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IRELAND

December 2013

TWELFTH REVIEW UNDER THE EXTENDED ARRANGEMENT AND PROPOSAL FOR POST-PROGRAM MONITORING

In the context of Twelfth Review Under the Extended Arrangement and Proposal for Post-Program Monitoring, the following documents have been released and are included in this package:

- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on December 13, 2013, following discussions that ended on November 7, 2013, with the officials of Ireland on economic developments and policies underpinning the IMF Arrangement. Based on information available at the time of these discussions, the staff report was completed on December 2, 2013.
- A **Staff Supplement** of December 12, 2013 updating information on recent developments.
- A **Press Release** including a statement by the Chair of the Executive Board.

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

Letter of Intent sent to the IMF by the authorities of Ireland*

*Also included in Staff Report

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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IRELAND

December 2, 2013

TWELFTH REVIEW UNDER THE EXTENDED ARRANGEMENT AND PROPOSAL FOR POST-PROGRAM MONITORING

KEY ISSUES

Steadfast policy implementation has been maintained through the final review of the program. Budget execution has once more been solid in 2013, with the fiscal deficit expected to remain within the Excessive Deficit Procedure ceiling. Budget 2014 targets a balanced adjustment path, with a primary balance in 2014 and an overall deficit below 3 percent of GDP in 2015. Efforts continue to address the high level of nonperforming residential mortgages and SME loans and key bank diagnostics have been completed.

Ireland has pulled back from a severe banking crisis with the support of the EU-IMF arrangements and broader European initiatives. Though below initial projections, growth has exceeded the euro area average and indicators suggest a recovery may be emerging. Banking reforms have supported financial stability. While the crisis and bank support led to a substantial rise in the deficit and a sharp increase in public debt, phased consolidation—initiated prior to the Fund arrangement but subsequently maintained—has significantly improved the fiscal position. Market access has been regained, also benefitting from EFSF/EFSM maturity extensions, the Promissory Notes transaction, and the broader easing in euro area market tensions.

Continued determined policy implementation is nonetheless needed on a range of fronts before Ireland can be judged to have fully recovered from the crisis:

- ***Steady fiscal consolidation***. With the fiscal deficit still high and public debt very elevated, sizable further consolidation is needed in coming years to put debt firmly on a declining path and help ensure Ireland's return to market financing is lasting.
- ***Addressing mortgage arrears and completing bank repairs***. Very slow progress in addressing mortgage arrears hinders a revival over time in lending that is needed for domestic demand recovery to become sustained. Intensified efforts are needed to ensure banks and mortgage borrowers in arrears conclude durable solutions. Banks also need to rebuild their profitability, although, in the context of low ECB policy rates, they face challenges from the structure of their assets.
- ***Reducing high unemployment***. Efforts to improve employment services should continue, especially for the long-term unemployed, to ensure that they remain in the workforce and acquire marketable skills.

After wide consultation, the Irish authorities have decided to not seek a financing backstop after the conclusion of their current EU-IMF arrangements. Ireland concludes its Fund arrangement in a much strengthened position and the authorities intend to press on with addressing the significant challenges that remain. Nonetheless, continued European support, especially during Ireland's transition to the Single Supervisory Mechanism and the banking union, remains important.

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Acronyms

AIB	Allied Irish Banks
BoI	Bank of Ireland
BSA	Balance sheet assessment
CBI	Central Bank of Ireland
CCMA	Code of Conduct on Mortgage Arrears
DIRT	Deposit Interest Retention Tax
ECOFIN	Economic and Financial Affairs
EDP	Excessive Deficit Procedure
EFSF	European Financial Stability Facility
EFSM	European Financial Stabilisation Mechanism
ELG	Eligible Liabilities Guarantee
ESM	European Stability Mechanism
ESRI	Economic and Social Research Institute
HICP	Harmonized index of consumer prices
IBRC	Irish Bank Resolution Corporation
IFAC	Irish Fiscal Advisory Council
IFRS	International Financial Reporting Standards
IFSC	International Financial Services Centre
MART	Mortgage Arrears Resolution Targets
MTES	Medium Term Economic Strategy
NAMA	National Asset Management Agency
NFC	Nonfinancial corporation
NPL	Nonperforming loan
NTMA	National Treasury Management Agency
PCAR	Prudential Capital Assessment Review
PDH	Primary dwelling home
PMI	Purchasing managers index
PPNR	Pre provision net revenue
PTSB	Permanent tsb
REER	Real effective exchange rate
RWA	Risk weighted assets
SGP	Stability and Growth Pact
SME	Small or Medium Enterprise
SSM	Single Supervisory Mechanism

OVERVIEW

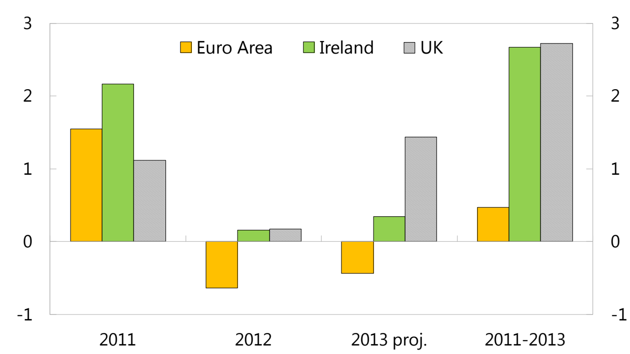
1. **The twelfth and final review of Ireland's EU-IMF supported program found policy implementation remains on track but significant challenges remain ahead**. Discussions focused on fiscal policy and on the bank diagnostics. Following further discussions on a potential EU-IMF financing backstop the authorities announced their decision not to request such arrangements from the ESM and IMF. The authorities' broader strategy to address remaining fiscal, financial sector and unemployment challenges and thereby ensure a durable return to market financing, as summarized in their attached Letter of Intent, was also discussed.

PROGRESS AND REMAINING CHALLENGES

2. **Ireland has pulled back from a severe banking crisis with the support of the EU-IMF program**. The program that began in December 2010 followed an exceptionally deep banking crisis, as described in the staff report for the 2012 Article IV consultation. Policy implementation has been steadfast although progress under the program has been mixed:

- ***Growth has been slower than projected, although exceeding the euro area average***. After an export-led expansion of 2.2 percent in 2011, real GDP growth slowed to 0.2 percent in 2012 and turned negative in H1 2013 as exports were hit by the "patent cliff" in pharmaceuticals and by slow trading partner recovery (Box 1). Expected cumulative growth in 2011–13 of about 2¾ percent falls short of the 5¼ percent originally projected. However, expected euro area growth of ½ percent in 2011–13 falls short of the October 2010 WEO projection of 5.2 percent to a greater extent. Ireland's cumulative growth in 2011–13 is expected to match the UK.

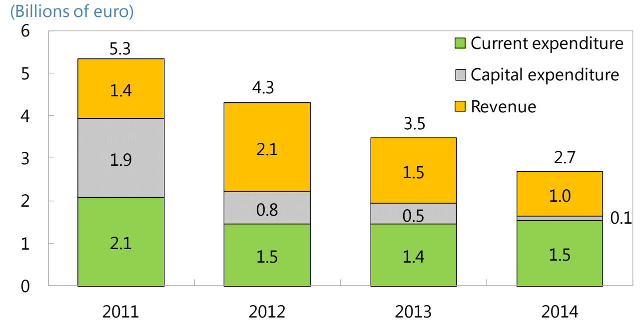
Real GDP Growth
(Percent)



Source: IMF WEO; and IMF Staff estimates.

- ***Phased consolidation effort has significantly improved the fiscal position***. Even before the start of the program, Ireland undertook substantial fiscal consolidation, reducing the structural primary deficit by 5¼ percent of GDP in 2009–10. Subsequently, every fiscal target under the program has been met. As a result, Ireland is expected to reduce its structural primary deficit to ½ percent of GDP in 2013, a cumulative

Composition of Fiscal Consolidation 1/
(Billions of euro)



Source: IMF staff estimates.
1/ Of the €6 billion in measures included in Budget 2011, some €0.7 billion related to the sale of assets and debt service savings are not part of staff estimates of the consolidation effort. Revenues for 2012 include €0.5 billion in carryovers from the Universal Social Charge and other measures not envisaged under the original program, but implemented under Budget 2011. For 2014, the estimate of consolidation does not include additional deficit reductions of €0.45 billion identified in the Budget related to unemployment benefits, interest payments, and central bank dividends.

decline of around 4½ percentage points since 2010 and of 10 percentage points since the onset of the crisis. Fiscal measures implemented under the program total over €13 billion or 8 percent of GDP, two-thirds on the expenditure side.

- ***The fiscal framework has been strengthened***. A general government budget balance rule and a general government debt rule were adopted as part of the Fiscal Responsibility Act 2012, consistent with the Stability and Growth Pact (SGP). Budget 2012 introduced three-year aggregate and ministerial level expenditure ceilings, put on a statutory basis in the recently approved Ministers and Secretaries (Amendment) Bill 2013. The Fiscal Responsibility Act also provides for the independence and adequate funding of the Irish Fiscal Advisory Council (IFAC). The Council is responsible for providing an *ex ante* endorsement of the macroeconomic forecasts underpinning the budget and for assessing the soundness of the government's budgetary projections and fiscal stance. Measures to enhance transparency include the authorities' action plan on fiscal reporting, forecasting and risk analysis (guided by the Fund's fiscal transparency assessment) and the launch of a quarterly Government Finance Statistics publication.

- ***Financial stability has been supported by determined efforts***. These include a €24 billion (15 percent of GDP) top up of banks' capital in 2011, coupled with a significant restructuring of the system.[1] These PCAR banks reported an aggregate core tier 1 risk based capital ratio of 14.1 percent as of mid 2013 (although the balance sheet assessment indicates a somewhat lower ratio, ¶29). Provisions doubled between end 2010 and June 2013 to account for 90 percent of aggregate loan losses projected under the stress scenario of the 2011 stress test.[2] Domestic deposits have stabilized since mid 2011 even as deposit rates have declined. The loan-to-deposit ratio has come down from 190 percent at end 2010 to

Aggregate Balance Sheet of PCAR Banks 1/

(In billions of euro unless otherwise indicated)

Balance Sheet	Q4 2010 € bn.	Q2 2013 € bn.	Percent change
Cash & due from Eurosystem	6.3	9.1	42.9
Net loans	273.6	186.0	-32.0
o/w Mortgages (Ireland, gross)	95.3	90.0	-5.6
Due from banks	n.a.	8.7	n.a.
Securities & derivatives	58.9	64.7	9.7
Other assets	29.2	13.4	-54.1
Total assets	368.1	281.8	-23.4
Due to Eurosystem	90.1	33.7	-62.6
Due to banks	27.0	19.1	-29.5
Deposits	144.3	159.0	10.2
Debt & derivatives	72.1	37.9	-47.4
Other liabilities	19.3	11.0	-43.0
Net equity	15.3	21.1	37.7
Total liabilities & equity	368.1	281.8	-23.4
Memorandum items:			
Gross loans 2/	310.8	213.5	-31.3
Loan loss provisions	14.3	28.2	97.0
Gross NPLs	33.5	56.8	69.4
Gross NPLs to gross loans (%)	10.8	26.6	15.8
Provisions to gross NPLs (%)	42.7	49.7	6.9
Loans (net) to deposits (%)	189.7	117.0	-72.7

Sources: CBI; and IMF staff estimates.

1/ PCAR banks are Bank of Ireland, Allied Irish Banks, and Permanent tsb.
2/ Includes loans held for sale, classified on balance sheet as other assets.

[1] The 2011 Prudential Capital Assessment Review (PCAR) stress tested Allied Irish Banks (AIB), Bank of Ireland (BoI), and Permanent tsb (PTSB), together the PCAR banks. See the Financial Measures Programme Report, March 2011, of the Central Bank of Ireland (CBI).

[2] In calculating this ratio, the PCAR loss estimate is increased by €3.9 billion to reflect the subsequent decision to not transfer smaller land and development loans to the National Asset Management Agency (NAMA).

117 percent in June 2013 and PCAR bank reliance on Eurosystem support is down from a peak of over €90 billion to about €31 billion. Bank support involved a heavy burden on the public sector, with gross costs of €64.1 billion (40 percent of GDP). Recovery of these costs is at an early stage, including through the sale of Irish Life and CoCos in BoI.

- ***Financial regulation and supervision have developed further and improvements continue***. In October 2011 a special resolution regime for banks and credit unions was enacted and in July 2013 the supervisory powers of the CBI were strengthened.[3] In December 2012 the new Personal Insolvency Act established three new essentially nonjudicial procedures for debt resolution and modernized the Bankruptcy Act 1988.[4] In May 2013 the CBI reinforced its Impairment Provisioning and Disclosure Guidelines, including clauses on loan modification and evergreening practices. The Credit Reporting Bill, though delayed, is expected to be enacted by December 2013 to provide for a statutory Central Credit Register system operated by the CBI. The CBI has been strengthening banking supervision by increasing resources and operationalizing its new risk based supervisory approach. Reports on Ireland's observance of the Basel Committee *Core Principles for Effective Banking Supervision* and the IOSCO *Objectives and Principles of Securities Regulation* are due to be completed shortly, and the authorities are committed to continue making improvements in regulation and supervision.

- ***Competitiveness is improving even as structural reform progress has been slower than hoped***. Competitiveness deteriorated during the boom but subsequent declines in the CPI and unit labor costs left Ireland with only a moderate degree of real effective exchange rate overvaluation, in the range of 5–10 percent (see 2012 Article IV Staff Report, Annex I). Flat nominal wages and low inflation suggest improvements in competitiveness will continue in coming years. Structural reforms have aimed to improve competition within the legal and medical services sectors, strengthen competition enforcement including by increasing resources, enhance activation and training of the unemployed, and facilitate labor market adjustment in sectors hit hard by the crisis, although the implementation of some reforms is yet to be completed.[5]

- ***Market access has been regained***. Financial market conditions have improved markedly, reflecting a combination of the above policy efforts and European support through interest rate reductions, EFSF/EFSM maturity extensions, and the Promissory Notes transaction, together with the broader easing in euro area market tensions since mid 2012. Two government bond issues totaling €7½ billion in early 2013 were heavily subscribed by an investor base that was diversified by region and investor class. Spreads on Irish sovereign bonds have fallen to their lowest level since early 2010 and, since its issuance in March, the 10 year bond yield has fallen from 4.15 percent to about 3.5 percent recently, some 60 basis points below Italy and Spain.

[3] On the resolution regime, see Box 2 in Ireland: First and Second Reviews Under the Extended Arrangement.

[4] See Annex II, Ireland—Ninth Review Under the Extended Arrangement.

[5] For elaboration on these reforms, see ¶36 of Ireland—Staff Report for the 2012 Article IV Consultation.

3. **Nonetheless, significant challenges remain that will require concerted action over the medium term before Ireland can be judged to have fully recovered from the crisis**:

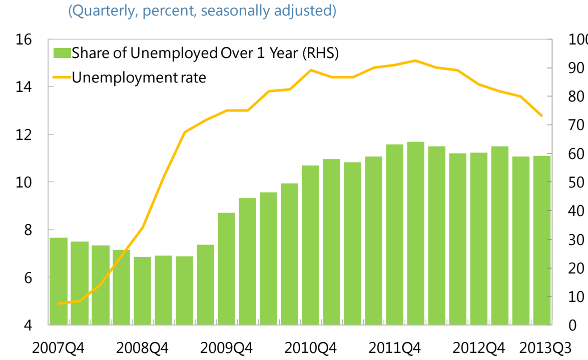
- ***Heavy private sector debts weigh on the level of domestic demand***. By boosting savings, households have reduced their nominal debts by 16 percent in the past 4½ years, but debt burdens remain high at 198.3 percent of disposable income in 2013 Q2 with saving likely to remain above normal levels for some time. SMEs face financing constraints on investment and job creation, often reflecting debt incurred for past property investments.[6]

- ***Banks' progress in resolving high nonperforming loans (NPLs) has been very slow and weak profitability also hinders a revival of lending***. NPLs stand at 26½ percent of PCAR bank loans, led by commercial real estate loans (41 percent), Irish residential mortgages (34 percent) and business and SME loans (19 percent). This high share of NPLs raises the cost of market funding including through overcollateralization requirements and drains management resources that could be used for new lending. High unemployment and other shocks have led to arrears over 90 days on 12.9 percent of mortgages for principal dwellings, while the figure for mortgages on buy-to-let properties is 21.2 percent. However, banks' progress in resolving NPLs has been very slow, prompting the CBI to establish targets for the resolution of residential mortgages and SME loans.[7] Even after significant profitability improvements in the first half of 2013—reflecting the removal of the Eligible Liabilities Guarantee (ELG) scheme, reductions in staffing and branch numbers made in 2012, and declines in deposit rates—bank profitability remains weak, limiting banks' capacity to generate the capital needed to sustain lending. The greatest challenge is faced by the smaller PTSB which is not expected to break even after provisioning expenses until 2017.

- ***The fiscal deficit remains high and putting public debt firmly on a downward path requires sizeable further fiscal consolidation***. Despite the major primary adjustment under the program, a rising interest bill has kept the fiscal deficit at 6½ percent of GDP (excluding one-off guarantee payments related to the liquidation of the Irish Bank Resolution Corporation, IBRC), and with debt projected at 124 percent of GDP at end 2013 further consolidation is needed while allowing room for recovery.

- ***High long-term unemployment, if unaddressed, could depress growth for years***. Reflecting a combination of job creation and emigration, unemployment eased from 15.1 percent in early 2012 to a still high 12.8 percent by Q3 2013. However, the long-term jobless constitute some 58.4 percent of all jobseekers, eroding labor force participation and work skills.

Unemployment Rate and Duration
(Quarterly, percent, seasonally adjusted)



Sources: Haver Analytics; and IMF staff calculations.

[6] See Box 4 in Ireland—Eleventh Review Under the Extended Arrangement.

[7] Factors behind prolonged mortgage forbearance are outlined in ¶19 of the Tenth Review.

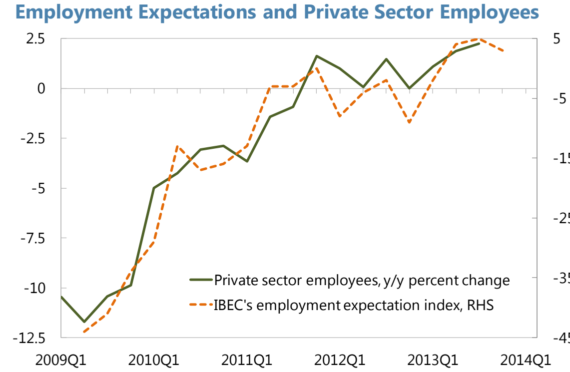
RECENT DEVELOPMENTS

4. **An output rise in Q2 2013 reversed only part of the sharp dip in Q1 but a range of indicators paint a more positive picture for the second half of the year**:

- ***Real GDP grew by 0.4 percent q/q in Q2 but still contracted 1.2 percent y/y***. Exports rebounded in Q2 to increase 1 percent y/y, led by services export growth of 3.6 percent. Final domestic demand contracted 0.3 percent q/q in Q2, to be down by 1.1 percent y/y, as a 0.7 percent q/q rise in private consumption was outweighed by weak investment and public consumption. Nonetheless, fixed investment ex-aircraft grew 11.8 percent y/y, driven by equipment spending and construction.

- ***Employment rose 3.2 percent y/y in Q3, the fastest increase in six years***. Job growth was recorded in 8 of 14 sectors, including construction, though public sector employment fell. Surveys of employers, together with the further decline in the unemployment rate in October, suggest that private sector job growth is continuing.

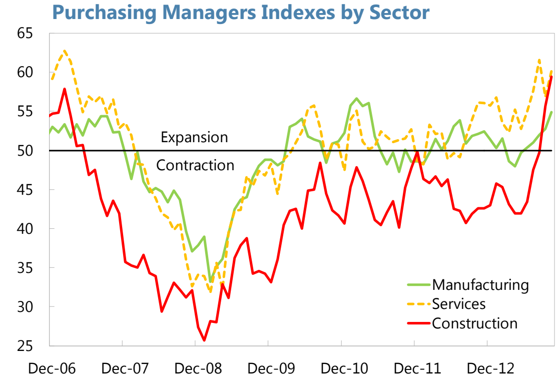
Employment Expectations and Private Sector Employees



Sources: IBEC's Business Sentiment Report (October 2013); and CSO.

- ***Signals of a broad-based recovery are provided by high frequency indicators in the second half***. Goods exports rose 4.9 percent q/q in Q3. The manufacturing PMI continued to rise through October to 54.9, the services PMI reached its highest level since March 2007, and the construction PMI for October is now firmly in expansion territory, with the overall index increasing to 59.4, the highest level observed since January 2006. Consumer sentiment also reached the highest level in 6 years in October and although core retail sales were flat in October, they are up 0.3 percent y/y in the first ten months of 2013.

Purchasing Managers Indexes by Sector



Source: Haver Analytics.

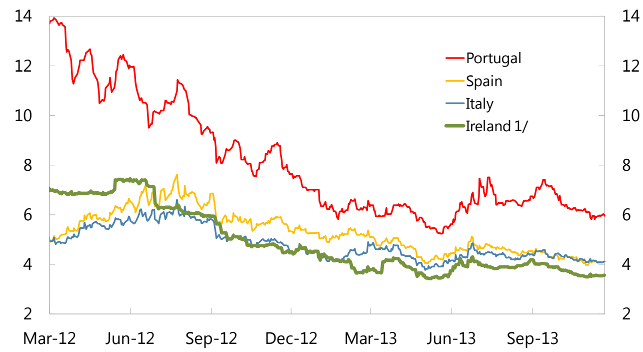
- ***Inflation remains low***. Helped by falling energy prices, harmonized index of consumer prices inflation was essentially flat y/y in October (-0.1) and below euro area inflation of 0.7 percent y/y during the same period.

- ***House prices are rising nationally, with strong growth in Dublin and increases emerging elsewhere, even as bank credit continues to contract***. Household credit outstanding shrank by 4.2 percent y/y in October and loans to nonfinancial corporations fell by 4.7 percent. Nonetheless, mortgage draw downs rose 12.5 percent y/y in Q3 and mortgage approvals increased 22.2 percent y/y in October. Residential property prices rose

6.1 percent y/y in October, led by a 15 percent y/y gain in Dublin while elsewhere house prices have edged up by 3.5 percent since March. Renewed house price increases and declining household indebtedness are contributing to a rebuilding of household net worth, although it remains some 34 percent below peak levels.

5. **Financial market conditions continued to improve, benefitting from international developments**. Yields eased following the Federal Reserve's postponement of the tapering, the German election outcome, and the recent ECB easing decision. In view of its relatively strong funding position, the National Treasury Management Agency (NTMA) decided to suspend its monthly Treasury bill auctions for the final quarter of 2013 and to defer consideration of any further medium/long-term bond issuance until early 2014.

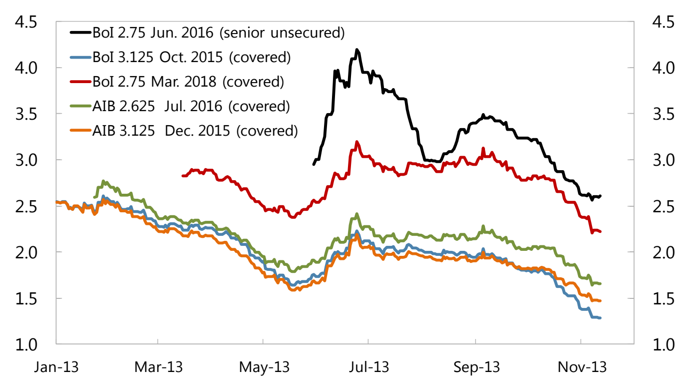
Ten-Year Sovereign Bond Yields
(Percent)



Source: Bloomberg.
1/ Prior to 15 March 2013 a treasury bond maturing in 2020 is used for Ireland.

6. **Funding conditions for banks have enjoyed a positive spillover from the strength of the Irish sovereign bond market in recent months**. Secondary market yields on three-year covered bonds from BoI and AIB have fallen by about 75 basis points since early September. Domestic banks have also issued €3 billion in bonds since September, with high bid-to-cover ratios and geographically diversified demand indicating strong investor interest.[8] After declining significantly, bank deposit rates have stabilized below 1 percent in recent months. ECB borrowing by domestic banks fell from €39.6 billion at end March to €30.8 billion at end October.

Bank Bond Yields
(Percent)



Source: Bloomberg.

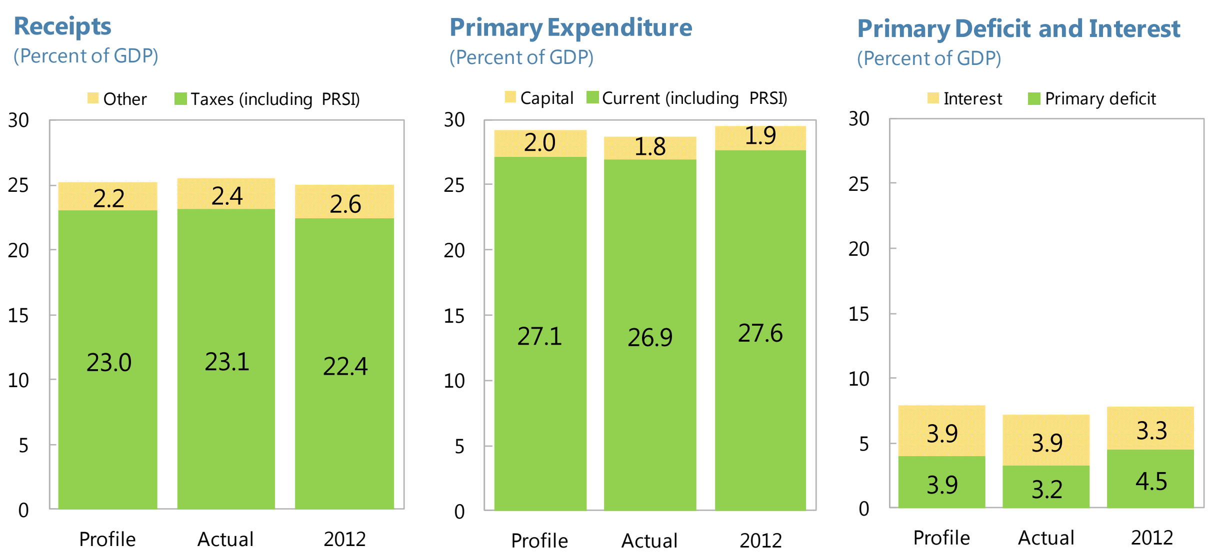
7. **NAMA continues to make progress towards its debt redemption targets and is preparing for the challenges of integrating IBRC loans**. In the year through mid-October NAMA generated cash receipts totaling €3.9 billion of which €2.9 billion was from asset disposals. From its inception, NAMA has generated total cash receipts of about €14.5 billion of which €9.7 billion was from asset disposals, helping to bring cumulative redemptions of its senior bonds to €7 billion to date out of a total of €30 billion by 2020. NAMA recorded a profit of

[8] BoI and AIB issued €1.5 and €0.5 billion of covered bonds, respectively. AIB also issued €0.5 billion of senior unsecured debt. PTSB's €0.5 billion asset backed security issuance is the first of this type since 2007.

€53 million in the first half of 2013, notwithstanding cumulative impairment provisions of €3.6 billion (14½ percent of gross loans and receivables). To support asset sales, NAMA has advanced €375 million in vendor financing and has spent €500 million in capital investment to date. Preparations are being made to acquire IBRC loans up to the value of the €12.9 billion floating charge acquired as part of the Promissory Notes transaction in the event the Special Liquidator is unable to sell IBRC's assets to the market. Loan servicing previously conducted by IBRC on behalf of NAMA on debt with a principal of €41 billion is being migrated to a loan servicing company, and staff and IT systems from IBRC are being integrated.

8. **The exchequer deficit remained on track through end October**. Cumulative primary expenditure (excluding ELG payments linked to the Promissory Notes transaction) was 0.7 percent of GDP lower than in the same period of 2012 on account of lower outlays in social protection, health, and education. Both current and capital spending remained below the authorities' profile as well. Cumulative revenues (after adjusting for one-offs) were 0.7 percent of GDP higher than a year earlier. Revenues remain marginally above budget projections as over-performance on corporate income tax, Pay Related Social Insurance, and stamp duties offset shortfalls in VAT and excise duties that have until now been weighed down by weak domestic demand. The exchequer primary deficit at end October was 3.2 percent of GDP, 1.3 percent of GDP smaller than in the corresponding period of 2012, and the end September performance criterion was met by a margin of 0.8 percent of GDP (Table 12).

Cumulative Exchequer Outturn vs. Authorities' Profile, January–October 2013



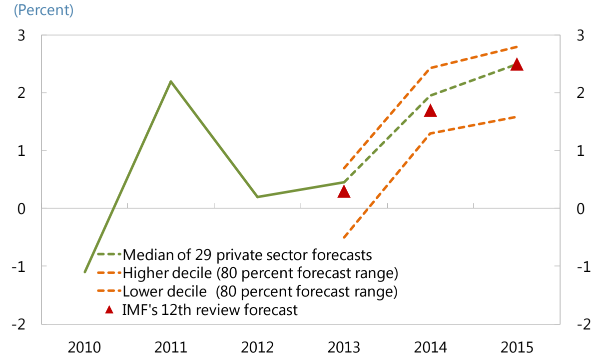
Sources: Department of Finance; and IMF staff estimates.
Note: To facilitate comparability: (i) 2012 tax revenues do not include the €251 million corporation tax payment delayed from December 2011; (ii) outlays in respect of Irish Life (€1.3 billion) and credit unions (€250 million) are excluded from 2012 capital spending; (iii) proceeds from the sale of Bank of Ireland contingent capital notes (€1 billion) and Irish Life (€1.3 billion) are excluded from 2013 other receipts; and (iv) Eligible Liabilities Guarantee scheme payments linked to the promissory note transaction of €1 billion are excluded from 2013 current expenditure.

