Quarterly Economic Observer

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Nevin Economic Research Institute

About NERI and this publication

The Nevin Economic Research Institute (NERI) was established to provide information, analysis and economic policy alternatives. Named in honour of Dónal Nevin, scholar, trade unionist and socialist who gave a life of service to the common good, the Institute aims to undertake research that will be of relevance to the Trade Union movement and the general public across the island of Ireland.

This is the 21st *Quarterly Economic Observer* (QEO) of the Institute. The purpose of the QEO is to provide regular, accessible and timely commentary so as to equip trade unions and others in articulating and advancing a new economic paradigm where the old has failed. Unless otherwise stated, the data cited in this Observer are the latest available as of 16th March 2017. The final draft of this document was completed on the 21st of March 2017.

This report has been prepared by staff of the Institute. The lead authors of section 2 of this QEO are Paul Goldrick-Kelly and Tom Healy. We are grateful to our external reviewers from the academic and research community who reviewed and commented on an earlier draft of this document. The analyses and views expressed in this publication are those of the NERI and do not necessarily reflect those of others including the Irish Congress of Trade Unions or the unions supporting the work of the Institute.

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The Nevin Economic Research Institute

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Executive Summary

This edition of the NERI's *Quarterly Economic Observer* (QEO) outlines our assessment of the economic prospects for both the Republic of Ireland and Northern Ireland (Section 1) and provides an analysis and set of policy recommendations for the development of a *European Cost Rental Model* to begin to tackle the current housing crisis in the Republic of Ireland (Section 2).

Economic Outlook for the Republic of Ireland (Section 1)

- Notwithstanding the distortion arising from activities of certain multinational companies, it is clear that the real economy of the Republic has been growing strongly. This is, also, in spite of Brexit related headwinds and the fall in the value of Sterling.
- Recent labour force data has been very positive. Employment growth averaged just under 3% in 2016 with end-year total employment reaching an estimated 2,048,100. This was the highest fourth quarter total since 2008, though employment is still 100,000 below its 2007 level. Unemployment and long-term unemployment are on steady downwards trajectories.
- The recovery in wages has been much more modest, by comparison. Average weekly earnings grew by 0.6% year-on-year in the fourth quarter with private sector earnings increasing by 1.4%.
- The deprivation rate declined from 29% of individuals in 2014 to 25.5% in 2015. Deprivation remains well in excess of pre-crisis levels.
- Exchequer tax receipts remain buoyant for now with an increase of 5.0% in 2016 compared to the previous year.
- Our baseline assumption is that the economy is not yet overheating and that there remains some limited scope for above trend growth and the working through of pent-up demand. We expect GDP to increase by 3.8% in real terms in 2017 before slowing to 3.0% growth in 2018.
- Domestic demand (consumption and investment) will drive the bulk of real GDP growth in 2017 and 2018.

- The outlook for trade is highly uncertain given the volatile policy environment and the outsize impact of a small number of multinationals. Brexit effects could manifest as weaker foreign demand while changes to US policy could affect the scale and type of economic activity undertaken by US multinationals in the Republic.

- Total employment should continue to grow strongly for the rest of 2017 before slowing in 2018. We project that unemployment will fall to 5.8% by the middle of 2018 as cyclical unemployment disappears.

Outlook for Northern Ireland (Section 1)

- Almost nine months on from the BREXIT referendum result last year there have been mixed indications of the fall-out from this result. It is too early to say what the overall regional impact is likely to be. However, is it clear that the economy is highly vulnerable to the medium-term impact of Brexit especially in particular sectors.
- The early indications of economic growth since June 2016 are not encouraging. The Northern Ireland Composite Economic Index (NICEI) declined by almost 1% in the third quarter of 2016, its first such decline in over a year.
- The reduction in public sector employment in Northern Ireland of almost 10,000 jobs since December 2014, explains much of this decline in public sector output.
- Wholesale & Retail and Accommodation & Food were the only sectors to post any positive growth in Q3 of 2016, with all other sectors experiencing a decline.
- For the production sector, this most recent contraction fits with a trend of decline that began in early 2015.
- The manufacturing sector is particularly vulnerable to Brexit not least in relation to UK membership of the EU Customs Union. Unless a compromise can be found which secures much of the existing arrangements on the border between Northern Ireland and the Republic of Ireland, further redundancies in the manufacturing sector are to be expected.
- Unemployment in Northern Ireland remained static at 5.7% in the three months ending in January 2017. There was a small increase in employment and no increase in economic inactivity but once again, fundamental indicators within the labour market appear to be broadly stable.

