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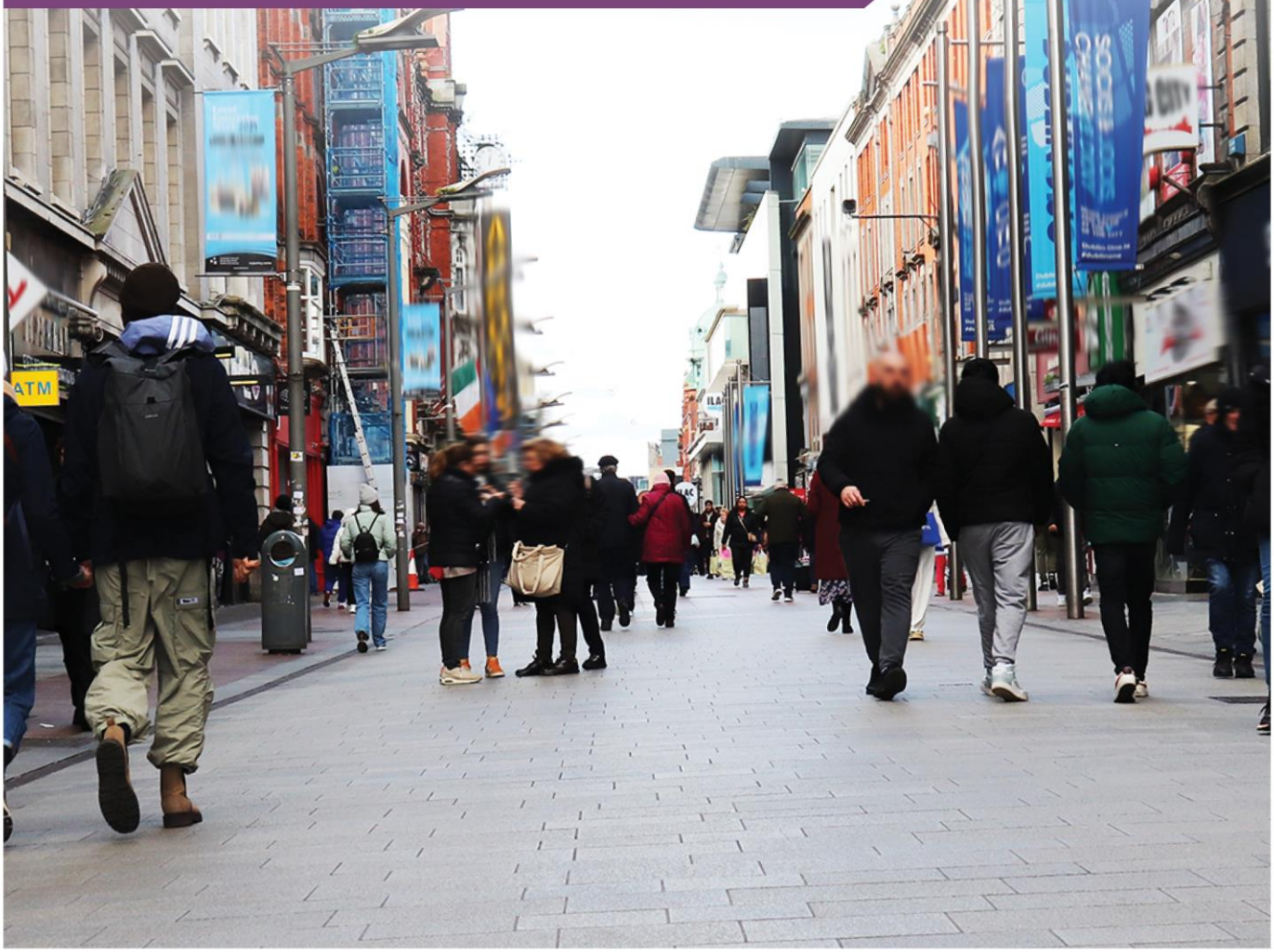

Contents

A Concentrated Tax Base and Rising Expenditure: Fiscal Risks in Ireland's Medium-Term Outlook

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Executive Summary

The economy has grown rapidly since 2021, faces capacity constraints and is subject to significant externally driven inflationary pressures. Government fiscal policy has been procyclical in recent years with net expenditure growing at an annual average rate of 9 per cent, almost twice the estimated nominal growth potential of the domestic economy. As a result, on a real per capita basis, spending is estimated to have increased by 15 per cent between 2019 and 2025, compared to growth of 11 per cent for the euro area. With the economy operating at capacity and inflation rising, fiscal policy should avoid unnecessarily stimulating demand at present.

The headline and underlying (excluding windfall CT) budget balances are forecast to deteriorate out to 2030. Government projections currently indicate an expected continuation of high growth in spending out to 2030, averaging 6.4 per cent per annum in general government terms, above the projected growth in government revenue (5.4 per cent). As a result, the headline and underlying (excluding windfall CT) general government (GG) balance are forecast to deteriorate over the medium term and the proportion of windfall CT being saved falls sharply. The lower level of windfall CT being saved out to 2030, relative to the proportion saved in 2025, appears to largely reflect additional current expenditure. An implication of this is that, from 2028, government borrowing will be required to finance transfers to the State's two savings funds.

In the absence of an effective fiscal anchor, a pattern of overspends relative to initial budgetary allocations has become established. Government spending outturns have exceeded initial budget allocations by an average of €5.4bn or 6 per cent per annum on average between 2021 and 2025. The expenditure path set out in the Government's Medium-Term Fiscal and

[1] Irish Economic Analysis Division. We would like to thank Daragh Clancy, Robert Kelly, Martin O'Brien and Gerard O'Reilly (Central Bank of Ireland), Niall Conroy (Irish Fiscal Advisory Council), David Purdue and Alan Mahon (National Treasury Management Agency) for comments. The views expressed in this Article are those of the authors and do not necessarily reflect those of the Central Bank of Ireland or the European System of Central Banks.

Structural Plan (MTFSP) is to be delivered through use of existing expenditure ceilings, but these have not – to date – been operated effectively. Expenditure has already been revised up for 2026 – largely reflecting the Government's announced energy-related supports – with overall net primary spending expected to rise by 7.4 per cent this year. Any additional support measures should be temporary, targeted and tailored and accommodated within existing budgetary allocations.

A lower rate of growth in net spending than currently projected would result in larger headline surpluses and see a greater proportion of CT revenue being saved. To maintain existing levels of public services out to 2030 and to increase public investment as envisaged in the revised NDP, average general government expenditure growth of around 5 per cent per annum would be required. Relative to current government projections, we estimate that maintaining spending growth at this lower rate would deliver larger headline budget surpluses out to 2030 and be consistent with one-third of estimated windfall CT being saved between 2028 and 2030, compared with just 20 per cent in the government's projections. Higher expenditure growth above that consistent with maintaining existing public services could be enabled while still achieving these outcomes, if additional revenue-raising measures were introduced.

A continuation of the established pattern of expenditure overruns would deplete fiscal buffers. If spending overruns continue – resulting in spending growth closer to that observed since 2022 – then the public finances would deteriorate significantly. The headline budget surplus would be broadly eliminated by 2030 with the underlying deficit deteriorating to 6 per cent of GNI* (or €25.7 billion). This would deplete fiscal buffers, limiting the government's capacity to respond to future negative shocks. Higher spending growth in the short term would also risk adding to existing inflationary pressures.

The tax base has become more dependent on uncertain corporation tax (CT). CT has been responsible for almost 40 per cent of all revenue growth since 2019 and, as a result, accounted for 23 per cent of total revenue last year, up from 12 per cent in 2019. There are material risks to the medium-term sustainability of CT revenue. These arise from its concentration among a small number of MNEs and its vulnerability to changes in US economic or tax policy – the latter could particularly impact the large, estimated windfall component of CT. Moreover, the income tax base has narrowed and is highly concentrated, with the top 10 per cent of earners responsible for around 60

per cent of income tax and USC receipts last year. Recent policy decisions have reduced the VAT base.

A broader tax base is needed to fund known spending pressures and to help mitigate the risks from a possible loss of corporation tax. Government expenditure will need to rise over the medium term by 6 percentage points of national income to fund higher age-related pressures and costs related to climate change and the green transition. The cost of servicing the national debt is also projected to increase. Long-term projections from the Department of Finance show that, in the absence of offsetting policy actions, it is likely the public finances would remain in a persistent deficit position in the coming decades. To mitigate risks to the tax base and to protect fiscal sustainability over the longer term, the government should broaden the tax base and increase revenue as a share of national income. This could be considered through various avenues, including reform of tax reliefs, property and consumption taxes, and social insurance contributions, while being cognisant of supply incentives and distributional effects.

The planned increases in government capital spending can alleviate bottlenecks and boost long-term growth, but effective implementation is needed to maximise these gains. The level of government investment has more than doubled in nominal terms since 2019 and is projected to rise further in the coming years – averaging 6 per cent of GNI* annually between 2027 and 2030. Higher investment spending could help to address known deficits in key national infrastructure, crowd in higher private investment and boost the economy's long-run growth potential. Actions to accelerate the decarbonisation of the economy and reduce fossil fuel dependency would also build resilience to future geopolitical shocks and contribute to achieving emission reduction targets. Achieving value for money in the delivery of a large infrastructure plan is challenging in an economy at full employment and in the face of externally driven cost shocks. In this context, rigorous expenditure management combined with prioritising public investment projects that yield the largest spillovers to the private sector and enhance potential output will be important. Achieving this would help to boost productivity, improve competitiveness and maximise the overall gain to the economy from the additional planned investment spending over the coming years.

An effective fiscal anchor would help to steer the public finances and economic growth onto a sustainable path over the medium term, even amid short-term political and economic volatility. An effective anchor would align

the growth in government spending to the State's sustainable revenue-raising capacity (making allowance for CT risks). It would help to prevent overheating during periods of strong demand and high inflation, while enabling supportive fiscal policy during downturns.

1. Introduction

The current economic and fiscal context has brought the trade-offs facing budgetary policy in Ireland into sharp focus. In the face of a challenging external economic environment, the Government must simultaneously manage upward pressures on government expenditure from a range of sources with the need to address vulnerabilities in its tax revenue base, while at the same time delivering on its planned expansion in public investment. While the headline budgetary position is favourable and the performance of the economy over the last five years provides some resilience with which to address these needs, significant vulnerabilities remain to be addressed to improve the long-term sustainability of both the economy and the fiscal position.

Government expenditure has increased sharply in recent years, growing by 54 per cent in nominal terms since 2019—substantially outpacing growth in the euro area. During this period, spending increased to fund temporary support measures responding to the Covid-19 pandemic and for cost-of-living supports, but as these temporary supports had largely dissipated by 2025, much of the increase from 2019 to 2025 reflects a rise in permanent spending. At the same time, the public finances have become more dependent on corporation tax, with this revenue source now accounting for nearly one-quarter of total government revenue, up from just 12 per cent in 2019. When windfall CT is excluded, the underlying budget deficit is estimated to have increased from €0.8 billion in 2019 to €7.2 billion in 2025. The growing dominance and concentration of corporation tax presents material risks for fiscal sustainability.

Putting these developments in expenditure and revenue together, the medium-term fiscal outlook presents a complex picture. Current government projections indicate that general government expenditure growth will moderate from recent high levels, but continue to grow strongly at an average of 6.4 per cent annually out to 2030. This outpaces projected average revenue growth of 5.4 per cent. This divergence would reduce the headline budget surpluses recorded in recent years, while implying an increasingly large share of uncertain corporation tax revenues would be deployed to finance permanent spending commitments out to 2030.

Looking beyond the medium term, Ireland faces formidable long-term fiscal pressures. The population is ageing rapidly, with the old-age dependency ratio expected to increase substantially by the mid-century. Age-related spending on pensions, healthcare and long-term care will rise significantly, potentially moving the public finances into persistent deficit by the 2030s and pushing national debt to high levels, in the absence of offsetting policy measures. Broadening the tax base over the coming years would help to ensure that additional known expenditure needs can be met sustainably and would improve the resilience of the public finances if corporation tax was to decline significantly. These structural challenges underscore the need for a credible fiscal framework that balances short-term economic stabilisation with long-term sustainability.

The Government has committed to substantially increasing public investment to address long-standing infrastructure deficits in housing, transport, health, energy and other critical sectors. While such investment is warranted, its delivery in an economy operating at full employment and with substantial externally driven inflationary pressures presents significant challenges, including rising construction costs and labour market constraints. The analysis in this *Article* illustrates how management of price pressures along with prioritisation of productivity-enhancing investment can deliver improved value for money and larger and more sustained gains to the economy overall from the planned increases in public capital spending.

This *Article* examines Ireland's fiscal position and medium-term outlook in the context of these challenges. Section 3 analyses recent expenditure and revenue developments in a euro area context. Section 4 assesses the implications for the public finances of scenarios involving differing assumptions for the future pace of government spending growth, economic growth and corporation tax revenues. Section 5 focusses on public investment and how policy choices around effective delivery can enhance the gain to the economy from additional spending. Section 6 outlines the core principles of an effective fiscal anchor and Section 7 concludes.