MACRO-FINANCIAL OUTLOOK AND RISKS

9. **Drag from a weak first half implies lower growth in 2013 despite recent signals of recovery**. GDP growth in 2013 is revised to 0.3 percent, down from 0.6 percent at the eleventh review, yet experience indicates that a significant range of uncertainty remains owing to the potential for large data revisions when the annual GDP data for 2013 are released in mid-2014.[9] Final domestic demand is forecast to contract 0.2 percent for the year, led by a 0.6 percent decline in private consumption. While investment is rising, the growth contribution is limited by its low share in GDP. Exports are expected to grow just 0.5 percent y/y owing to the weak first half, still outpacing import growth of 0.2 percent.

10. **Higher trading partner growth is a key driver of gradual recovery to 1.7 percent y/y growth in 2014**. Recent WEO projections show Ireland's trading partner growth picking up from 0.4 percent y/y in 2013 to 1.6 percent in 2014, which is expected to allow net exports to boost growth by just over 1 percentage point. Recent employment growth appears to be continuing and is expected to support household incomes and confidence, helping consumption growth turn modestly positive in 2014 at 0.5 percent y/y. Public consumption will contract at a faster pace than in 2013 owing to the implementation of the agreement on public sector wages.

Real GDP Growth–Private Sector Projections, October 2013
(Percent)



Sources: Bloomberg; and IMF staff estimates.

Macroeconomic Projections, 2009–15

(Percentage change unless indicated otherwise)

	2009	2010	2011	2012	2013	2014	2015
Real GDP	-6.4	-1.1	2.2	0.2	0.3	1.7	2.5
Final domestic demand	-9.7	-5.0	-3.0	-1.1	-0.2	0.4	1.0
Private consumption	-5.1	0.9	-1.6	-0.3	-0.6	0.5	1.0
Public consumption	-3.4	-6.9	-2.8	-3.7	-1.0	-2.8	-2.5
Fixed investment	-26.9	-22.6	-9.5	-1.0	2.9	4.4	5.4
Change in stocks 1/	-0.7	0.6	1.0	-0.4	0.2	0.0	0.0
Net exports 1/	4.6	3.0	5.7	1.6	0.3	1.4	1.7
Exports	-3.8	6.4	5.4	1.6	0.5	2.5	3.7
Imports	-9.8	3.6	-0.4	0.0	0.2	1.4	2.7
Nominal GDP (billions of euros)	162.3	158.1	162.6	163.9	165.4	169.5	175.4
GDP deflator	-3.8	-1.5	0.7	0.7	0.6	0.7	1.0
Current account (percent of GDP)	-2.3	1.1	1.2	4.4	4.2	4.6	4.7
Consumer Prices (HICP)	-1.7	-1.6	1.2	1.9	0.8	0.9	1.1
Unemployment rate (percent)	12.0	13.9	14.6	14.7	13.3	12.3	11.7
Household savings rate (percent of disp. income)	14.9	12.0	10.7	10.2	10.9	10.8	10.6
Household debt (percent of disp. income)	218	215	212	206	202	193	188
Credit to households and NFCs (eop)	-1.5	-3.4	-2.9	-4.0	-3.9	-1.9	0.2

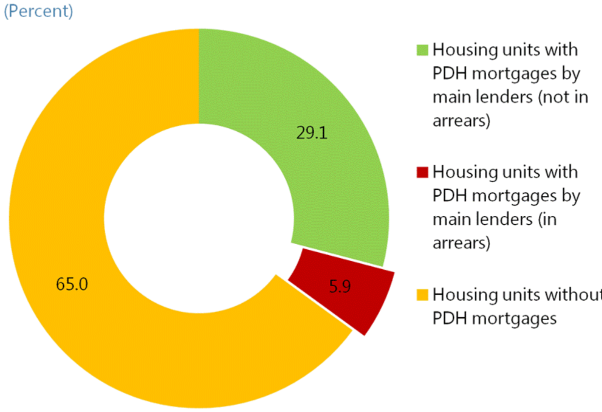
Source: IMF staff projections.
1/ Contributions to growth.

[9] In 2011, initial estimates for real GDP growth of 0.7 percent were subsequently revised up to 2.2 percent, while initial estimates for growth in 2012 of 0.9 percent have since been revised down to 0.2 percent.

11. **Growth is projected to firm to 2½ percent from 2015 even as heavy private sector debt burdens imply a protracted domestic demand recovery**. Improvements in the external economic environment, less drag from fiscal consolidation, and a gradual revival of lending are key drivers. Export growth is projected to return to its long-term trend by 2015. Domestic demand recovers slowly, growing just 1 percent by 2015, amidst high household and SME indebtedness. Growth of 2½ percent is sustainable into the medium term as demographic trends support growth in the working age population of around 1 percent over the next ten years, as declines in unemployment allow a period of employment growth on the order of 1½ percent without igniting wage pressures, and as Ireland's productivity rises about 1 percent annually including as a result of continuing FDI inflows.

12. **Mortgage restructuring needs to advance, yet also achieve durable solutions, to support economic recovery in the medium term**. Currently some 6 percent of households are running arrears and others are struggling to uphold debt service. As discussed in Box 2, sustainable loan restructures will entail adjustments in consumption in some cases while providing relief in others. These direct near term effects on consumption are likely to be outweighed by the broader medium term benefit of improving banks' asset quality, thereby enabling banks to attract cheaper funding and facilitating a revival of mortgage lending. Furthermore, resolving nonperforming mortgages will ease fears around the "shadow housing inventory" from underwater mortgages, enhancing housing market turnover and reducing household uncertainty about wealth, altogether supporting domestic demand recovery. These benefits could however be reversed if widespread redefaults were to occur or debt service discipline were to weaken further.

Housing Units, Mortgages, and Arrears
(Percent)



Source: Department of Finance, "Mortgage restructures data", September 2013.

13. **Risks continue to surround recovery prospects, with near-term risks significant yet broadly balanced but risks tilt to the downside in the medium term**:

- ***External environment***. Ireland's high degree of openness (exports account for around 110 percent of GDP) makes it vulnerable to trading partner growth fluctuations. Weak external recovery could also spill over to domestic demand through consumer and business confidence. Nonetheless, recent indicators in some of Ireland's main trading partners are relatively positive, providing scope for upside risk.

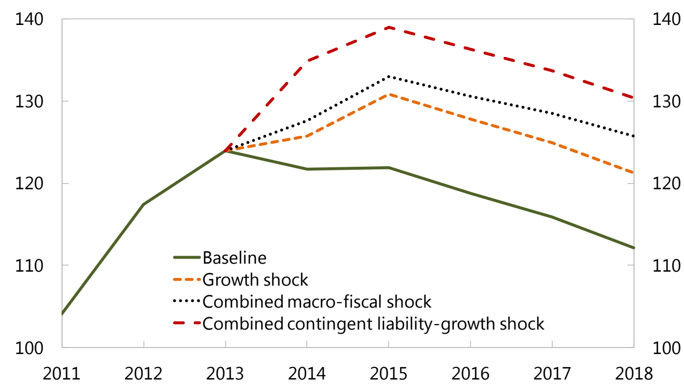
- ***Domestic demand***. Consumption prospects hinge importantly on a continuation of recent employment gains, supporting incomes and reducing uncertainties. The ongoing house price recovery is yet to be tested by the depressive effects of a potential rise in disposals of repossessed properties. Investment recovery is a potential upside risk given its low base (around 11 percent of GDP).

- ***Financial conditions***. The revival in credit growth and investment needed to sustain recovery over the medium term would be hindered if current efforts to resolve NPLs and improve bank profitability were to fall short. If a later U.S. Federal Reserve tapering were to impact the euro area periphery more strongly there could be adverse impacts on banks' access to and costs of market funding and thus to credit availability.

14. **Public debt sustainability remains fragile (Annex I)**. Declines in public debt are subject to risk from lower growth, contingent liabilities, or a combination of both. Under the baseline scenario, the public debt-to-GDP ratio is projected to peak at 124 percent at end 2013 and to decline to 112 percent by 2018 as the economic recovery gains traction. A temporary growth shock (with annual growth about 2 percentage points lower at -0.3 percent y/y in 2014 and 0.5 percent in 2015) would increase the debt-to-GDP ratio to 131 percent in 2015 before declining to 121 percent of GDP by 2018. If slower growth in 2014–15 were compounded by a temporary primary balance shock during the same period (with a worsening of the primary balance by 1½ percentage points of GDP on average in each year) and by interest rates on newly contracted debt rising by 2 percentage points through the medium term, the debt ratio increases to 133 percent of GDP in 2015 and falls to 126 percent by 2018. As discussed in Annex I, a range of contingent liabilities remain in the financial sector, and without estimates of their potential realization, a scenario of a 10 percent of GDP shock is used. Such a shock, if combined with the above growth shock, would push gross public debt to 139 percent of GDP in 2015 before declining to 130 percent by 2018.

Public Debt Paths under Various Scenarios

(Nominal gross debt in percent of GDP)



Source: IMF staff estimates.

POLICY DISCUSSIONS

A. Fiscal Policy

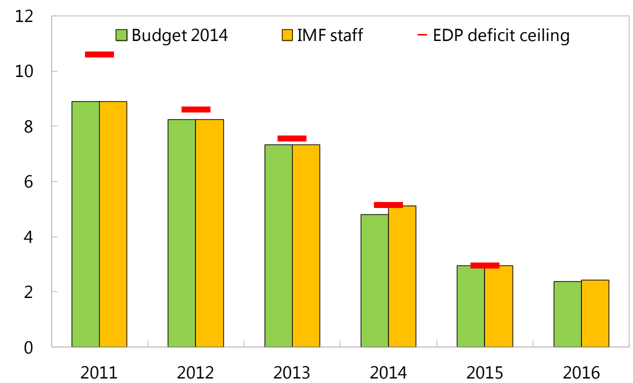
15. **The deficit for 2013 is expected to remain within the 7.5 percent of GDP ceiling under the Excessive Deficit Procedure (EDP)**. Though revenue outturns are currently on track, they could fall short at end-2013 by some 0.2 percent of GDP if receipts from consumption related taxes continue to disappoint. Overall, expenditure is expected to remain within budget, as modest overruns in the health sector (0.1 percent of GDP) are expected to be offset by lower capital spending. However, the deficit would be raised if AIB dividend payments are reclassified

as capital transfers (0.2 percent of GDP).[10] Nonetheless, the risks of exceeding the EDP deficit ceiling are limited as the budget will benefit from lower than expected interest payments and the later than expected recording of a telecom license sale.[11]

16. **Budget 2014 targets primary balance in 2014 and the Irish authorities are firmly committed to reaching a fiscal deficit below 3 percent of GDP by 2015, which is sufficient to put debt on a declining trajectory**.[12] The corresponding structural benchmark is met:

- ***The targets for the fiscal deficit in 2014–15 are in line with the nominal ceilings set out in the 2010 Council Recommendation under the EDP***. For 2014, the budget targets primary balance and an overall deficit of 4.8 percent of GDP, providing a buffer relative to the 5.1 percent of GDP ceiling under the EDP. Staff projects a deficit equal to the ceiling as revenues are expected to be somewhat lower in the context of more subdued domestic demand than budgeted. For 2015, the authorities target a deficit of 2.9 percent of GDP to meet the EDP target for a deficit below 3 percent of GDP. This would imply a primary surplus of 2 percent of GDP based on staff's forecast, above the debt stabilizing primary surplus in 2015 of 1 percent of GDP.

Overall Fiscal Deficit
(Percent of GDP)



Sources: Department of Finance; and IMF staff estimates.

- ***The cumulative fiscal consolidation in 2014–15 is consistent with the fiscal effort set out in the 2012 Medium Term Fiscal Strategy and April 2013 Stability Programme.*** The fiscal consolidation effort in 2014 is estimated at €2.7 billion (1.6 percent of GDP), including carryovers from measures implemented in previous years and 0.1 percent of GDP in higher dividends from state owned companies (Box 3).[13, 14] For 2015, staff estimates under its

[10] The deficit could also be affected with the ruling of Ireland's High Court on the amount that the state will have to pay out in compensation for lost pension benefits in the Waterford Crystal case. The net present liabilities to the state could amount to some 0.1 percent of GDP, spread out over the lifetime of the pensions.

[11] In consultation with Eurostat, the authorities are to record €0.7 billion from the telecom license sale that took place in 2012 in 2013 instead, as the license became operational only in February 2013. Similarly, €0.4 billion from the sale of the national lottery license that took place in 2013 will be recorded in 2014.

[12] In its recent Fiscal Assessment Report the IFAC assessed the Government's planned fiscal stance in Budget 2014 to be conducive to prudent economic and budgetary management. At the same time, it cautioned that the decision to reduce the planned fiscal adjustment in 2014 compared with the April 2013 Stability Programme had eliminated the previously existing margin of safety relative to the 3 percent of GDP deficit ceiling for 2015.

[13] Consistent with European Commission practice, additional dividends from state owned enterprises are treated as a consolidation measure because the total dividend remains within historical profit generation, indicating that this measure is sustainable, and projections are for higher dividends to continue for a number of years.

[14] This consolidation measure may be understated as it does not include the expenditure restraint needed to offset additional demographic pressures in a no policy change scenario, which the authorities estimate at €0.3 billion. The authorities identify additional deficit reductions of €0.45 billion from lower unemployment benefits, lower interest payments, and higher central bank dividends, for a total adjustment of €3.1 billion.

macroeconomic projections that €2.4 billion (1.4 percent of GDP) in fiscal measures would be needed to achieve the 2.9 percent of GDP target. This would bring the cumulative fiscal consolidation effort in 2014–15 to €5.1 billion (3 percent of GDP).[15] This pace of fiscal adjustment is appropriately slower than in 2012–13 (4¾ percent of GDP), recognizing the need to reduce drag on economic recovery and the credibility built up by the authorities.

- ***The fiscal effort projected for 2016 is in line with the authorities' national fiscal rules and SGP***. Expenditure growth is expected to be contained at 1 percent in nominal terms, which would keep it within the expenditure benchmark under the SGP. This would result in a 0.5 percent of GDP improvement of the structural balance (based on the authorities' calculations), complying with the authorities' national fiscal rule.[16] This pace of improvement is sufficient to raise the primary balance to almost 4 percent of GDP by 2018, reinforcing the decline in the debt to GDP ratio while avoiding undue drag on economic growth.

17. **Firm implementation will remain critical to achieve the 2014 fiscal target, with the main risk stemming from possible disappointment in domestic demand growth**. The Finance and Social Welfare Bills needed to implement all the new measures announced in the budget have been published and are expected to be adopted by year end once approved by Parliament. The authorities noted that some of health overruns in 2013 were related to delayed implementation of some measures (such as approval of the Haddington Road Agreement and charging of private patients for use of public beds), which have already been resolved. They also indicated that close monitoring of the sector will continue. Hence, risks from potential spending pressures in the health sector are not expected to be substantial, but may require contingency measures to keep spending within allocations. More broadly, the main risk to the budget is that domestic demand is weaker than budgeted. The authorities acknowledged this risk, but also pointed to possible upsides, as recent reforms to broaden the tax base are likely to result in larger elasticities that could lead to stronger revenue performance if economic activity is robust.

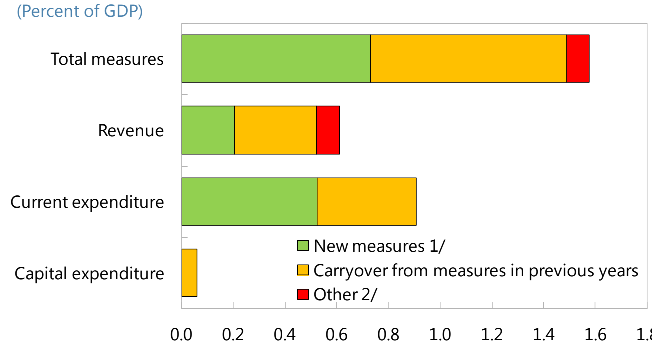
18. **Expenditure savings will be achieved through measures with a durable impact, although they do not tackle costly universal payments nor advance structural reform**. The budget reduces or eliminates some untargeted social support schemes (see Box 3). The reduction in the unemployment benefit rate for those 22 to 25 years of age is intended to provide greater incentive for the transition to work through a reduction in the reservation wage and by encouraging access to education and training where the benefit rate is significantly higher. Nonetheless, measures to better target costly universal supports and subsidies (such as the child benefit, medical cards, and subsidies on college fees) were not part of the budget package, which fails to address the schemes likely to be subject to strong demographic pressures. Furthermore,

[15] Staff's estimate of a structural primary balance rise of 3¼ percent of GDP in 2014–15—an alternative measure of fiscal adjustment—is consistent with the calculated scale of the cumulative fiscal consolidation effort.

[16] The authorities' structural balance figures differ modestly from staff estimates due to differences in macroeconomic forecasts and the methodologies used, including for calculation of the output gap.

the budget does not develop structural measures to reform key public services.[17] The authorities underscored that universal supports were reduced in past budgets, and there was currently no political appetite for changing the principal of universality. They also indicated that some of these issues would be taken up in the context of the Comprehensive Review of Expenditure and review of the Capital Investment Framework to be launched next year.

Composition of 2014 Consolidation
(Percent of GDP)



Sources: Department of Finance; and IMF staff estimates.
1/ Includes lower proceeds due to retention of 9 percent reduced VAT rate for the tourism sector of (€0.3 billion).
2/ Includes highed dividends from state-owned companies.

19. **Revenue measures both increase rates and broaden bases, but new collections would be partly offset by the extension of the reduced VAT rate in the tourism sector**. Base broadening measures included the introduction of a bank levy and reduction of some personal income tax exemptions. Such measures, including the bank levy – which is comparable to levies in place in several European countries such as France, Germany and the UK – can help pay for the direct fiscal cost of any future government support to the sector. The impact on banks is expected to be somewhat mitigated by the lifting of the restriction on the use of deferred tax assets for losses incurred when banks transferred loans to NAMA. Looking ahead, if the levy is retained beyond its initial 3-year period, it could be refined to reflect institutions' riskiness and contributions to systemic risk. The budget also raises rates on the deposit interest retention tax (DIRT) and excise duties. However, the reduced VAT rate of 9 percent in the tourism industry will not be allowed to expire at end-2013, with an estimated negative impact of €0.3 billion. The authorities considered that the reduced VAT rate has had a significant positive impact in the sector and on employment, and did not want to cause a setback to the sector before it is on stronger footing.

20. **The distributional impact of Budget 2014 is uncertain given the composition of measures**. The tax-benefit model used by the Economic and Social Research Institute (ESRI) to assess the distributional impact of the budget each year is not equipped to deal with indirect taxes or taxes on wealth, such that it covers less than 20 percent of the total consolidation package in Budget 2014. On the taxation side, the reduction in tax relief for high valued pensions, the increase in DIRT, and restriction on tax relief for health insurance premia are expected to have a broadly progressive impact. By contrast, the ESRI's SWITCH model indicates that the full year impact of the indicative but not final version of the local property tax to be felt in 2014 would have likely been regressive. Also, the reduction in unemployment payment rates for those aged 22

[17] Staff recommendations on reform of key public services such as health, education, and social protection, are outlined in the 2012 Article IV Staff Report.

to 25 could have a more severe impact on individuals in low income households, though this will depend in the availability of suitable training which would provide a higher payment.

21. **Recent institutional reforms came into effect in Budget 2014.** Aggregate exchequer and ministerial level expenditure ceilings were set through to 2016, with spending growth to remain within the SGP expenditure benchmark. The authorities indicated that the upward revision to the 2014 ceiling as compared to Budget 2013 by €0.4 billion was in compliance with the recently issued circular, which stipulates that changes are permisible if compensatory discretionary measures are introduced. The budget also announced that the number of public service employees would not decline in 2014 as anticipated under the previous employment control framework target but the authorities emphasized their commitment to the existing wage bill envelope. Staff underscored the need to keep employment numbers in check, as spending pressures could mount once the freezes on automatic increments expire at end 2016. The authorities considered that the moratorium on new hires since 2008 was affecting the provision of public services and there was a need to recruit frontline staff. They also indicated that this issue would be assessed as part of the next Comprehensive Review of Expenditure in 2014. The process by which the IFAC provided the *ex ante* endorsement of the macroeconomic forecast underpinning the budget went smoothly. The slight revision to the growth forecast after IFAC endorsement due to a change in the policy stance was within the expectations of IFAC. Staff suggested that a trigger be considered beyond which a modification to the macroeconomic forecast would need to be consulted with IFAC.

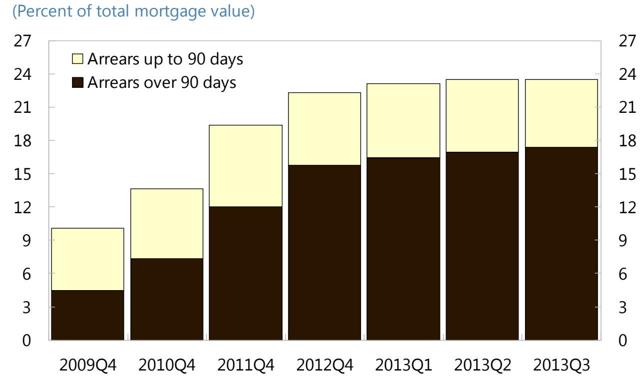
B. Financial Sector Policy

22. **The twelfth review focused on NPL resolution and bank diagnostics**. The mission reviewed ongoing initiatives to drive forward arrears resolution on residential mortgages and SME loans. The mission also consulted on the Balance Sheet Assessment (BSA), reviewing both the process and findings, and discussing the policy actions to follow. It assessed the authorities' recent reviews of bank operating profits and tracker funding solutions that will help inform the development of options to bolster bank profitability, which are especially relevant for PTSB.

Resolving NPLs

23. **The rise in mortgage arrears appears to be slowing and the personal insolvency reforms have become operational**. Mortgages on primary dwelling homes (PDH) in arrears for more than 90 days rose from 15.8 percent of the total value of PDH mortgages outstanding at end 2012 to 17.4 percent at end September, a slower increase than in recent years. The stabilization of house prices and decline in unemployment likely contributed and banks' improved collection efforts also appear to be containing early arrears cases. A small initial number of Debt Settlement and Personal Insolvency

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



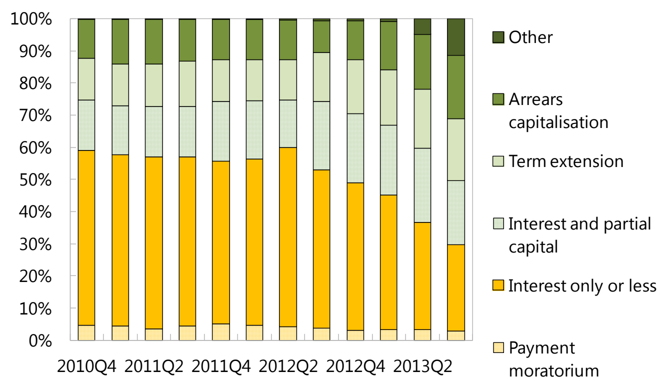
Source: Central Bank of Ireland.

Arrangements are being processed, and the Insolvency Service expects the case load to increase, complementing the other options for case-by-case resolution (Box 4).

24. **Banks are reporting progress in line with the CBI's Mortgage Arrears Resolution Targets (MART) framework yet the use of solutions that are not expected to be durable needs to be averted**.[18] The CBI announced that banks reported they have met the end September target for proposing solutions to 30 percent of mortgages with arrears over 90 days. Proposed solutions involving a loss in ownership for PDH became less prominent, while the portion of long-term loan modifications increased. A third-party audit commissioned by the CBI has reviewed banks' solutions proposed until June, including an analysis of a sample of arrears cases relative to CBI guidelines on sustainable solutions.[19] The audit identified some instances where the proposed situations were not considered sustainable, e.g., a short-term solution was proposed without tangible evidence to expect an improvement in a borrower's debt servicing capacity. The CBI will follow up with lenders on the issues identified by the audit and develop further guidance for future targets, including for solutions concluded. Staff recommends that future audits also assess debt service sustainability.

25. **Overcoming inadequate engagement between banks and borrowers is critical to move from proposals to conclusions in a timely manner**. Banks now face targets to conclude solutions in 15 and 25 percent of mortgage arrears cases by end December 2013 and March 2014, respectively. Banks' improving loan workout efforts are reflected in a lower share of short term forbearance in mortgage restructurings. While roughly half of borrowers seeking loan modifications have no arrears or arrears of less than 90 days, banks note that a large portion of borrowers with longer term arrears are not cooperating, even in cases where repossession has been threatened. A recent initiative by one bank to provide free advice from an independent consumer advocate is a welcome step to promote reengagement. Nonetheless, creating a clear expectation among borrowers that repossession is a consequence for a lack of engagement toward resolution also remains important.[20]

Restructured Mortgages by Type
(Percent of total restructured mortgages on principal dwelling houses)



Sources: CBI; and IMF staff calculations.

[18] The MART framework from March 2013 is described in the staff reports for the Tenth and Eleventh Reviews.

[19] Amendments to the CBI's guidelines on sustainable mortgage arrears solutions allow a significant change in the payment structure for an extended period—such as concessional interest rates for seven years—and remove constraints on the warehoused portion of split mortgages.

[20] In the four years to September 2013, repossessions and voluntary surrenders have totaled 2,384 or just 1.8 percent of all PDH mortgages with arrears over 90 days, which is very low relative to the UK and US.

26. **The authorities are examining the repossession system and procedures to ensure they are efficient and timely and have decided not to proceed with two staff proposals at this time**.[21] Efficient repossession proceedings encourage borrowers to continue debt service or engage constructively when encountering debt distress. The authorities have therefore instituted an expert group to review by year end the length, predictability, and cost of proceedings, and propose appropriate measures to be brought forward quickly where necessary. A new monitoring system for the case load and processing times of repossession cases is being considered in this context. In the interim, the authorities assessed two options proposed by staff, but they decided to not proceed at this time:

- ***Assigning Specialist Judges to also deal with repossession cases***. The authorities' assessment notes synergies with judicial consideration of personal insolvency proposals and the potential to increase judicial capacity to deal with repossessions. But it deems the measure untimely as the case load is still manageable and recourse to repossession may be contained by the comprehensive set of recent reforms to facilitate loan modification.

- ***Introducing tight deadlines on plenary proceedings for non-principal private residences***. Under this proposal, procedures would be further streamlined, building on the positive experience with expedited proceedings in the Commercial Court. While such rules could be established under the powers of the court's Rules Committees, the authorities do not deem this measure necessary unless bottlenecks within the courts system are being expected.

27. **Staff considers that intensified efforts are needed to reach the goal of largely completing sustainable solutions for mortgage arrears by end 2014**. In late 2013, the CBI is expected to announce end June 2014 targets, where targets may need to be adapted to allow an increased focus on completions. On the bank side, incentives to offer durable restructurings should be reinforced by introducing rules-based policies on the accounting for provisions, charge-offs, and interest accrual for unrestructured loans with prolonged arrears at end 2014. Where a bank falls materially behind targets, more directive supervisory guidance on resolution or outsourcing of workouts may be needed, where staff supports any needed strengthening of CBI powers. Measures to strengthen borrowers' engagement toward sustainable solutions are needed, combining information and incentives. Implementation of measures to be developed by the expert group on repossession is critical and lenders should have in place a strategy to address potential shortfalls from voluntary surrenders of collateral. For cases where a loss of ownership is unavoidable, enhanced support for mortgage to rent solutions would help contain social costs.

28. **The workout of SME arrears is also progressing and staff urges consideration of streamlining procedures for SME examinership**. SME loan restructuring is progressing with the number of loan restructures substantially exceeding cases of legal enforcement. Both banks that dominate SME lending have met their end June and September workout targets set by CBI. The

[21] For background on enhancing the efficiency of the repossession regime, see Box 4 in the Ninth Review.

CBI remains closely involved in assessing progress and reviewing banks' operational effectiveness in SME loan workouts. To permit small businesses to apply for examinership in Circuit Courts, where legal fees are generally lower, the authorities intend to fast track recently published amendments to the Companies Bill with the aim to enact them before the end of 2013. This is a welcome step forward, yet further gains could be realized by further streamlining the role of Courts in examinership, drawing on experience with the Insolvency Service for households.

Bank Diagnostics

29. **The BSA has been implemented by the authorities and independently validated yet uncertainties remain, including owing to limited resolution experience in Ireland**. Focused on the three PCAR banks, the BSA analyzed the adequacy of provisions on an IFRS incurred loss basis and the appropriateness of internally generated Basel risk weights, which fed into a point-in-time assessment of capital as of June 2013 (Box 5). As envisaged, the CBI-led exercise engaged private sector contractors in project execution and a consulting firm for oversight and independent validation. EC/ECB/IMF staff were consulted on the methodology and updated on its implementation. The BSA took time to get underway, however, and with the second round of loan file reviews still in progress, the preliminary BSA report provided at end October was not complete. The analysis was completed during November and has been independently validated as having followed an appropriate, conservative and robust process in line with its terms of reference. Nonetheless, such analysis is by its nature subject to uncertainties, which may be more acute in this case given the lack of experience in Ireland with recovery of loan collateral—including as a result of past unintended legal impediments to repossessing residential property—together with risks to the durability of ongoing residential and SME loan modifications, for which there is also limited experience. The authorities will undertake further analysis in close cooperation with the ECB, as the ECB conducts its Comprehensive Assessment.

30. **The BSA finds a significant increase in provisioning is appropriate but this analysis does not imply an immediate need for capital**. The finding that higher provisioning levels are appropriate in some portfolios primarily reflects issues with collateral valuation and lack of seasoning for restructured loans that are now more appropriately classed as impaired, consistent with the May 2013 update of the CBI's Impairment Provisioning and Disclosure Guidelines. At the same time, standardized probabilities of default and recovery values indicate somewhat higher risk weighted assets for some of the banks. Nonetheless, given the higher reported average capital ratio of 14.1 percent as of June 2013, the BSA results do not imply a capital need, with the point-in-time assessment of capital adequacy estimated to remain above the regulatory floor of 10.5 percent on a core tier 1 basis. Nonetheless, these BSA results are on an incurred loss basis, and do not exclude the potential for a capital need to be identified in the forward looking part of the Comprehensive Assessment being conducted by the ECB in 2014, though some buffer is provided by the 8 percent common equity tier 1 capital floor announced for the AQR.