The housing emergency in the Republic of Ireland – time for a game changer (Section 2)

- Lack of access to affordable quality homes constitutes a significant crisis for workers, families and communities in the Republic of Ireland.
- Current Government plans appear to be insufficient to make a significant impact. Pressure and strain on individuals and families is a direct consequence of under-investment over many years as well as a failure on the part of a market-led and property developer-led model of housing to deliver enough homes to meet the demands of a growing population.
- We propose a carefully planned programme to add 70,000 new homes to the existing stock of normally occupied housing in the Republic of Ireland. A key part of this plan is the putting in place of a *European Cost Rental Model* (ECRM) on lines already outlined by the *National Economic and Social Council* (NESC) and referred to in a recent report of the *Oireachtas Committee on Housing and Homelessness*.
- The optimum solution, we propose, is the establishment of *The Housing Company of Ireland*, which will draw on long-term borrowing combined with an equity injection from the *Ireland Strategic Investment Fund*, and undertake or commission, on a commercial basis, a programme of planning, building, acquiring and renting of new homes.
- This investment will supplement and further strengthen that of the Local Authorities as well as the voluntary housing associations in the area of social housing.

1 Economic Trends and Outlook

1.1 World

The Republic of Ireland and Northern Ireland are both small open economies and the Republic is particularly open. The performance of both Irish economies is heavily linked to the performance of their major regional and national trading partners. Table 1.1 provides an overview of recent performance in the most important trading partners namely, the euro area, the United Kingdom (UK) and the United States (US).

Table 1.1 Dashboard of Macroeconomic Indicators, Selected Regions*

	2012	2013	2014	2015	2016	2017
Real GDP			*Percentage volume change over previous year*			
Euro area	-0.9	-0.3	1.1	2.0	1.7	1.6
United Kingdom	1.3	1.9	3.1	2.2	2.0	1.5
United States	2.2	1.7	2.4	2.6	1.6	2.3
Unemployment**			*Percentage of labour force*			
Euro area	11.3	11.9	11.6	10.9	10.0	9.5
United Kingdom	8.0	7.6	6.2	5.4	4.9	5.0
United States	8.1	7.4	6.2	5.3	4.9	4.7
Inflation			*Percentage annual average rate of change*			
Euro area (HICP)	2.5	1.3	0.4	0.0	0.3	1.1
United Kingdom (HICP)	2.8	2.6	1.5	0.1	0.7	2.5
United States (CPI)	2.1	1.5	1.6	0.1	1.2	2.3
Compensation per Employee			*Percentage change from previous period*			
Euro area	1.1	1.4	1.4	1.4	1.3	1.8
United Kingdom	1.7	1.5	0.7	1.3	1.7	2.3
United States	2.4	1.1	2.6	2.6	2.0	3.8
Current Account Balance			*Percentage of Gross Domestic Product*			
Euro area	1.3	2.2	2.5	3.2	3.4	3.1
United Kingdom	-3.7	-4.4	-4.7	-5.4	-5.9	-4.3
United States	-2.8	-2.2	-2.3	-2.6	-2.5	-2.7
Fiscal Balance			*Percentage of Gross Domestic Product*			
Euro area	-3.7	-3.0	-2.6	-2.1	-2.0	-1.7
United Kingdom	-7.7	-5.7	-5.6	-4.2	-3.3	-2.7
United States	-7.9	-4.4	-4.2	-3.5	-4.1	-3.7

Notes: *2017 figures for *GDP* are latest IMF projections. 2016 and 2017 figures for *Inflation*, *Current Account* and *Fiscal Balance* are latest IMF projections. 2016 and 2017 figures for *Unemployment Rate* and *Compensation per Employee* are latest OECD projections.
**National definitions.

Sources: IMF *World Economic Outlook*, IMF *Fiscal Monitor*, OECD *Economic Outlook*

Real output growth has been weakest over the medium-term in the euro area although there are signs of recovery and stabilisation. Brexit and associated uncertainties and deterioration in the trading relationship with the EU will weigh on trade and output growth in a number of European economies over the next few years with the scale of the impact likely to be most pronounced in the Republic of Ireland and in the UK itself.

The medium-term trend has been one of gradually improving labour market conditions in most advanced economies. However, unemployment remains stubbornly high in the euro area. This may be a consequence of the euro area's less activist policy response to the post-2008 crisis relative to the nature and scale of the response in the US and the UK. On the other hand, the US and in particular the UK, have both maintained substantial fiscal and current account deficits since the crisis broke and this will restrict future scope for expansionary policies.