2. Macroeconomic context for Budget 2027

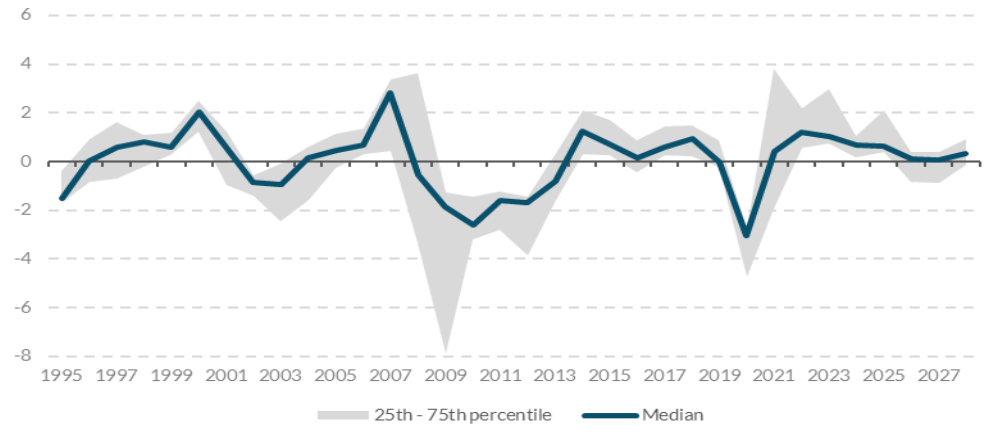
For a small open economy in a monetary union, fiscal policy has a key role to play in managing the economic cycle. This is also true for Ireland, where monetary policy is set at the euro area level and therefore may not be fully appropriate to the particular stage of the business cycle in Ireland. To maintain sustainable economic growth and inflation, the fiscal stance should aim to support the economy when it is operating below potential (i.e. when

unemployment is high) and conversely, fiscal policy should reduce demand when the economy is operating above its sustainable potential and excessive inflationary risks are present. Historically, however, fiscal policy has been largely procyclical in Ireland (Fitzgerald, 2025).

A helpful summary indicator for assessing the position of the economy and the appropriateness of the corresponding fiscal stance is the output gap. This measures the difference between the current level of output in the economy and what could be produced if all the economy's resources were employed at a sustainable level. The output gap is not observed and must be estimated using historical data. Given the problems with using GDP as an indicator of economic activity in Ireland, we estimate a range of methods using MDD, GNI* and the GVA of domestically dominated sectors. These measures of economic activity are less distorted by the presence of large, global multi-nationals than GDP (see Conefrey et al., 2024). The median range of the derived estimates indicates that the positive gap of the post-pandemic recovery years diminished over 2024 and 2025, but the economy overall is operating at its potential [Figure 1]. The estimates of the output gap since 2020 are consistent with the evidence from the labour market, in particular an unemployment rate at or below 5 per cent since 2021 and the employment rate (for the population aged 15-64 years) increasing to a record peak of 71.8 per cent in Q3 2024.[2]

The estimated output gap reflects an economy operating at its potential

Figure 1
Per cent of potential output (%)



Source: Central Bank of Ireland calculations

Notes: Median and percentile range are calculated by taking the 25, 50th, and 75th percentile across a range of output gap estimates generated using a variety of methods. Only globalisation-adjusted measures of output are included in the estimations: MDD, GNI*, and GVAD.

[2] The only exception to this limit was Q3 2025, where the LFS indicates the unemployment rate rose to 5.3 per cent.

From a fiscal perspective, the estimates of the economy's cyclical position summarised by the output gap do not support the need for a fiscal stimulus to boost demand. With the economy operating at capacity, budgetary policy should not add further demand to the economy at this time. Moreover, as outlined in *Quarterly Bulletin 2*, forecasts for inflation have been revised up in recent months largely reflecting the impact of higher global commodity prices since the start of the US-Iran war. Inflation in the central scenario is forecast to average 3.5 per cent in 2026 but could be higher than this if Middle East tensions persist. With these externally driven forces already putting upward pressure on Irish inflation, fiscal policy should avoid unnecessarily stimulating demand. As the fiscal stance for 2026 is already stimulatory (as discussed below), any further support measures deemed necessary to protect vulnerable households or firms should be targeted, tailored and temporary and be funded within existing budgetary allocations.

3. The outlook for government expenditure, revenue and the budget balance

Recent expenditure developments

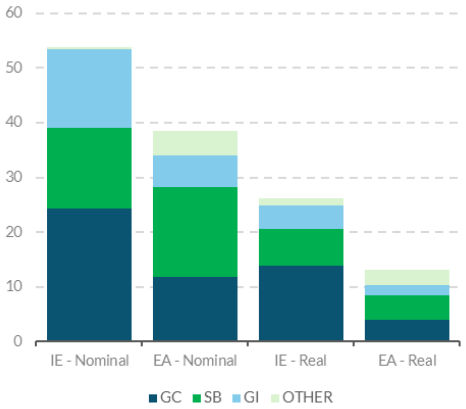
Temporary spending measures introduced in response to the Covid-19 pandemic and to provide cost of living supports following the Russian invasion of Ukraine are estimated to have totalled close to €40bn (11.5 per cent of GNI*) between 2020 and 2024. These measures were necessary to shield vulnerable households, businesses and the wider economy from the impact of these negative shocks. However, in the case of the cost of living supports implemented over 2022 to 2024, analysis suggests greater targeting of measures could have reduced the fiscal cost while protecting the most vulnerable (Boyd & McIndoe-Calder, 2025). A new set of measures costing €755 million were introduced in March and April this year in response to the increase in energy prices following the Middle East conflict.

Permanent expenditure has also increased strongly since the turn of the decade. With most of the temporary interventions having been withdrawn by the end of 2024, comparing government spending between 2019 and 2025 allows a clearer assessment of how the permanent expenditure base has changed from the pre- Covid-19 period, both in absolute and relative terms. Nominal general government expenditure grew by 54 per cent over this period, an annual average increase of 9 per cent per annum. Annual growth rates in core spending in the most recent years were the strongest since prior to the financial crisis, when expenditure was partly financed by unsustainable

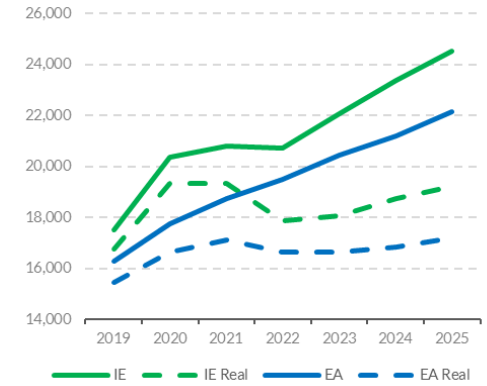
property-related revenues. Spending growth in Ireland has also been notably stronger than in the euro area since the turn of the decade, where government expenditure increased by 39 per cent (annual average increase of 6.4 per cent) despite facing similar external shocks. Capital expenditure played a bigger role in driving government spending in Ireland over this period – generating just over one quarter of the increase between 2019 and 2025, compared to 15 per cent in the euro area – but primary current expenditure has also grown at a stronger pace in Ireland [Figure 2a].

The increase in government spending in Ireland is significantly higher than in the euro area

Nominal and real government spending
Figure 2a
Per cent change between 2019-2025 (%)



Government expenditure per capita
Figure 2b
€, millions



Source: CSO, Eurostat and Central Bank of Ireland calculations

Notes: In the left-hand chart, GC refers to Government Consumption; SB refers to Social Benefits; GI refers to Government investment and Other refers to other spending. In the chart on the right, per capita is determined by dividing expenditure by the respective populations in Ireland (IE) and euro-area (EA). For more information on how real expenditure is calculated see Box C, Quarterly Bulletin 4, 2025.

While nominal government expenditure is particularly important from a fiscal perspective, real government spending per capita – which adjusts the nominal figure for inflation and population change – provides a more relevant indicator of how actual resources available to provide services to the public have changed over time. Population growth since 2019 has been significantly higher in Ireland than in the euro area. Despite this, we estimate that real government expenditure per capita has recorded a stronger increase since the turn of the decade in Ireland (15 per cent compared to 11 per cent in the euro area), with the gap between the level of spending per head also widening over time [Figure 2b].

Estimating the cost of maintaining Existing Level of Services

A useful starting position for assessing the medium-term fiscal outlook is estimating the level of spending necessary to ensure the government can carry out its core functions. Government expenditure required to maintain existing levels of supports and services - referred to as the 'Existing Level of Services' (ELS) - must take account of expected price, demographic and other changes in the underlying economy that drive nominal spending growth. Once the necessary spending increase to finance ELS is established, new expenditure policy measures can be introduced with any remaining fiscal space (which can be increased or decreased by discretionary taxation changes).

Table 1: Average general government expenditure growth of around 5 per cent per annum would be required to maintain ELS and deliver the NDP[3]

	2026	2027	2028	2029	2030	Average 2026-30
Maintain Existing Level of Services (€bn)	5.8	5.1	4.5	4.6	4.8	5.0
Capital Investment / NDP (€bn)	1.8	1.5	3.6	2.2	0.9	2.0
Total €bn	7.6	6.7	8	6.9	5.7	7.0
% Change in Expenditure Base	5.8	4.8	5.5	4.5	3.6	4.8

Source: Central Bank of Ireland calculations

Looking ahead, we find that average general government expenditure growth of around 5 per cent per annum would allow the Government to both maintain ELS and deliver the very large investment plan outlined in the revised National Development Plan (NDP) out to 2030 [Table 1]. We estimate that primary current spending would need to increase by an average of €5bn per annum between 2026 and 2030 to maintain ELS taking account of

[3] To estimate the cost of maintaining the Existing Level of Public Services (ELS) we adjust each expenditure component's 2025 base to take account of expected changes in prices, demographics and other key factors that impact spending levels. For Intermediate Consumption, Other Current Transfers and Capital Transfers, we increase the 2025 base by projected HICP inflation and population growth rates. This ensures that real expenditure per capita remains unchanged in each year. For Compensation of Employees, we increase the base by the forecast change in whole economy compensation per employee. This assumes that public sector compensation grows in line with that in the private sector. The required increase in Social Benefits is broken down into pension expenditure (driven by the change in population aged 65+ and the projected increase in HICP inflation – keeping real expenditure per capita constant), unemployment payments (reflecting the expected number of unemployed in each year and the average annual payment per unemployed person in 2025 adjusted for the HICP) and other social benefits (driven by the change in population and HICP inflation). Government Investment expenditure is fully consistent with the forecast annual change in gross fixed capital formation in the Annual Progress Report. The estimates, which are presented on a general government basis, are sensitive to the choice of assumptions.

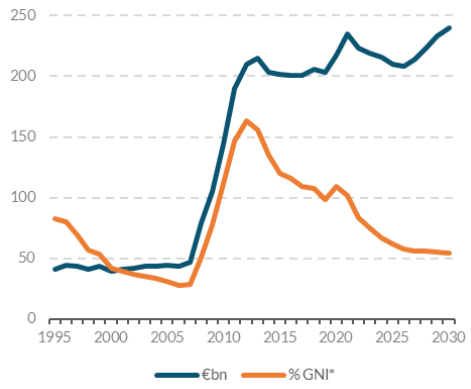
demographic and inflationary developments. This figure is broadly in line with IFAC's recent 'stand still' estimate (average of €5.2bn per annum over the slightly shorter period of 2027 to 2030). When planned capital investment is also included, general government spending would need to increase by an average of €7bn per annum to maintain ELS and deliver the NDP. This represents average growth of 4.8 per cent each year in the expenditure base. These growth rates are in gross terms. The net spending outturn would depend on tax changes (tax cuts or increases) implemented over the period. Additional revenue raising measures would allow for increases in expenditure above that required to maintain existing services and the planned public investment.

Interest costs and the national debt

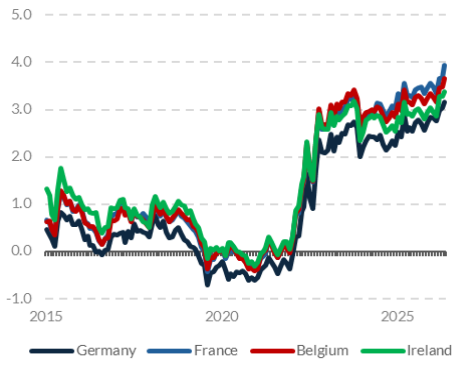
The general government debt ratio is expected to continue its downward trend in the coming years, with the Government's Annual Progress Report (APR) forecasting an 8-percentage point decline to 54 per cent of GNI* in the five years to 2030. The improvement is expected to be driven by large headline primary budget surpluses and the expectation that the growth rate of the economy will continue to outstrip the interest rate on public debt. At the same time the nominal debt level - which increased sharply during the housing crash and subsequent financial crisis - is forecast to increase further in the coming years, rising by €30 billion from end-2025 to €240 billion by 2030 [Figure 3a].