31. **Banks need to use the BSA results to guide a reallocation of their risk buffers from capital to provisions, which will also encourage more timely loan resolution**. The BSA will inform the CBI's continuing supervisory dialogue with each of the banks on the adequate level of provisioning at year end. Considering the evidence provided by the loan file reviews and

provisioning model reviews that take account of the updated CBI provisioning guidelines, banks will need to consider the BSA results carefully when preparing their end 2013 financial statements, and will be aware that the CBI will also use the BSA results as a benchmark in its annual ex post review of provisioning adequacy. In relation to risk weighted assets, the CBI will issue risk mitigation actions to banks as needed for implementation by end December 2013. The CBI will also draw on the qualitative findings of the BSA to guide its supervisory focus.

32. **The needed strengthening in bank profitability is sensitive to the macroeconomic outlook, including any recovery in credit demand**. The CBI completed its review of bank operating profits at end September (structural benchmark).[22] Both BoI and AIB show steady improvements in net operating income, whereas PTSB is not expected to achieve positive net operating income until 2014 and positive net income after provisioning expenses until two years later. The analysis highlighted the sensitivity of the improvement in bank profitability to prospects for new business volume, repricing of loans, and funding costs—each of which will depend on the macroeconomic environment and progress in balance sheet repair. A key weakness in the analysis owing to banks' data deficiencies is the failure to assess revenue contributions from nonperforming, modified, and forborne loans, as the banks continue to accrue and capitalize an unspecified amount of interest income that is not actually paid.

33. **The review of options to fund tracker mortgages at a lower cost identified significant implementation challenges**. In aggregate the PCAR banks hold €48 billion in tracker mortgages in Ireland and a further €21 billion in the UK, with an average margin of 100 basis points over the policy rates of the ECB and Bank of England respectively. Declines in these policy rates had outpaced reductions in bank funding costs, resulting in a significant cost of carry for tracker mortgages, although the profitability drag has eased somewhat with recent declines in deposit and market funding rates. Further technical analysis by the authorities of options to lower these funding costs explored the potential to pool loans indexed to policy rates into government-guaranteed asset backed security structures for repurchase with various counterparties. The analysis suggested that maximizing net income benefits would require the inclusion all of these assets in the repurchase structure. However, attracting funding from private counterparties at sufficiently low rates will be challenging.

34. **PTSB still needs external support to become a sustainable source of lending in support of Ireland's recovery**. PTSB is projected to run persistent losses until 2017 owing to high NPLs and tracker mortgages exceeding half of total assets. With assets of €38 billion or 23 percent of GDP, and a heavy market discount on its loan book, resolution would have a large fiscal cost. Accordingly, PTSB's restructuring plan, yet to be approved by the European Commission, envisages a split—in anticipation of which the bank has been internally separated into a core retail banking and an asset workout unit and a non-core unit. Executing this planned legal separation requires an affordable funding solution for the workout operation. European

[22] The analysis does not reflect the Budget 2014 levy on banks—both domestic and foreign owned—which is expected to total some €150 million annually.

support could take the form of official funding or guarantees to facilitate low cost market funding—both of which would hasten the bank's return to profitability, thereby enabling it to rebuild its market position and eventually attract private investor interest.

C. Structural Reforms

35. **The authorities are advancing steps to combat high unemployment and staff continued to urge stronger engagement with the long-term unemployed**:

- ***To enhance employment services the authorities are rolling out Intreo offices, redeploying staff, and tendering for private sector providers.*** Some 43 Intreo offices providing integrated employment services will be opened by end 2013, in line with the target set by the Pathways to Work plan. Of the doubling in front-line case officers, all have been identified and about half have been reassigned, in line for reaching the target of 300 staff redeployed by year end. Preparations have continued for the tender for private sector employment service providers expected in early December, with it envisaged that payments for activation services for the long-term unemployed will be outcome-based. However, initial targets for one-on-one engagement with job-seekers for Q3 were slightly missed, and staff urged more ambitious targets for individual and group engagement with jobseekers.
- ***Staff welcomed the strategic priorities set out by the review of Further Education and Training policies and emphasized the need for timely implementation***. Better aligning training services provided with the needs of prospective employers will improve benefits for the long-term unemployed. This requires (i) better local labor market intelligence and data collection; (ii) more systematic involvement of private sector parties in the design and delivery of the training program; and (iii) more flexible provision of shorter duration work placements and on the job training involving private sector providers. The review also emphasized the need to strengthen the strategic cooperation between SOLAS, local Education and Training Boards and local Intreo offices.
- ***Sanctions for uncooperative jobseekers have been reviewed but their application should be strengthened***. Legislation enacted in July 2013 extended the form of sanctions and the range of circumstances in which sanctions could be applied, allowing social payments to be reduced incrementally for job seekers failing to engage with activation activities. Following an increase in the number of sanctions, attendance at group and individual engagements had increased. Nonetheless, staff noted that the number of penalties applied overall remained small and encouraged more effective steps to maximize jobseekers engagement.

36. **Preparations for the disposal of up to €3 billion in state assets are proceeding yet an initial transaction was not concluded**. The sale process for Board Gáis Energy attracted significant interest from a broad range of potential international acquirers. However, the authorities determined that none of the final bids received were at an acceptable value, noting that current conditions in the power and commodity markets were not favorable. The authorities indicate that they will continue developing the Bord Gáis Energy business and will review options for its future. EBS has sold its 50 percent stake in a UK-based company and the sale of its stake in a Spanish company is expected in early 2014. The growth enhancing projects to be funded with up to half of the resulting sales proceeds via public-private partnerships are under preparation,

with 6 out of the 9 projects announced due to be tendered in the coming months. The €150 million in budget resources assigned to these investments will be spent on road construction, school buildings and retrofitting of public buildings.

37. **Initiatives to improve the financing conditions for the SME sector are being rolled out**. In anticipation of the establishment of the Ireland Strategic Investment Fund, the National Pension Reserve Fund has committed, in partnership with private sector players, up to €950 million in investments dedicated to providing equity financing and new lending to SMEs. A large number of potential transactions are at various stages of underwriting. Separately, the Credit Review Office will now be able to review loan applications rejected by banks for amounts up to €3 million rather than €0.5 million.

PROGRAM MODALITIES AND FINANCING

38. **All end September quantitative performance criteria were met but performance related to the structural benchmarks was mixed** (Tables 11–13). The January–September exchequer primary deficit of €2.3 billion was well within the adjusted target of €3.7 billion.[23] The indicative target on the stock of central government net debt was also met with a margin. The end September benchmark on conducting a forward-looking analysis of PCAR banks' operating profits was partially observed due to a significant shortfall in relation to the analysis of revenue contributions from nonperforming, modified, and forborne loans owing to weaknesses in banks' information systems. The authorities published Budget 2014 by October 15 in line with the corresponding structural benchmark. A preliminary BSA of the PCAR banks was provided at end October, although it was not complete, but the structural benchmark was observed by late November.

39. **The significant volume of funding activity earlier this year helped build a sizeable cash buffer and Ireland remains comfortably financed through 2014**. Syndicated bond sales in January and March totaled €7.5 billion and the disposal of Irish Life and BoI contingent capital notes generated a further €2.3 billion. End-year cash buffers are projected at some €20 billion, covering more than 12 months of prospective financing needs. In light of the NTMA's relatively strong cash position, in October the authorities decided to suspend monthly Treasury bill auctions for the remainder of 2013 and to defer consideration of any further bond issuance until 2014. Looking ahead, the authorities indicate long-term bond issuance in 2014 of €6–10 billion taking into account an exchequer funding need of about €9½ billion, while the cash buffer could be partially drawn down, especially to meet a €6.9 billion bond redemption in January 2014.

40. **Recognizing the significant challenges remaining, the authorities are preparing a Medium Term Economic Strategy (MTES) for 2014–20.** The MTES is intended to provide a robust framework to ensure that policy efforts are consistent and are aligned in a manner that

[23] Adjustments reflected the underperformance of revenues, ELG payments related to the Promissory Notes transaction, and proceeds from the sale of BoI contingent convertible notes and Irish Life.

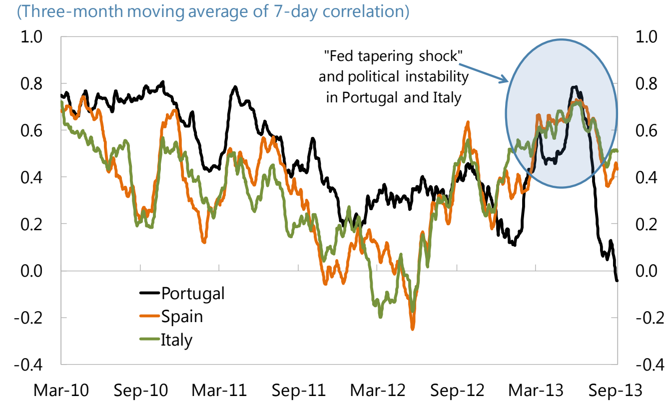
will provide financial market stability and also underpin consumer and business confidence for investment. The strategy will focus on three pillars: macro-fiscal, structural, and financing. A macro-fiscal pillar will analyze possible economic policy measures and the conduct of fiscal policy under SGP requirements, and within these constraints consider how revenue and expenditure policies can best promote economic growth. The structural pillar will focus on raising potential growth, including through policies in relation to industry/innovation, labor markets including the long-term unemployed, education and skills, competition and taxation. A sectoral element will address growth impediments and provide a framework within which existing sectoral strategies operate. Broad consultation on the MTES is ongoing with a view to completing it before the end of 2013. As a strategy of the government, the MTES is expected to be monitored and reported to the government over time.

41. **After wide consultation, the Irish authorities have decided to not seek a financing backstop after the expiry of their current EU-IMF arrangements**. Given uncertainties remaining for Irish and European prospects, and in the global economy more broadly, staff noted that such a backstop could cushion financing against a range of potential risks in the immediate post-program period. While recognizing these potential insurance benefits, the authorities also took note of their strong cash buffer and reasonable terms for market access, their reduced financing needs owing to the extension of EFSF/EFSM loan maturities and the Promissory Notes transaction, and their intention to signal their commitment to steadfastly address remaining challenges through their MTES. On balance, the authorities consider that this combination of safeguards will ensure a durable return to market financing, but they also take comfort from the evolution of the European framework in recent years including the establishment of the ESM.

42. **Though subject to significant risks, the exceptional access criteria continue to be met**:

- ***Debt sustainability and the systemic risk exception***. Under the baseline macroeconomic framework, debt sustainability is expected to be maintained over the medium term, although it continues to be subject to significant risks if growth does not strengthen as anticipated or if further contingent liabilities materialize. Crucially, this relies on ongoing steadfast policy implementation, along with European policymakers' delivering on their commitments to reduce strains in countries facing stress and ensure financial stability in the euro area. As debt sustainability is not assured with a high probability, the program continues to be justified on the basis of the systemic international spillover risks posed by Ireland. Given Ireland's strong financial and

Correlation of 10-year Yields of Ireland with Other Countries
(Three-month moving average of 7-day correlation)



Sources: Bloomberg; and IMF staff calculations.

trade interlinkages, most notably with the euro area and UK, the risk of significant potential spillovers should Ireland face financing pressures remains, especially as Ireland is perceived in markets as having performed well under its EU-IMF supported program. Such spillover risks would be heightened in period of international financial volatility, when linkages for spillovers can strengthen—this was evident most recently during the period of uncertainty around tapering by the US Federal Reserve.

- ***Adequate prospects to retain and expand market access***. In view of Ireland's strong program performance and commitments and its regained market access, there are adequate prospects to retain and expand access to private capital markets within the timeframe over which Fund resources will remain outstanding, yet this access remains at some risk over time:

  - **On a range of indicators Ireland currently has gained solid market access**. Since mid 2012, Ireland has issued debt ranging from Treasury bills to bonds at 5 year, 8 year, and 10 year maturities, and has also sold longer-term amortizing bonds designed for the domestic pensions industry. The 10 year benchmark issue on March 13, 2013 raised €5 billion on the back of total bids of €13 billion from about 400 investors, the majority of whom were European, especially UK, German, Nordic and French, with further uptake by Irish residents and US investors. Investors included fund managers, banks, pension funds, and insurance companies. Ireland enjoys yields significantly below those of Italy and Spain which have strong market access.

  - **Market access is expected to be retained, subject to risks linked to the fragility of debt sustainability**. The volume of market financing needed appears manageable in 2014–15, and while these requirements increase from 2016 onward they are still not a major share of the debt stock. It appears reasonable to expect Ireland to retain market access in the baseline scenario of declining debt ratios, while recognizing that the risks to debt sustainability from growth and contingent liabilities also imply risks to market access. In particular, there is a risk of inadequate European support for potential remaining challenges in Ireland's financial sector during the ECB's Comprehensive Assessment in 2014, despite the availability of the ESM direct recapitalization instrument under the November 15 ECOFIN Council statement, which would weaken the assurances of adequate and durable market access given Ireland's public debt vulnerabilities.

- ***Sound policies***. Ireland's policy program is sound and adjustment is being delivered, providing reasonable prospects for success. More effective policy action and delivery on commitments at the European level is needed to strengthen prospects for success.

STAFF APPRAISAL

43. **Steadfast policy implementation has been maintained through the final review of Ireland's program and signs of nascent recovery are emerging.** The first half of the year was characterized by mixed signals, with weak GDP figures partly related to the "patent cliff" affecting pharmaceutical exports occurring alongside significant growth in private sector employment.

More recently a range of indicators signal that Ireland is completing its EU-IMF supported program with the potential for a more sustained recovery.

44. **Significant risks to Ireland's growth prospects and to debt sustainability remain nonetheless, requiring concerted policy implementation progress**. Setbacks to the recoveries in major trading partners would hurt exports, with adverse effects on confidence and domestic demand. Sustaining a recovery into the medium term will increasingly depend on a revival of lending to households and SMEs, which would be at risk if banks fail to address high nonperforming loans and weak profitability. High nonperforming loans imply that contingent liabilities in the financial sector remain a risk to debt sustainability and these risks rise in an environment of weak growth owing to declining loan performance and collateral values. Accordingly, as recognized by the authorities' ongoing preparation of a Medium Term Economic Strategy, Ireland must maintain determined efforts to address its high public debt and deficit levels, heavy private sector debt burdens, financial sector repair needs, and substantial long-term unemployment before it can be judged to have fully recovered from the crisis.

45. **Steady fiscal consolidation, which has been a hallmark of the program and key to restoring Ireland's policy credibility, needs to continue**. Budget execution has once more been solid in 2013, including the smooth introduction of the local property tax and the social cohesion demonstrated by reaching the Haddington Road agreement on public sector pay and pensions. Budget 2014 sets out a path with a balanced pace of adjustment in coming years that is expected to put public debt on a declining trajectory, though subject to risks from growth prospects and contingent liabilities. Continued sound implementation of fiscal consolidation will be especially critical after the completion of the program. Looking to the medium term, the further consolidation needed should be centered on reforms of health, education, and social protection spending that realize durable savings while protecting core services and the most vulnerable. Revenue increases should focus on broadening the tax base.

46. **Intensified efforts are needed to reach the goal of largely completing sustainable solutions for mortgage arrears by end 2014**. Although the rise in mortgage arrears appears to be slowing, the stock of distressed mortgages remains unacceptably high. The initiation of operations by the Insolvency Service is a welcome step to create new resolution options and establish useful precedents for solutions. Banks report they are meeting CBI targets for proposing solutions, yet there are concerns that a portion will not prove sustainable. Moreover, after a prolonged period of forbearance, restarting the engagement between banks and borrowers needed to conclude solutions is proving difficult. Making progress will involve both providing supervisory guidance to ensure that banks adjust their solutions to address household's circumstances in a lasting manner, while also providing households and buy-to-let investors with appropriate information and incentives to engage. In particular, timely and predictable repossession procedures are needed to help promote engagement on loan modifications and also help ensure that such modifications can provide lasting resolution at manageable cost. For cases where retaining ownership is not sustainable, enhanced support to facilitate mortgage to rent and other solutions that contain social costs is appropriate.

47. **The quantitative and qualitative findings of the bank BSA should inform the CBI's supervisory work and banks' preparations for the ECB's upcoming Comprehensive Assessment**. The Balance Sheet Assessment independently assessed loan classification, quantified incurred loan losses, and reviewed risk weights. It is vital that the CBI ensures that banks increase provisioning for some portfolios in line with the findings of the assessment, which will also improve incentives for loan workout. Nonetheless, uncertainties remain, including owing to the limited experience with loan resolution in Ireland and also with respect to the potential findings of a forward-looking assessment of profitability and loan losses. Given Ireland's still fragile debt sustainability, an ESM direct recapitalization backstop to the ECB's Comprehensive Assessment would be desirable to protect market confidence and financial stability.

48. **Reviving lending in coming years remains important to sustain a recovery in domestic demand, where external support could play a critical role**. Encouragingly, the two larger domestic banks appear to be returning to the profitability needed to support lending, although risks remain to their profitability prospects. However, PTSB is not expected to break even after provisioning expenses until 2017 given its heavy exposure to tracker mortgages, limiting its potential to rebuild its market position and attract private investment. With other banking systems in the euro area also facing challenges that hinder credit expansion, a European solution to better align bank funding costs with official interest rates would facilitate recovery in the euro area as well as Ireland.

49. **Reducing high unemployment must remain an overarching policy priority**. Initiatives to promote credit to SMEs, with the support of European partners, are positive for investment and job creation. Yet it is also important to ensure SMEs are creditworthy through banks completing resolution of SME loans in arrears and also by facilitating SME restructuring where needed, including by considering further streamlining the role of courts in SME examinership. Efforts to strengthen employment services for jobseekers should continue in order to achieve adequate engagement, with further redeployment of staff needed in addition to bringing in private sector providers. Timely initiatives to achieve the strategic priorities set out in the review of Further Education and Training are critical to better align training with the needs of the economy and especially to ensure the long-term unemployed gain skills enabling them to return to work.

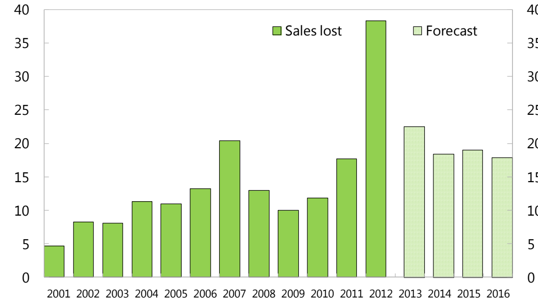
50. **On the basis of the progress made under Ireland's program, staff supports the authorities' request for completion of the twelfth review**. Staff also recommends that Ireland be brought back to the standard 12-month consultation cycle for Article IV consultations upon expiration of the Extended Arrangement. In accordance with Executive Board Decision No. 14747(10/96), Ireland shall be placed on a 12-month consultation cycle because it currently has an outstanding Fund credit exceeding 200 percent of quota. In light of the amount of the outstanding credit, and given that the authorities have decided not to request a successor arrangement from the Fund, the Managing Director also recommends the initiation of post-program monitoring.

Box 1. The Impact of the "Patent Cliff" Revisited

Ireland is a leading exporter of pharmaceutical products and the sector accounts for a quarter of total exports. Nine out of the top ten pharmaceutical companies are located in Ireland, and seven of ten blockbusters (global benchmark products generating annual sales over 1 billion) were produced in Ireland in 2011.

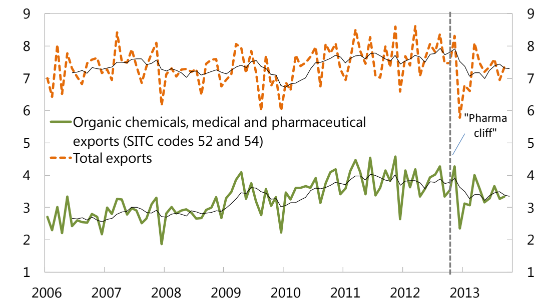
The global pharmaceutical industry had an exceptional year for patent expiry in 2012. Accenture evaluated the impact of patent expiry in terms of global lost sales at US$38 billion in 2012 compared with around US$20 billion per annum thereafter, highlighting 2012 as an exceptional year relative to a yearly run-off in the US$10-20 billion range.

Global Pharmaceutical Sales Lost Due to Patent Expiry
(Billions of US dollars)



Source: Accenture.

Monthly Pharmaceutical Exports and Total Exports
(Billions of euros, with 6-monthly moving average)



Sources: CSO; and Haver Analytics.

Ireland's pharmaceutical exports have registered a significant contraction since mid-2012 as a set of blockbuster drugs manufactured locally went off patent. This "patent cliff" resulted in a 6.7 percent y/y contraction of pharmaceutical exports in value over the first nine months of 2012. While some slowdown in contraction was visible in H1 2013, the year-on-year decline resumed again in value terms in Q3 2013.

Uncertainty remains as to the overall economic impact of these developments. Preliminary analysis suggested that the impact on net trade should be dampened by the high import content of blockbuster drugs (in the form of royalties paid to the mother company as well as other chemical imports for intermediate consumption), and by the comparatively small contribution of the sector to total employment in Ireland. More recent analysis by Department of Finance staff provides illustrative simulations based on the overall estimation of the remaining impact of patent expiry for the industry. In case pharmaceutical exports decline 4 percent annually through 2014, they estimate a cumulative GDP loss of 2 percent over 5 years, while if the pace of decline is 8 percent annually, the cumulative GDP loss is 4 percent.

Moreover, the national accounts impacts are affected by firm's accounting models. Research by ESRI illustrates how the national accounts impacts are affected by whether pharmaceutical firms booking their profits locally versus making royalty payments to their multinational parent. When the patent expiry impacts royalty payments, the offsetting changes in exports and imports yield little net effect on GDP. When profits are booked locally the patent expiry reduces exports, net trade, and GDP but the fall in profit outflows dampens the impact on GNP and the current account. Irrespective of the accounting treatment used patent expiries are unlikely to have a large effect on GNP, as the sector is dominated by foreign-owned companies.

Although patent expiry is a drag on prospects for the pharmaceutical sector, investments in new areas signal opportunities for expansion. Ireland's competitiveness in the sector is underpinned by a stable regulatory environment, strong human capital and efforts made to improve the investment climate, notably for R&D. Irish based subsidiaries are being gradually refocused towards higher-value "niche" products like biopharmaceuticals, where Ireland already has 10 large scale biopharmaceutical facilities. Biopharmaceuticals, though more R&D intensive, have shorter development and testing cycles, and in some cases faster regulatory approval. Investment plans total €2 billion over the next three years after €1 billion over the last three years. The industry expects these "nichebusters" (for global sales between US$½-1 billion) should help improve pharmaceutical company business models in the long run through a more diversified supply of drugs, and a lesser reliance on blockbuster revenues.

Box 2. Mortgage Arrears Resolution and Consumption

In considering the implications of mortgage loan restructuring for household consumption, it is important to distinguish the effects of high household debt from those of arrears. In Ireland, many households are highly indebted and are saving to reduce their debts, which has a first order impact on aggregate consumption. The vast majority of these households will not have access to any form of resolution as their adjustment in living standards is sustainable. Resolution efforts affect about 6 percent of households in arrears and possibly some other households in distress that are not yet in arrears, but—consistent with the slowing in new arrears cases—these are not expected to be substantial relative to the stock already in arrears.

The net direct impact of mortgage restructuring depends on the status of the households affected, especially whether they are already receiving forbearance:

- ***Relief of debt overhang***. For households making significant payments under strain a restructuring that reduces due debt service in line with affordability may reduce uncertainties and raise consumption. CBI analysis suggests that households with debt problems spend 18 percent less on consumption controlling for other characteristics, though there is the possibility that this finding is driven by unobserved factors.

- ***Unwinding of forbearance***. Widespread forbearance, including temporary restructures, helped some households to smooth consumption at a time when incomes were falling sharply.[1] Converting households back into paying borrowers according to a sustainable debt service schedule could reduce income available to consume, even where the total debt being serviced is cut significantly.

Estimates suggest that the aggregate near term direct impact on consumption is likely to be small. A rough estimate of the impact of the flow of arrears plus debt service savings provided by temporary restructures is €1.2 billion (1½ percent of consumption). The portion of this forbearance that would be expected to be paid under sustainable loan terms is difficult to estimate, but even if it were as high as one-third or one-half, the drag on consumption would not be large, and would be counter balanced to some extent by other households in distress receiving some debt relief.

In the medium term, any direct impact from loan resolution on consumption is expected to be outweighed by second round benefits from reducing uncertainties for borrowers and lenders:

- ***Resolving household NPLs could improve confidence in banks' balance sheets***. The extent and the depth of mortgage arrears—one third of defaulted loans have not been serviced for two years or longer—in part explains banks' less favorable funding conditions, as reflected in the pricing of covered bond issues and the high degree of over collateralization required. Durably reducing mortgage NPLs could improve market confidence in the quality of banks' loan books, in turn reducing market funding cost and making a restart of bank lending a profitable proposition.

- ***Reducing non performing mortgage loans could also support housing demand***. While repossessions may add to housing supply over time, resolving unsustainable mortgage loans could reduce concerns about a large "shadow inventory" from underwater mortgages that deters potential buyers. As three-quarters of Irish households own their homes, reduced uncertainty around the value of these assets could support consumption by reducing precautionary saving.

[1] The CBI reports that for distressed borrowers, debt service represents a remarkably small portion of current income for a relatively high fraction of borrowers, with available income after living expenditures sufficient to meet all debt service in 17 percent of distressed households.

Box 3. Fiscal Measures in Budget 2014

Achieving the 2014 deficit target entails the implementation of €2.7 billion in total consolidation. This includes €1.2 billion in new measures, €1.3 billion in carryovers from policies implemented in previous years (most notably the additional yield in 2014 from the local property tax and the reduction in the standard fund threshold for pensions, together with additional savings from the Haddington Road Agreement), and €0.2 billion in the form of higher dividends from state-owned enterprises. Two-thirds of the total consolidation effort will fall on spending.

Revenue measures include both the broadening of the tax base and rate increases. However, some of the proceeds will be offset by the retention of the reduced VAT rate in labor intensive services mainly in tourism of 9 percent that was to expire at end-2013 (0.2 percent of GDP). The package also includes measures to stimulate the economy through tax relief targeted at the tourism, agri-food, construction and property sectors and startups. The cost of these measures is expected to be modest based on preliminary estimates, with the impact mostly felt in 2015. Base broadening steps include: (i) the introduction of a levy on financial institutions, while removing the restriction on the use of deferred tax assets for losses on assets transferred to NAMA; (ii) making the tax credit for single parents available only to the principal carer of the child; and (iii) restricting the tax relief for medical insurance. Rate increases include: (i) the introduction of an additional pension fund levy of 0.15 percent for 2014 and 2015; (ii) raising rates on the deposit income retention tax to 41 percent; and (iii) increasing excise duties on tobacco and alcohol.

Savings from New Revenue Measures in Budget 2014

	€ million	Base	Rate
Income tax	**216**		
One-parent family tax credit	18	↑	
Medical Insurance tax relief	94	↑	
Deposit income retention tax	105		↑
Stamp duties	**285**		
Bank levy	150	↑	
Pension levy	135		↑
VAT	**-313**		
Retention of 9 percent reduced VAT rate	-290	↓	
Other	-23		↓
Excise duties	**132**		
Air travel tax	-28		↓
Alcohol and tobacco	161		↑
Other	**29**		
Total	**350**		

The package for current expenditure collects a range of measures, mainly in health and social protection. Savings in the health sector (€0.4 billion excluding pay-related savings) are to be achieved through a reduction in drug costs, the enforcement of medical card eligibility requirements, and an increase in prescription charges, among others. While protecting basic social welfare rates, measures in social protection (€0.3 billion) include the elimination of certain schemes (telephone allowance, bereavement grant, and mortgage interest supplement for new applicants) and the reduction of some benefits (maternity benefits maximum rate, jobseeker's allowance for certain recipients aged 22-25, and illness benefit). To support service delivery, additional staffing will be recruited for schools, hospitals and front-line services, but the wage bill is expected to remain within its envelope.

Along with the budget, a new international tax strategy was published. The government's strategy will be to remain active and supportive of the work of the EU and OECD on international tax matters. In addition, changes are to be implemented to ensure that Irish registered companies cannot be "stateless" in terms of their tax residency. The authorities estimate that a limited number of companies have made use of this loophole, so they do not expect any direct budget impact.