In the case of the UK the large trade deficit suggests that the weaker post-Brexit value of Sterling may partially reflect underlying macroeconomic fundamentals and is not simply a short-term response to Brexit related uncertainty. The scale of the fiscal deficit in the US may act to constrain the US President's plan for fiscal stimulus in the form of business and corporate tax cuts and increased spending on infrastructure. In any event the US Federal Reserve will tighten monetary policy gradually over the next 12 months. Tightening monetary policy in the US will weaken financing conditions in a number of emerging economies.

Inflation has been very low in most advanced economies in recent years reflecting the general fall in energy and commodity prices and relatively subdued growth. Growth in compensation per employee was running about 1 percentage point ahead of inflation in the euro area and in the UK in 2016. Inflation will pick-up in the UK as the impact of weaker Sterling feeds through into production costs and consumer prices.

Seasonally adjusted GDP rose by 1.7% in the euro area and by 1.8% in the EU during the fourth quarter of 2016 compared to the same quarter in 2015. The UK and the US grew by 2.2% and 1.9%, respectively, during the same period. However, the euro area's relatively solid performance should be understood in the context of a very supportive monetary policy stance that may not be sustainable over the medium-term.

World output increased by 3.1% in 2016 and advanced economy output increased by 1.6%. Most institutional forecasters are expecting global growth to pick up in 2017 and 2018 after a lacklustre performance in 2016 with fiscal stimulus in the US and China expected to contribute to this pick-up. The risk of a medium-term slowdown in the Chinese economy remains a concern for the wider Asian and global economy.

1.2 Republic of Ireland

Trends

The headline national accounts, including GDP, GNP and the Current Account Balance, have become increasingly distorted by multinational activity. Indeed the distortion is now so pronounced that it has become difficult to interpret the Republic's economic performance and cyclical position using aggregate indicators (see Box 1.1). Even so, it is clear that the real economy has been growing strongly despite Brexit related headwinds and the fall in the value of Sterling (see Table 1.2 for an overview). Year-on-year personal consumption grew by 3% in real terms in 2016 while investment in dwellings and building and construction grew strongly with construction sector output up 11.4% in real terms in 2016. Agricultural activity grew strongly at 6.4%. In addition, activity indicators such as retail sales have also been strong with year-on-year growth of 5% in the fourth quarter of 2016 and 4.9% in January.

Recent labour force data has been very positive. Net employment grew by a robust 2.9% in 2016 with end-year total employment reaching 2,048,100. This was the highest fourth quarter total since 2008, albeit employment is still over 100,000 below its 2007 level. Unemployment and long-term unemployment are on steady downwards trajectories. The fourth quarter seasonally adjusted unemployment rate fell year-on-year from 9.1% in 2015 to 7.1% in 2016, and then to 6.6% in February. Long-term unemployment was 3.6% in the fourth quarter. There is significant regional variation with unemployment highest in the *South-East*.

Average weekly earnings grew by 0.6% year-on-year in the fourth quarter with private sector earnings increasing by 1.4%. Average hourly earnings grew by 1.1% in the same period with average private sector hourly earnings increasing by 1.9% and public sector earnings declining by 0.2%. Hourly earnings increased in 10 of the 14 principal sectors. Real wages are benefiting from the general lack of inflation in the economy. Growth in the CPI inflation index was flat (+0.0%) on average in 2016. The CPI was 0.5% in February compared to the previous year. The CPI for *Goods* was down 1.5%, while *Services* were up 2%. Prices for *Energy Products* were up 8.6%.

Table 1.2 Dashboard of Macroeconomic Indicators, Republic of Ireland

	2011	2012	2013	2014	2015	Latest
	Percentage volume change over previous year					
Gross Domestic Product	0.0	-1.1	1.1	8.5	26.3	5.2 *(2016)*
Domestic Demand	0.7	1.4	-1.9	7.7	9.9	16.8 *(2016)*
Personal Consumption	-1.0	-1.0	-0.8	1.7	4.5	3.0 *(2016)*
Retail Sales	-0.9	-0.9	0.8	6.4	8.6	5.9 *(2016)*
Industrial Production	-0.4	-1.5	-2.2	22.9	34.8	-9.4 *(M1'17)*
	Percentage annual average rate of change					
Employment	-1.8	-0.6	2.4	1.7	2.6	3.3 *(Q4'16)*
Average Hourly Earnings	-0.4	0.2	-0.3	-0.1	0.2	1.1 *(Q4'16)*
Average Weekly Earnings	-1.1	0.6	-0.5	0.3	1.2	0.6 *(Q4'16)*
Inflation (HICP)	1.2	1.9	0.5	0.3	0.0	0.3 *(M2'17)*
	Percentage of gross domestic product					
Investment	17.2	19.4	18.2	20.5	21.1	29.3 *(2016)*
Current Account Balance	-1.6	-2.6	2.1	1.7	10.2	4.7 *(2016)*
Government Balance	-12.6	-8.0	-5.7	-3.7	-1.9	-2.6 *(Q3'16)*
Government Gross Debt	109.6	119.5	119.5	105.2	78.6	77.1 *(Q3'16)*
	Percentage of labour force					
Unemployment	14.6	14.7	13.0	11.3	9.4	6.6 *(M2'17)*
Long-term Unemployment	8.6	9.0	7.8	6.6	5.3	3.6 *(Q4'16)*
	Percentage of households					
Deprivation	24.5	26.9	30.5	29.0	25.5	25.5 *(2015)*
At Risk of Poverty	16.0	17.3	16.5	17.2	16.9	16.9 *(2015)*
	Percentage					
Gini Coefficient	31.1	31.8	32.0	32.0	30.8	30.8 *(2015)*