Government borrowing costs are increasing

Irish general government debt
Figure 3a
Per cent of GNI* (%) and €, billions



10-year government bond yield
Figure 3b
Per cent (%)



Source: CSO, Annual Progress Report and LSEG

The State's borrowing costs are also expected to increase over the medium term. Amidst highly accommodative monetary policy, Ireland faced exceptionally favourable financing conditions between 2015 and end-2021,

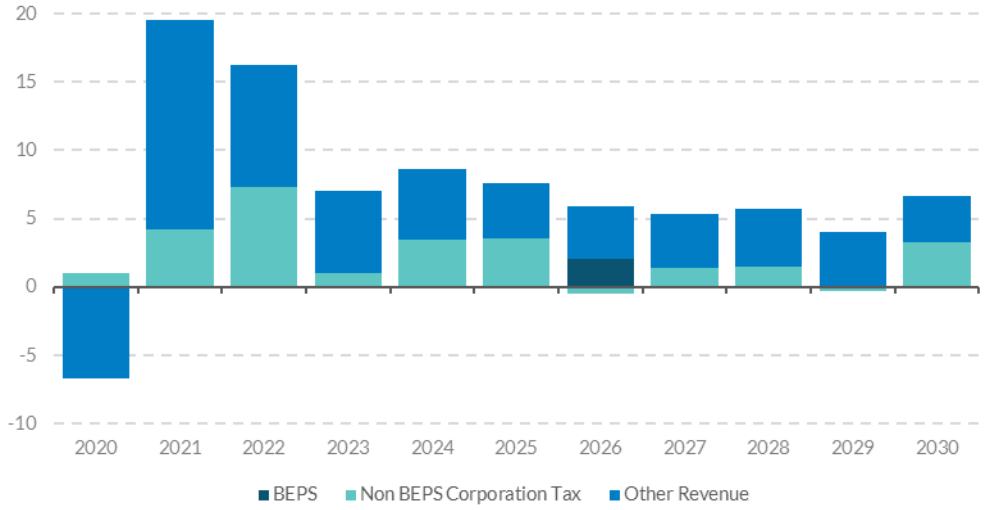
with the yield on 10-year Treasury bonds averaging around 0.5 per cent over this period [Figure 3b]. This allowed the NTMA to refinance high interest debt at more favourable rates and over a longer period. But, as is the case across the euro area, borrowing costs have trended upwards in recent years (Irish 10-year Treasury bond yields averaged just above 3 per cent in the first five months of the year) and, as a result, debt maturing in the coming years will be more expensive to refinance [Figure 3b]. Five Treasury bonds totalling €44bn (13 per cent of 2025 GNI*) are set to mature by end-2030, all of which pay interest below the current 10-year yield. Reflecting this, the Government forecast in the APR that annual interest expenditure would double from €3bn in 2025 to €6bn in 2030, with the effective (average) interest rate on the debt stock forecast to increase from 1.4 per cent to 2.6 per cent over the same period.

Recent revenue developments

Irish government revenue continues to grow strongly. Between 2019 and 2025, general government revenue increased by 64 per cent, or an annual average increase of 10.7 per cent per annum. This was double the pace of increase recorded in the euro area over the same period. Driving this has been a remarkable tripling of CT receipts (from €10.9bn in 2019 to €32.9bn in 2025, when the Apple state aid case is excluded). This growth in CT has been responsible for almost 40 per cent of all revenue growth since 2019 [Figure 4]. Consequently, CT as a share of total general government revenue has increased from 12 per cent in 2019 to 23 per cent last year (or one-third of all Exchequer tax revenue [Figure 5]). As a result, the State's revenue base is now much more reliant on CT receipts than at any time in the past.

Corporation tax drove almost 40 per cent of all revenue growth between 2019 and 2025, and will continue to play a key role supporting revenue growth in the coming years

Factors driving change in general government revenue growth
Figure 4
Per cent (%)



Source: CSO, Department of Finance

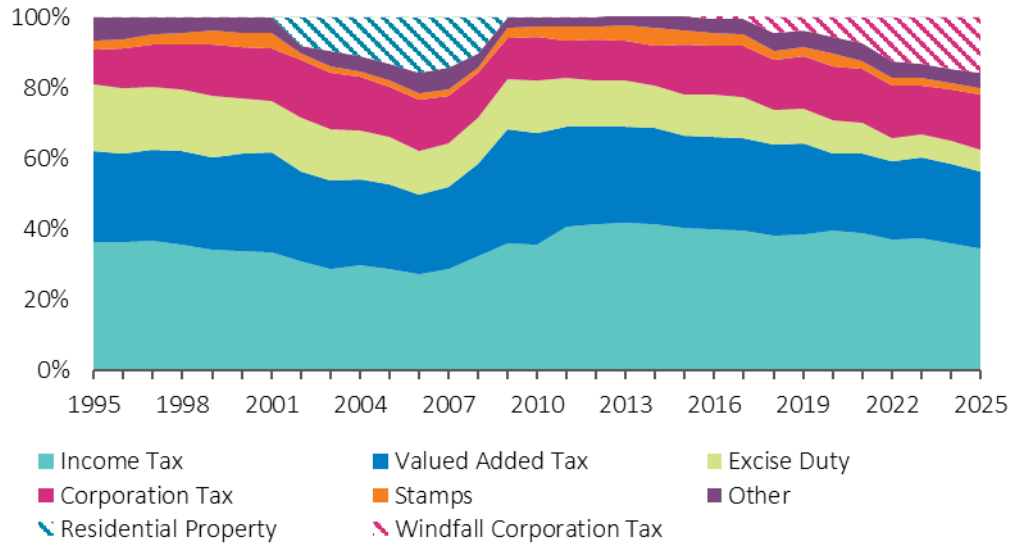
Notes: Chart excludes revenue from Apple state aid case. BEPS is projected revenue from introduction of Pillar Two of BEPS reforms. Chart shows latest Department of Finance revenue projections taken from Annual Progress Report.

Corporation tax revenue is likely to increase further in 2026, supported by reforms to the global tax system, and is expected to continue to play a key role in driving total revenue growth [Figure 4]. Nevertheless, concerns remain over the long-term sustainability of the current high levels of revenue from this source. A significant proportion of Ireland's CT receipts are potentially transitory, i.e. in excess of what may be expected to be sustained in the medium to long term (see for example IFAC, 2023). These receipts, typically referred to as 'windfall' or 'excess' CT, are vulnerable to external shocks and/or the activities of a small number of companies and changes in international tax regimes, particularly changes in US tax policy [Box A]. We estimate that around half of all CT receipts in 2025 were potentially transitory (broadly in line with the Government's latest estimates), accounting for 15 per cent of all tax receipts last year.[4] Notably, the contribution that potentially transitory windfall CT receipts have made to total tax revenue in 2025 is estimated to be broadly in line with the contribution made by residential property related taxes at their peak in 2006 [Figure 5].

[4] The Central Bank's methodology for estimating windfall CT is discussed in more detail in 'Managing the public finances in a full employment economy', Central Bank of Ireland Signed Article, Quarterly Bulletin 2, June 2023.

CT is increasingly dominating the revenue base

Figure 5
Share of Exchequer tax revenue (%)



Source: Department of Finance, Central Bank or Ireland

Notes: The chart reflects tax revenue on an Exchequer basis. Residential property related tax data is taken from 'Quantifying Revenue Windfalls from the Irish Housing Market', Addison-Smyth and McQuinn, November 2009.

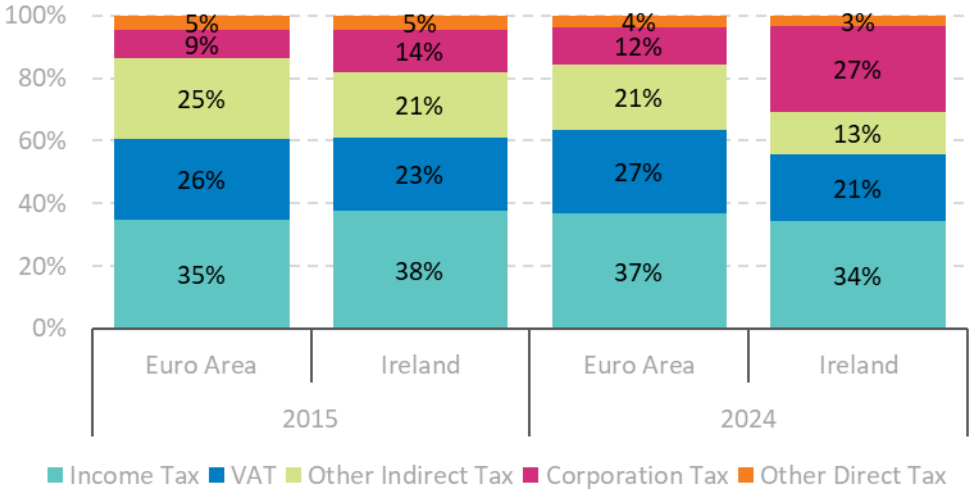
Concerns also reflect the exceptionally narrow nature of the CT tax base. Data from Revenue shows that 10 companies were responsible for 56 per cent of all CT receipts in 2025, up from 41 per cent in 2015. Other estimates suggest the base is even narrower with just three corporate groups responsible for 46 per cent of all CT receipts in 2024 (IFAC, 2026). The narrowness also relates to the sectors that generate Irish CT revenue. Two sectors – Information and Communication Technology (ICT) and Pharmaceuticals – were responsible for at least half of all CT revenue in 2025, with some estimates suggesting this figure could be higher (Cronin, 2025). In addition, foreign-owned MNEs in these sectors account for a large share of employment, meaning they are also an important driver of revenue from income tax, USC and PRSI (Boyd et al, 2025). A negative shock affecting MNE activity and employment in Ireland would therefore result in lower tax revenue across all key tax headings.

Comparison to the euro area further highlights the dominance of CT in the Irish tax base. Between 2015 and 2024, the tax composition for the euro areas as a whole remained relatively stable, with small increases in the share of income, VAT and CT in total receipts [Figure 6]. In contrast, over the same period, Ireland experienced a more than doubling in the share of CT in total tax receipts and in turn, a sizeable reduction in the importance of other taxes, notably indirect taxes. While these shifts in tax composition for Ireland are

driven in the main by the exceptional growth in CT, discretionary tax policy has narrowed the tax base in some areas.

Exceptional CT growth has significantly changed the tax composition in Ireland, compared to the euro area

Figure 6
Share of General Government total tax receipts (%)



Source: Eurostat and Central Bank of Ireland calculations

Notes: The chart reflects tax receipts on a General Government basis. Net social insurance contributions and capital transfers from general government to relevant sectors (representing taxes and social contributions assessed but unlikely to be collected) are excluded. Euro-area estimates are calculated as the aggregation of individual country data. Due to missing data, in two (three) countries, taxes on households (corporations) holdin gains were also included in income (corporation) tax. 'Other indirect tax' is the residual of taxes on products and imports minus VAT type taxes. It includes all non-VAT type taxes on production and imports, such as import taxes, excise duty, stamps and taxes on insurance premiums and financial transactions. 'Other direct tax' include capital taxes and other current taxes such as licence payments.

These measures include for example, reductions in USC rates particularly over 2015-2019, which have contributed to narrowing an already highly concentrated income tax base. Data from Revenue shows that the top 10 per cent of earners were responsible for around 60 per cent of total income tax and USC payments last year. The introduction of the Local Property Tax in 2013 represented an important step in broadening the tax base but the yield from the tax has not increased in line with general housing market activity. The tax is expected to raise €557mn in 2026, up only around €60mn (or 12 per cent) on the amount collected in 2014 (Revenue, 2026). This is despite a doubling in the residential property prices over the decade and Census data showing the housing stock increased by over 100,000 between 2016 and 2022. Revenue from recurrent property tax is, as a share of national income, significantly lower in Ireland than the OECD average (O'Brien, Staunton and Wosser, 2022).

Ireland also remains one of the most extensive users of reduced and exempt VAT rates in Europe (Commission on Taxation & Welfare, 2022).[5] In recent years, further VAT reductions have been deployed as temporary measures, later extended. For example, VAT on residential gas and electric was reduced in 2022 and subsequently extended to end 2030. From July this year, the VAT in the hospitality sector is being permanently reduced at an estimated annual full-year cost of €681mn. These actions run counter to establishing a broad tax base that builds resilience in the public finances.

