest available.

ALMP: Active Labour Market Policy expenditures as a share of GDP over the share of unemployed in the population.
Source: EUROSTAT. 2011 data or latest available.

Benefit replacement rate: Share of a worker's pre-unemployment income that is paid out by the unemployment insurance scheme. Average of net replacement rates over 60 months of unemployment.
Source: OECD, Benefits and Wages Statistics.
www.oecd.org/els/benefitsandwagesstatistics.htm. 2012 data.

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[59] The real estate sector is excluded because of statistical difficulties of estimating a mark-up in this sector. The sector renting of machinery and equipment and other business activities is conceptually part of intermediate goods sector.