Box 4. Case-by-Case Restructuring of Mortgage Loans in Ireland

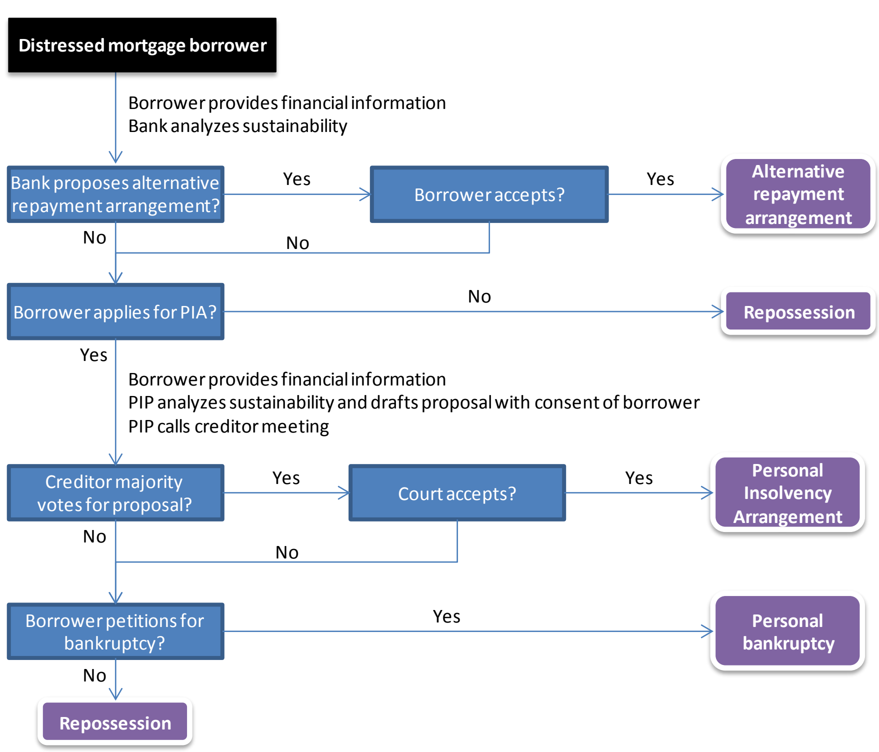
Resolving distressed mortgage debts is guided by a two-step approach to facilitate case-by-case loan modifications before banks can pursue a change in ownership. Borrowers in mortgage distress on personal dwelling homes are protected by the CBI's Code of Conduct on Mortgage Arrears (CCMA), which sets out a clear process towards a bilateral arrangement to address debt servicing difficulties between borrowers and lenders. If the bilateral approach does not succeed, borrowers can apply for a Personal Insolvency Arrangement (PIA) to settle secured debt of up to €3 million. In case neither leads to an acceptable solution or the borrower is uncooperative, lenders can pursue a change in ownership, including repossession. For mortgages on buy-to-let properties, lenders can appoint rent receivers to re-direct rental payments to lenders or pursue repossession.

The terms of loan restructurings are determined by households' current debt servicing capacity after applying ceilings on common expenditure categories. The Insolvency Service Ireland (ISI) has issued detailed guidelines for reasonable household expenditures which provide ceilings for typical spending categories conditional on borrowers' circumstances during the five-to-six year duration of the Arrangement. Banks apply similar internal guidance for determining the terms for bilateral arrangements.

Repossession or a voluntary change in ownership remain as last resort. Given limited scope for schemes such as mortgage-to-rent, which converts repossessed residences into social housing, repossession or voluntary sales remain as last resort to unsustainable borrowers. The full recourse nature of mortgage loans means that banks can collect any shortfall between outstanding loan amount and collateral value. In this case, borrowers can apply for a debt settlement for unsecured debt under the new personal insolvency framework, or avail of personal bankruptcy with a charge off period of three years.

Case-By-Case Workout of Mortgage Arrears in Ireland

(Flow chart for distressed holders of mortgage on principal residences)



Source: IMF staff illustration.

Box 5. Balance Sheet Assessment Methodology

In the second half of 2013 the Central Bank of Ireland undertook a BSA of the three PCAR banks. The exercise assessed the capital adequacy of the banks as of June 30, 2013 on a point-in-time basis, in preparation for the Comprehensive Assessment for the SSM in 2014. To this end, the CBI analyzed banks' loan classification, provisioning, and risk weighted assets and calculated new point-in-time capital ratio. To augment its in-house capacity, the CBI contracted independent consultants to perform loan file reviews and provisioning analysis while a separate independent third party was tasked with guiding the project and validating the exercise as a whole. The main areas of work were:

- ***Loan file reviews***. Combined with tests of data integrity, a two-phased testing of loan files was conducted. It aimed to assess whether banks correctly classify loans by risk characteristics and whether provisions are consistent with IFRS and the CBI's Impairment Provisioning and Disclosure Guidelines as amended at end May 2013. The first phase of reviews covered about 3,500 loan files, including 1,800 residential mortgages and 1,650 commercial connections (commercial real estate, corporate, and SME loans). Issues identified in the first phase guided a second phase of examining 850 additional loans. Both the Irish and the UK loans were included, and the biggest loans within cohorts were examined separately. On average, 93 percent of total loans and receivables are within the scope of the exercise through extrapolation, with only small and highly provisioned portfolios excluded.

- ***Provision estimation***. Using cohorts identified for the loan file review purposes, estimation of any point-in-time provisioning shortfall was performed based on a two part process that considered (i) review of models that determine provisions for collectively assessed loans (e.g., for mortgages); and (ii) sample and extrapolation of reassessed provisioning for individually assessed loans (e.g., the commercial loans).

    - ***Collectively assessed loans***. Independent consultants reviewed banks' collective provisioning models and also developed their own independent frameworks for benchmarking purposes. Such benchmarking used a range of parameter sets including (i) the parameters in the banks models; (ii) common parameters set across banks (emergence period, house price index and peak-to-trough fall, fire-sale discounts, time to work-out, total work-out costs, cure rates) while keeping default probabilities bank-specific. These were compared with banks' own provisioning estimates, accounting for any revisions due to misclassifications and the transition process to full compliance with the CBI provisioning and disclosure guidelines (due at end December). Sensitivity analysis was also performed to determine impact of changes in model parameters.

    - ***Individually assessed loans***. The independent consultants determined differences between their assessment of provisioning and those of the bank for each loan in a sample of individually reviewed loans. Taking into account outliers, the sample results were subsequently extrapolated to the rest of each cohort.

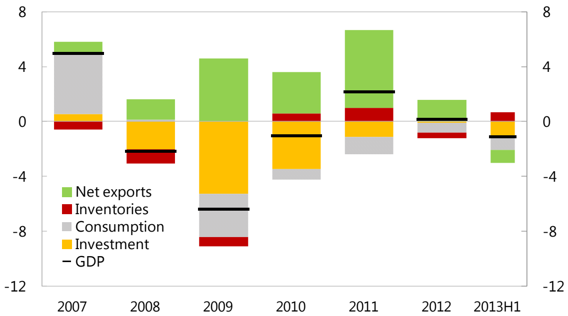
- ***A review of risk weights and risk weighted assets***. The CBI reviewed the appropriateness of banks' risk weighted asset (RWA) calculations based on the Internal Risk Based models for regulatory capital purposes, including key model inputs like Probability of Default or Loss Given Default and other assumptions. The aim of the exercise was to extrapolate changes in risk classification from the review of asset quality to estimate the overall impact on RWAs. Sensitivity analysis with respect to main parameters was also performed.

The results of the review of loan file classification, provisioning, and risk weighted assets were combined to produce a point-in-time capital assessment of each of the three PCAR banks.

Figure 1. Ireland: Real Sector and Inflation Indicators, 2006–13

Net exports became a drag on growth as the "patent cliff" impacted pharmaceutical exports...

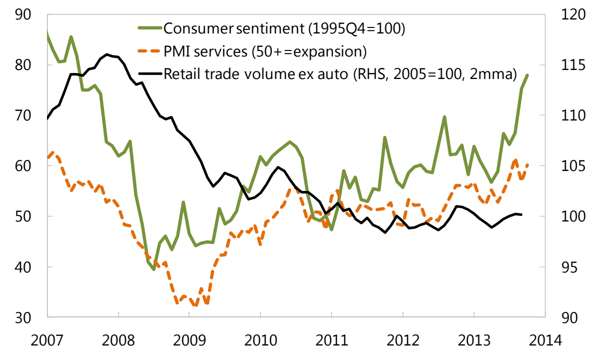
Contributions to Real GDP Growth
(Percent y/y)



Sources: CSO; and IMF staff calculations.

...but high frequency indicators suggest stronger domestic demand with consumer sentiment at its highest level since mid 2007.

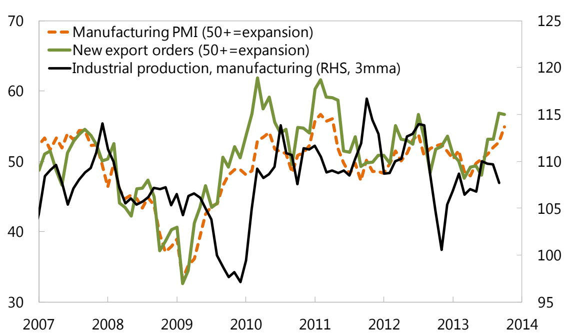
Retail Trade and Sentiment Indicators



Sources: ESRI; NCB Stockbrokers/Markit; CSO; and Haver Analytics.

Export orders are strong and the manufacturing PMI is now firmly into expansion territory.

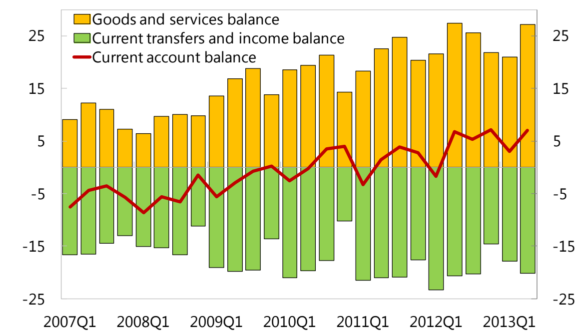
Export Indicators and Industrial Production



Sources: CSO; NCB; and Haver Analytics.

The current account surplus remained strong in H1 as net exports outweighed income outflows.

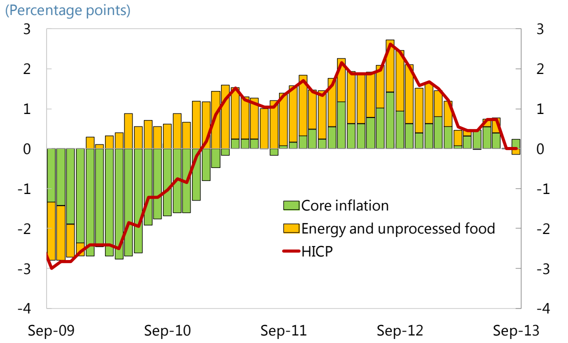
Current Account Balance Composition
(Percent of nominal GDP)



Sources: CSO; and Haver Analytics.

Inflation was absent during August-October owing to falling goods prices possibly due to euro appreciation.

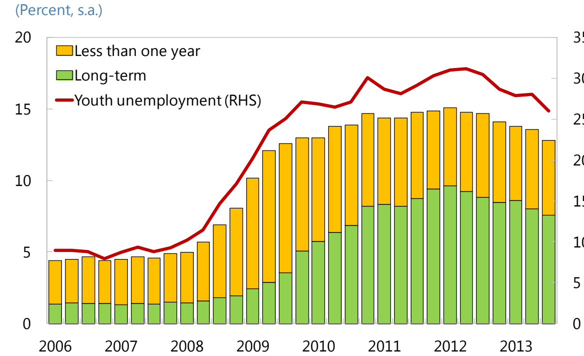
Contribution to Annual HICP Inflation
(Percentage points)



Sources: CSO; and IMF staff calculations.

Unemployment eased to 13.7 percent in Q2, with youth unemployment increasing towards 29.6 percent.

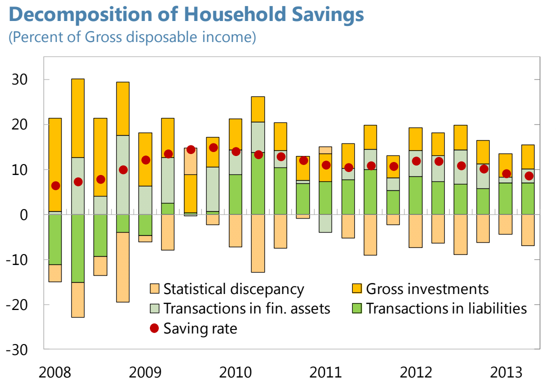
Unemployment Rates
(Percent, s.a.)



Sources: CSO; and Haver Analytics; and IMF staff calculations.

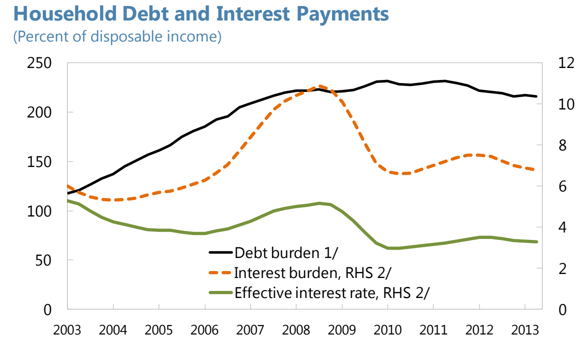
Figure 2. Ireland: Household Finance and Housing Developments, 2003–12

Household savings remain elevated, with three-quarters of savings devoted to debt reduction since 2010…



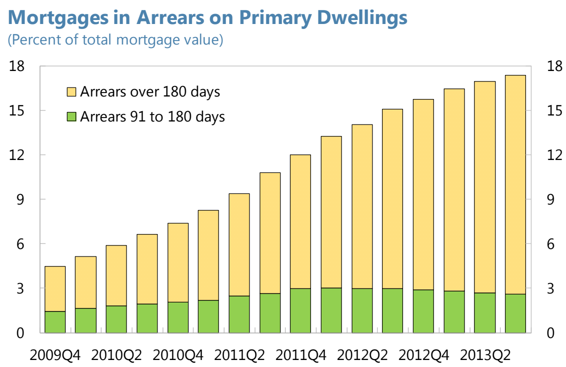
Sources: CBI; Eurostat; Haver Analytics; and IMF staff calculations.

…but household balance sheets remain burdened with high debt, although interest payments are low.



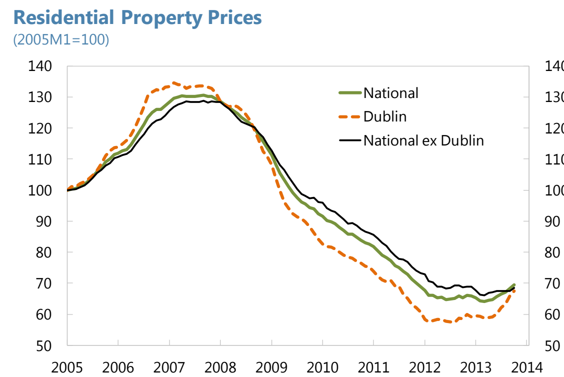
Sources: CBI; Haver Analytics; and IMF staff calculations.
1/ Total household liabilities in percent of four-quarter gross disposable income.
2/ Four quarter interest payments (excluding FISIM adjustment) in percent of four-quarter gross disposable income or previous quarter's total household liabilities, respectively.

Mortgage arrears continue to increase, although the flow of new arrears is abating.



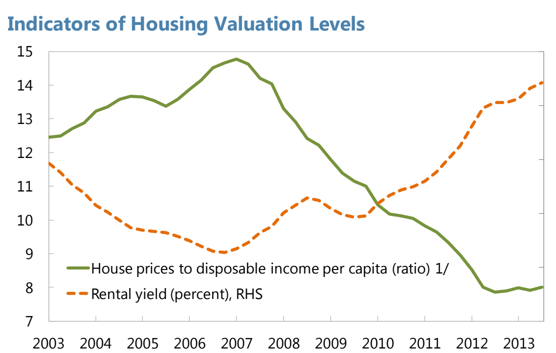
Source: Central Bank of Ireland.

Nationwide property prices are rising driven primarily by strong gains in the Dublin market while prices in the rest of the country have been edging up since March.



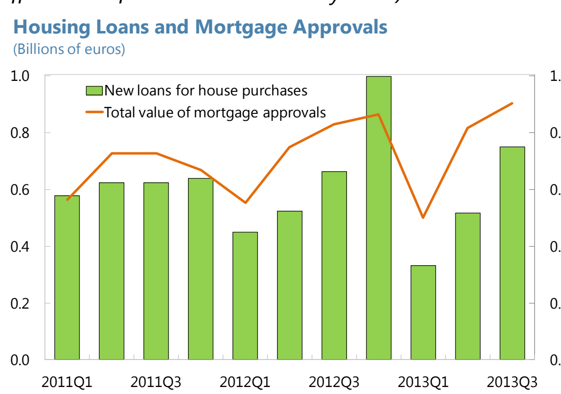
Sources: CSO; and Haver Analytics.

Rental yields stand at their highest level in ten years, suggesting favorable housing valuation.



Sources: PTSB/ESRI; CSO; and Haver Analytics.
1/ Average house prices divided by moving 4-quarter adjusted GDI per capita.

New mortgage lending rose in Q3 to be up 12.5 percent y/y. (The expiry of mortgage interest tax relief at end 2012 affects data for late 2012 and early 2013).



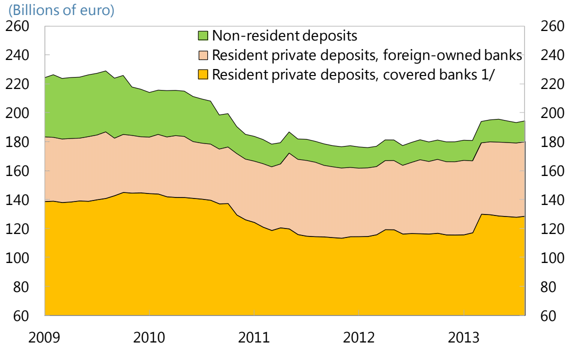
Source: Irish Banking Federation.

Figure 3. Ireland: Credit Developments, 2003–13

The level of private sector deposits has stabilized…

Bank Deposits

(Billions of euro)



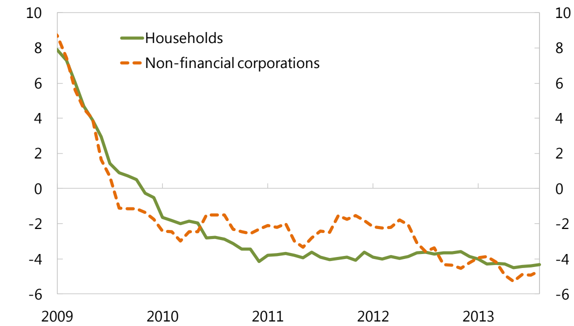
Source: Central Bank of Ireland.

1/ Credit institutions covered by the Irish Government Eligible Liabilities Guarantee Scheme.

…but deleveraging continues and credit to households and corporations continue to contract at a 4 percent y/y rate.

Loans Outstanding to Irish Residents

(Year-on-year percentage change)

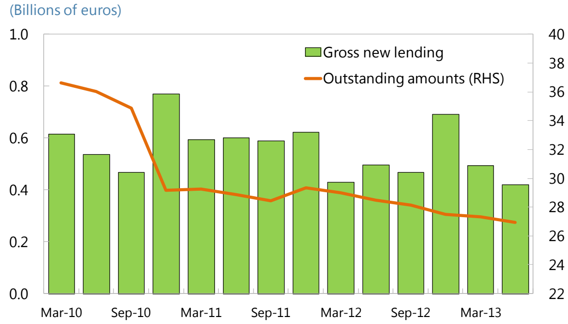


Source: Central Bank of Ireland.

Total SME outstanding credit is steadily declining…

Outstanding SME Credit 1/

(Billions of euros)



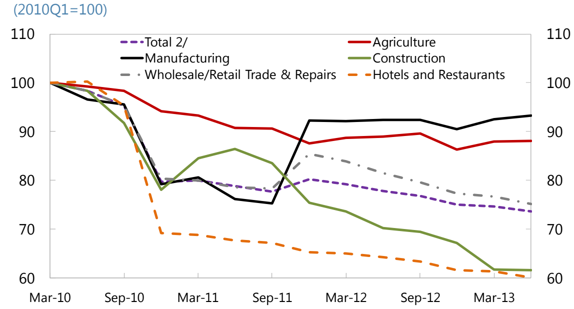
Source: Central Bank of Ireland.

1/ All resident credit institutions, excluding real estate and financial intermediation.

…across all sectors, though to a lesser extent in manufacturing and agriculture.

Outstanding SME Credit by Sector 1/

(2010Q1=100)



Source: Central Bank of Ireland.

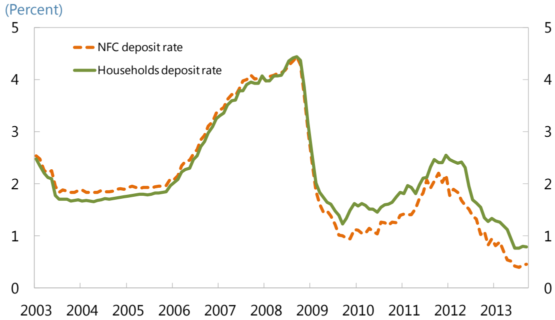
1/ All resident credit institutions.

2/ Excludes real estate and financial intermediation.

New deposit rates have started to stabilize at much reduced levels this summer…

Median Deposit Rates, New Business 1/

(Percent)



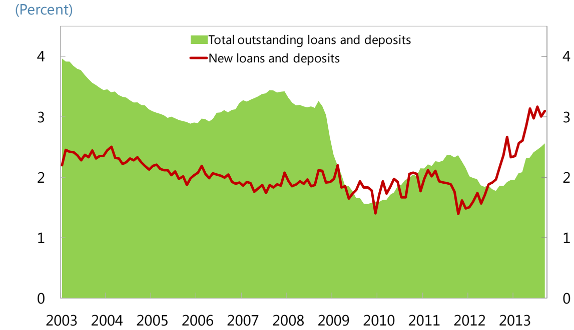
Source: Central Bank of Ireland.

1/Data relate to new business conducted through resident offices of a sample of banks and include IBRC. Refers to median deposit rates (excludes overnight). Last observation July 2013.

…but average margins between loans and deposits keep improving as long-term deposits roll-off.

Interest Rate Margins Between Loans and Deposits 1/

(Percent)

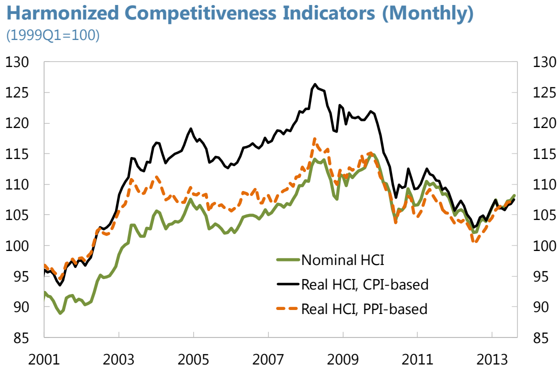


Source: Central Bank of Ireland.

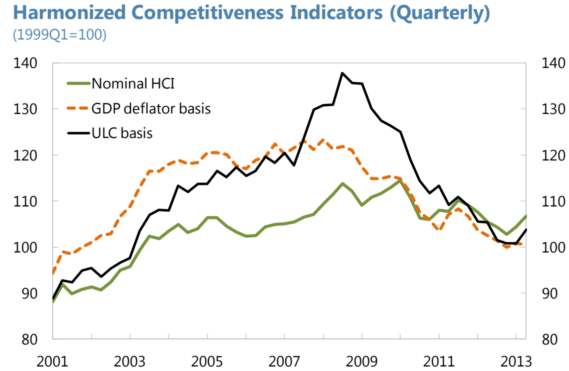
1/ Weighted average loan rate minus weighted average deposit rate.

Figure 4. Ireland: Competitiveness Indicators, 1996–2013

Appreciation of the euro in the recent months slowed the improvement in competitiveness indicators.



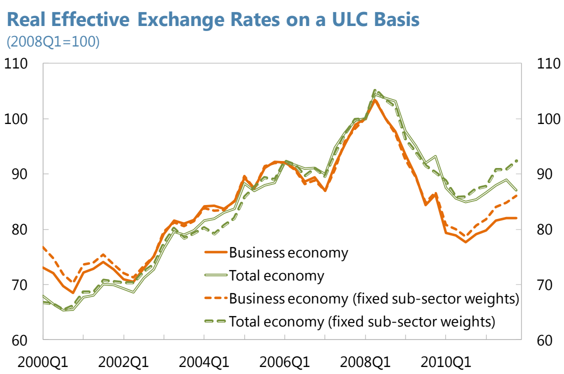
Sources: CBI; and Haver Analytics.



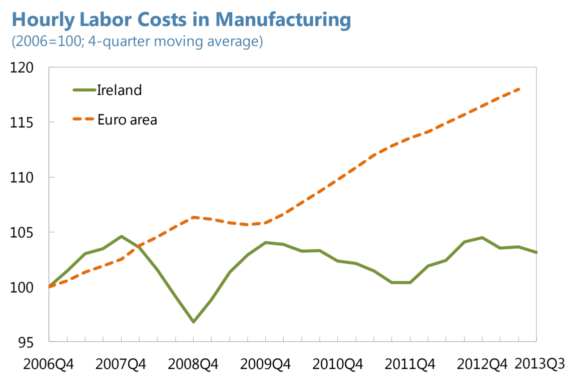
Sources: CBI; and Haver Analytics.

Though part of that earlier improvement reflects a shift to higher value-added sectors.

Private wages have been broadly flat in recent years, while growth has continued in the euro area…



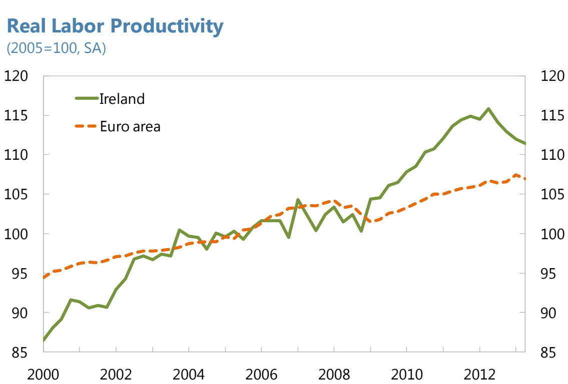
Source: Bruegel.



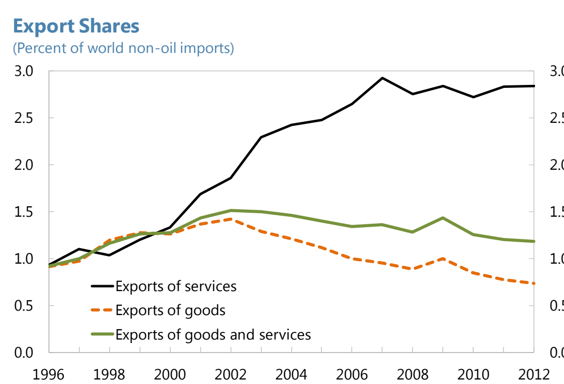
Sources: CSO; Eurostat; Haver Analytics; and IMF staff calculations.

…while labor productivity continues to outpace the euro area, this gap has narrowed recently as employment data showed gains while output in the high-productivity pharmaceutical sector stalled due to patent expiry.

As yet, competitiveness improvements have not been reflected in rising market shares, with the impact of patent expiry on the goods market share evident.



Source: Eurostat.

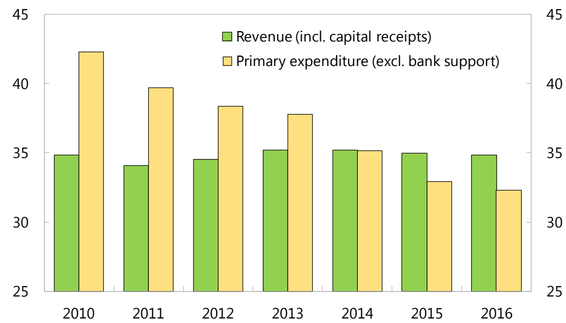


Sources: IMF WEO; and IMF staff calculations and projections.

Figure 5. Ireland: Selected Trends in General Government Finances, 2007–16

Of an 11 percent of GDP primary balance improvement (2010–16), more than half is expected by 2013.

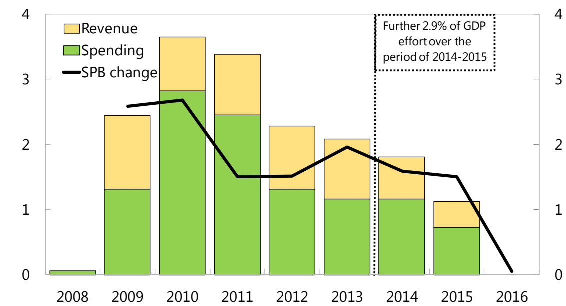
Revenues and Primary Expenditure
(Percent of GDP)



Sources: Department of Finance; and IMF staff estimates.

Fiscal consolidation is programmed to moderate over time and is expenditure-led.

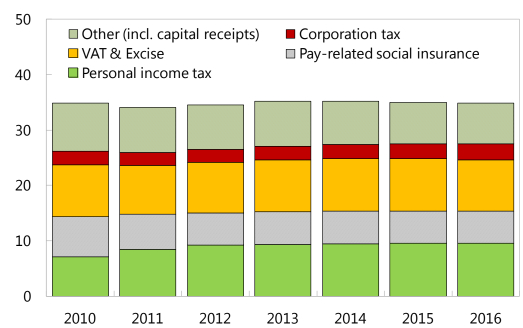
Composition of Fiscal Consolidation
(Percent of GDP)



Source: IMF staff estimates.
SPB denotes structural primary balance ratio.

Given the weaker recovery in nominal domestic demand, tax measures will only modestly raise revenues as a share of GDP.

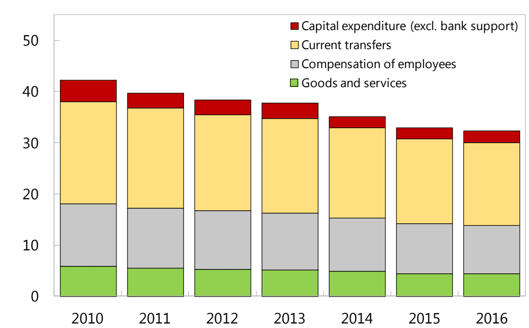
Revenue Composition
(Percent of GDP)



Sources: Department of Finance; and IMF staff estimates.

Primary expenditures will fall by 10 percent of GDP, reflecting evenly spread durable savings.