Box A: Risks related to US Worldwide Taxation

By Radek Sauer

Higher estimated excess CT in recent years has coincided with rising Intellectual Property (IP) imports (Figure A). This highlights the role that the onshoring of IP by foreign – particularly US – MNEs has played in generating CT receipts. However, receipts from these activities are exposed to changes in the global economy, the activities of a small number of companies and changes in US tax policy. The US CT regime has not experienced structural changes under the current Trump administration. Changes that were enacted last year as part of the One Big Beautiful Bill Act represent primarily adjustments to the existing system. The US continues to rely on a hybrid CT regime, which consists of a territorial and a worldwide component. The worldwide component effectively ensures a minimum taxation of intangible income that US multinationals declare in their overseas affiliates. In 2026, this minimum tax—known under the abbreviations GILTI or NCTI—increased from 10.5 to 12.6 per cent.[6] Because the Irish CT for large firms stands at 15 per cent and so exceeds the new minimum of 12.6 per cent, Irish affiliates of US MNEs remain unaffected by the US worldwide taxation.

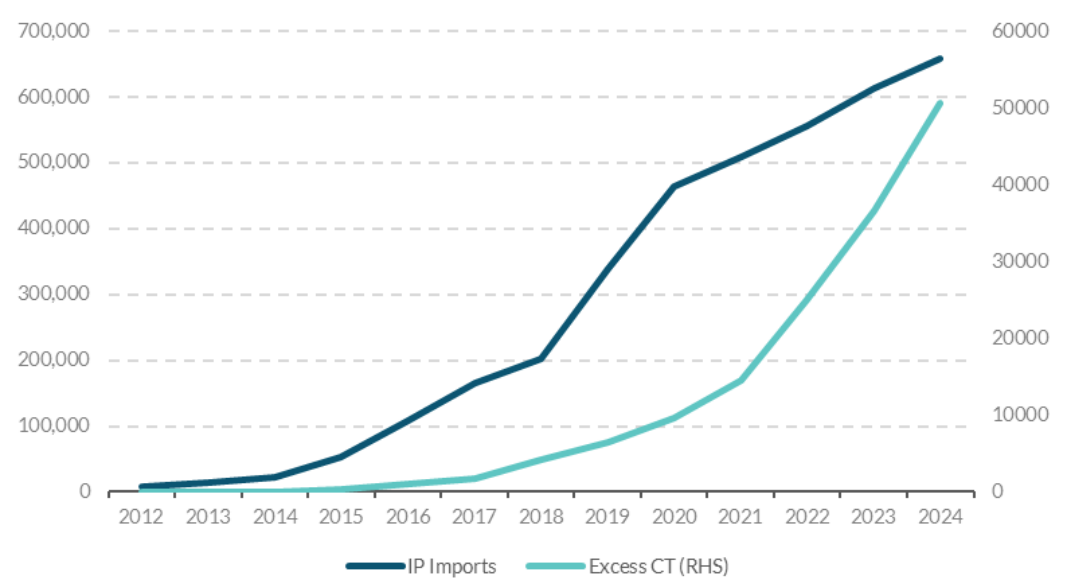
However, the worldwide component of the US tax system could potentially undergo further reforms in the future and could possibly become binding in Ireland. To assess how a stricter US worldwide tax could affect the Irish economy, we carry out the following simulation. We simulate a scenario in which the US increases its minimum tax on overseas intangible income to 17.5 per cent. Under such a scenario, Irish affiliates of US multinationals

[5] As a result, relative to other OECD countries, Ireland has a low VAT-to-revenue ratio. A report from the OECD (2024) reports the ratio as 0.51 in 2022, indicating the government was collecting around half of the VAT revenue it could collect under a hypothetical full application of the standard rate to all goods and services. The OECD average for that same year was 0.58.
[6] The acronym GILTI stands for Global Intangible Low-Taxed Income; NCTI is an abbreviation of Net Controlled foreign corporation Tested Income. The effective rate may vary when relevant income exclusions are taken into account.

would be still subject to the Irish CT of 15 per cent. Additionally, they could potentially be required to pay a US top-up tax of 2.5 per cent on their intangible income. The simulation of the scenario is conducted by means of a structural macroeconomic model, in which multinational firms engage in tangible as well as intangible foreign direct investment (Sauer, 2026).

Increased excess CT receipts have coincided with rising intellectual property imports

Figure A
€ millions



Source: CSO and Central Bank of Ireland calculations

Note: The Figure shows cumulative IP imports and excess CT receipts from 2012. Excess CT is an estimate of corporation tax receipts that are disconnected from activity in the Irish economy.

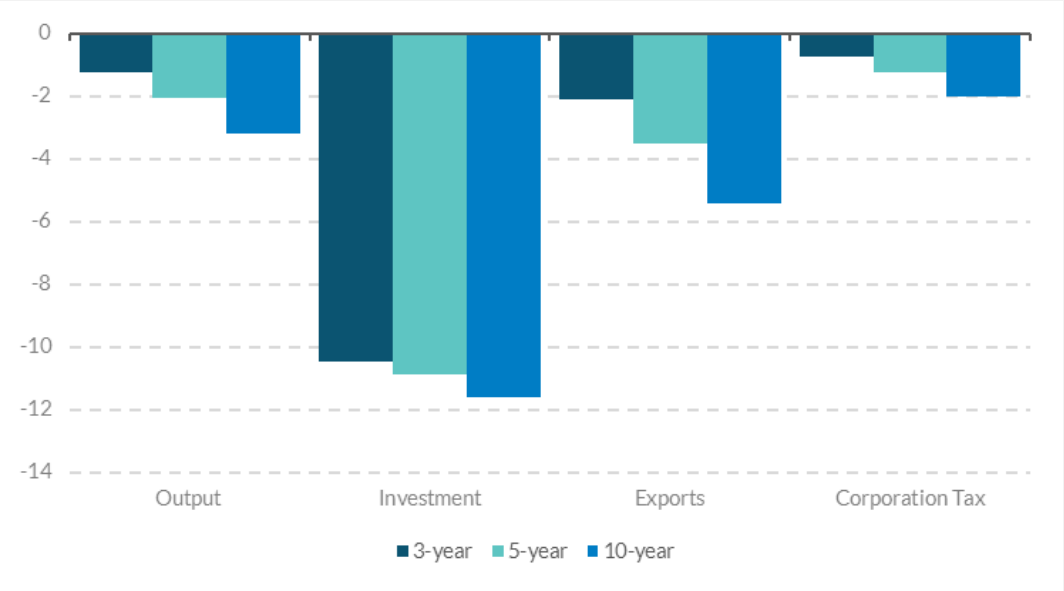
Simulation results suggest that stricter US worldwide taxation has the potential to have significant negative effects on the Irish economy (Figure B). A higher US tax on overseas intangible income would weaken the willingness of US-parented multinationals to place intangible assets in Ireland. Instead, US multinationals would keep newly developed intangibles at the headquarters, where the vast majority of their research and development takes place. The simulation results suggest that Ireland would therefore face an immediate drop in intellectual property imports and a corresponding reduction in investment.

Existing intangible assets that US multinationals previously located in Irish affiliates are assumed to be less affected as these are subject to exit taxes that could discourage such cross-border relocations of intangible capital. The combination of depreciation and lower investment would inevitably lead

to a gradual decline in the stock of intangible capital. The declining stock of intangibles would be accompanied by decreasing exports of royalty services, which would in turn depress GDP.

Response of the Irish Economy to Higher US Worldwide Taxation

Figure B
Per cent deviations from baseline scenario (%)



Source: Central Bank of Ireland calculations

Note: The simulation assumes an increase in the GILTI/NCTI tax rate to 17.5 per cent. Variables are presented as 3-year, 5-year and 10-year deviations from the baseline scenario.

Moreover, the weak export of royalty services would shrink the aggregate corporate-tax base. The Irish Exchequer would consequently need to cope with a decline in CT receipts.[7] Finally, the labour market would stay widely unaffected by the lower intangible investment. This is due to the fact that imported intangible assets exhibit only loose links to the local Irish economy.

A number of caveats should be borne in mind when interpreting the results in this Box. The Box considers a change in US tax affecting intangible assets with little assumed spillover to physical FDI in Ireland. If the latter occurred, the effects on the economy would be more severe and broad based than reported in this exercise, with lower employment and tax revenue across a range of headings. Furthermore, the precise response of individual MNEs to a change in the relative attractiveness of the Irish tax system is uncertain. This would depend on a range of factors including how MNEs would reorganise their reported activities in different jurisdictions. As a result, the estimated magnitude of the effects in Figure B should be treated with

[7] In the model simulation, the technical assumption is made that losses in corporation tax are offset by issuance of new government debt.

caution. Lastly, Ireland's attractiveness to intangible and other FDI relates not only to its taxation regime but to other factors such as EU membership; the skills composition of the workforce; and robust legal system which ensures strong protection of intellectual property.

General government balance

When revenue linked to the Apple state aid case is excluded, the general government budget (GGB) surplus increased from 2.8 per cent of GNI* in 2024 to an estimated 3.3 per cent in 2025. Looking ahead, the Government now projects declining surpluses out to 2029 based on the APR 2026 projections.[8] The declining headline surplus arises because general government expenditure, which incorporates all components of Government (including for example local government, the Social Insurance Fund and non-commercial semi-state bodies), is forecast to grow at an annual average rate of 6.4 per cent over the medium term in the APR. This is not only higher than projected average revenue growth (5.4 per cent) but also projected nominal GNI* growth and implies a stimulus to the economy at a time when it is expected to be performing strongly.

Excluding estimates of windfall CT and temporary revenue linked to the Apple state aid case, the 'underlying' general government balance has remained in deficit in every year since the financial crisis, highlighting the key role that exceptional growth in CT has played in supporting the recovery of the public finances and financing strong expenditure growth. The underlying general government deficit is expected to deteriorate in the coming years as headline budget surpluses decline and estimated windfall CT receipts continue to grow [Figure 7a].

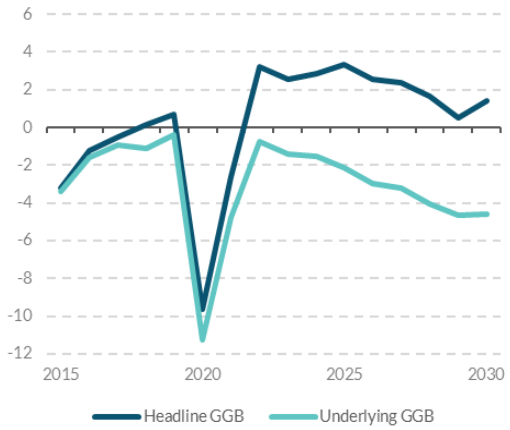
This means that the proportion of windfall CT being saved will decline over the medium term. The APR estimates that 61 per cent of windfall CT receipts were saved last year, either transferred directly to the States's medium term savings funds – the Future Ireland Fund (FIF) and the Infrastructure, Climate and Nature Fund (ICNF) – or by the running of a budget surplus. By 2029, however,

[8] The improvement in the GGB in 2030, which goes against the trend of preceding years, is driven by a strong increase in revenue growth and a moderation in expenditure growth, in particular capital spending. Revenue growth is forecast to increase from an average of 5.1 per cent between 2026 and 2029 to 6.7 per cent in 2030. This primarily reflects a sharp increase in direct tax revenue, with CT receipts forecast to increase by almost €6bn in 2030. Expenditure growth is forecast to moderate from an average of 6.9 per cent between 2026 and 2029 to 4.4 per cent in 2030. This is driven by weaker growth across most expenditure components, with notable moderations in government investment and other current transfers.

only 10 per cent windfall receipts are expected to be saved, a figure that increases to 25 per cent in 2030 – still well below recent levels [Figure 7b].

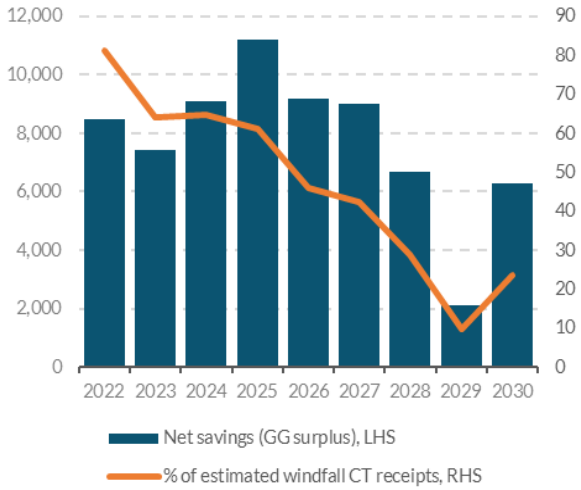
The government's headline budget surplus (net savings) will fall as a share of windfall CT receipts

Headline and underlying GGB CT
Figure 7a
Per cent of GNI* (%)



Per cent (%)

Budget surplus as share of windfall
Figure 7b
€m



Source: CSO, Annual Progress Report

Notes: Underlying GGB excludes Central Bank estimates of excess corporation tax receipts and receipts from Apple State aid case. Figure 6b excludes receipts from Apple state aid case in 2024.

