Submission to the Mid-Term Review of Capital Plan 2017

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Summary

In essence we respectfully suggest that the overall investment level foreseen in the Mid-Term Review remains too low and must be increased. This Submission argues why this is the case and how investment can be increased.

There are three key messages which we think that the Department should consider.

1. There should be a considerable increase in the level of public investment in Ireland.
2. Part of the proceeds of the sale of AIB shares currently owned by the government should be used to increase the level of public investment over the next number of years
3. A Commission on Investment should be established to oversee future investments and ensure that they are consistent and planned.

1. The case for increased investment

TASC is delighted that the government has increased the original level of investment on that originally proposed in *Building on Recovery*, although this possible increase was mooted in that paper. However the additional increase is still insufficient to meet the country's needs for infrastructure, housing, health and indeed human capital investment.

Our proposal sets out that the level of public investment needs to be substantially increased. There is some confusion around definitions. In this instance, we are referring to direct public investment. This excludes indirect investments by state-owned bodies and of course the very volatile private investment in Ireland.

The level of debt proposed in the TASC report *A Time for Ambition* would allow investment to rise to 3.25% of GDP by 2020 and 2021. This would require exchequer funding of almost €42bn in the years to 2021- substantially more than the €27bn proposed in the *Building on Recovery* six-year plan. The original government plan proposed an investment level of only 1.84% of GDP to 2021. This as we pointed as is very low. We suggested a level of 2.25% percent of GDP rising to 3.25% in 2021 - an average of 2.8%. This compares to that achieved in the six years to 2007 of 3.9% and is thus still modest.

Bodies like the National Competitiveness Council have long warned that the level of investment in Ireland has been too low. There is now also a need to catch up on the very low levels of investment from the recession. There is a great need for direct public investment in infrastructure, housing and healthcare.

Direct public investment, if it can be afforded, is cheaper and quicker than undertaking the investment through various acronyms such as PPPs, REIT, etc. These are essentially tax-avoidance mechanisms and strongly promoted by the financial, legal and accounting "professional" bodies and firms.

"It may be conservative, but it is not prudent"

It is time the dominance of the fiscal hawks in Europe is challenged by Ireland which is in a much stronger position to do so today. Indeed, there is more scope for investment then many conservatives have argued. In response to the high levels of criticism of its apparent conservatism, the European Commission itself published "Making the best use of the flexibility within the existing rules of the Stability and Growth Pact" in early 2015 which was welcome. It says it clarifies how three specific policy dimensions "can best be taken into account in applying the rules…These relate to: (i) investment, in particular as regards the establishment of a new European Fund for Strategic Investments as part of the Investment Plan for Europe; (ii) structural reforms; and (iii) cyclical conditions." Thus investment is a key issue.

The report states that the Pact envisages flexibility in the way its rules should be applied, both over time and across countries" and "that some discretion is left, within the agreed rules, for the Commission and the Council to assess the soundness of public finances in the light of country-specific circumstances". In Ireland's case, the situation is far better than just a few years ago and investment in Ireland is needed. Since some debt is now actually at a negative interest rate, it would appear that further debt repayment is inane, however "hawkish" one's economic ideology.

Our proposal refers not to capital which is raised in taxation, but related to the repayment (albeit only in part) to taxpayers for the €64bn taken to fund the six failed Irish banks. On contributions from Member States such as this AIB capital, Section 2.1.1 "provides guidance on how these various contributions will be assessed under the Pact." More work needs to be done by Ireland with the Commission to allow the intelligent use of these funds.

However, this is still not sufficient, particularly since the Commission accepts that investment levels are too low. Europe should also consider moving from gross debt to net debt in assessing the ability to borrow and to invest. The anti-European sentiment evident in Europe is a natural reaction to this fiscal conservativism which is impacting on too many people. Access to decent housing and health care is denied to many because of overly conservative economics. It may be conservative, but it is not prudent.

The strongest case against substantial increase in public investment is that it will inevitably lead to increased construction inflation. This is a challenge but one which can be overcome with the analysis and strategy. For example, the work of the Department of Finance on the Labour Intensity of Investment in the PCP published in December 2015, is a contribution. The other problem is less challenging and that is potential skills shortages which can be overcome by immigration (including the return of recent emigrants).

Indeed, the 2017 DEPER staff paper points out that "The continued recognition of the critical role of capital expenditure in supporting the development of the economy's long-term growth potential (e.g. through the capital smoothing under the EB rule) is also central to long-term economic prospects."

2. We Must Invest the Capital from the AIB share sales

With the Irish 10 year bonds being at very low levels and some of our borrowing is leaving at negative rates, it is extraordinary that the government could even consider using the capital from the AIB share sales to repay the national debt more rapidly. The National Debt is in steady decline, regardless of this AIB boost. Ireland has a housing crisis which is best addressed immediately with this capital.

3. Why a Commission on Investment should be established

A Commission on Investment should be established to ensure greater certainty in major capital planning over the years. When recession hits the first thing to get hit is capital investment.

Most public investment is postponed in such periods and this has its costs in lost employment and delay in providing the physical assets. Stop-start funding of major infrastructure projects also has negative consequences for the national skill base. Major projects such as Luas have long lead times and then take a long time to carry out. They require skilled workers and specialist construction professionals. However, the more such projects are not part of any long-term programme, the less incentive there is for firms to invest in developing the necessary skills. Once the project is completed, the workers move on to another job, leave the industry, or emigrate. The skill base within firms and within the industry as a whole is weakened. Firms do not build up specialist expertise with which they could compete in export markets – and tackle the next project more efficiently.

All of this has been exemplified by the sad story of rail construction in Ireland. The first Luas lines were proposed, stopped, re-started. DART Underground – the one project that would really dramatically enhance Dublin's public transport – was abandoned even after millions had already been spent on planning. Tackling Ireland's transport infrastructure deficits is crucial for social cohesion, for business competitiveness and for meeting Ireland's climate change targets.

TASC also proposed that there should be consideration of the "golden rule" of investment which had applied in countries such as Germany in the past.

In conclusion, TASC welcomes the new thinking on the need for greater public investment.

References

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