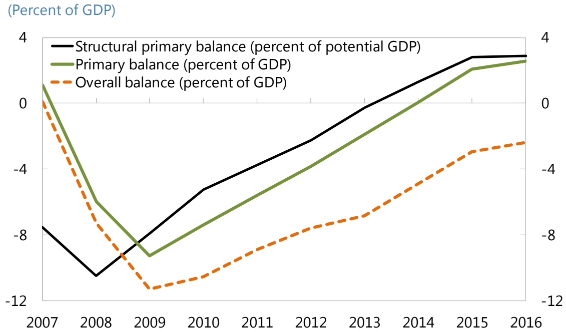
Primary Expenditure Components
(Percent of GDP)



Sources: Department of Finance; and IMF staff estimates.

An overall deficit below 3 percent of GDP is targeted for 2015, with a primary balance targeted for 2014.

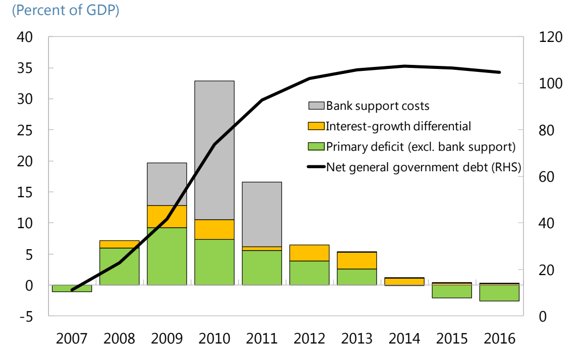
Headline, Primary and Structural Balance 1/
(Percent of GDP)



Sources: Department of Finance; and IMF staff estimates.
1/ Excluding bank support; for 2013, includes exchequer outlays for guarantees paid out under the ELG scheme in the context of the liquidation of IBRC.

It will take time to unwind the increase in net debt, half of which arose from bank support costs.

Sources of Increase in Net Debt-to-GDP Ratio
(Percent of GDP)



Sources: Department of Finance; and IMF staff estimates.

Table 1. Ireland: Selected Economic Indicators, 2008–14

(Annual percentage change unless indicated otherwise)

	2008	2009	2010	2011	2012	2013	2014
						Proj	
National accounts (constant prices)							
Real GDP	-2.2	-6.4	-1.1	2.2	0.2	0.3	1.7
Final domestic demand	-2.2	-9.7	-5.0	-3.0	-1.1	-0.2	0.4
Private consumption	0.1	-5.1	0.9	-1.6	-0.3	-0.6	0.5
Public consumption	0.6	-3.4	-6.9	-2.8	-3.7	-1.0	-2.8
Gross fixed investment	-9.6	-26.9	-22.6	-9.5	-1.0	2.9	4.4
Net exports 1/	1.5	4.6	3.0	5.7	1.6	0.3	1.4
Exports of goods and services	-1.1	-3.8	6.4	5.4	1.6	0.5	2.5
Imports of goods and services	-3.0	-9.8	3.6	-0.4	0.0	0.2	1.4
Real GNP	-1.8	-9.1	0.5	-1.6	1.8	0.2	1.3
Gross national saving (in percent of GDP)	16.3	13.8	13.3	11.8	15.1	15.2	15.7
Private	18.4	21.3	20.4	18.3	21.4	20.7	19.3
Public 2/	-2.0	-7.6	-7.1	-6.4	-6.4	-5.5	-3.5
Gross investment (in percent of GDP)	22.0	16.1	12.2	10.6	10.6	10.9	11.2
Private	16.7	12.3	8.7	8.1	8.8	9.1	9.6
Public	5.3	3.7	3.5	2.5	1.9	1.8	1.6
Prices, wages and employment (annual average)							
Harmonized index of consumer prices	3.1	-1.7	-1.6	1.2	1.9	0.8	0.9
Average wage, whole economy	5.8	0.0	-1.9	-0.5	0.5	0.5	0.8
Employment	-0.7	-7.8	-4.0	-1.8	-0.6	1.6	1.5
Unemployment rate (in percent)	6.4	12.0	13.9	14.6	14.7	13.3	12.3
Money and credit (end-period) 3/							
Irish resident private sector credit 4/	8.8	-1.5	-3.4	-2.9	-4.0	-4.6	…
Financial and asset markets (end-period) 3/							
Three-month interbank rate	2.9	0.7	1.0	1.4	0.2	0.2	…
Government bond yield (in percent, 10-year) 5/	4.4	4.9	9.2	8.5	4.5	3.5	…
Annual change in ISEQ index (in percent)	-47.3	28.8	5.1	5.2	16.3	25.6	…
House prices	-12.4	-18.6	-10.5	-16.7	-4.5	3.6	…
Public finance (in percent of GDP)							
General government balance (excl. bank support) 6/	-7.3	-11.3	-10.6	-8.9	-8.2	-7.3	-5.1
Primary balance (excl. bank support)	-6.0	-9.3	-7.4	-5.6	-4.5	-2.7	-0.3
General government gross debt	44.2	64.4	91.2	104.1	117.4	123.9	121.7
General government net debt		38.6	70.4	85.1	92.8	99.1	101.8
External trade and balance of payments (percent of GDP)							
Balance of goods and services	9.0	15.8	18.4	21.5	24.1	24.3	25.4
Balance of income and current transfers	-14.6	-18.1	-17.3	-20.3	-19.7	-20.1	-20.8
Current account	-5.6	-2.3	1.1	1.2	4.4	4.2	4.6
Effective exchange rates (1999:Q1=100, average) 3/							
Nominal	111.6	112.5	107.8	108.6	105.1	107.3	…
Real (CPI based)	123.1	121.0	111.6	110.2	105.3	106.6	…
Memorandum items:							
Population (in millions)	4.5	4.5	4.6	4.6	4.6	4.6	4.6
GDP per capita (in euros)	40,189	35,797	34,710	35,542	35,752	35,857	36,520
GDP (in billions of euros)	180.2	162.3	158.1	162.6	163.9	165.4	169.5

Sources: Bloomberg; Central Bank of Ireland; Department of Finance; International Financial Statistics; and IMF staff estimate
1/ Contribution to growth.
2/ Excludes bank restructuring costs.
3/ Data refers to end-June for private sector credit, end-May for interbank rate, end-June for house prices and effective exchange rate, and end-July for other indicators.
4/ Adjusted growth rate of credit to households and non-financial corporations.
5/ Since mid-2012, 8 year government bond yield is shown as no 10 year benchmark exists.
6/ General government balance per ESA95 definition. For 2013, includes exchequer outlays for guarantees paid out under the ELG scheme in the context of the liquidation of IBRC.

Table 2. Ireland: Medium-Term Scenario, 2009–18

(Annual percentage change, unless indicated otherwise)

	2009	2010	2011	2012	2013	2013	2014	2015	2016	2017	2018
					11th Review	Proj.					
Real GDP	-6.4	-1.1	2.2	0.2	0.6	0.3	1.7	2.5	2.5	2.5	2.5
Domestic demand	-10.4	-4.4	-1.8	-1.6	0.0	0.0	0.4	1.0	1.8	2.0	2.2
Final domestic demand	-9.7	-5.0	-3.0	-1.1	0.0	-0.2	0.4	1.0	1.8	2.0	2.2
Private consumption	-5.1	0.9	-1.6	-0.3	-0.3	-0.6	0.5	1.0	1.3	1.6	1.6
Public consumption	-3.4	-6.9	-2.8	-3.7	-0.6	-1.0	-2.8	-2.5	0.3	0.0	0.5
Gross fixed investment	-26.9	-22.6	-9.5	-1.0	2.0	2.9	4.4	5.4	6.0	6.0	6.5
Change in stocks 1/	-0.7	0.6	1.0	-0.4	0.0	0.2	0.0	0.0	0.0	0.0	0.0
Net exports 1/	4.6	3.0	5.7	1.6	0.6	0.3	1.4	1.7	1.2	1.1	0.9
Exports of goods and services	-3.8	6.4	5.4	1.6	1.1	0.5	2.5	3.7	4.1	4.2	4.2
Imports of goods and services	-9.8	3.6	-0.4	0.0	0.6	0.2	1.4	2.7	3.9	4.3	4.4
Real GNP	-9.1	0.5	-1.6	1.8	0.3	0.2	1.3	2.1	2.1	2.1	2.2
Current account 2/	-2.3	1.1	1.2	4.4	2.3	4.2	4.6	4.7	4.5	3.8	2.9
Gross national saving 2/	13.8	13.3	11.8	15.1	13.1	15.2	15.7	16.2	16.2	15.7	15.2
Private	21.3	20.4	18.3	21.4	19.0	20.7	19.3	17.7	17.1	16.1	15.1
Public	-7.6	-7.1	-6.4	-6.4	-5.9	-5.5	-3.5	-1.5	-1.0	-0.4	0.1
Gross investment 2/	16.1	12.2	10.6	10.6	10.8	10.9	11.2	11.5	11.6	11.9	12.3
Private	12.3	8.7	8.1	8.8	9.1	9.1	9.6	10.0	10.2	10.5	11.0
Public	3.7	3.5	2.5	1.9	1.6	1.8	1.6	1.5	1.4	1.4	1.3
Prices											
Harmonized index of consumer prices	-1.7	-1.6	1.2	1.9	1.0	0.8	0.9	1.1	1.2	1.7	1.7
GDP deflator	-3.8	-1.5	0.7	0.7	1.0	0.6	0.7	1.0	1.0	1.6	1.6
Average wage, whole economy	0.0	-1.9	-0.5	0.5	0.4	0.5	0.8	0.5	1.4	1.5	1.2
Labor market											
Employment	-7.8	-4.0	-1.8	-0.6	0.6	1.6	1.5	1.2	1.2	1.7	1.7
Unemployment rate (in percent)	12.0	13.9	14.6	14.7	13.7	13.3	12.3	11.7	11.3	10.9	10.4
Public finance											
General government balance 2/ 3/	-11.3	-10.6	-8.9	-8.2	-7.5	-7.3	-5.1	-2.9	-2.4	-1.8	-1.2
General government gross debt 2/	64.4	91.2	104.1	117.4	123.3	123.9	121.7	121.9	118.8	115.8	112.2
General government net debt 2/	38.6	70.4	85.1	92.8	105.5	99.1	101.8	102.8	100.9	98.7	95.7
Output gap	-3.0	-3.8	-1.6	-1.6	-1.8	-1.9	-1.3	-0.4	0.1	0.3	0.4
Nominal GDP (in billions of euros)	162.3	158.1	162.6	163.9	166.6	165.4	169.5	175.4	181.7	189.2	197.2

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

1/ Contributions to growth.

2/ In percent of GDP, excludes bank restructuring costs. For 2013, includes exchequer outlays for guarantees paid out under the ELG scheme in the context of the liquidation of IBRC.

3/ General government balance per ESA95 definition.

Table 3. Ireland: General Government Statement of Operations, 2009–18

(consistent with *GFSM* 2001; in billions of Euros)

					Projections 1/					
	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	56.0	55.1	55.4	56.5	58.5	60.4	62.6	64.3	66.4	68.9
Taxes	35.9	34.8	37.6	39.5	41.4	43.3	45.2	46.8	48.7	50.7
Personal income tax	11.8	11.3	13.8	15.2	15.7	16.3	17.0	17.6	18.3	19.1
Corporate income tax	3.9	3.9	3.8	4.0	4.4	4.7	5.1	5.5	5.7	6.0
Value-added tax	10.7	10.1	9.7	10.2	10.4	10.5	10.8	11.2	11.6	12.0
Excise tax	4.7	4.7	4.7	4.7	4.7	4.9	5.1	5.3	5.5	5.7
Other 2/	4.8	4.9	5.6	5.4	6.2	6.9	7.1	7.3	7.6	7.9
Social contributions 3/	12.0	11.5	10.3	9.7	9.9	10.3	10.6	10.9	11.2	11.5
Other revenue 4/	8.1	8.8	7.5	7.4	7.2	6.8	6.8	6.6	6.5	6.7
Expenditure (excl. fin. sector support)	74.4	71.8	69.9	70.0	70.7	69.0	67.8	68.6	69.8	71.4
Expense (excl. fin. sector support)	68.3	66.3	65.8	67.0	67.7	66.4	65.2	66.0	67.2	68.7
Compensation of employees	20.7	19.3	19.1	18.8	18.7	18.4	17.7	17.7	18.0	18.3
Use of goods and services	10.4	9.3	8.9	8.4	8.3	8.1	8.2	8.3	8.3	8.7
Interest	3.3	5.0	5.3	6.1	7.6	8.2	8.8	9.2	9.5	9.8
Subsidies	0.9	0.9	0.6	1.5	1.3	1.3	1.3	1.3	1.3	1.3
Social benefits 3/	28.3	28.2	28.8	29.0	28.4	27.9	26.6	26.8	27.3	27.7
Other expense (excl. fin. sector support) 5/	4.7	3.6	3.1	3.1	3.3	2.5	2.7	2.6	2.8	2.8
Gross fixed capital formation	6.1	5.5	4.0	3.1	3.0	2.6	2.6	2.6	2.6	2.7
Financial sector support costs	4.0	31.6	6.8	0.0	0.0	0.1	0.1	0.1	0.0	0.0
Net lending/borrowing (excl. fin. sector support)	-18.4	-16.7	-14.4	-13.5	-12.1	-8.6	-5.2	-4.3	-3.4	-2.5
Net lending/borrowing (incl. fin. sector support)	-22.4	-48.3	-21.3	-13.5	-12.2	-8.7	-5.3	-4.4	-3.4	-2.5
Primary balance (excl. fin. sector support)	-15.1	-11.7	-9.1	-7.4	-4.5	-0.4	3.6	4.9	6.1	7.4
Net financial worth, transactions	-22.4	-48.3	-21.3	-13.5	-12.2	-8.7	-5.3	-4.4	-3.4	-2.5
Net acquisition of financial assets	2.6	-8.1	3.2	5.2	0.8	-7.3	-0.3	-1.0	0.0	0.0
Net incurrence of liabilities	24.9	40.1	24.4	18.7	12.9	1.5	5.0	3.4	3.4	2.5
Statistical discrepancy	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items (in percent of GDP, unless indicated otherwise)										
Revenue	34.5	34.9	34.1	34.5	35.4	35.6	35.7	35.4	35.1	35.0
Taxes and social contributions 3/	29.5	29.3	29.4	30.0	31.0	31.6	31.8	31.8	31.6	31.6
Other revenue 4/	5.0	5.6	4.6	4.5	4.3	4.0	3.9	3.6	3.5	3.4
Expenditure (excl. fin. sector support)	45.8	45.4	43.0	42.7	42.7	40.7	38.6	37.8	36.9	36.2
Current primary (excl. fin. sector support) 5/	40.1	38.8	37.2	37.1	36.3	34.3	32.2	31.3	30.5	29.9
Interest	2.0	3.1	3.3	3.7	4.6	4.8	5.0	5.1	5.0	5.0
Gross fixed capital formation	3.7	3.5	2.5	1.9	1.8	1.6	1.5	1.4	1.4	1.3
Net lending/borrowing (excl. fin. sector support)	-11.3	-10.6	-8.9	-8.2	-7.3	-5.1	-2.9	-2.4	-1.8	-1.2
Net lending/borrowing (incl. fin. sector support)	-13.8	-30.5	-13.1	-8.2	-7.3	-5.2	-3.0	-2.4	-1.8	-1.2
Primary balance (excl. fin. sector support)	-9.3	-7.4	-5.6	-4.5	-2.7	-0.3	2.0	2.7	3.2	3.7
Net financial worth, transactions	-13.8	-30.5	-13.1	-8.2	-7.3	-5.2	-3.0	-2.4	-1.8	-1.2
Net acquisition of financial assets	1.6	-5.1	1.9	3.2	0.5	-4.3	-0.2	-0.5	0.0	0.0
Net incurrence of liabilities	15.4	25.4	15.0	11.4	7.8	0.9	2.8	1.9	1.8	1.2
Statistical discrepancy	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Structural balance	-10.2	-8.6	-7.1	-6.2	-5.3	-4.2	-2.3	-2.3	-2.0	-1.7
Structural primary balance 6/	-7.9	-5.3	-3.8	-2.5	-0.6	0.6	2.6	2.8	3.0	3.2
General government gross debt	64.4	91.2	104.1	117.4	123.9	121.7	121.9	118.8	115.8	112.2
General government net debt	38.6	70.4	85.1	92.8	99.1	101.8	102.8	100.9	98.7	95.7
Output gap (percent of potential GDP)	-3.0	-3.8	-1.6	-1.6	-1.9	-1.3	-0.4	0.1	0.3	0.4
Nominal GDP (in billions of euros)	162.3	158.1	162.6	163.9	165.4	169.5	175.4	181.7	189.2	197.2

Sources: Department of Finance; and IMF staff estimates.

1/ Projections are consistent with the adjustment path set out in Budget 2014.

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

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

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

5/ For 2013, includes exchequer outlays for guarantees paid out under the ELG scheme in the context of the liquidation of IBRC.

6/ In percent of nominal potential GDP.

Table 4. Ireland: Indicators of External and Financial Vulnerability, 2009–13

	2009	2010	2011	2012	2013 7/
External indicators					
Exports (annual percent change, value in euros)	-2.5	8.0	6.1	5.8	1.5
Imports (annual percent change, value in euros)	-9.9	6.8	2.9	3.9	1.5
Terms of trade (goods, annual percent change)	1.7	-1.6	-2.7	0.4	-0.3
Current account balance (in percent of GDP)	-2.3	1.1	1.2	4.4	4.2
Capital and financial account balance (in percent of GDP)	-2.2	3.8	5.9	-0.8	-4.4
Of which:					
Inward portfolio investment	13.8	47.8	18.2	44.7	41.2
Inward foreign direct investment	11.4	20.4	10.4	18.2	18.4
Other investment liabilities	-53.3	-39.2	-51.2	-67.5	-45.5
U.S. dollar per euro (period average)	1.40	1.32	1.40	1.29	1.32
U.K. pound per euro (period average)	0.89	0.86	0.87	0.81	0.86
Financial markets indicators					
General government debt (in percent of GDP)	64.4	91.2	104.1	117.4	123.9
Government bond yield (in percent, 10-year, end-period) 1/	4.9	9.2	8.5	4.5	3.5
Spread of government bond yield with Germany (in percent, end of period)	1.3	6.0	6.5	3.2	1.7
Real government bond yield (in percent, 10-year, period average, based on HICP)	6.9	7.6	8.4	4.1	3.1
Annual change in ISEQ index (in percent, end of period)	28.8	5.1	5.2	16.3	25.6
Personal lending interest rate (in percent)	11.1	11.4	11.6	11.6	11.6
Standard variable mortgage interest rate (in percent)	3.3	4.0	4.2	4.3	4.4
Financial sector risk indicators					
Annual credit growth rates (to Irish resident private sector, in percent) 2/	-1.5	-3.4	-2.9	-4.0	-4.6
Personal lending as a share of total Irish resident credit (in percent)	35.6	35.5	30.0	33.0	33.4
Of which:					
House mortgage finance	30.1	30.7	25.4	28.7	29.2
Other housing finance	0.2	0.4	0.3	0.3	0.3
Other personal lending	5.3	4.8	4.6	4.3	4.2
Irish resident household mortgage debt annual growth rates (in percent) 3/	-3.9	-9.0	-19.3	5.6	4.4
Foreign-currency denominated assets (in percent of total assets)	34.3	30.3	29.4	28.4	28.1
Foreign-currency denominated liabilities (in percent of total liabilities)	31.1	25.8	26.3	25.4	25.6
Non-performing loans (in percent of total loans) 4/	9.0	8.6	9.1	11.3	11.5
Total provisions for loan losses (in percent of total loans)	4.0	4.2	4.8	5.4	4.5
Regulatory capital to risk-weighted assets of domestic banks (in percent)	10.9	10.4	17.7	16.6	15.9
Bank return on assets (before tax, in percent)	-1.6	-3.1	-0.8	-0.8	…
Bank return on equity (before tax, in percent)	-40.6	-67.6	-16.9	-14.1	…
Deposits to M3 ratio 5/	1.3	1.5	1.2	1.3	1.4
Loan-to-deposit ratio vis-à-vis Irish residents 6/	2.1	2.1	2.1	1.9	1.7
vis-à-vis total 6/	2.2	2.1	2.1	1.9	1.7
Concentration ratios in the banking sector					
No. of banks accounting for 25 percent of total assets	2.0	2.0	2.0	2.0	2.0
No. of banks accounting for 75 percent of total assets	13.0	13.0	14.0	14.0	14.0
Share of state-owned banks in total assets (in percent)	6.0	8.0	18.0	19.1	15.8
Share of foreign-owned banks in total assets (in percent)	65.0	65.0	61.6	57.6	61.3

Sources: Bloomberg; Central Bank of Ireland; International Financial Statistics; and IMF staff estimates.

1/ Since mid-2012, 8 year government bond yield is shown as no 10 year benchmark exists.

2/ Adjusted growth rate of credit to households and non-financial corporations.

3/ Including securitisations.

4/ Owing to differences in classification, international comparisons of nonperforming loans are indicative only.

5/ Deposits vis-à-vis Irish and nonresidents.The M3 compiliation methodology has been amended in line with Eurosystem

6/ Nongovernment credit/nongovernment deposits ratio.

7/ For 2013, staff projections for macroeconomic variables and debt, end-July 2013 for bond yields and stock market index, and end-June 2013 for other indicators. Financial sector indiators cover all credit institutions licensed in Ireland except for personal lending rate, which is calculated based on a sample of retail banks, and a mortgage interest rate, which is calculated excluding IFSC.

Table 5. Ireland: Summary of Balance of Payments, 2009–18

	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
					Proj.					
	(In billions of euros)									
Current account balance	-3.8	1.8	2.0	7.3	7.0	7.8	8.3	8.2	7.1	5.7
Balance of goods and services	25.6	29.1	35.0	39.6	40.2	43.1	47.1	49.7	52.2	54.6
Trade balance	32.5	35.8	36.7	36.4	35.0	35.8	37.5	39.4	41.5	43.7
Exports of goods	77.6	82.6	85.0	85.9	83.7	85.5	88.8	92.7	96.9	101.3
Imports of goods	-45.2	-46.9	-48.3	-49.5	-48.8	-49.7	-51.4	-53.3	-55.4	-57.6
Services balance	-6.9	-6.6	-1.7	3.2	5.2	7.3	9.6	10.2	10.7	10.9
Credit	67.6	74.3	81.5	90.3	95.1	99.2	104.7	110.9	117.6	124.7
Debit	-74.5	-81.0	-83.2	-87.1	-89.9	-91.9	-95.1	-100.6	-106.8	-113.9
Income balance	-27.9	-25.9	-31.8	-31.1	-32.0	-34.1	-37.3	-39.9	-43.5	-47.0
Credit	55.1	57.1	57.1	57.2	57.2	57.3	57.2	58.0	58.5	59.3
Debit	-83.0	-83.0	-88.9	-88.4	-89.2	-91.4	-94.5	-97.9	-102.0	-106.3
Current transfers (net)	-1.4	-1.4	-1.2	-1.2	-1.2	-1.2	-1.5	-1.5	-1.6	-1.8
Capital and financial account balance	-2.3	6.6	-24.7	-22.3	-17.9	-8.6	-8.3	-8.2	-7.1	-5.7
Capital account balance	-1.3	-0.7	-0.3	-0.3	-0.3	-0.3	-0.3	-0.3	-0.3	-0.3
Financial account	-1.1	7.3	-24.4	-22.1	-17.7	-8.3	-8.0	-7.9	-6.8	-5.4
Direct investment	-0.6	15.4	17.8	15.4	15.9	16.1	16.2	16.9	17.6	18.3
Portfolio investment	22.6	86.0	26.9	-0.2	2.4	-0.7	-0.3	3.2	14.5	26.7
Other investment	-23.1	-94.1	-69.4	-35.5	-30.1	-20.4	-19.2	-19.9	-21.5	-28.6
Change in reserve assets 1/	0.1	0.0	0.3	0.0	-5.8	-3.3	-4.7	-8.2	-17.3	-21.8
Net errors and omissions	6.1	-8.4	-11.8	-6.2	0.0	0.0	0.0	0.0	0.0	0.0
Financing gap	0.0	0.0	34.5	21.3	11.0	0.8	0.0	0.0	0.0	0.0
Program financing	0.0	0.0	34.5	21.3	11.0	0.8	0.0	0.0	0.0	0.0
IMF	0.0	0.0	12.6	6.4	3.5	0.0	0.0	0.0	0.0	0.0
EU	0.0	0.0	21.9	14.8	7.5	0.8	0.0	0.0	0.0	0.0
	(In percent of GDP)									
Current account balance	-2.3	1.1	1.2	4.4	4.2	4.6	4.7	4.5	3.8	2.9
Balance of goods and services	15.8	18.4	21.5	24.1	24.3	25.4	26.8	27.3	27.6	27.7
Trade balance	20.0	22.6	22.6	22.2	21.1	21.1	21.4	21.7	21.9	22.2
Services balance	-4.3	-4.2	-1.0	2.0	3.2	4.3	5.5	5.6	5.7	5.5
Income balance	-17.2	-16.4	-19.6	-19.0	-19.3	-20.1	-21.3	-22.0	-23.0	-23.8
Current transfers (net)	-0.9	-0.9	-0.7	-0.7	-0.7	-0.7	-0.8	-0.8	-0.8	-0.9
Capital and financial account balance	-1.4	4.2	-15.2	-13.6	-10.8	-5.1	-4.7	-4.5	-3.8	-2.9
Of which:										
Direct investment	-0.4	9.8	10.9	9.4	9.6	9.5	9.3	9.3	9.3	9.3
Portfolio investment	13.9	54.4	16.5	-0.1	1.4	-0.4	-0.2	1.8	7.6	13.6
Other investment	-14.2	-59.5	-42.7	-21.6	-18.2	-12.0	-11.0	-11.0	-11.4	-14.5
Change in reserve assets 1/	0.0	0.0	0.2	0.0	-3.5	-1.9	-2.7	-4.5	-9.2	-11.1
Net errors and omissions	3.7	-5.3	-7.3	-3.8	0.0	0.0	0.0	0.0	0.0	0.0
Financing gap	0.0	0.0	21.2	13.0	6.6	0.5	0.0	0.0	0.0	0.0
Program financing	0.0	0.0	21.2	13.0	6.6	0.5	0.0	0.0	0.0	0.0
IMF	0.0	0.0	7.7	3.9	2.1	0.0	0.0	0.0	0.0	0.0
EU	0.0	0.0	13.5	9.0	4.5	0.5	0.0	0.0	0.0	0.0
Memorandum items:										
Current account balance excluding undistributed profits 2/	-3.3	-2.1	-2.3	-0.1						

Sources: Central Bank of Ireland; Central Statistics Office; and IMF staff estimates.
1/ Includes financing need to build reserves for bank support.
2/ Undistributed profits of redomiciled firms, as estimated by FitzGerald (2013).