If the proportion of windfall CT being saved remained at its 2025 level, this would imply additional savings of €35bn by 2030. The lower projected actual savings relative to this figure appears to mainly reflect the Government's planned increases in current spending.[9] The APR notes that €36.6bn will be transferred to the FIF and ICNF between 2026 and 2030, just one-third of projected windfall CT receipts over the period.[10] Moreover, contributions to the funds are expected to exceed the size of the annual headline budget

[9] If the Government were to continue to save 61 per cent of these receipts for the remainder of the decade, it is estimated that surpluses would be – in cumulative terms - €35.5bn higher by 2030 than forecast in the APR (in 2030, for example, when windfall CT receipts are forecast to be €26.7bn, the surplus would be €16.3bn rather than the €6.3bn currently projected). Lower savings reflect a government decision to use additional windfall receipts to finance higher expenditure, discretionary tax cuts or some combination of the two. The APR has forecast that current expenditure will increase by €38.6bn between 2025 and 2030, while capital spending will increase by a cumulative €10.1bn over this period. This suggests that the additional windfall receipts utilised by government in the coming years will primarily be used to finance additional current rather than capital spending.

[10] The Social Insurance Fund has accumulated large surpluses in recent years, holding assets of €13.5bn at end-2025 (NTMA, 2026). The Government is forecasting further large surpluses in the coming years which, in annual terms, are expected to increase from €4.6 billion in 2025 to €10 billion in 2030.

surplus from 2028, meaning that Government borrowing will be required to fund the transfers to the funds from that year.

4. Scenarios for Medium-Term Expenditure Growth

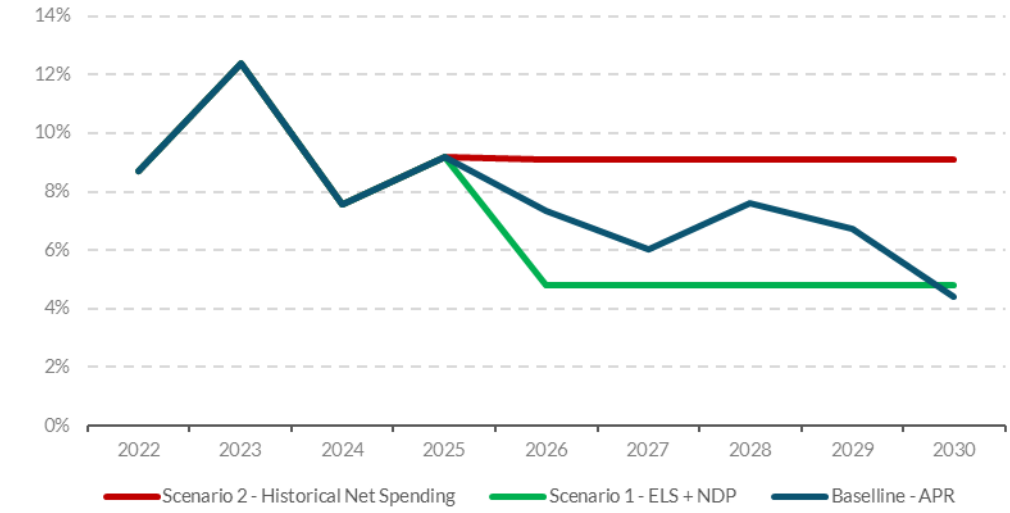
There is a clear risk that actual government spending growth exceeds the projections set out in the APR 2026. This reflects the established pattern of overspends of recent years and the lack of an effective rule to anchor fiscal policy. We estimate that net core general government expenditure increased by an average of 9 per cent per annum in the five years to 2025, well above both the pace of growth allowable by the expenditure rule of the time and the planned spending increase in the coming years in current government plans. This figure excludes temporary expenditure linked to the Covid-19 pandemic and cost of living crisis and so represents the permanent change to the expenditure base that has occurred.

Government expenditure scenarios

To assess the impact of higher and lower spending – relative to the APR baseline – on the GGB and wider economy, we run two scenarios using the Central Bank's semi-structural model. In the first scenario, government spending grows in line with the estimated pace required to maintain ELS and deliver public investment in the NDP, as outlined in section 2 [Figure 8]. This assesses the impact of increasing spending at a slower pace than currently planned, while still ensuring public services are maintained and necessary capital investment continues. In the second scenario government spending continues to increase by its recent estimated net annual average rate of 9 per cent for the remainder of the decade, rather than the 6.4 per cent annual average in the APR. This scenario captures the risks associated with expenditure continuing to exceed initial forecasts in the coming years.

Continued overruns in line with recent outturns would see spending growth increase well above current government projections

Figure 8
Per cent (%)



Source: CSO and Central Bank of Ireland

In the first scenario, where government expenditure grows at just below 5 per cent per annum, the lower spending path implies a reduction in economic activity relative to the APR baseline. Total output (gross value added) in this scenario would be 2 per cent lower in 2030 when compared to the baseline [Figure 9a]. The reduction in demand would result in looser labour market conditions and dampen wage pressures and prices. As a result, inflation would be lower by around 0.1 to 0.2 percentage points per annum out to 2030 [Figure 9b]. While overall output is lower in this scenario, the traded sector, which is a key driver of productivity growth and long-term economic growth for the Irish economy, would benefit from a gain in competitiveness owing to lower labour costs and increase its level of output [Figure 9c].

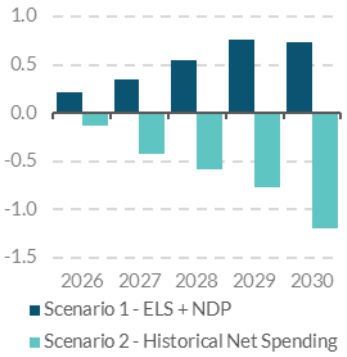
This more balanced macroeconomic situation is accompanied by an improvement in the public finances with the headline GG surplus 0.7 percentage points of GNI* higher by 2030 [Figure 9d]. As a result, the headline budget surplus would improve to 2.2 per cent of GNI* compared with 1.4 per cent in the APR 2026 baseline [Figure 10a]. The underlying GGB, which excludes estimates of windfall CT, would record a deficit of 3.9 per cent of GNI* in 2030 compared with 4.6 per cent in the government's current baseline [Figure 10b].

Lower expenditure growth could reduce inflation and crowd in traded sector activity

Total Output

Figure 9a

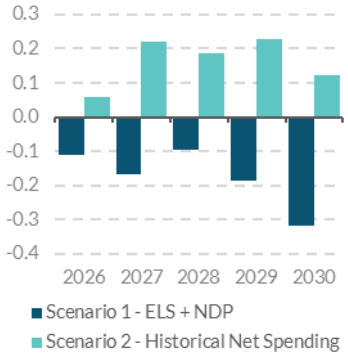
Per cent deviation from baseline (%)



Inflation

Figure 9b

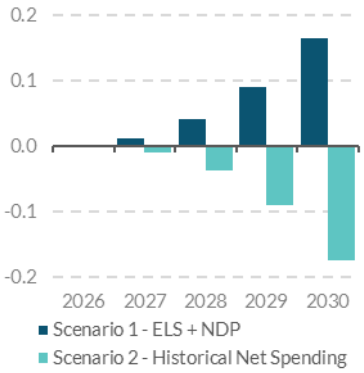
Percentage point deviation from baselir (pp)



Traded Sector Output

Figure 9c

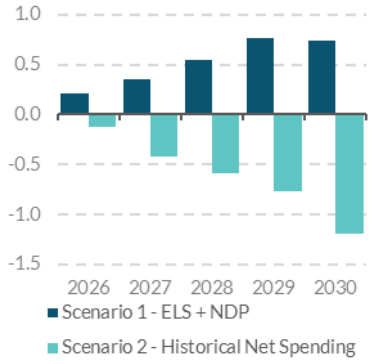
Per cent deviation from baseline (%)



GG Balance (% of GNI*)

Figure 9d

Percentage point deviation from baselir (pp)

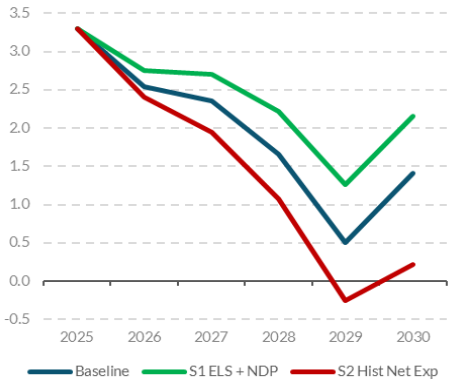


Source: CSO and Central Bank of Ireland

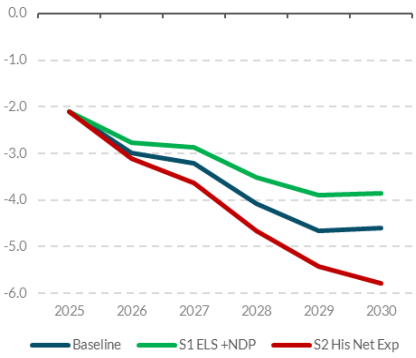
In the second scenario, where expenditure grows above the APR baseline, the economy would be stimulated further with total output (gross value added) increasing by 3.5 per cent by 2030. This additional activity would be driven by the less productive non-traded sector, increase inflation by over 0.2 percentage points per annum, and gradually reduce traded sector output due to a deterioration in cost competitiveness. By 2030, the headline GGB ratio would be 1.2 percentage points lower and would move from a surplus in the baseline to a broadly balanced position.

Continued expenditure overruns would deplete fiscal buffers

General Government Balance
Figure 10a
Per cent of GNI* (%)



Underlying General Government Balance
Figure 10b
Per cent of GNI* (%)



Source: CSO and Central Bank of Ireland

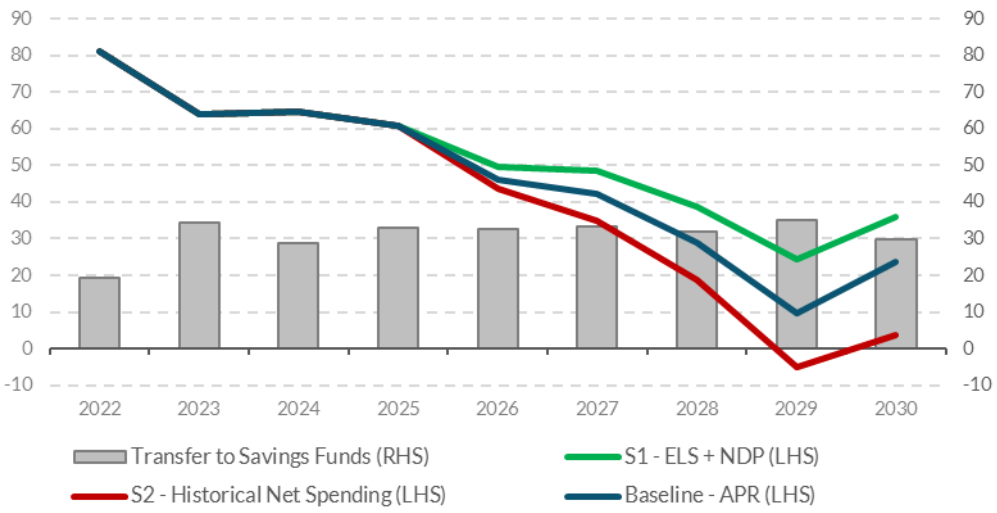
Notes: S1 = Scenario 1; S2 = Scenario 2; underlying GGB excludes estimates of windfall corporation tax receipts.

This would result in a smaller proportion of windfall CT being saved and reduce fiscal buffers to respond to future shocks [Figure 11]. In both the baseline and this higher spending scenario, the government would be borrowing to ensure agreed contributions to the State's medium-term savings funds are fulfilled. The underlying GG deficit would deteriorate to almost 6 per cent of GNI* in 2030 under this scenario. The loss of all excess CT by 2030 could be considered a somewhat extreme outcome. In a situation where half – rather than all – of the estimated excess CT was lost, the GG deficit would be closer to 3 per cent of GNI* in 2030.