Table 6. Ireland: Monetary Survey, 2009–13

(In billions of euros, unless otherwise indicated; end of period)

	Dec-09	Dec-10	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13	Jun-13	Jul-13
Aggregate balance sheet of domestic market credit institutions										
Assets	801	747	639	614	610	571	550	498	487	484
Claims on Central Bank of Ireland	12	8	4	5	6	7	2	2	3	2
Claims on Irish resident Other MFIs	129	123	92	86	81	55	53	50	50	50
Claims on Irish resident non MFIs	364	359	340	338	333	331	326	292	288	287
General government	9	43	42	44	45	47	47	19	20	20
Private sector	355	316	298	294	288	285	279	274	269	267
Households	47	26	55	58	57	79	73	59	55	54
Non-Financial Corporations	177	159	143	144	144	145	147	160	159	159
Non-Bank Financial Intermediaries	131	132	99	92	87	60	59	55	54	53
Claims on non-residents	243	209	150	141	143	132	122	112	105	105
Other assets	54	48	52	44	46	46	47	42	41	41
Liabilities	801	747	639	614	610	571	550	498	487	484
Liabilities to Eurosystem 1/	58	95	72	75	78	71	59	44	39	37
Liabilities to Irish resident Other MFIs	131	132	99	92	87	60	59	55	54	53
Deposits of Irish resident non MFIs	180	162	146	147	147	148	153	169	172	173
General government	3	3	2	2	3	3	6	10	13	13
Private sector	177	159	143	144	144	145	147	160	159	159
Deposits of non-residents	230	140	100	93	91	84	76	77	74	77
Debt securities	98	64	52	44	41	40	38	34	29	27
Capital and reserves	53	72	91	93	97	97	98	94	94	94
Other liabilities (incl. Central Bank of Ireland)	50	83	79	70	69	71	66	24	25	24
Money and credit 2/										
Net foreign assets	-421	-480	-340	-34	-23	-15	-14	-9	…	…
Central Bank of Ireland 3/	-37	-128	-101	-76	-77	-67	-62	-42	…	…
Commercial banks	-384	-352	-239	42	54	52	48	33	31	33
Net domestic assets	629	652	509	203	191	185	183	194	…	…
Public sector credit	10	43	43	44	46	47	48	19	20	20
Private sector credit	375	335	324	319	313	309	302	297	292	287
Other	244	274	143	-160	-167	-171	-166	-122	…	…
Irish Resident Broad money (M3) 4/	208	173	169	169	168	170	170	185	189	189
Irish Resident Intermediate money (M2) 4/	188	173	167	167	166	168	168	182	183	182
Irish Resident Narrow money (M1)	100	97	90	89	89	90	92	105	109	109
					(percent of GDP)					
Public sector credit 5/	5.3	27.6	27.0	27.9	28.4	29.0	29.4	11.5	12.2	12.2
Private sector credit 5/	221.0	202.4	190.1	186.9	180.7	177.3	173.5	170.4	167.4	166.3
					(y-o-y percentage change)					
Broad money - Irish contribution to euro area M3 6/	-6.6	-19.6	1.3	-3.3	-10.2	-7.5	-7.3	-0.5	6.1	6.1
Irish Public sector credit 6/ 7/	176.9	369.4	1.5	11.0	15.3	8.5	8.5	-58.6	-57.1	-57.3
Irish Household and non-financial corporations credit 6/ /7	-1.5	-3.4	-2.9	-3.2	-3.4	-4.0	-4.0	-4.2	-4.6	-4.6
Memorandum items: 8/										
Credit to deposits (in percent) 9/	200.5	199.2	207.6	204.0	199.7	195.9	189.9	171.1	168.5	167.6
Deposits from Irish Private Sector (y-o-y percent change)	42.5	-16.4	-11.7	-18.8	-24.9	-25.2	-26.1	-31.2	-34.4	-34.9
Wholesale funding (billions of euros)	59	31	22	18	16	15	15	15	12	10
Deposits from MFIs	12	10	8	7	7	7	8	8	7	6
Debt securities	47	21	14	10	8	8	8	7	6	4
Wholesale funding (y-o-y percent change) 10/	-19.0	-48.9	-28.1	-34.8	-39.7	-35.3	-30.8	-15.1	-21.0	-32.7
Wholesale funding (percent of assets) 10/	7.4	4.4	3.4	2.9	2.6	2.7	2.8	3.0	2.5	2.1

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

Table 7. Ireland: General Government Financing Requirements and Sources, 2008–13

(In billions of euros)

	2008	2009	2010	2011	2012	2013 *Proj.*
Gross borrowing need	**15.9**	**63.4**	**71.4**	**45.3**	**29.8**	**27.8**
Exchequer cash deficit 1/	12.7	24.6	18.7	19.1	17.1	11.3
Amortization	3.1	27.7	17.3	9.7	11.1	16.5
Medium-and long-term	0.1	5.1	1.2	4.8	6.8	6.2
Short-term 2/	3.0	22.6	16.2	4.9	4.4	10.2
Official creditors	0.0	0.0	0.0	0.0	0.0	0.0
European Union	0.0	0.0	0.0	0.0	0.0	0.0
IMF	0.0	0.0	0.0	0.0	0.0	0.0
Bank recapitalization	0.0	11.0	35.3	16.5	1.6	0.0
Gross financing sources 3/	**15.9**	**63.4**	**71.4**	**10.8**	**8.5**	**16.8**
Market financing (incl. retail) 4/	34.9	53.3	23.2	1.4	10.1	18.4
Net retail funding	1.3	1.8	3.4	1.4	1.3	1.6
Other market financing	33.6	51.6	19.8	0.0	8.8	16.8
Promissory notes	0.0	0.0	30.9	0.0	0.0	0.0
Bond placement for Promissory notes 5/				…	3.5	…
Cash drawdowns 6/	-19.0	10.0	17.3	9.4	-5.2	-0.8
Financing gap	**0.0**	**0.0**	**0.0**	**34.5**	**21.3**	**11.0**
EFSM/EFSF	0.0	0.0	0.0	21.5	12.3	5.6
Bilateral EU	0.0	0.0	0.0	0.5	2.5	1.9
IMF	0.0	0.0	0.0	12.6	6.4	3.5
Memorandum items						
Exchequer cash balance	22.0	21.8	12.3	13.0	19.3	20.1
General government debt 7/	79.6	104.5	144.2	169.2	192.5	205.0
Official creditors	0.0	0.0	0.0	34.5	56.0	66.6
European Union	0.0	0.0	0.0	21.9	37.1	44.1
IMF	0.0	0.0	0.0	12.6	18.9	22.5
Other	79.6	104.5	144.2	134.7	136.5	138.4
Treasury bills, bonds and retail	72.0	96.3	110.4	101.6	104.2	131.2
Promissory notes	0.0	0.0	30.9	28.3	25.3	0.2
Other	7.6	8.4	2.9	4.8	7.0	7.0
General government debt (in percent of GDP) 7/	44.2	64.4	91.2	104.1	117.4	123.9
Official creditors	0.0	0.0	0.0	21.2	34.1	40.3
European Union	0.0	0.0	0.0	13.5	22.6	26.6
IMF	0.0	0.0	0.0	7.7	11.5	13.6
Other	44.2	64.4	91.2	82.8	83.3	83.7
Treasury bills, bonds and retail	39.9	59.3	69.8	62.5	63.6	79.3
Promissory notes	0.0	0.0	19.5	17.4	15.4	0.1
Other	4.2	5.1	1.9	2.9	4.3	4.2

Sources: Department of Finance; National Treasury Management Agency; and IMF staff estimates.

1/ Includes allowance for amortization of Promissory notes and contingency for collateral on hedging transactions.

2/ Gross amortization of Treasury bills, Exchequer notes, and commercial paper, including intra-year rollovers.

3/ Includes stock-flow adjustment arising from the March 2012 payment of Promissory notes.

4/ Gross issuance including rollovers.

5/ Placement of a bond for the March 2012 payment of Promissory notes to IBRC.

6/ Forecast includes cash outflow for posting collateral.

7/ Includes local debt, other national debt, and other general government debt on consolidated level.

Table 8. Ireland: Schedule of Reviews and Purchases

Review	Availability Date	Action	Purchase	
			SDRs	Percent of quota
	December 16, 2010	Board approval of arrangement	5,012,425,200	399
First and Second Reviews	May 16, 2011	Observance of end-March 2011 performance criteria, completion of First and Second Reviews	1,410,000,000	112
Third Review	August 15, 2011	Observance of end-June 2011 performance criteria, completion of Third Review	1,319,000,000	105
Fourth Review	December 14, 2011	Observance of end-September 2011 performance criteria, completion of Fourth Review	3,309,000,000	263
Fifth Review	February 15, 2012	Observance of end-December 2011 performance criteria, completion of Fifth Review	2,786,000,000	222
Sixth Review	June 13, 2012	Observance of end-March 2012 performance criteria, completion of Sixth Review	1,191,000,000	95
Seventh Review	September 5, 2012	Observance of end-June 2012 performance criteria, completion of Seventh Review	758,000,000	60
Eight Review	December 12, 2012	Observance of end-September 2012 performance criteria, completion of Eight Review	758,000,000	60
Ninth Review	March 15, 2013	Observance of end-December 2012 performance criteria, completion of Ninth Review	831,000,000	66
Tenth Review	June 15, 2013	Observance of end-March 2013 performance criteria, completion of Tenth Review	831,000,000	66
Eleventh Review	September 15, 2013	Observance of end-June 2013 performance criteria, completion of Eleventh Review	681,000,000	54
Twelth Review	November 15, 2013	Observance of end-September 2013 performance criteria, completion of Twelth Review	579,374,800	46
Total			19,465,800,000	1,548

Source: IMF staff projections.

Table 9. Ireland. Indicators of Fund Credit, 2010–23 1/

(In millions of SDR)

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Fund credit														
Disbursement	-	11,050	5,493	2,922	-	-	-	-	-	-	-	-	-	-
Stock 2/	-	11,050	16,543	19,466	19,466	18,931	16,757	13,862	10,617	7,373	4,129	1,420	349	-
Obligations	-	109	332	346	647	1,211	2,803	3,427	3,653	3,521	3,389	2,748	1,083	351
Repurchase	-	-	-	-	-	535	2,173	2,896	3,244	3,244	3,244	2,709	1,071	349
Charges	-	109	332	346	647	676	630	532	409	277	144	39	12	3
Stock of Fund credit														
In percent of quota	-	879	1,315	1,548	1,548	1,505	1,332	1,102	844	586	328	113	28	-
In percent of GDP	-	7.7	12.0	13.4	12.9	12.0	10.2	8.1	5.9	3.9	2.1	0.7	0.2	-
In percent of exports of goods and services	-	7.5	11.1	12.4	11.8	10.9	9.1	7.2	5.2	3.5	1.9	0.6	0.1	-
Obligations to the Fund														
In percent of quota	-	9	26	27	51	96	223	273	290	280	269	219	86	28
In percent of GDP	-	0.1	0.2	0.2	0.4	0.8	1.7	2.0	2.0	1.9	1.7	1.4	0.5	0.2
In percent of exports of goods and services	-	0.1	0.2	0.2	0.4	0.7	1.5	1.8	1.8	1.7	1.5	1.2	0.4	0.1

Source: IMF staff estimates.

1/ Calculated based on existing credit and full disbursements of the prospective available amounts under the extended arrangement under the Extended Fund Facility.

2/ End of period.

Table 10. Ireland: PCAR Banks' Aggregated Summary Financial Statements, H1 2012–H1 2013 1/

(In billions of euro unless otherwise indicated)

Balance Sheet	H1 2012	H1 2013	H1/H1 change	
	€ bn.	€ bn.	€ bn.	%
Cash & due from Eurosystem	17.2	9.1	-8.1	-47.3
Net loans	208.2	186.0	-22.2	-10.6
Due from banks	17.5	8.7	-8.8	-50.3
Securities & derivatives	64.1	64.7	0.5	0.8
Other assets	13.9	13.4	-0.5	-3.8
Total assets	320.9	281.8	-39.1	-12.2
Total average assets (TAA)	322.5	292.0	-30.5	-9.5
Due to Eurosystem	64.1	33.7	-30.4	-47.5
Due to banks	16.1	19.1	3.0	18.5
Deposits	155.5	159.0	3.6	2.3
Debt & derivatives	51.6	37.9	-13.8	-26.6
Other liabilities	8.4	11.0	2.7	32.1
Total liabilities	295.7	260.7	-35.0	-11.8
Net equity	25.2	21.1	-4.2	-16.4
Total liabilities & equity	320.9	281.8	-39.1	-12.2

Profit and Loss Account	H1 2012		H1 2013	
	€ bn.	% of TAA	€ bn.	% of TAA
Interest income	4.7	2.9	4.1	2.8
Interest expense	-3.4	-2.1	-2.5	-1.7
Net interest margin	1.3	0.8	1.5	1.1
Net fee income	0.4	0.3	0.4	0.3
Net trading gains	-0.2	-0.1	0.1	0.0
Other nonrecurrent items	0.0	0.0	-0.1	-0.1
Gross operating income	1.5	0.9	1.9	1.3
Operating expenses	-2.1	-1.3	-1.8	-1.2
o/w: administration & other	-0.9	-0.5	-0.8	-0.5
o/w: staff	-1.3	-0.8	-1.0	-0.7
Preprovision profits (PPP)	-0.7	-0.4	0.1	0.1
Loan loss & NAMA provisions	-2.5	-1.5	-1.9	-1.3
Loss on derecognized assets	-0.1	0.0	0.4	0.3
Net income before tax	-3.2	-2.0	-1.5	-1.0
Tax effects & other 3/	0.3	0.2	0.1	0.1
Net income	-2.9	-1.8	-1.4	-0.9

Memorandum items:

	H1 2012	H1 2013	€ bn.	%
Gross loans 2/	233.7	213.5	-20.2	-8.6
Loan loss provisions	25.4	28.2	2.8	11.1
Gross NPLs	51.8	56.8	5.0	9.6
Gross NPLs to gross loans (%)	22.2	26.6		4.4
Provisions to gross NPLs (%)	49.0	49.7		0.7
Net NPLs to net equity (%)	104.7	135.5		30.8

	H1 2012 € bn.	H1 2012 % of TAA	H1 2013 € bn.	H1 2013 % of TAA
PPP net of other nonrecurrent items	-0.7	-0.4	0.2	0.2
Return on equity		-21.2		-12.4
Provisions to gross loans		10.9		13.2
Risk weighted assets (RWA)	157.8	48.9	138.9	47.6
Core tier 1 capital (CT1) and CT1 to RWA (%)	25.7	16.3	19.5	14.1
CT1 to total assets = leverage ratio (%)		8.0		6.9

Sources: CBI; and IMF staff estimates.

1/ PCAR banks are Bank of Ireland, Allied Irish Banks, and Permanent tsb.
2/ Includes loans held for sale, classified on balance sheet as other assets.
3/ Includes profits from discontinued operations of €1.6 billion and tax credits of €1.5 billion in 2011.

Table 11. Ireland: Program Monitoring

Measure	Date	Status
Quantitative Performance Criteria		
Cumulative exchequer primary balance	End-June 2013	Observed
Indicative Target		
Ceiling on the stock of central government net debt	End-June 2013	Observed
Continuous Performance Criteria		
Ceiling on the accumulation of new external payments arrears on external debt contracted or guaranteed by the central government	Continuous	Observed
Structural Benchmarks		
Define the criteria to run stringent stress tests scenarios.	End-December 2010	Observed
Agree on terms of reference for the due diligence of bank assets by internationally recognized consulting firms.	End-December 2010	Observed
The Central Bank will direct the recapitalization of the principal banks (AIB, BoI and EBS) to achieve a capital ratio of 12 percent core tier 1.	End-February 2011	Not observed[1/]
Submit to Dáil Éireann the draft legislation on a special resolution regime.	End-February 2011	Observed[2/]
The Central Bank to complete the assessment of the banks' restructuring plans.	End-March 2011	Observed
Complete the diagnostic evaluation of banks' assets.	End-March 2011	Observed
Complete stress tests (PCAR 2011).	End-March 2011	Observed
Complete a full assessment of credit unions' loan portfolios	End-April 2011	Observed
Finalize plans for the recapitalization of Irish Life and Permanent.	End-May 2011	Observed
Establish a Fiscal Advisory Council.	End-June 2011	Observed
Complete the recapitalization of Allied Irish Banks, Bank of Ireland, Irish Life and Permanent and EBS Building Society.	End-July 2011	Observed
Submit the Supervision and Enforcement Bill to Oireachtas.	End-July 2011	Observed
Complete the legal merger procedures of Allied Irish Bank and EBS Building Society.	End-September 2011	Observed
Publish a memorandum of understanding governing the relationship of the Department of Finance and the Central Bank in relation to banking sector oversight.	End-October 2011	Observed[3/]
The merger of Irish Nationwide Building Society and Anglo-Irish bank.	End-December 2011	Observed
Central Bank to issue guidance to banks for the recognition of accounting losses incurred in their loan book.	End-December 2011	Observed
Finalize a strategy to guide the development of broader legal reforms around personal insolvency, including significant amendments to the Bankruptcy Act 1998 and the creation of a new structured non-judicial debt settlement and enforcement system.	End-December 2011	Observed
Introduce a medium-term expenditure framework with binding multi-annual expenditure ceilings with broad coverage and consistent with the fiscal consolidation targets.	2012 Budget day in early December 2011	Observed
Updated restructuring plan for the PTSB detailing the actions needed to ensure viability of its core businesses.	End-June 2012	Observed
Submit to parliament, as part of the Fiscal Responsibility Bill, a legal framework for the Fiscal Advisory Council ensuring its independence	End-September 2012	Observed

Table 11. Ireland: Program Monitoring (concluded)

Measure	Date	Status
Publish legislation to strengthen the regulatory framework for credit unions, including making legislative provision for effective governance standards and prudential requirements.	End-September 2012	Observed
Approve regulations to establish a charge levied across credit institutions to recoup over time the costs of resolving vulnerable institutions.	End-September 2012	Observed
Request an external BCP assessment in support of efforts to strengthen financial supervision and regulation.	End-March 2013	Observed
Publish an update, where necessary, of the 2011 Impairment Provisioning and Disclosure Guidelines.	End-May 2013	Observed
Undertake a review of progress in addressing mortgage arrears.	End-June 2013	Observed
Conduct a forward looking analysis of PCAR banks' operating profits.	End-September 2013	Partially observed
Publish 2014 Budget.	October 15, 2013	Observed
Complete a preliminary balance sheet assessment of PCAR banks.	End-October 2013	Observed with delay

1/ Central Bank directions were issued within the required timeframe. However, completion of the capital injections required was postponed by the Minister for Finance until after the General Election. These directions are now superseded by the Central Bank's PCAR directions of 31 March 2011.
2/ In practice this was submitted to the Seanad as discussed in paragraph 21 of the MEFP, as the Dáil was dissolved owing to the elections.
3/ Effective end-October 2011 and posted on November 8, 2011.

Table 12. Ireland: Quantitative Performance Criteria and Indicative Targets Under the Economic Program for 2011–13

	31-Dec-11		31-Mar-12		30-Jun-12		30-Sep-12		31-Dec-12		31-Mar-13		30-Jun-13		30-Sep-13	
	Target1/	Outcome	Target1/	Outcome	Target1/	Outcome	Target1/	Outcome	Target1/	Outcome	Target1/	Outcome	Target1/	Outcome	Target1/	Outcome
	(In billions of euro)															
	Performance Criterion		Performance Criterion		Performance Criterion		Performance Criterion		Performance Criterion		Performance Criterion		Performance Criterion		Performance Criterion	
1. Cumulative exchequer primary balance 2/	-22.3	-21.0	-6.9	-5.7	-9.6	-8.7	-11.4	- 10.1	-13.2	-12.3	-3.2	-1.8	-4.0	-2.2	-3.7	-2.3
2. Ceiling on the accumulation of new external payments arrears on external debt contracted or guaranteed by the central government 3/	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
	Indicative Target		Indicative Target		Indicative Target		Indicative Target		Indicative Target		Indicative Target		Indicative Target		Indicative Target	
3. Ceiling on the stock of central government net debt	117.2	115.7	125.0	123.0	130.1	128.2	132.5	130.0	135.8	133.7	167.9	161.8	171.1	164.6	171.0	165.4

1/ Adjusted. For details on the adjustments, see Annex II in Ireland—Eleventh Review Under the Extended Arrangement.
2/ Measured by the exchequer balance excluding interest payments. Cumulative from the start of the relevant calendar year.
3/ Applies on a continuous basis.

Annex I. Debt Sustainability Analysis

This Annex presents the public and external debt sustainability analysis (DSA) based on staff's medium-term macroeconomic framework and the Irish authorities' fiscal consolidation plan.

Public Debt Sustainability Analysis

1. **Public debt sustainability risks remain largely unchanged from the eleventh review (IMF Country Report No. 13/305)**. Since the last review, Ireland's debt trajectory has developed in line with staff projections, and principal risks to debt sustainability have not changed substantially. Under the baseline scenario, public debt is projected to peak this year at 124 percent of GDP before declining to 112 percent in 2018 as the fiscal deficit narrows and economic recovery gains traction. Gross financing needs are forecast to remain below 15 percent of GDP over the medium term, providing a mitigating factor for the risks associated with the debt level. The downward trajectory of Ireland's public debt remains fragile given its vulnerability to lower growth and contingent liabilities, mainly from the financial sector.

2. **A heat map and fan charts indicate that Ireland faces high risks to debt sustainability (Figure 1)**. The debt burden benchmark for advanced economies of 85 percent of GDP is already exceeded, which suggests that Ireland's debt level is highly vulnerable under all scenarios regardless of the extent to which a shock increases debt. Gross financing needs are only vulnerable to the contingent liability shock, as the benchmark of 20 percent of GDP is only exceeded under this stress test. The debt profile is also subject to high risks from external financing requirements (excluding debts of the IFSC) and public debt held by non-residents which exceed the upper risk assessment benchmarks for these indicators.[1] It is useful to note, however, that a large proportion of external financing requirements reflects non-IFSC private sector debt and trade operations. The fan charts illustrate the possible evolution of the debt-to-GDP ratio over the medium term, based on both a symmetric and an asymmetric distribution of risks. The asymmetric fan chart (where only negative shocks to the primary balance are considered) is more relevant given the large planned fiscal adjustment and shows that risks to the debt outlook are skewed to the upside.

3. **There is no evidence of a systematic projection bias in the baseline assumptions for key macroeconomic variables** (Figure 2). Ireland's forecast track record is comparable to that of all other countries with Fund-supported programs. The median forecast errors for real GDP growth and the primary balance during 2004–12 are below 1 percent and in line with other countries. Individual large forecast errors for growth, primary balance, and inflation mostly arise during the crisis period, especially for the primary balance where there were very large unforeseen bank recapitalization costs.

[1] Note that Irish government bonds held by non-residents are considered to be external debt for this analysis.

4. **Reflecting the sizable fiscal effort, Ireland's fiscal adjustment is projected to improve its primary balance to above its debt stabilizing threshold** (Figure 2). The estimated change in the cyclically adjusted primary balance of 4½ percent of GDP over three years during the projection period is in the top quartile of fiscal adjustments observed in advanced and emerging market countries with debt greater than 60 percent of GDP. While sizable, this projected adjustment is consistent with Ireland's track record of steadfast efforts under its program, and is further underpinned by Ireland's commitments under the Excessive Deficit Procedure and fiscal rules entrenched in the Fiscal Responsibility Act. Nonetheless, the baseline debt path remains vulnerable in the event of a primary balance shock.

5. Under the baseline macroeconomic projection, Ireland's debt ratio will enter a declining path from 2014 (Figures 3 and 4). Ireland's primary surplus is projected to rise above its debt-stabilizing threshold in 2015, while the planned reduction in the large cash buffer after a major debt amortization in January 2014 allows gross public debt to decline from 2014. Automatic debt dynamics arising from the interest rate-growth differential will on average add 3 percentage points per year to the debt-to-GDP ratio in 2013–14, before stronger growth takes hold from 2015.

6. The projected decline in public debt remains fragile, vulnerable to both lower growth and contingent liabilities, which could compound each other (Figure 5). Key risk factors include:

- ***Growth shock.*** Slower growth remains the principal risk to debt sustainability. If projected real GDP growth rates for 2014–15 are lowered by 0.5 standard deviation (implying annual growth about 2 percentage points lower at -0.3 percent y/y in 2014 and 0.5 percent in 2015), the debt-to-GDP ratio peaks at 131 percent in 2015 (compared with 122 percent under the baseline) before declining.[2]

- ***Interest rate shock***. An interest rate shock does not pose a significant risk given that a 200 basis point increase on new borrowing affects the debt trajectory only marginally.[3] The baseline is built on conservative interest rate projections, which have not taken into account the full extent of recent declines in spreads, thus including a safety margin. In the medium term, Ireland is shielded from a rise in interest rates by its still-high share of fixed rate and official borrowing. While the swapping of the fixed coupon promissory note against €25 billion of floating-rate long-term bonds reduces the share of fixed-rate borrowing, there is an option to exchange a portion of them against fixed-rate bonds at the time the CBI is

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

[3] A 200 basis point interest rate shock, instead of a larger shock derived from the difference between average real interest rate level over the projection period and maximum real historical level (equivalent to 514 basis points), appears more appropriate given the exceptionally high interest rates during the crisis years (2008–10).

selling them in the market. The CBI will make such sales subject to a minimum disposal schedule and if financial stability conditions permit.

- ***Macro-fiscal shock***. If slower growth in 2014–15 were compounded by a primary balance shock[4] and by an increase in interest rates on new borrowing by 2 percentage points, the debt ratio rises to 133 percent of GDP in 2015 and falls to 126 percent by 2018. In this scenario, gross financing needs increase by about 2½ percentage points of GDP on average over the medium term compared with the baseline.

- ***Contingent liability shock***. Potential sources of financial sector contingent liabilities include: (i) shortfalls in the crystallized value of NAMA assets (including those acquired in February 2013 from the liquidated IBRC);[5] (ii) any further bank capital needs identified in the 2014 Comprehensive Assessment that could not be sourced in the market or through ESM direct recapitalization; and (iii) costs related to the ongoing restructuring of the credit union sector, although these are contained by the size of the sector, with net loans being only 2½ percent of GDP. Without estimates of the potential realization of these contingencies, a scenario assuming a 10 percent of GDP shock is used.[6] Such a shock, if combined with the above growth shock, would push gross public debt to 135 percent of GDP and 139 percent in 2014 and 2015, respectively, before declining to 130 percent by 2018.

7. **Debt reductions from asset sales present an upside risk**. Current baseline assumptions do not incorporate proceeds from state asset disposals of up to €3 billion (around 1¾ percent of GDP) in the areas of energy generation and aviation, at least half of which are to be used for debt reduction. Similarly, no allowance is made for further transactions reducing the cost incurred in supporting the banking system beyond the sales of interests in BoI and Irish Life earlier this year.

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[4] A shock equivalent to one-half of the planned fiscal adjustment over the medium term is used, instead of a larger temporary shock derived from baseline primary balance minus one-half of the 10-year historical standard deviation, given the exceptionally high primary balances (reflecting bank recap costs) during the crisis years.

[5] Based on the progress to date in preparing and valuing portfolios for sale, and the extent of interest evident in the initial sales process, the authorities do not anticipate a significant call on the budget will arise from the liquidation of IBRC assets during the remainder of 2013 and early 2014.

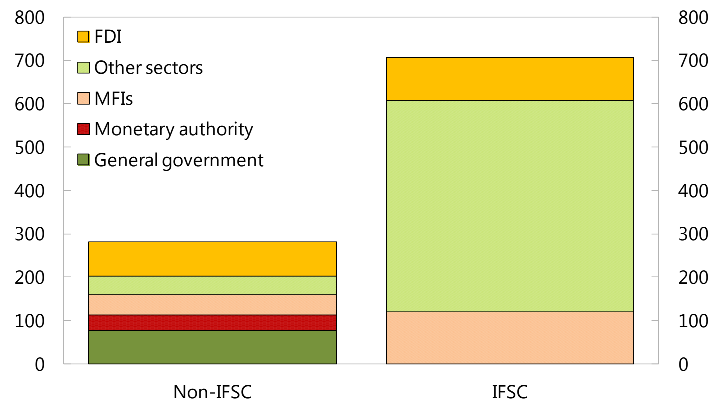
[6] A 10 percent of GDP shock is used, instead of a default shock of 10 percent of banking sector assets (equivalent to around 30 percent of GDP), taking into account the 40 percent of GDP of financial sector support already incurred.

External Debt Sustainability Analysis

8. **External debt excluding the IFSC sector stood at 282 percent of GDP at the end of Q2 2013, while the total external debt (IFSC and non-IFSC) amounted to 990 percent of GDP**:

- Compared with end 2012, the non-IFSC debt declined by 17 percentage points of GDP while total external debt increased by 6 percentage points of GDP. Net international investment liabilities in Q2 2013 stood at 108 percent of GDP, which was mostly accounted for by the non-IFSC sector. Since end-2012, total external debt has fallen by 10 percentage points of GDP, while the non-IFSC debt declined by around 17 percentage points of GDP.

External Debt Composition, 2013-Q2
(Percent of nominal projected 2013 GDP)



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

Ireland: Net International Investment Position
(In percent of GDP)

	2005	2006	2007	2008	2009	2010	2011	2012	2013 Q2
Assets	1,032	1,133	1,197	1,267	1,493	1,680	1,650	1,718	1739
Direct investment abroad	54	52	54	67	126	161	149	165	189
Portfolio investment abroad	615	693	706	701	833	922	881	971	988
Other investment abroad	362	388	437	498	533	595	619	581	561
Reserve assets	0	0	0	0	1	1	1	1	1
Liabilities	1,057	1,138	1,216	1,342	1,586	1,768	1,744	1,814	1847
Direct investment to Ireland	85	67	73	75	107	135	120	138	168
Portfolio investment to Ireland	630	689	701	711	903	1,055	1,061	1,157	1182
Other investment to Ireland	342	382	442	557	576	578	563	519	497
Net investment position	-25	-5	-19	-76	-92	-88	-94	-96	-108
Direct investment, net	-31	-15	-19	-8	19	26	30	28	21
Portfolio investment, net	-15	4	5	-9	-69	-133	-180	-186	-193
Other investment, net 1/	20	6	-5	-59	-44	18	56	62	63
Reserve assets	0	0	0	0	1	1	1	1	1
Memorandum items									
Net IIP of the IFSC	32	35	44	4	-1	-1	15	-2	1
Net IIP of the non-IFSC	-56	-41	-63	-79	-91	-87	-108	-94	-110

Source: Central Statistics Office.
1/ Includes valuation changes and errors and omissions.

- The non-IFSC debt is largely comprised of official external liabilities of the general government and the central bank (around 40 percent of the total), which increased six-fold as a result of the crisis. This portion of the external debt is likely to decline gradually in line with the public debt profile and with the ongoing reduction of the Target II liability of the Central Bank of Ireland. Around 28 percent of the non-IFSC debt is accounted for by FDI-related liabilities, which are not usually considered to be a source of vulnerability given their intra-company nature. The minority remaining is split between foreign liabilities of domestic financial institutions and other sectors.

9. **By end 2018, total external non-IFSC debt is expected to decline to 219 percent of GDP, though significant risks surround this projection** (Table 1). This revised debt projection is around 3.5 percentage points of GDP higher than at the 11th Review. Risks to the debt outlook remain (Figure 6). With growth remaining at historical averages, in 2018 debt would be over 55 percentage points of GDP higher than under the baseline, though it would remain on a declining path. A permanent ½ standard deviation shock to growth, implying a contraction of around ¼ percent in 2014 (about 2 percentage points below the baseline) and slow growth of ½ percent annually thereafter, would raise the debt-to-GDP ratio to 245 percent, 26 percentage points above the baseline. A permanent ½ standard deviation shock to the non-IFSC current account (excluding interest payments) would raise debt by around 21 percentage points of GDP above the baseline. A combined shock of ¼ of the standard deviation to the current account balance, real interest rate, and GDP growth rate would increase medium-term debt to 251 percent of GDP.