Higher expenditure growth, above the APR baseline, would result in a smaller proportion of windfall CT being saved

Figure 11
Share of windfall saved (%)
(%)

Share of windfall to funds



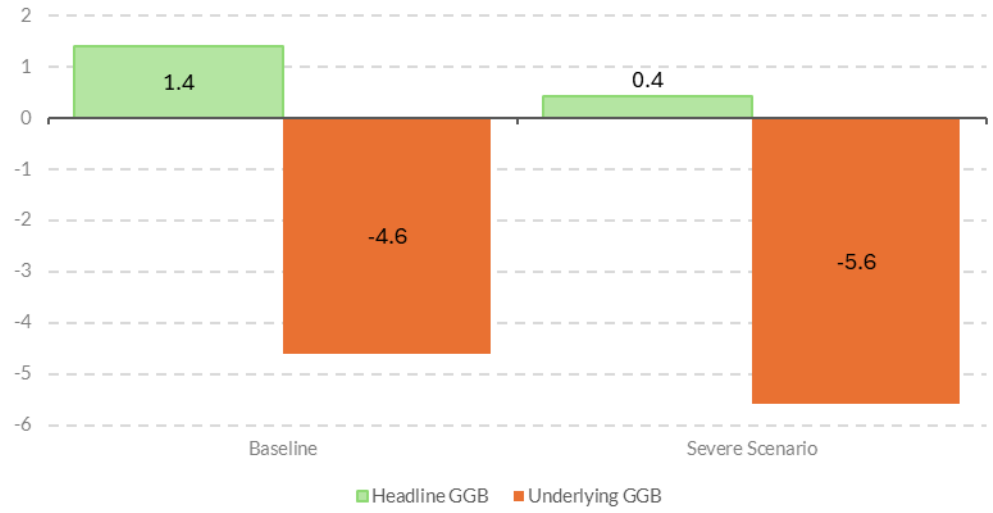
Source: CSO, Department of Finance, Central Bank of Ireland

The public finances in a *severe* economic scenario

Quarterly Bulletin 2 includes a set of alternative scenarios which illustrate the potential impact of prolonged trade disruption and higher energy prices associated with the Middle East conflict on economic growth and inflation in Ireland. We use the Central Bank's semi-structural model to assess the potential impact of the *severe* scenario outlined in *Quarterly Bulletin 2* on the public finances, relative to the baseline forecasts in *APR 2026*. Under the *severe* scenario the headline GG surplus would be 1 percentage point lower at just 0.4 per cent in 2030 [Figure 12], while the underlying balance would deteriorate to 5.6 per cent.

A severe scenario would see a further deterioration in the public finances

Headline and underlying GGB under Central Bank's baseline and severe scenarios
Figure 12
Per cent of GNI* (%)



Source: CSO and Central Bank of Ireland

Notes: For more information on the severe scenario, see Central Bank of Ireland Quarterly Bulletin 2026

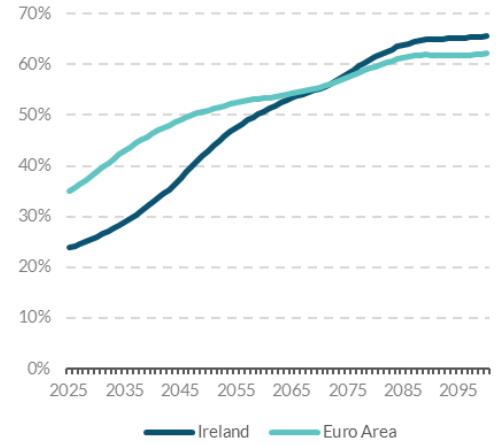
Preparing for the impact of long-term spending pressures

Baseline projections show a declining headline budget surplus and a persistent underlying deficit out to 2030 and, as shown above, the budgetary outlook could be less favourable than this in the presence of weaker economic growth or a decline in corporation tax. The risks associated with this profile for the public finances will grow as Ireland is expected to undergo one of the largest demographic shifts in Europe. Currently, there are around four citizens aged 15-64 years for every one aged 65 or over (Figure 13a). By 2045 however, this ratio is expected to reduce to less than 3:1, according to Eurostat projections. This is driven by a substantial expected increase of over 630,000 in the older aged population, from 16 per cent of the population today to 24 per cent in

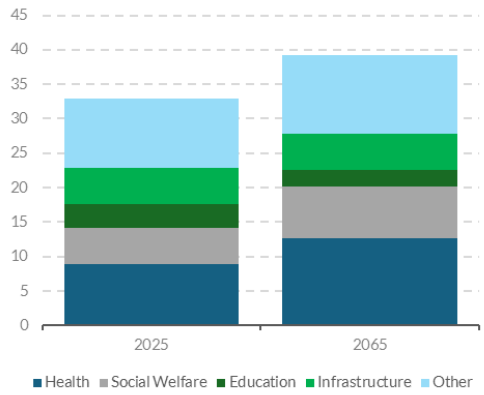
2045. Given this trajectory, Ireland's old age-dependency ratio (OADR) is expected to broadly match the euro area equivalent by around the mid-2060s, before overtaking in the early 2070s.

An ageing population will lead to an increase in government expenditure

OADR
Figure 13a
Per cent (%)



Forecast government expenditure
Figure 13b
Per cent of GNI* (%)



Source: Eurostat and Central Bank of Ireland

Notes: Old age dependency ratio (OADR) is calculated as the proportion of the population aged 65 divided by the proportion of the population aged 15 to 64.

These changes in the demographic structure have major implications for the public finances, as clearly outlined in recent analysis by the Department of Finance. Age-related spending on areas such as pensions, healthcare and long-term care will record large increases, with a smaller proportion of the population to finance them. Overall Exchequer expenditure is forecast to increase by over 6 percentage points of GNI* – from 33 per cent of GNI* in 2025 to 39.2 per cent in 2065 [Figure 13b].

By 2065, age-related expenditure (healthcare, long-term care and pensions) will be equivalent to 18 per cent of GNI*, up from 12 per cent in 2025, and just 7 per cent in 1995 with large increases also needed in other areas such as climate expenditure. It is worth noting that ageing will bring some benefits which could help partially offset the costs of an older population. In particular, increases in labour force participation have been observed for older workers in recent years reflecting improved health outcomes and higher life expectancy. Extended working lives at career-high earnings can boost tax revenues and there is some evidence that extended labour market participation by older workers can lift productivity.[11]

[11] See https://oecdecoscope.blog/2023/01/24/population-ageing-and-government-revenue-it-is-not-all-bad-news/

Nevertheless, in the absence of offsetting policy measures (reductions in spending elsewhere or higher tax revenue), the increase in spending from ageing could result in the headline budget position moving into deficit from the early 2030s. Based on the Department's analysis, the projected deficit would rise over time to almost 8 per cent of GNI* by 2065 with the debt-to-GNI* ratio increasing to just under 150 per cent of GNI*. This scenario assumes that excess CT is phased out gradually from 2030 to 2040 so that the share of overall CT in tax revenue returns to its historical (1995 to 2017) average.

Even in a more optimistic scenario where windfall CT remains unchanged from 2030 onwards, the public finances would still move into deficit in the 2050s and the debt ratio would begin to rise. These estimates assume that payments into the FIF continue up to 2041 and that from that point onwards, 3 per cent of the fund's value is withdrawn to cover public expenditure. Even with this assumption, the Department's central scenario shows the public finances moving into a deficit position from the early 2030s. While the existence of the FIF is welcome, this analysis indicates the need for additional revenue-raising measures over the coming years and / or fiscal restraint on expenditures, so that the public finances can be maintained on a sustainable footing while age-related pressures build.

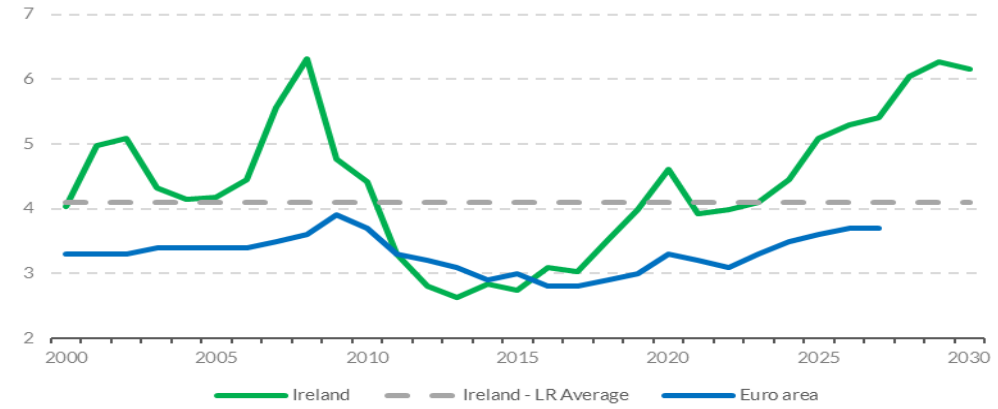
5. Public Investment

A key development that will affect the public finances and the economy over the coming years is the scale of planned increases in public capital expenditure. In general government terms, growth in gross fixed capital formation is expected to average 11.6 per cent per annum in the five years to 2030. This would see gross fixed capital formation surpass 6 per cent of GNI* from 2028 onwards, well ahead of its long run average and current euro area levels [Figure 14].[12] Analysis by IFAC finds that Ireland's capital stock is currently around 25 per cent lower than other high-income European countries, with four key areas of deficit: housing, health, transport and electricity (see IFAC, 2024).

[12] Capital transfers increased significantly in 2025 and are expected to remain at an elevated level for the remainder of the decade reflecting transfers to bodies such as Uisce Eireann and Eirgrid. When capital transfers are also included, investment spending surpasses 7 per cent of GNI* from 2028 onwards.

Public investment is expected to rise sharply in Ireland

Government gross fixed capital formation
Figure 14
Per cent of GNI* (%)



Source: CSO, Department of Finance and Central Bank of Ireland calculations

Notes: Long run average defined over the period 2000-2025. Expected growth over 2026 to 2030 is based on the APR.

Increasing public investment: challenges and opportunities

Given the extent of the known infrastructure deficits in key areas, increasing public capital investment is an important medium-term policy goal. Ideally, the delivery of higher capital spending would be conducted in an efficient and timely manner to ensure the economy and society benefit fully. While the planned rebalancing of expenditure towards capital investment is necessary and warranted, the Government will face several challenges in maximising the overall impact of this additional capital expenditure on the economy.

The envisaged acceleration in public investment arises in a context of sharply rising construction costs as well as capacity pressures in the domestic economy. Wholesale prices for building and construction materials have risen sharply since 2022, with some subcomponents of the index, such as concrete and copper pipes, increasing by over 7 per cent over the last year. At the same time, labour market conditions remain tight, particularly in the construction sector, which recorded an increase in average hourly earnings of over 18 per cent between Q1 2023 and Q1 2026.

Against this backdrop, an investment surge that is not sequenced carefully could exacerbate overheating pressures in an economy with binding absorptive capacity constraints. This, together with notable cost overruns on a number of large-scale public projects, places increasing importance on selecting projects which have the strongest impact on raising the economy's productive capacity.

Moreover, an important motivation for the public provision of large infrastructure projects is the productivity effects they can generate for the wider economy, which can 'crowd in' or stimulate complementary private sector investment. The need to prioritise investment expenditure which could raise the aggregate productivity of the economy is particularly stark given projections show the contribution of total factor productivity to potential growth declining from its long-run historical average (1971 to 2023) of 1.2 percentage points to an estimated 0.6 percentage points in the decade from 2030 to 2040.[13]

To explore the macroeconomic implications of these challenges in more detail, we use the Central Bank's macroeconomic models of the Irish economy to examine the impact of investment under a range of assumed conditions. We outline the implications for the stock of public capital - and overall output - if the price of relevant goods increases while the government is ramping up investment. We then highlight how the composition of investment, along with the domestic and international macroeconomic environment, can influence the ultimate impact on the economy of the additional government spending. It is important to note, however, that the discussion in this section focuses on the fiscal and macroeconomic impact of different types of public investment, and thus necessarily abstracts from other societal or non-pecuniary benefits of these investments.

The investment stimulus

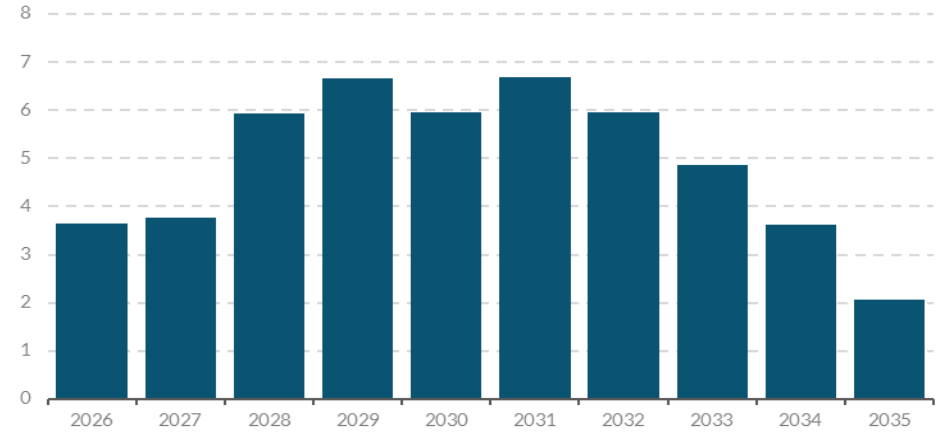
To calibrate the size of the investment stimulus, we compare the planned increase in government investment between two vintages of National Development Plans (2021 and 2025) for the horizon from 2026 to 2035. The APR (2026) presents the path of public gross fixed capital formation for each year over the period 2026 to 2030, and is therefore consistent with revisions to planned capital expenditure published since the latest update of the NDP published in July 2025. We extend this path to 2035 by interpolating the difference between this amount and the total investment that is planned over the next ten years under the National Development Plan 2026-35.[14] This yields total planned investment of €275 billion from 2026-2035, an increase of around €50 billion on the equivalent figure (€225 billion) published in the original iteration of the current NDP in 2021.

[13] See Conefrey *et al.* (2024) and Department of Finance (2025).
[14] *National Development Plan 2026-2035*, Department of Housing, Local Government and Heritage, November 2025.

Figure 15 presents the annual path of additional public investment over the next decade that constitutes the investment 'shock' that is simulated in the macroeconomic models. The path is hump-shaped, with the investment stimulus peaking towards the end of this decade and beginning of the next. Since this additional expenditure reflects the current NDP path and is already included in baseline forecasts for the public finances, the extra investment is assumed not to impact the general government balance or debt except through the operation of the automatic stabilisers in the simulations.

The revised NDP announced an additional €50 billion of investment, most of which relates to the end of this decade and beginning of next

Figure 15
€, billions



Source: DoF (2026), DoHLGH (2021) and Central Bank of Ireland calculations

Notes: The bars up to 2030 reflect the difference in investment announced in the original 2021 NDP and the subsequently revised 2025 NDP, as presented in the APR 2026. The 2031 to 2035 bars were generated by interpolating based on the total investment that is planned over the next ten years under the revised NDP.

Impact of government investment with and without price increases

As a net importer of energy, construction materials and certain capital goods, Ireland is exposed to fluctuations in international prices which can significantly raise the cost of individual projects. In addition, cost overruns are a frequent occurrence when public spending is concerned. These can be caused by uncertainty when planning the outlays, delays between planning and implementation, by suppliers responding to increased demand by increasing prices by more than they would otherwise, or by poor expenditure control. Regardless of the underlying cause, increases in prices result in a lower increase in public capital in real terms, and correspondingly lower benefits to the economy.

To illustrate these effects, we simulate the impact of the additional increase in government investment shown in Figure 16a-f, under two price scenarios. In

the first scenario, there is no additional increase in the price of goods purchased by the government (beyond the general-equilibrium effects), while in the second scenario the price of goods purchased by the government increases.[15]

In both scenarios, there are beneficial effects on output, private consumption and – after a delay – on private investment.[16] However, when the price of goods purchased by the government increase disproportionally, this erodes the real amount of new public capital that can be obtained for the given amount of nominal investment spending. This means that the beneficial supply-side effect is lower, resulting in a lower trajectory of output, private consumption and private investment.[17] These results highlight the importance of rigorous expenditure management and careful, continuous appraisal of public capital projects to ensure value for money from higher nominal government spending.

The composition of government spending: the productivity spillover channel

As well as careful management of price pressures, the composition of public investment is also an important determinant of its long-run economic impact. Here, we consider two scenarios that illustrate how the macro-fiscal impact of the public investment stimulus, such as that shown in Figure 15, depends on its composition.

In the first scenario, government investment has typical Keynesian effects in the short run by stimulating aggregate demand and, although raising the public capital stock over time, does not affect the productivity of the private sector. The second scenario, in contrast, assumes that government investment rises by the same amount as in the first scenario, but that part of this investment also raises the productivity of the private sector.

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[15] The increase in prices has been simulated by increasing markups in the sectors producing goods purchased by the government. The increase lasts as long as government investment remains elevated. The calibration of the price increase is illustrative, but consistent with the observed increase in the prices of concrete and copper pipes by about 7 per cent mentioned above. In particular, it is not meant to proxy extreme price increases in outlier cases such as those analysed in IFAC (2019). The price increase is assumed to have no effect on the nominal quantity of public investment.

[16] The reason for the delayed increase on private investment is that the full effect of public capital on productivity and therefore supply and income comes only after public capital has increased sufficiently. Households expect this increase in future resources and increase consumption. But before resources increase sufficiently, they do not suffice to increase all (public investment, private consumption, and private investment), so private investment temporarily falls.

[17] The simulations were obtained using the Central Bank of Ireland version of the model in Clancy, Jacquinot, Lozej (2016), which is a model of Ireland as a small open economy, member of the monetary union, and embedded in a global model with a rich trade structure. For the purposes of this simulation, the model has been modified to include a sector that produces goods purchased by the government.

An increase in government investment has a positive impact on output, private consumption and private investment, but the impact is reduced after accounting for price effects

Public Investment

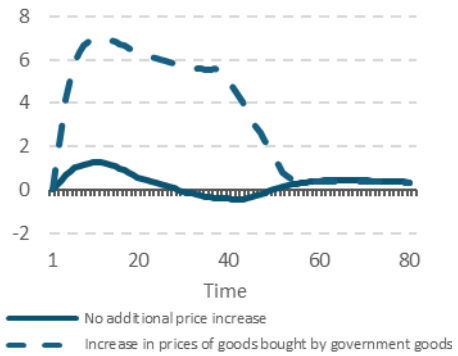
Figure 16a

Per cent of GNI* (%)

Price of public good

Figure 16b

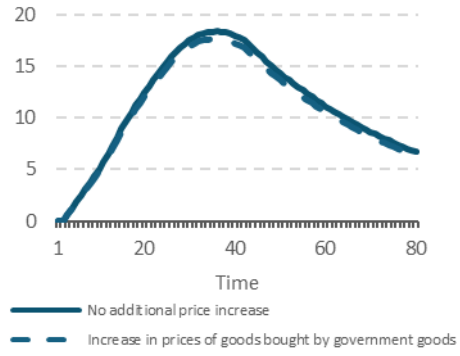
Per cent deviation from baseline (%)



Public capital

Figure 16c

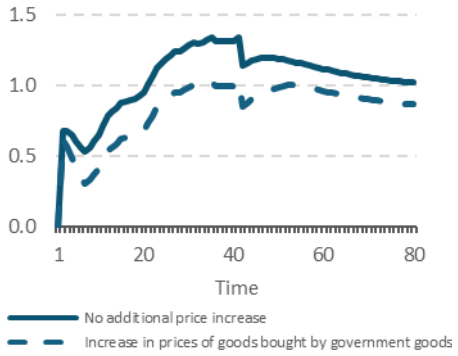
Per cent deviation from baseline (%)



Output

Figure 16d

Per cent deviation from baseline (%)



Private consumption

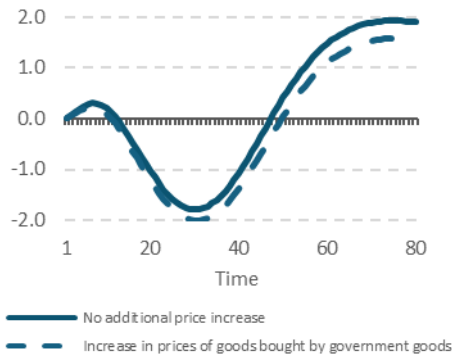
Figure 16e

Per cent deviation from baseline (%)

Private investment

Figure 16f

Per cent deviation from baseline (%)



Source: Central Bank of Ireland calculations

Notes: Public investment is shown as percent of GNI*, while all other variables are in per cent deviations from the baseline. The path of public investment corresponds to the difference in in public investment between the 2021 and 2025 NDPs for the period until 2035. The scenarios are run twice to reflect different price assumptions: one incorporates an additional increase in the price of goods purchased by the government and no increases in the other.

To capture this productivity-enhancing channel, we modify the Central Bank's semi-structural model to distinguish between the *actual* and *effective* public capital stock, with the latter generating the productivity spillover to the private sector. The effective stock differs from the actual (measured) stock to the extent that only a portion of public investment is assumed to deliver productivity-enhancing capital, with the remainder treated as consumption-type capital that supports welfare but does not directly augment the marginal productivity of factors in the private sector. This distinction recognises the evidence from previous research that different types of public investment raise productivity through different channels and over different horizons. Investment in network infrastructure, such as transport, energy, and digital networks, represents a direct input to private production, and is associated with comparatively large productivity spillovers that can occur relatively quickly. Investment in social infrastructure, such as health and education buildings, facilitates the accumulation of human capital, which is a key driver of long-run labour productivity. However, these effects materialise with a considerable lag and operate through wider channels beyond the direct effects of higher investment on the capital stock, such as a healthier or more highly-skilled workforce.

Our simulations therefore draw the distinction between investment whose productivity effects interact with the private sector within the scenario horizon, and investment whose returns accrue primarily though welfare and the long-term accumulation of human capital. They, accordingly, do not provide a ranking of the societal value of different types of investment, but rather can help guide the prioritisation and sequencing of planned capital expenditure.[18]

The scenario assumes that around half of the additional investment adds to the effective public capital stock. This is calculated based on the share of additional investment in the NDP allocated to areas such as housing, health and public buildings. Based on estimates from the international literature, we further assume the elasticity of output in each sector with respect to this effective

[18] Investment in the energy and digital infrastructure, along with research and development, generally yields the highest estimated productivity spillovers (Röller and Waverman, 2001; Calderón and Servén, 2010; Czernich et al., 2011), reflecting the network effects inherent in these capital projects, which generate strong complementarities with private capital. For example, the development of road networks can generate elasticities of 0.10 to 0.15 (Fernald, 1999), while expanding telecommunications and digital infrastructure, such as broadband networks, can generate elasticities of between 0.10 and 0.20 (Röller and Waverman, 2001; Czernich et al., 2011). Similar elasticities are also found for public research capital (Coe and Helpman, 1995; Frantzen, 2000). Investment in the expansion and upgrading of energy infrastructure is associated with elasticities of around 0.08 to 0.12 (Egert et al, 2009; Calderón and Servén, 2010).

capital stock is 0.08.[19] This modification of the model thus allows us to examine the macroeconomic impact of increasing public investment whilst accounting for whether that investment generates productivity spillovers.

During the period when the additional investment is being delivered, the level of total investment in the economy rises by over 7 per cent in the first five years of the shock in both cases (Figure 17a). However, the profile of investment begins to diverge in subsequent periods as the effective public capital stock raises the marginal product of private capital and thus, 'crowds in' additional private investment in the scenario with productivity spillovers. At the end of the scenario, total investment remains above baseline, while total investment in the scenario without productivity spillovers falls below baseline as the level of the private capital stock built up during the boom exceeds the level consistent with the long-run equilibrium path of the economy.

The productivity channel is most clearly exhibited in the path of traded-sector output (Figure 17d). In the scenario without productivity spillovers, traded-sector output falls in the short to medium term, as wages rise due to higher labour demand in the wider economy with a resulting deterioration in competitiveness relative to Ireland's trading partners. In the longer term, output rises marginally above baseline as wages fall following the ending of the investment stimulus, leading to a depreciation of the real exchange rate. When public investment generates productivity spillovers, these productivity effects can mitigate the loss in competitiveness (Figures 17b and 17c) in the short to medium term, and lead to a material improvement in the long term, as reflected in traded sector output rising significantly above baseline by the end of the scenario horizon.

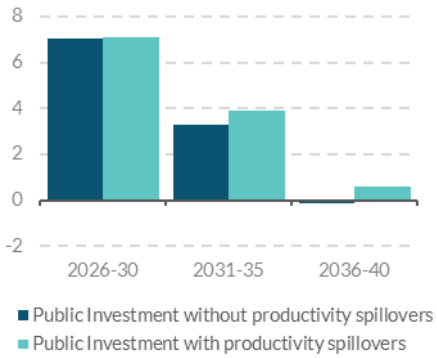
[19] This is based on Bom and Ligthart (2014) who conduct a meta-analysis of existing studies and find a long-run elasticity of around 0.08.