Annex I. Figure 1. Ireland Public DSA—Risk Assessment

Heat Map

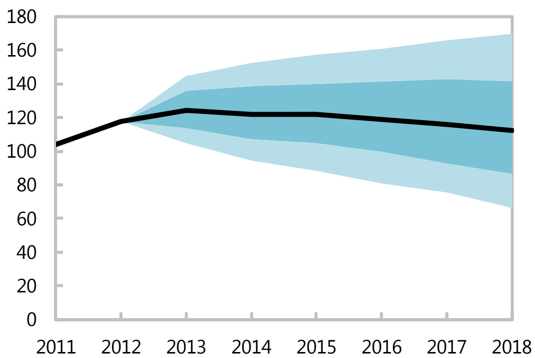
Debt level [1/]	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability shock
Gross financing needs [2/]	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability Shock
Debt profile [3/]	Market Perception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

Evolution of Predictive Densities of Gross Nominal Public Debt

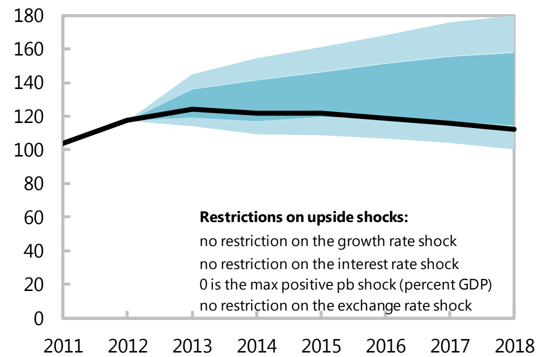
(in percent of GDP)

Baseline Percentiles: 10th-25th 25th-75th 75th-90th

Symmetric Distribution



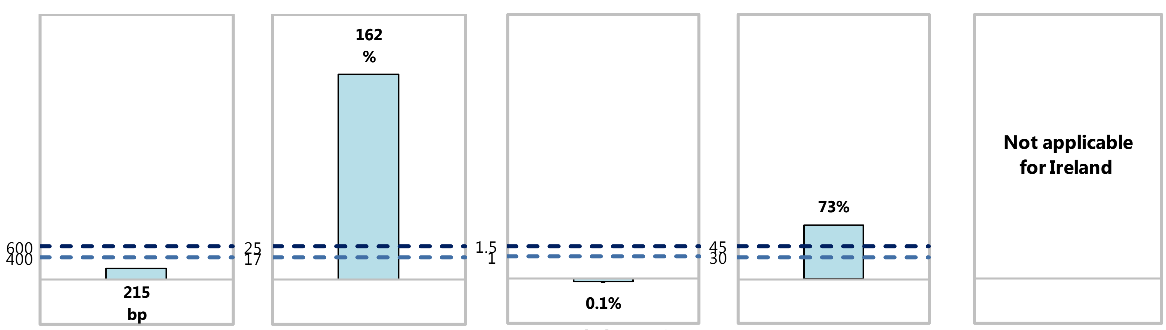
Restricted (Asymmetric) Distribution



Debt Profile Vulnerabilities

(Indicators vis-à-vis risk assessment benchmarks)

Ireland Lower early warning Upper early warning



Bond Spread over German Bonds	**External Financing Requirement**	**Annual Change in Short-Term Public Debt**	**Public Debt Held by Non-Residents**	**Public Debt in Foreign Currency**
(in basis points) 4/	(in percent of GDP) 5/	(in percent of total)	(in percent of total)	(in percent of total)

Source: IMF staff.

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

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

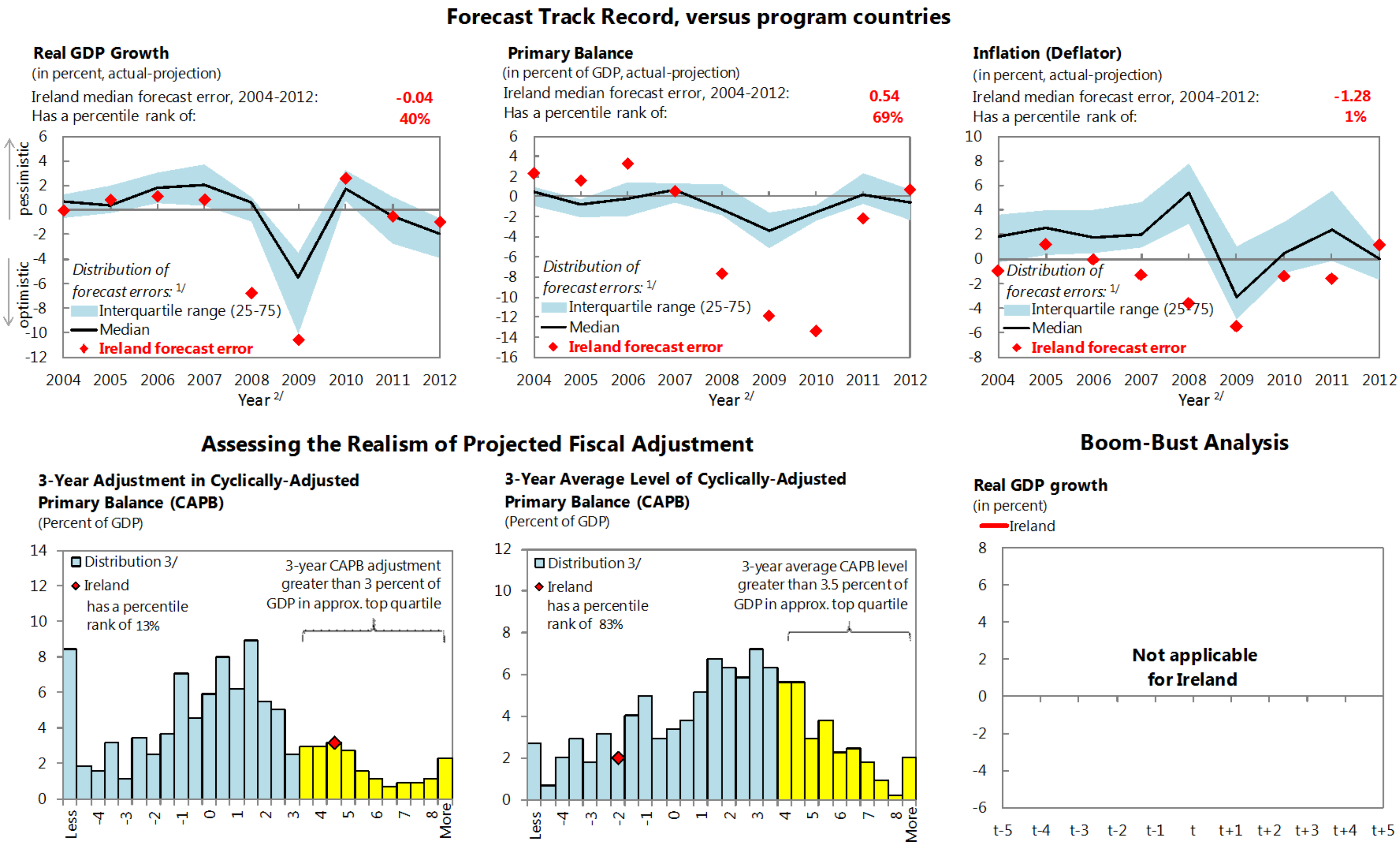
3/ The cell is highlighted in green if country value is less than the lower risk-assessment benchmark, red if country value exceeds the upper risk-assessment benchmark, yellow if country value is between the lower and upper risk-assessment benchmarks. If data are unavailable or indicator is not relevant,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

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

4/ Average over the last 3 months, 06-Jul-13 through 04-Oct-13.

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

Annex I. Figure 2. Ireland Public DSA—Realism of Baseline Assumptions



Source : IMF staff.
1/ Plotted distribution includes program countries, percentile rank refers to all countries.
2/ Projections made in the spring WEO vintage of the preceding year.
3/ Data cover annual obervations from 1990 to 2011 for advanced and emerging economies with debt greater than 60 percent of GDP. Percent of sample on vertical axis.

Annex I. Figure 3. Ireland Public DSA—Baseline Scenario

(In percent of GDP unless otherwise indicated)

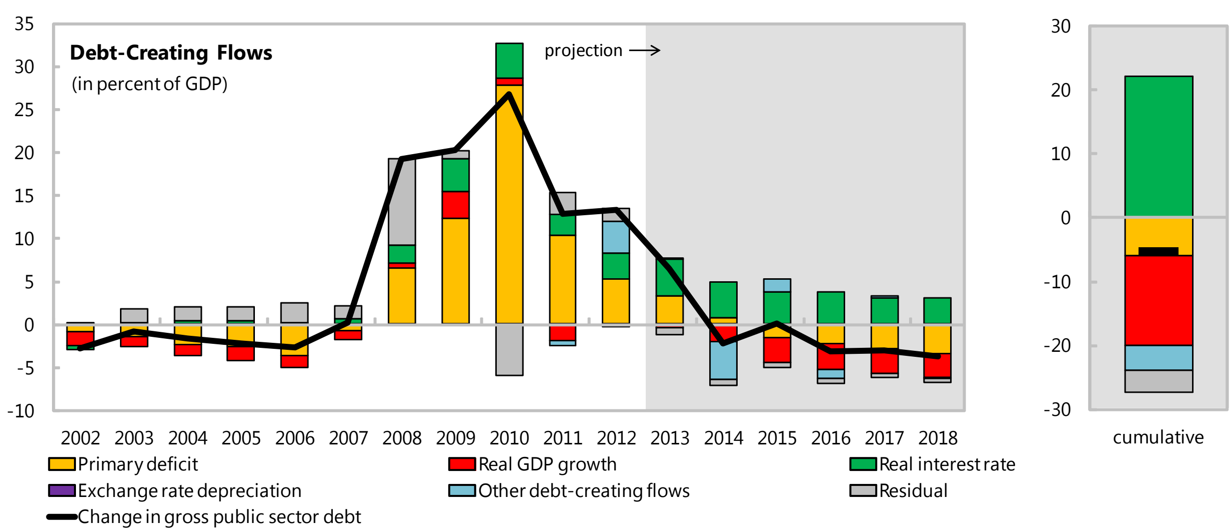
Debt, Economic and Market Indicators [1/]

	Actual			Projections					
	2002-2010	2011	2012	2013	2014	2015	2016	2017	2018
Nominal gross public debt	41.0	104.1	117.4	123.9	121.7	121.9	118.8	115.8	112.2
Public gross financing needs	...	19.0	15.7	13.5	10.6	6.8	11.6	9.0	12.3
Real GDP growth (in percent)	2.3	2.2	0.2	0.3	1.7	2.5	2.5	2.5	2.5
Inflation (GDP deflator, in percent)	1.2	0.7	0.7	0.6	0.7	1.0	1.0	1.6	1.6
Nominal GDP growth (in percent)	3.6	2.8	0.8	0.9	2.5	3.5	3.6	4.1	4.2
Effective interest rate (in percent) [3/]	4.4	3.7	3.6	4.2	4.1	4.2	4.2	4.4	4.4

As of November 27, 2013		
Sovereign Spreads		
Spread (bp) 2/		180
CDS (bp)		121
Ratings	Foreign	Local
Moody's	Ba1	Ba1
S&Ps	BBB+	BBB+
Fitch	BBB+	BBB+

Contribution to Changes in Public Debt

	Actual			Projections							
	2002-2010	2011	2012	2013	2014	2015	2016	2017	2018	cumulative	debt-stabilizing primary balance [7/]
Change in gross public sector debt	6.3	12.9	13.3	6.5	-2.2	0.2	-3.1	-2.9	-3.7	-5.2	
Identified debt-creating flows	4.8	10.4	11.8	7.2	-1.7	0.6	-2.7	-2.6	-3.4	-2.6	
Primary deficit	3.9	10.4	5.2	3.3	0.8	-1.5	-2.3	-2.9	-3.4	-5.9	0.0
Revenue and grants	34.8	33.5	33.7	34.8	35.1	35.2	35.0	34.8	34.6	209.5	
Primary (noninterest) expenditure	38.7	43.9	39.0	38.1	35.9	33.7	32.7	31.9	31.2	203.5	
Automatic debt dynamics [4/]	0.8	0.5	2.9	3.6	1.8	0.7	0.6	0.1	0.2	7.2	
Interest rate/growth differential [5/]	0.8	0.5	2.9	3.8	2.0	0.9	0.8	0.2	0.3	8.0	
Of which: real interest rate	1.3	2.5	3.1	4.2	4.1	3.8	3.7	3.1	3.1	22.0	
Of which: real GDP growth	-0.4	-1.9	-0.2	-0.4	-2.1	-2.9	-3.0	-2.9	-2.8	-14.1	
Other identified debt-creating flows	0.0	-0.5	3.7	0.2	-4.3	1.4	-1.1	0.1	-0.2	-3.9	
Drawdown of deposits (negative)	0.0	-5.7	3.2	0.5	-4.3	-0.2	-0.5	0.0	0.0	-4.5	
Other, incl. stock-flow adjustment	0.0	5.2	0.6	-0.3	-0.1	1.6	-0.6	0.1	-0.2	0.7	
Residual, incl. interest revenue [6/]	1.5	2.5	1.5	-0.8	-0.7	-0.6	-0.5	-0.4	-0.4	-3.4	



Source: IMF staff.

1/ Public sector is defined as general government.

2/ Bond Spread over German Bonds.

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

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

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

6/ Includes asset and exchange rate changes.

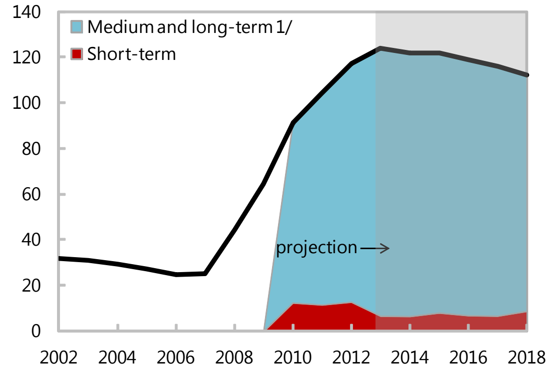
7/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Annex I. Figure 4. Ireland Public DSA—Composition of Public Debt and Alternative Scenarios

Composition of Public Debt

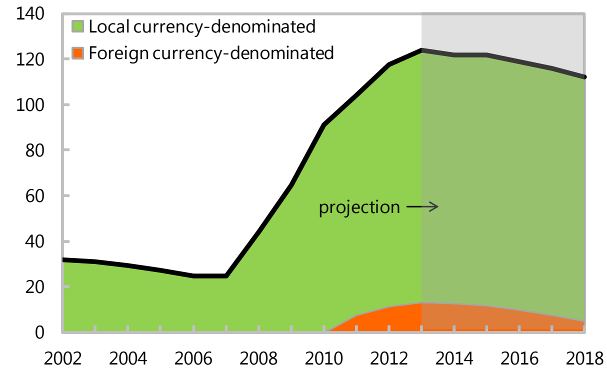
By Maturity

(in percent of GDP)



By Currency

(in percent of GDP)

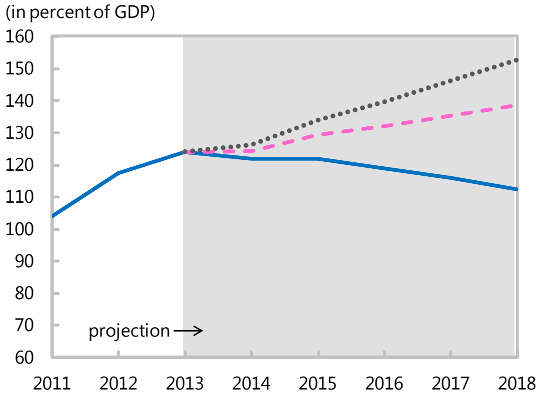


Alternative Scenarios

Baseline Historical Constant Primary Balance

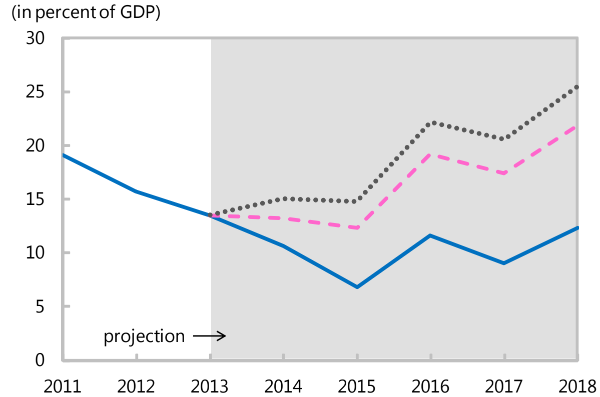
Gross Nominal Public Debt

(in percent of GDP)



Public Gross Financing Needs

(in percent of GDP)



Underlying Assumptions

(in percent)

Baseline Scenario	2013	2014	2015	2016	2017	2018
Real GDP growth	0.3	1.7	2.5	2.5	2.5	2.5
Inflation	0.6	0.7	1.0	1.0	1.6	1.6
Primary Balance	-3.3	-0.8	1.5	2.3	2.9	3.4
Effective interest rate	4.2	4.1	4.2	4.2	4.4	4.4
Constant Primary Balance Scenario						
Real GDP growth	0.3	1.7	2.5	2.5	2.5	2.5
Inflation	0.6	0.7	1.0	1.0	1.6	1.6
Primary Balance	-3.3	-3.3	-3.3	-3.3	-3.3	-3.3
Effective interest rate	4.2	4.1	4.2	4.3	4.4	4.5

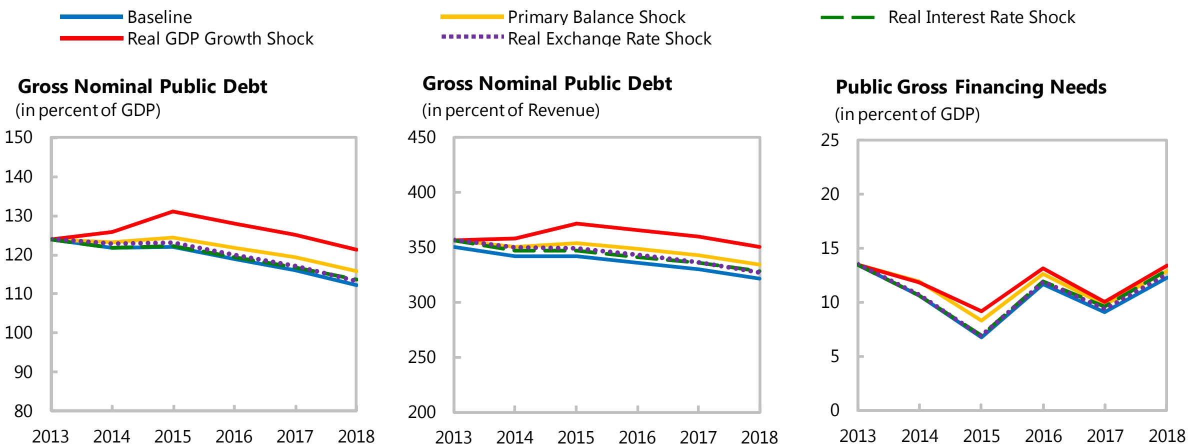
Historical Scenario	2013	2014	2015	2016	2017	2018
Real GDP growth	0.3	1.7	1.7	1.7	1.7	1.7
Inflation	0.6	0.7	1.0	1.0	1.6	1.6
Primary Balance	-3.3	-5.2	-5.2	-5.2	-5.2	-5.2
Effective interest rate	4.2	4.1	4.3	4.4	4.5	4.7

Source: IMF staff.

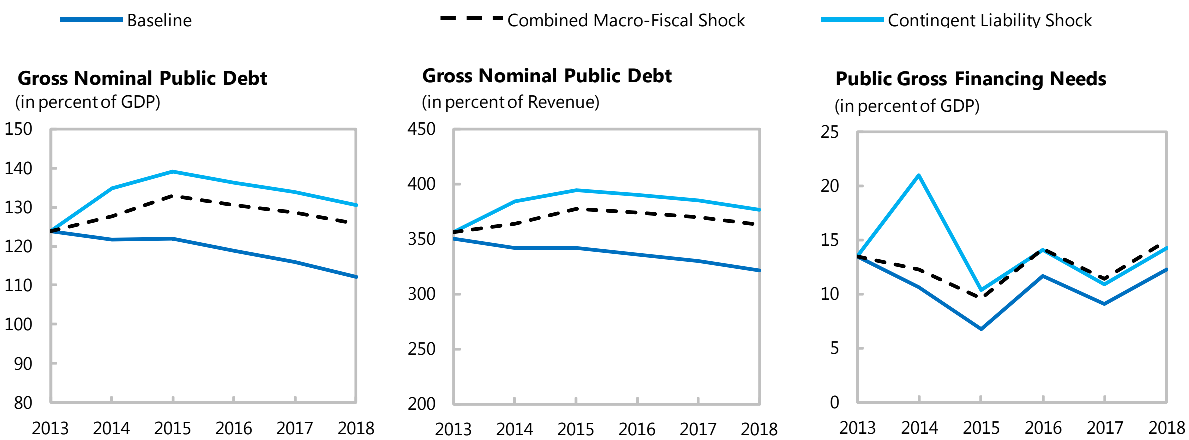
1/ Includes retail debt.

Annex I. Figure 5. Ireland Public DSA—Stress Tests

Macro-Fiscal Stress Tests



Additional Stress Tests



Underlying Assumptions

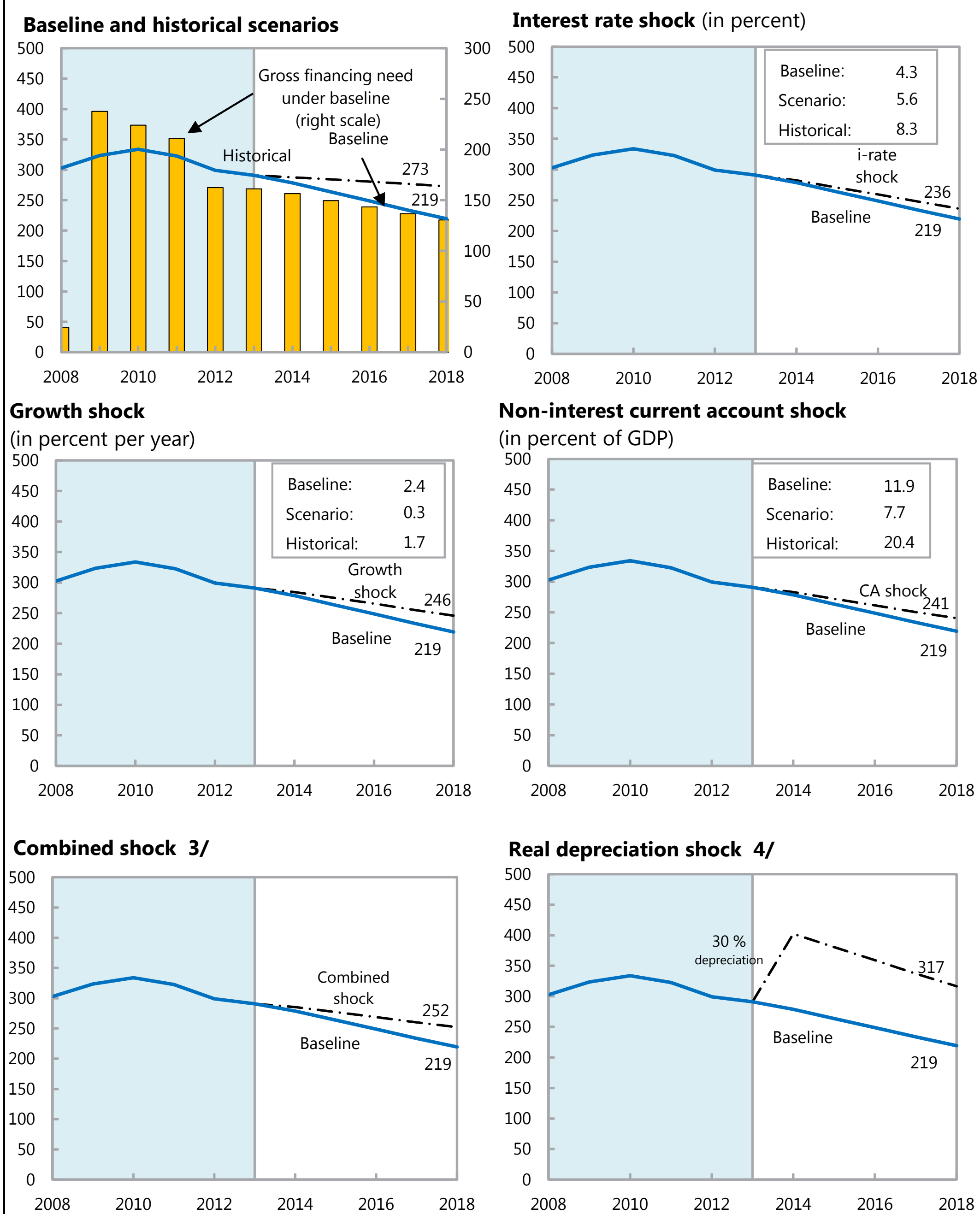
(in percent)

	2013	2014	2015	2016	2017	2018
Primary Balance Shock						
Real GDP growth	0.3	1.7	2.5	2.5	2.5	2.5
Inflation	0.6	0.7	1.0	1.0	1.6	1.6
Primary Balance	-3.3	-2.1	0.4	1.9	2.6	3.2
Effective interest rate	4.2	4.1	4.2	4.3	4.4	4.5
Real Interest Rate Shock						
Real GDP growth	0.3	1.7	2.5	2.5	2.5	2.5
Inflation	0.6	0.7	1.0	1.0	1.6	1.6
Primary Balance	-3.3	-0.8	1.5	2.3	2.9	3.4
Effective interest rate	4.2	4.1	4.3	4.5	4.7	4.9
Combined Macro-Fiscal Shock						
Real GDP growth	0.3	-0.3	0.5	2.5	2.5	2.5
Inflation	0.6	0.2	0.5	1.0	1.6	1.6
Primary Balance	-3.3	-2.1	-0.2	1.9	2.6	3.2
Effective interest rate	4.2	4.2	4.4	4.5	4.8	5.0

	2013	2014	2015	2016	2017	2018
Real GDP Growth Shock						
Real GDP growth	0.3	-0.3	0.5	2.5	2.5	2.5
Inflation	0.6	0.2	0.5	1.0	1.6	1.6
Primary Balance	-3.3	-1.7	-0.2	2.3	2.9	3.4
Effective interest rate	4.2	4.1	4.2	4.3	4.4	4.5
Real Exchange Rate Shock						
Real GDP growth	0.3	1.7	2.5	2.5	2.5	2.5
Inflation	0.6	1.1	1.0	1.0	1.6	1.6
Primary Balance	-3.3	-0.8	1.5	2.3	2.9	3.4
Effective interest rate	4.2	4.2	4.2	4.3	4.4	4.4
Contingent Liability Shock						
Real GDP growth	0.3	-0.3	0.5	2.5	2.5	2.5
Inflation	0.6	0.2	0.5	1.0	1.6	1.6
Primary Balance	-3.3	-10.8	1.5	2.3	2.9	3.4
Effective interest rate	4.2	4.2	4.5	4.5	4.6	4.7

Source: IMF Staff.

Annex I. Figure 6. Ireland: External Debt Sustainability: Bound Tests 1/ 2/
(External debt in percent of GDP)



Sources: International Monetary Fund, Country desk data, and staff estimates.
1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.
3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.
4/ One-time real depreciation of 30 percent occurs in 2014.

Annex 1. Table 1. Ireland: External Debt Sustainability Framework, 2008-2018

(In percent of GDP, unless otherwise indicated)

	Actual							Projections						
	2008	2009	2010	2011	2012	10-Year Historical Average	10-Year Standard Deviation	2013	2014	2015	2016	2017	2018	Debt-stabilizing non-interest current account 6/
Baseline: External debt	302.7	323.6	334.0	322.7	299.2			**291.1**	**278.7**	**263.2**	**248.2**	**233.1**	**218.9**	**-2.6**
Change in external debt	45.1	20.8	10.4	-11.3	-23.5			-8.2	-12.4	-15.4	-15.0	-15.1	-14.2	
Identified external debt-creating flows (4+8+9)	15.1	31.9	11.6	-9.1	-5.1			-6.6	-10.1	-12.4	-11.9	-11.2	-10.5	
Current account deficit, excluding interest payments	-26.6	-20.6	-22.9	-35.8	-16.1			-13.6	-12.2	-12.0	-11.4	-11.9	-11.8	
Deficit in balance of goods and services	-137.8	-143.9	-158.2	-161.4	-167.7			-165.7	-166.8	-167.6	-169.6	-171.5	-173.5	
Exports	71.4	77.5	85.9	89.0	93.0			91.8	92.3	93.2	94.4	95.4	96.4	
Imports	-66.4	-66.4	-72.3	-72.3	-74.7			-73.9	-74.5	-74.4	-75.2	-76.1	-77.1	
Net non-debt creating capital inflows (negative)	0.4	-1.9	3.1	0.6	-1.6			-4.3	-4.3	-4.2	-4.2	-4.2	-4.1	
Automatic debt dynamics 1/	41.2	54.4	31.3	26.1	12.5			11.3	6.4	3.8	3.7	4.9	5.4	
Contribution from nominal interest rate	27.8	20.9	22.7	35.4	15.2			12.3	11.3	10.4	10.2	10.9	11.0	
Contribution from real GDP growth	5.9	21.5	3.5	-7.0	-0.5			-1.0	-4.9	-6.7	-6.4	-6.0	-5.7	
Contribution from price and exchange rate changes 2/	7.6	12.0	5.0	-2.2	-2.1			...	...	...	...	...	...	
Residual, incl. change in gross foreign assets (2-3) 3/	30.0	-11.1	-1.2	-2.2	-18.4			-1.6	-2.3	-3.0	-3.2	-3.9	-3.7	
External debt-to-exports ratio (in percent)	423.9	417.7	388.7	362.4	321.6			317.0	301.9	282.3	262.9	244.4	227.1	
Gross external financing need (in billions of euro) 4/	44.4	385.8	354.3	342.8	266.2			266.7	265.3	262.1	260.6	259.0	257.6	
in percent of GDP	24.7	237.7	224.1	210.8	162.4			161.2	156.5	149.2	143.0	136.4	130.3	
Scenario with key variables at their historical averages 5/								**291.1**	**287.8**	**284.4**	**280.8**	**277.0**	**273.0**	**16.1**
Key Macroeconomic Assumptions Underlying Baseline														
Real GDP growth (in percent)	-2.2	-6.4	-1.1	2.2	0.2	1.7	4.0	0.3	1.7	2.5	2.5	2.5	2.5	
GDP deflator (change in percent)	-2.9	-3.8	-1.5	0.7	0.7	0.7	2.6	0.5	0.8	1.1	1.2	1.6	1.6	
Nominal external interest rate (in percent)	10.3	6.2	6.8	10.9	4.7	8.3	2.6	4.2	4.0	3.9	4.0	4.6	4.9	
Growth of exports (in percent)	-1.2	-2.3	8.0	6.6	5.4	4.2	4.3	-0.5	3.1	4.6	5.1	5.2	5.3	
Growth of imports (in percent)	0.0	-10.0	6.0	3.0	4.1	2.9	6.5	-0.3	3.4	3.4	5.0	5.3	5.6	
Current account balance, excluding interest payments	26.6	20.6	22.9	35.8	16.1	20.4	8.4	13.6	12.2	12.0	11.4	11.9	11.8	
Net non-debt creating capital inflows	-0.4	1.9	-3.1	-0.6	1.6	-0.4	2.1	4.3	4.3	4.2	4.2	4.2	4.1	

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

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

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

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

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

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

Annex II. Fund Relations

(As of October 31, 2013)

Membership Status: Joined August 8, 1957; Article VIII

General Resources Account:	**SDR Million**	**Percent of Quota**
Quota	1,257.60	100.00
Fund holdings of currency	19,885.41	1,581.22
Reserve position in Fund	258.66	20.57

SDR Department:	**SDR Million**	**Percent of Allocation**
Net cumulative allocation	775.42	100.00
Holdings	647.56	83.51

Outstanding Purchases and Loans:	**SDR Million**	**Percent of Quota**
Extended Arrangements	18,886.43	1,501.78

Financial Arrangements:

Type	**Approval Date**	**Expiration Date**	**Amount Approved (SDR million)**	**Amount Drawn (SDR million)**
EFF	12/16/10	12/15/13	19,465.80	18,205.43

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

	2013	2014	2015	2016	2017
Principal			535.20	2,173.15	2,895.74
Charges/Interest	124.11	627.09	654.38	607.96	509.42
Total	124.11	627.09	1,189.58	2,781.11	3,405.16

Exchange Rate Arrangement and Exchange Restrictions:

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

Safeguards Assessment:

The safeguards assessment of the Central Bank of Ireland (CBI) was finalized in March 2011. The safeguards assessment of the Central Bank of Ireland (CBI) found that the CBI has a relatively strong safeguards framework in place. Its financial statements are audited in accordance with international standards and published. Governance and control systems adhere to good practices. The assessment recommended measures to address heightened risks emanating from the financial crisis, notably liquidity lending, and to improve transparency. Recommendations were also made to strengthen the de-jure autonomy of the central bank. Progress has been made in implementing these recommendations: the CBI has strengthened internal governance and control procedures for ELA; brought forward the publication dates for its audited financial accounts; clarified its accounting framework for areas not covered by ECB guidelines; and formally approved revised investment guidelines. The CBI and DoF are considering how to strengthen the arrangements for financial autonomy of the CBI, which may require changes to central bank legislation and changes in other related regulations, which would be prepared in consultation with the ECB.