Accounting for productivity spillovers mitigates the loss in competitiveness associated with higher public investment

Total Investment

Figure 17a

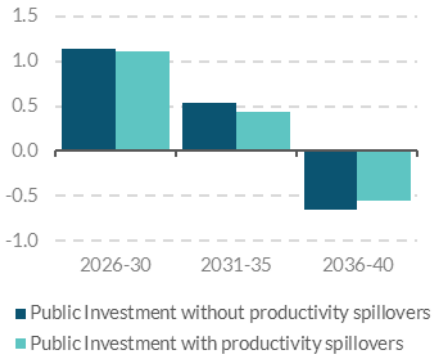
Per cent deviation from baseline (%)



Employment

Figure 17b

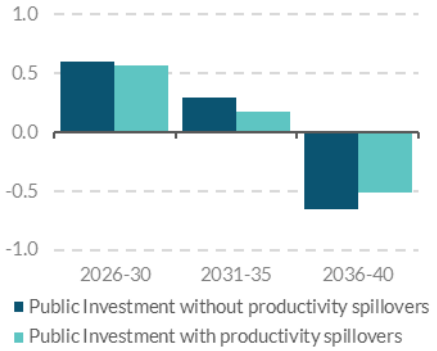
Per cent deviation from baseline (%)



Wages

Figure 17c

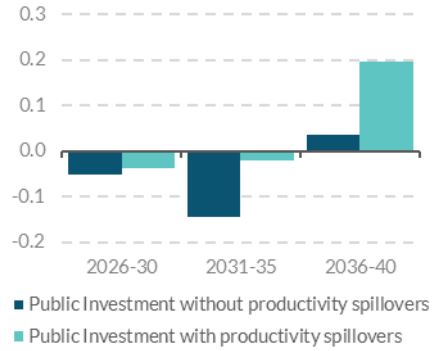
Per cent deviation from baseline (%)



Traded Sector Output

Figure 17d

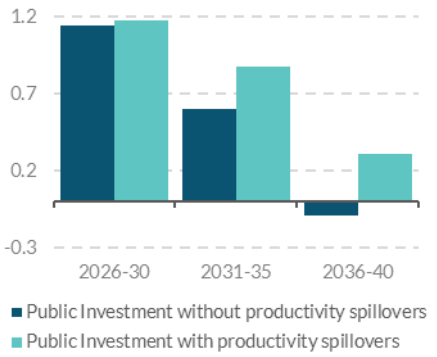
Per cent deviation from baseline (%)



Total Output

Figure 17e

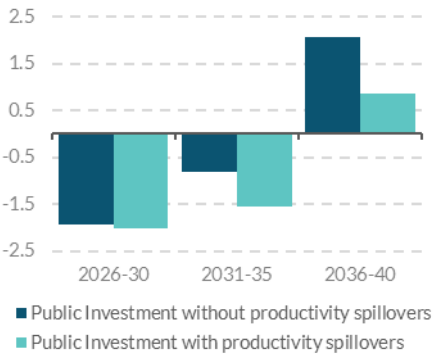
Per cent deviation from baseline (%)



Public Debt Ratio

Figure 17f

Per cent deviation from baseline (%)



Source: Central Bank of Ireland calculations

Notes: Scenario is estimated twice; to account for different assumptions around productivity spillovers.

The impact of the additional investment on total output highlights how the gains from productivity spillovers accrue over time (Figure 17e). The response of total output is similar in the short run in both scenarios. However, over the medium to long-term, the productivity gain mitigates the decline in activity from the tapering of the public investment shock by stimulating private investment and raising the output of the traded sector. With spillovers, the long-run output gain is around 0.3 per cent relative to baseline, while the long-run output loss in the case without spillovers is around 0.1 per cent.

The increase in productivity is an important channel through which cost pressures can be contained in normal times, but especially when capacity constraints are binding. External demand conditions are a key determinant of the performance of the MNE-dominated traded sector but Ireland's competitiveness relative to other countries is also important. For a given stimulus in a capacity constrained economy, raising the productivity of the private sector through 'productive' public investment can cushion the economy from a crowding out of private investment and a loss in competitiveness that reduces external demand for Irish goods.

Finally, the public debt ratio is lower in the productivity-spillover scenario than in the scenario without spillovers (Figure 17f). Higher economic activity increases tax revenue and reduces the cyclical component of expenditure, thereby boosting the budget balance. At the same time, higher nominal output also reduces the debt ratio mechanically through the denominator effect. Together, these effects mean that, in the long run, the productivity channel substantially attenuates the indirect debt impact of the additional investment.

6. Medium-Term expenditure management and the principles of an effective anchor

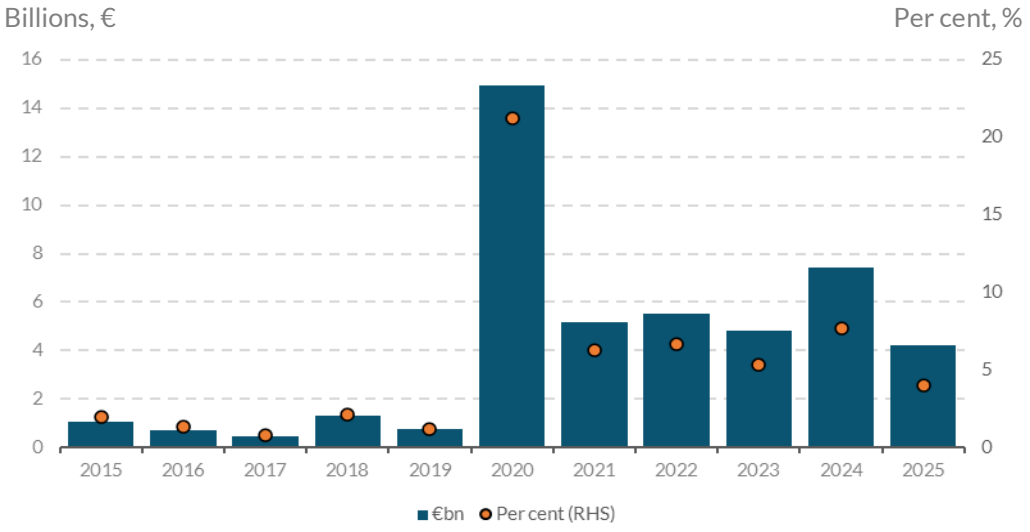
Fiscal rules are an important policy tool which help governments ensure that fiscal policy is supportive of both economic stability and fiscal sustainability. The European Union introduced revised fiscal rules for all Member States in April 2024. The reformed framework contains many beneficial elements that aim to address weaknesses in the previous rules. In particular, the new rules put a greater focus on medium-term fiscal sustainability with an expenditure rule as the single operational anchor. However, the effectiveness of the EU rules in an Irish context is limited. This is partly because the rules are defined using GDP, but also because they do not account for windfall corporation tax revenue (IFAC, 2024). As a result, the presence of an effective national fiscal anchor is particularly important in Ireland to help guide policy.

In December's Medium Term Fiscal Structural Plan (MTFSP) the Government outlined the core pillars of its fiscal strategy. These are (1) to more closely align day-to-day spending with economic and revenue growth; (2) significant investment in productivity and competitiveness-enhancing infrastructure; and (3) building fiscal buffers. The Government did not introduce an explicit fiscal or expenditure rule to support delivering on these core principles. Rather, it committed to achieving its planned medium term expenditure ceilings (which allow average expenditure growth of 6 per cent per annum in Exchequer terms and 6.7 per cent per annum for net primary general government terms).

Medium-term expenditure ceilings have been a key aspect of Irish and EU fiscal policy since the post-financial crisis years and but have not yet been effectively operationalised. This is evidenced by government expenditure targets being consistently increased within year since the turn of the decade. In 2025, for example, an initial ceiling of €105.2bn for voted Exchequer spending was revised up three times during the year resulting in an outturn of €109.4bn. This continued a trend of previous years which saw overspends – relative to initial allocations – average €5.4bn or 6 per cent per annum between 2021 and 2025 [Figure 18].[20]

Government spending ceilings have been regularly revised up from initial targets, particularly since the pandemic

Figure 18



Source: Department of Finance, Central Bank of Ireland calculations

The ceiling for 2026 has already been revised up, from €117.8bn in December's MTFSP to €118.5bn in APR, published just four months later. A

[20] For a more detailed look at overspends in recent years see 'Box 5: Revisions to Government Expenditure Ceilings', Central Bank of Ireland Quarterly Bulletin 1, March 2025. The largest overspend in recent years occurred in 2020 against the backdrop of the Covid-19 pandemic. We have excluded it from calculations here however, as the measures required to respond to such an exceptional shock could not have been anticipated at the time of Budget 2020.

positive initiative has been the Government's proposed introduction of a €446 million expenditure levy on Departments in 2027 to offset an additional funding requirement of €646 million by the Department of Education and Youth this year. Applying a levy in this manner potentially allows resources to be reallocated across Government Departments as required while ensuring that overall medium term expenditure ceilings are maintained.

Principles of an effective fiscal anchor

In the context of non-binding EU rules, these trends highlight the clear risk from relying on expenditure ceilings, as currently operated, to guide overall policy. With the exception of the pandemic period when an effective counter-cyclical fiscal stance was pursued, Ireland's fiscal stance has been predominantly pro-cyclical over the last half century (FitzGerald, 2026). This procyclicality has seen expansionary bias in good times, although the underlying "deficit bias" can be temporarily hidden by unsustainable revenue windfalls. The pro-cyclicality then continues in bad times through fiscal contractions, typically forced by the need to ensure debt sustainability and preserve borrowing capacity (IFAC, 2014). Although other factors have sometimes played a role, such as unsustainable credit dynamics in the 2000s, this pro-cyclical stance of fiscal policy has contributed to the severe boom-bust cycles experienced by the Irish economy over time. These cycles have, in turn, been reflected in the dynamics of inflation in Ireland compared with the euro area. In the first decade after EMU, strong relative output growth was accompanied by above-average relative inflation with the subsequent decline in output following the financial crisis matched by a stronger relative decline in inflation in Ireland (Lane, 2011).

These considerations mean that a credible domestic fiscal anchor is critical for Ireland and could help lessen the risk of repeated boom-bust cycles. While the specific design of a fiscal rule is a matter for Government, the following four guiding principles are needed for an effective anchor.

1. It should provide a clear medium-term operational anchor linking spending growth to the underlying potential growth of the economy and the State's sustainable revenue-raising capacity, ensuring that transitory revenues are not used to fund permanent increases in spending. The rule should facilitate sustainable increases in capital expenditure that improve the productive capacity of the economy. It should be based on the broader concept of general government expenditure rather than Exchequer spending.

2. An anchor should aim to smooth the economic cycle rather than amplify it. While automatic stabilisers, such as unemployment benefits, naturally respond to the cycle, an anchor should prevent discretionary tax and/or spending changes from acting in a pro-cyclical way.

3. It should be clearly defined and favour simplicity reflecting the unique difficulties in measuring the output gap for the Irish economy.

4. It should balance flexibility with discipline. There should be limited, transparent deviations for exceptional shocks, but any deviation must be temporary and accompanied by a clear plan to return to compliance.

7. Conclusion

The pace of growth in economic activity and employment since 2021 – well above long-run historical averages – has significantly benefitted the public finances. When combined with surging CT revenue, the headline budgetary position has been in surplus since 2022, despite large increases in government expenditure and some tax cuts. However, this favourable headline position rests on somewhat unstable foundations.

The State's revenue base has never been more reliant on CT receipts, but a significant proportion of CT is estimated to be windfall revenue, not related to actual economic activity in Ireland and highly exposed to the accounting decisions and performance of a very small number of firms in a very small numbers of sectors. The surge in CT – including this windfall component – mean that despite growing, the share of total tax accounted for by more stable tax heads (income tax, VAT and excise duty) has declined over the past decade, while some parts of the State's non-corporation tax revenue base have narrowed. At the same time, government expenditure has continued to grow at a fast pace. On the basis of current Government projections, expenditure growth is forecast to outstrip the pace of increase in revenue over the coming years, resulting in a sharp decline in the share of at-risk CT receipts being saved. This would reduce fiscal buffers and limit the government's capacity to respond to future economic shocks. If the recent pattern of expenditure overruns relative to initial budgetary allocations continues, then an even less favourable outturn than this is possible with the underlying budget deficit projected to rise to €25.7 billion or 5.8 per cent of GNI* by 2030. Such a

scenario would also add to domestic inflationary pressures at a time when externally driven price pressures are rising.

The planned expansion of capital expenditure—averaging 6 per cent of GNI* between 2027 and 2030—also has an important role to play but its delivery presents significant challenges. Rising construction costs, tight labour market conditions and the risk of cost overruns on large-scale projects mean that nominal spending increases may translate into smaller real gains in productive capacity than anticipated. The analysis presented in this *Article* shows that the macroeconomic impact of this investment stimulus will be influenced by two factors: rigorous management of price pressures and prioritisation of projects that generate substantial productivity spillovers to the private sector. When public investment is productivity-enhancing, it can "crowd in" private investment, mitigate competitiveness losses and deliver long-lasting output gains. Conversely, investment that does not generate productivity spillovers risks crowding out private investment and reducing external competitiveness, particularly in an economy with binding capacity constraints. Achieving value for money from the planned investment therefore requires disciplined expenditure management and careful project selection focused on maximising economy-wide productivity gains.

To ensure the long-term sustainability of both the economy and public finances, an effective fiscal anchor is needed. This would help to guard against the pro-cyclical fiscal policy that has characterised much of Ireland's recent history and contributed to repeated boom-bust cycles. Such an anchor should link government spending growth to the economy's sustainable revenue-raising capacity, accounting for corporation tax risks and should prevent discretionary fiscal policy from amplifying economic cycles. Second, broadening the tax base and increasing revenue as a share of national income must be prioritised. This could be achieved through reform of tax reliefs, property and consumption taxes and social insurance contributions. Third, a higher proportion of windfall corporation tax receipts should be saved, building larger fiscal buffers to absorb future shocks and to finance the substantial increases in age-related spending projected over the coming decades. Moreover, there is a need to broaden the tax base to ensure that the public finances could withstand the impact of a decline in corporation tax in future, if this occurred. Without these measures, long-term projections suggest the public finances could move into persistent deficit by the 2030s. With economic conditions still relatively favourable, a window of opportunity exists within which to improve the resilience of the public finances and the economy to the structural pressures and external shocks that lie ahead.

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