Article IV Consultations:

The last Article IV consultation was concluded on September 5, 2012 (IMF Country Report No. 12/264). Article IV consultations with Ireland are on the 24-month cycle.

Twelfth Review Under the Extended Arrangement:

Discussions were held in Dublin during October 29–November 7, 2013. The IMF team comprised Craig Beaumont (head), Ashok Bhatia, Alexandre Chailloux, Jochen Andritzky, and Emilia Jurzyk (all EUR); Laura Jaramillo (FAD); Michael Moore and Joaquin Gutierrez Garcia (both MCM), and Varapat Chensavasdijai (SPR). Teams from the EC and ECB as well as Mary O'Dea and Michael Hough from the Executive Director's office participated in the discussions. The mission met with the Minister for Finance, the Minister for Public Expenditure and Reform, the Governor of the Central Bank and the Deputy Governor for Financial Regulation, the Chief Executive of the National Treasury Management Agency, the Chief Executive of the National Asset Management Agency, and senior officials from these institutions. The mission also met with representatives of the Fiscal Council; the Department of Jobs, Enterprise and Innovation; the Department of Justice and Equality; the Department of Social Protection; Central Statistics Office; the Economic and Social Research Institute; banks and market analysts.

Technical Assistance:

Department	Purpose	Date
STA	Balance of Payments Statistics	January 2011
STA	Monetary and Financial Statistics	January 2011

Resident Representative:

Mr. Peter Breuer assumed his post in September 2011.

Appendix I. Ireland: Letter of Intent

Dublin, 29 November 2013

Ms. Christine Lagarde
Managing Director
International Monetary Fund
Washington, D.C. 20431

Dear Ms. Lagarde:

1. **Our economic programme has achieved its main objectives and has underpinned Ireland's emergence from the crisis.** The key objectives of our programme were to address financial sector weaknesses, to put Ireland's economy on a path of sustainable growth, to strengthen our public finances, to boost job creation, and to fully regain international capital market access. Now, as we approach the conclusion of our programme we are beginning to reap the rewards of our sustained efforts. Economic growth has returned, albeit at a slower pace than was anticipated at the start of the programme. The public finances have been put on a sustainable footing and unemployment is declining slowly but steadily. Importantly, we have also successfully returned to financial market funding. The financial sector has undergone significant restructuring since the beginning of the crisis and we will continue to progress this agenda. All of this has been achieved by steadfast implementation and delivery of our commitments under the programme and complemented by European decisions that led to a reduction of the interest rates on the EU sourced loans and an extension of the maturities of the EFSF and EFSM loans. This effort has encompassed the completion of over 260 actions to date. Looking ahead we intend to maintain our momentum and press on with our reform agenda. We are preparing a Medium-Term Economic Strategy (MTES), which will articulate the key principles that will underpin economic policy for the period to 2020. It will address the key policy areas such as education and training, labour market activation, industrial/innovation, access to credit, competition and budgetary policy. Through this strategic, medium-term perspective, the MTES will not duplicate – but will complement – the necessarily more short-term focus of other related policy efforts such as the *Action Plan for Jobs*. Although the Extended Fund Facility arrangement is ending we will keep our close dialogue with the Fund and will consult with it semi-annually under the usual Post-Program Monitoring.

I. MACROECONOMIC OUTLOOK

2. **Economic growth has resumed and has supported programme objectives.** Real GDP is forecast to grow by a modest 0.2 per cent this year. The impact of the patent cliff is weighing on pharma-chem activity, given its large weight in Irish output and exports. Developments in the domestic economy have been considerably more favourable though. Employment returned to

year-on-year growth of nearly 2 per cent in the second quarter, and unemployment, while still high, is continuing to fall. High-frequency indicators for the third and fourth quarters are also positive. Purchasing managers' indices have recorded some multi-annual highs, tourism numbers are up substantially and house prices have shown consistent growth since early in the year. 2014 GDP is forecast to grow by about 2 per cent. Net exports are expected to make a positive contribution to growth again, as the fast-growing service export sector offsets some drag from pharma-chem activity. Expectations for trading partner growth are also supportive as are continuing strong inflows of foreign direct investment. Domestic demand is expected to expand modestly, as increased employment and incomes spill over into real activity and construction output continues to rise from very low levels. The recovery is expected to strengthen with GDP growth set to average 2½ per cent over 2015 and 2016.

II. FISCAL POLICY

3. **In each year of the programme we have met or exceeded the fiscal headline targets.** The level of consolidation is significant with Budget 2011 to Budget 2014 achieving consolidation of over €16.4 billion. This is equivalent to 9.6 per cent of the forecast GDP for 2013, and approximately 90 per cent of the consolidation required in the period 2011 to 2015. All of this was achieved against a background of much lower growth than was projected when the programme started. We have also introduced important structural changes to the management of our public finances with the enactment of the Fiscal Responsibility Act 2012, the establishment of the Irish Fiscal Advisory Council on a statutory basis, the introduction of regular wide-scale reviews of public spending (the next Comprehensive Review of Expenditure to take place in advance of Budget 2015), and the implementation of multi-annual expenditure budgeting and Ministerial expenditure ceilings. The improved fiscal frameworks that have been put in place over recent years are testament to the commitment of the Government to ensuring that the mistakes of the past will not be repeated.

4. **The 2013 Budget position remains on track and we will ensure the 2013 fiscal deficit target of 7.5 per cent of GDP is met.** Building on the actions taken since mid-2008, which were designed to yield savings around €28 billion, *Budget 2014* introduced a set of adjustment measures aimed at reducing the deficit next year to 4.8 per cent of GDP, below the 5.1 per cent of GDP requirement under the Excessive Deficit Procedure (EDP). The measures are also intended to achieve a primary balance or a small surplus next year. Broadening the revenue base, reforming the health sector, and targeting social supports towards the most vulnerable will help achieve the further fiscal consolidation needed in a durable and growth-friendly manner.

5. **A clear focus on reducing the deficit below 3 per cent of GDP in 2015 has been the cornerstone on which budgetary planning over recent years has been anchored.** The Government remains steadfast in its commitment to meet this deficit target and will do whatever is necessary to achieve this. Beyond 2015, Ireland will be subject to the conditions of the stability and growth pact which necessitates continued fiscal prudence and structural improvement over the medium term.

III. FINANCIAL SECTOR

6. **Confidence in the Irish banks is beginning to return and has helped reduce their reliance on Eurosystem funding, which is now a fraction of what it was at the beginning of the programme.** As part of the 2011 Financial Measures Programme Irish banks were recapitalised to meet a capital requirement identified at €24 billion which was sourced from the private market, burden sharing with subordinated bondholders and from the State. The banking system has been restructured including deleveraging undertaken as part of the Financial Measures Programme and the merger of Allied Irish Banks with EBS. Exceptional Liquidity Assistance (ELA) has been removed from the system following the liquidation of IBRC. NAMA has maintained a strong financial position, generating considerable cash, leaving it on track to redeem €7.5 billion of bonds by the end of this year. Private capital has been introduced to the banking system including the sale of equity (in 2011) and contingent capital notes (in 2013) in Bank of Ireland and the sale of Irish Life (in 2013).

7. **We will press ahead with further restructuring of the banking sector.** We have prepared a preliminary assessment of the balance sheets of the PCAR banks. A rigorous review is being performed incorporating an assessment of impairment provisions and a review of the appropriateness of risk weights for regulatory capital purposes. The review has the benefit of extensive sampling of loan files by independent third parties and engagement with staff of the EC, ECB and IMF on an ongoing basis on progress, methodology, inputs, outputs and findings. The review will inform the continuing supervisory dialogue with each of the banks on the adequate level of provisioning at year end, in line with the Central Bank's guidelines. We will agree restructuring plans for AIB and PTSB with the European Commission and these plans will be implemented along with the already agreed restructuring plan for Bank of Ireland. Returning the banks to profitability will continue to be a key focus. The legacy banking assets now housed in NAMA will be run down over time together with assets that will be transferred to it from the liquidated IBRC. We will continue our policy of exiting our banking investments in a manner that maximises the proceeds to be returned to taxpayers. The main Irish banks will undergo a comprehensive risk assessment, including a stress test in 2014, in the context of the upcoming euro area-wide exercise prior to the establishment of the SSM.

8. **Building on the recommendations of the 2011 Inter-Departmental Mortgage Arrears Working Group, we have put in place a broad suite of measures to address the problem of mortgage arrears in a way that seeks to maintain credit discipline while providing appropriate relief to borrowers who are experiencing genuine repayment difficulty.** We have significantly reformed and updated our personal insolvency law and practice and also made changes to vindicate the legitimate rights of creditors. The Personal Insolvency Act 2012 introduced new insolvency resolution frameworks and also modernised the judicial bankruptcy system. The Land and Conveyancing Law Reform Act 2013 removed an uncertainty regarding the rights of some secured creditors. We have also put in place a process to require mortgage lenders to resolve, on a sustainable basis, cases of mortgage arrears. In particular, performance targets have been set for six credit institutions requiring them to propose and conclude sustainable mortgage solutions for their mortgages which are more than 90 days in arrears.

9. **Financial sector repair will continue with a view to ensuring that significant progress is made in the resolution of mortgage and SME difficulties in 2014.** The ongoing work on durable resolution of mortgages in arrears will reduce uncertainties that weigh on economic recovery. The Mortgage Arrears Resolution Targets process will be implemented in a resolute manner with a view to addressing most mortgages in arrears by the end of next year. The Insolvency Service of Ireland is now fully operational and will process insolvency applications from insolvent debtors in a fair and efficient way. In addition, we are continuing to address the SME distressed portfolios (which include considerable property-related exposures) through targets which require the banks to implement sustainable long-term debt resolution strategies for all distressed SME loans. Overall, we will continue to monitor and assign a high priority to the resolution of the arrears problem. Ensuring an adequate flow of credit for SMEs remains a priority and active consideration is being given to alternative provision of non-bank financing for the enterprise sector.

IV. STRUCTURAL REFORM

10. **Structural reform focusing on improved competitiveness has also been progressed.** This included the enactment of the Competition (Amendment) Act (2012) (to support the Competition Authority in the investigation and prosecution of anti-competitive practices) and the implementation of Sectoral Wage Reforms. As a result, over the last three years, we have won back much of the competitiveness we lost during the boom. Having seen significant erosion in competitiveness during the boom years, the European Commission is now estimating a 22 per cent improvement in unit labour costs in Ireland vis-à-vis the euro area over the period 2008-2014. The economic path for the years ahead will be directed by the Medium Term Economic Strategy 2014-2020 which we are preparing (see paragraph 1 also).

11. **There has been significant reform in the Health Sector, with significant reduction in the cost of drugs to the State.** The implementation of generic substitution and reference pricing has been prioritised by the Department, the Health Service Executive and the Irish Medicines Board. Reference pricing is expected to deliver at least €50 million savings in 2014. The Health (Pricing and Supply of Medical Goods) Act 2013 also includes a process for the review of existing prices outside of reference pricing. Each medicinal product, which was on the Reimbursement List when the legislation was commenced, must be reviewed by the HSE within three years to determine whether it should remain on the List and, if so, the price that should apply.

12. **Structural reform in other areas including labour market activation is well underway.** The labour activation effort will prioritise the reduction and prevention of long-term unemployment, combatting youth unemployment and helping to reduce the number of jobless households; this will involve greater engagement on job seeking activity and appropriate referral to activation or further education and training programmes. We also intend to deliver a Strategic Implementation Plan for Further Education and Training that will draw on the analysis and

recommendations of the FET Strategic Review carried out under the Programme this year. Legal services reform is also being advanced. The Legal Services Regulation Bill has completed Second Stage and commenced Committee Stage in July 2013. The resumption of Committee Stage is expected in early 2014 with a view to the Bill's earliest enactment and the expedited establishment of the new Legal Services Regulatory Authority. Water sector reforms are also continuing at pace. The Water Services Bill is progressing and is expected to be published shortly.

V. FUNDING

13. **Strong policy implementation of the programme has improved funding conditions even as domestic challenges and external uncertainties remain.** Ireland remains on course to end the year with a cash buffer sufficient to cover more than 12 months of Exchequer financing needs. The 7-year extension in EFSM/EFSF maximum average maturities and the February IBRC Promissory Note transaction significantly reduce funding needs in the coming years. These positive developments strengthen Ireland's ability to access long-term market funding on sustainable terms. The NTMA is guiding for €6 billion to €10 billion of market issuance in 2014 by way of pre-funding for 2015. In the context of euro area sovereign issuance requirements this is relatively modest. The NTMA looks forward to normalised engagement with the debt markets, following an exit from the EU-IMF programme, through 2014 and beyond using the standard issuance mechanisms, such as bond auctions and syndications.

14. **In light of our strong performance and the policies outlined in this letter, we request the completion of the twelfth review under the Extended Arrangement.** This would complete the disbursements of international assistance under the programme. We request the drawdown of the remaining programme funding in an amount equivalent to SDR 579.3748 million at the time of the completion of the review.

15. **We authorise the IMF to publish this Letter of Intent and the related staff report.**

This letter is being copied to Messrs. Draghi, Dijsselbloem, Rehn, and Šadžius.

Sincerely,

/s/	/s/
Michael Noonan, T.D.	Patrick Honohan
Minister for Finance	Governor of the Central Bank of Ireland

IRELAND

TWELFTH REVIEW UNDER THE EXTENDED ARRANGEMENT AND PROPOSAL FOR POST-PROGRAM MONITORING—SUPPLEMENTARY INFORMATION

December 12, 2013

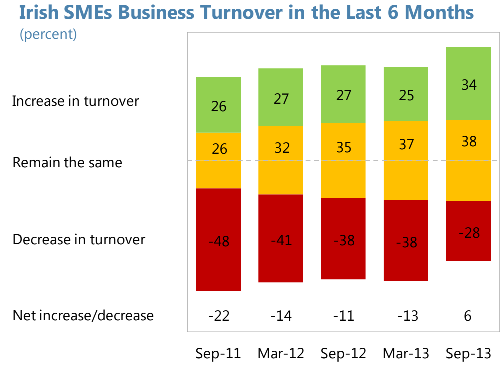
Prepared By European Department

This supplement provides information that has become available since the issuance of the staff report on December 2, 2013. The information does not alter the thrust of the staff appraisal.

Recent high-frequency indicators continue to signal stronger economic growth in H2. The unemployment rate eased to 12.5 percent in November, its lowest reading since June 2009. Although PMIs for manufacturing, services, and construction all eased in November, they all remained significantly above the 50 mark signifying expansion. In November, the KBC Ireland/ESRI consumer confidence index retreated from a six-year high reached in the prior month, perhaps reflecting the impact of Budget 2014, but the index level remained relatively high. HICP inflation edged up to 0.3 percent y/y in November as increases in excise duties in Budget 2014 came into effect.

A survey of Small and Medium Enterprises found a significant improvement in trading conditions in Q2-Q3 along with a rise in credit approvals rates. The survey found 34 percent of SMEs experienced an increase in turnover, up from 25 percent in the previous six months, turning the net increase in turnover positive for the first time since the survey's inception in 2011. Trading conditions improved for all sizes of SME, with micro and small-sized companies gaining most. Although fewer SMEs sought credit, they report 80 percent of applications were approved in full or partially (excluding pending applications), an improvement of

Irish SMEs Business Turnover in the Last 6 Months
(percent)



Sources: RedC survey; and DoF.

4 percentage points. To further improve financing conditions for SMEs, the Department of Jobs, Enterprise, and Innovation will follow up on the expert review of the SME Credit Guarantee Scheme, which proposes several amendments to increase its take-up and future performance.

November exchequer figures suggest the general government deficit target for 2013 will be achieved with a more comfortable margin. Budget outturns for November showed strong revenues while spending remained within allocations. Cumulative revenues (after adjusting for one-offs) through end November were slightly above budget projections, as corporate tax, Pay Related Social Insurance, and stamp duties continued to over-perform, and earlier shortfalls on VAT and excise duties narrowed somewhat, indicative of rising consumer spending. Cumulative primary expenditure (excluding ELG payments stemming from the liquidation of IBRC) was 0.4 percent of GDP below the authorities' profile, though some of this underspending is likely to unwind by year end. The cumulative exchequer primary deficit through end November was 1.9 percent of GDP, 0.5 percent of GDP below the authorities' profile. Overall, these figures suggest a general government deficit closer to 7 percent of GDP in 2013, somewhat below the staff report estimate of 7.3 percent of GDP, resulting in a larger buffer relative to the target of 7.5 percent of GDP for 2013.

Cumulative Exchequer Out-Turn vs. Authorities' Profile,
January to November 2013
(Percent of GDP)

	Out-turn Nov-13	Authorities' Profile Nov-13	Out-turn Nov-12
Revenue	29.7	29.6	28.9
Tax revenue	27.4	27.1	26.3
Other revenue	2.4	2.5	2.6
Expenditure	35.7	36.1	36.0
Current primary	29.6	29.7	30.4
Interest payments	4.1	4.1	3.5
Capital	2.0	2.3	2.1
Overall balance	-6.0	-6.5	-7.1
Primary balance	-1.9	-2.4	-3.7

Sources: Department of Finance; and IMF staff estimates.
Note: To facilitate comparability: (i) 2012 tax revenues do not include the €251 million corporation tax payment delayed from December 2011; (ii) outlays in respect of Irish Life (€1.3 billion) and credit unions (€250 million) are excluded from 2012 capital spending; (iii) proceeds from the sale of Bank of Ireland contingent capital notes (€1 billion) and Irish Life (€1.3 billion) are excluded from 2013 other receipts; and (iv) Eligible Liabilities Guarantee scheme payments linked to the promissory note transaction of €1 billion are excluded from 2013 current expenditure.

Balance sheet assessment (BSA) results had limited impact on financial markets. The CBI finalized intensive work on bank diagnostics in late November as scheduled, and communicated the results to each of the three banks covered by the assessment. Banks in turn made short announcements. Secondary market yields on three-year covered bonds from BoI and AIB as well as Irish government bond yields remained stable. BoI's share price declined about 3 percent on the day of its announcement of the BSA results.

Soon afterwards, the government recouped its investment in BoI preference shares made to inject capital in 2009. The transaction consisted of two components: (i) BoI placed €580 million of new ordinary shares, repaying the state €537 million (at par) after expenses; and (ii) the government sold the remaining €1.3 billion of preference shares to private investors. The transaction reduces the government's stake in BoI by about one percentage point to 14 percent. The authorities have recouped around €2.05 billion from the transaction, consisting of €1.837 billion in principal value, a profit of €62 million, and accumulated interest of €151 million. The CBI confirmed that, in line with EBA's Q&A decision of October 31, 2013, BoI will be able to include €1.3 billion of preference shares sold to private investors in its common equity tier 1 calculations under Basel III grandfathering rules until end 2017. However, it is not BoI's intention to retain the 2009 preference shares as regulatory common equity tier 1 capital after July 2016, provided the capital buffer remains adequate.

NAMA has met its target to redeem a quarter of its outstanding senior bonds by end 2013. On December 4, NAMA announced the redemption of €500 million in senior bonds, reaching its goal of €7.5 billion in total, while also holding a cash balance of €3 billion. To guide its asset disposal and other activities, the NAMA Board has set a target of redeeming another €7.5 billion in senior bonds by end 2016 and expects to redeem all €30.2 billion by 2020. NAMA also announced the redemption of €200 million in the senior bonds which had been issued following its purchase of the IBRC floating charge from the CBI when IBRC was put into liquidation in February 2013, bringing the total redemption of these bonds to €500 million.

Recent statistics on mortgage arrears show a stabilization in overall arrears in Q3 but longer dated arrears continue to rise. In relation to mortgages on primary dwellings, the value of mortgages in arrears remained stable at about 23.6 percent of the total in Q3. There was a change in the composition of these arrears, with mortgages in arrears of less than 90 days past due declining 6.5 percent by value in Q3. In contrast, mortgages in arrears of 90 days or more rose by 1.8 percent, with this increase entirely driven by rising arrears of over 720 days. For buy-to-let mortgages, the flow of mortgages into early arrears also slowed, but the share of mortgages in arrears by value edged up further, from 35.7 percent at end June to 36.2 percent at end September.

Loan modifications increased in Q3 with a continued shift away from short-term forbearance and a sharp rise in legal proceedings. For primary dwelling mortgages, 23,776 new restructuring arrangements were agreed in Q3, representing 3.1 percent of mortgage contracts. The share of short term forbearance modifications on primary dwelling mortgages, under which debtors pay interest only or less, declined further, from 37 percent of total restructurings at end June to 30 percent at end September. The share of restructured loans on which payments are meeting the terms of the arrangement improved slightly to 78.9 percent. Following the removal of the unintended legal barriers to certain repossession proceedings in July, legal proceedings to enforce collateral on primary dwelling mortgages were issued in 1,830 cases in Q3, up sharply from 270 in Q2.

On December 5 the CBI published its Mortgage Arrears Resolution Targets (MART) for end June 2014. Each bank is subject to targets for proposed solutions of 75 percent of arrears cases over 90 days by end June 2014, and for concluded solutions of 35 percent of cases. As the banks have made substantial progress in initiating proposed solutions, the CBI intends to shift its supervisory focus to conclusions of solutions and their durability. Considering that empirical experience with concluded solutions under the MART framework is still limited, the Q2 2014 targets appear to strike a reasonable balance between the challenging goal of largely completing sustainable solutions by end 2014 and the need for solutions to be durable if they are to have the benefits intended.

Residential Mortgage Arrears Resolution Targets

Targets 1/	2013			2014			
	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Sustainable solutions proposed							
(percent of customers 90+ days in arrears)	20	30	50	70	75	*2/*	*2/*
Arrangements concluded							
(percent of customers 90+ days in arrears)	*No target*	*No target*	15	25	35	*2/*	*2/*
Terms being met							
(percent of arrangements concluded)	*No target*	*No target*	*No target*	75	75	75	75

Source: CBI.
1/ The targets cover ACC Bank, AIB, BoI, KBC Bank Ireland, PTSB, and Ulster Bank.
2/ Announced on a rolling quarterly basis.

The reform of personal bankruptcy has become effective, shortening the automatic discharge period from 12 years to 3 years. The long discharge period under the original Bankruptcy Act 1988 had resulted in very little use of bankruptcy to address financial distress. Under the 2012 statutory amendments, borrowers must attest to having been unable to agree other insolvency solutions, such as a Personal Insolvency Arrangement, before pursuing bankruptcy. Once debtors are declared bankrupt, the court may require them to enter into payment plans for up to five years under which income in excess of that required to meet reasonable living expenses is distributed to creditors. Alternatives such as Debt Relief Notices and Personal

Insolvency Arrangements provided for under Ireland's new personal insolvency framework may help contain the number of bankruptcies, as was the case following the introduction of Debt Relief Orders in the United Kingdom. To ensure smooth processing, the Insolvency Service has increased its staff resources and published detailed guidance. With this step, Ireland's reformed personal insolvency framework has become fully operational.

Press Release No. 13/507
FOR IMMEDIATE RELEASE
December 13, 2013

International Monetary Fund
Washington, D.C. 20431 USA

IMF Completes Twelfth and Final Review Under the Extended Fund Facility Arrangement for Ireland

The Executive Board of the International Monetary Fund (IMF) today completed the twelfth and final review of Ireland's performance under an economic program supported by a three-year arrangement under the Extended Fund Facility (EFF). The completion of the review enables the disbursement of an amount equivalent to SDR 0.579 billion (about €0.65 billion, or about US$0.89 billion), bringing total disbursements under the EFF to the equivalent of SDR 19.4658 billion (about €21.81 billion, or about US$29.94 billion) or the equivalent of 1,548 percent of Ireland's IMF quota.

The arrangement for Ireland, approved on December 16, 2010 (see Press Release No. 10/496), was part of a financing package amounting to €85 billion (about US$116.68 billion), also supported by the European Financial Stabilisation Mechanism and European Financial Stability Facility, bilateral loans from Denmark, Sweden, and the United Kingdom, and Ireland's own contributions.

This is the last review under the EFF arrangement, which will expire on December 15. Owing to steadfast policy implementation by the authorities, the EU-IMF supported program has been completed successfully. Ireland has pulled back from an exceptionally deep banking crisis, significantly improved its fiscal position, and regained its access to the international financial markets. Growth, though slower than initially projected, has exceeded the euro area average. Key policy actions have included necessary bank support, restructuring and downsizing, improvements in bank supervision and regulation, fiscal consolidation measures totaling some 8 percent of GDP and improvements in the institutional framework for fiscal policy. These and other efforts leave Ireland in a much strengthened position and a range of economic indicators suggest a recovery is emerging in the second half of 2013.

Yet important challenges remain. Public debt is projected to reach 124 percent of GDP this year, although this partly reflects Ireland's strong cash buffer. The fiscal deficit is expected at about 7 percent of GDP, within the target of 7.5 percent of GDP, yet still high. Banks remain weighed down by low-yielding indexed mortgages and by 26.6 percent of loans being nonperforming, including some 17.4 percent of the total values of mortgages in primary residences being in arrears for over 90 days. Unemployment, though significantly below its peak of 15.1 percent in early 2012, remains unacceptably high at 12.5 percent in November, with almost 60 percent of job seekers out of work for over a year

After the expiration of the EFF arrangement, Ireland and the IMF will continue to maintain a constructive policy dialogue. In accordance with Fund policy, Post-Program Monitoring (PPM)[1] will now be initiated.

Following the Executive Board's discussion, Ms. Christine Lagarde, Managing Director and Chair, said:

"With today's approval of the 12th review Ireland has successfully completed its EU-IMF supported program. Steadfast policy implementation by the Irish authorities has underpinned the achievement of core program objectives: stabilizing the financial sector, significantly improving the fiscal position, and regaining market access. Renewed job creation and a range of positive indicators signal an emerging recovery. As a result, Ireland is now in a much stronger position than when its program began.

"Yet Ireland still faces significant economic challenges. Unemployment is too high, public debt sustainability remains fragile, and heavy private sector debts and banks' slow progress in resolving nonperforming loans weigh on domestic demand. Continued concerted policy implementation is therefore necessary for Ireland to recover fully from the crisis.

"Steady fiscal consolidation has been a hallmark of Ireland's program with deficit targets again expected to be met in 2013. Budget 2014 sets out a balanced pace of adjustment in coming years, as needed to put public debt on a declining trajectory. To limit the drag on growth, revenue increases should focus on further broadening the tax base, and reforms of health, education, and social protection spending should be undertaken while protecting core public services and the most vulnerable.

"To help revive lending and sustain a recovery in demand, efforts to resolve mortgages in arrears should be intensified. The recent bank balance sheet assessment—an intensive analysis conducted by the Central Bank—found additional provisioning to be appropriate. Results should inform banking supervision and banks' preparations for the Comprehensive Assessment in 2014, for which an ESM recapitalization backstop is desirable.

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[1] The central objective of PPM is to provide for closer monitoring of the policies of members that have substantial Fund credit outstanding following the expiration of their arrangements. PPM is discussed in more detail in this factsheet.

“Reducing unemployment is a central priority, requiring improved employment services and training for jobseekers, together with steps to promote credit to SMEs, where the support of European partners is welcome.

“The government’s decision not to request a successor program is welcome. Ireland’s track record within its EU-IMF supported program bodes well for its success in tackling these remaining challenges and the Fund looks forward to continued constructive engagement with the Irish authorities.”