Notes: Quarterly ('Q'), half year ('H'), and monthly ('M') data is compared to same period of previous year. Rates of change represent the average value over the four quarters, or twelve months. *Gross Debt* is end-year figure as a % of annualised GDP or latest quarterly figure as % of quarterly GDP. *Unemployment* is average for four quarters or latest quarter seasonally adjusted.

Sources: *All CSO: National Income and Expenditure, Quarterly National Accounts, Retail Sales Index, Industrial Production and Turnover, Quarterly National Household Survey, Earnings and Labour Costs Annual, Earnings and Labour Cost Quarterly, Consumer Price Index, Balance of Payments, Government Finance Statistics, Monthly Unemployment, Survey on Income and Living Conditions.*

The deprivation rate declined from 29% of individuals in 2014 to 25.5% in 2015. However, deprivation remains well in excess of pre-crisis levels (13.7% in 2008). The '*at risk of poverty'* rate declined from 17.2% in 2014 to 16.9% in 2015 but is still above pre-crisis levels (14.4% in 2008). Household debt fell to €145.3 billion or 144.8% of disposable income in third quarter 2016. However, the Republic is the 4th most indebted country in the EU by this measure. Household net worth increased 3.9% in the third quarter driven by a rise in housing assets. Residential property prices were up 7.9% in the year to January with prices outside of Dublin increasing 11.3%.

Exchequer tax receipts were up 5.0% in 2016 compared to the previous year with total government revenue up 3.1%. Gross voted public expenditure was up 2.4% over the previous year. The final 2016 general government deficit is likely to come in at either 0.8% or 0.9% of GDP. Exchequer tax receipts were up 4% to end-February compared to the previous year with VAT receipts up 16.9% and income tax down 0.4%.

Box 1.1 GNI* and Current Account*

The headline national accounts, including GDP, GNP and the Current Account Balance are heavily distorted by multinational activities and are becoming less relevant as measures of economic activity occurring in the Republic itself and of the Republic's trading relationships with other countries. The 26% increase in real GDP in 2015 was mainly the result of the relocations of balance sheets to the Republic from outside of the EU and the economic activity related to these mainly intellectual property assets. The scale of distortion is now so great that it is difficult to interpret what is happening in terms of real economic activity. The headline national accounts figures such as GDP and GNP, while not statistically wrong; do not accurately reflect economic activity within the Republic and care is required when interpreting the data.

The distortions have implications for the scale of the contribution to the EU budget, while indicators measured as a ratio of GDP are now of reduced usefulness, for example the debt to GDP ratio and other fiscal indicators, as well as the private debt to GDP ratio. The distortions also make it difficult to assess the cyclical position of the economy and to determine whether the economy is either overheating or operating below its potential. Ultimately the distortion of the national accounts acts as an information barrier in relation to good economic policymaking.

In this context the **report** of the Economic Statistics Review Group (ESRG) made 13 recommendations mainly seeking decompositions of certain existing indicators as well as the development of new indicators. In light of the ESRG report the national accounts data as presented by the Central Statistics Office (CSO) will contain a number of additions starting in mid-2017. The CSO is to take an incremental approach with the focus in 2017 on the introduction of a modified Gross National Income indicator known as GNI* and a related Current Account indicator known as Current Account*. GNI* is a modified measure of the size or level of the economy and is calculated as GNI adjusted for retained earnings of re-domiciled firms and depreciation on foreign-owned domestic capital assets. It is understood that estimates for GNI* will be provided back to 1995.

In addition, in order to support understanding of the structure of the economy the non-financial corporations' part of the sector accounts will be decomposed into *foreign-owned multinationals including large case firms* and *domestic including Irish multinationals*. Finally, additional detail will be provided on the expenditure side of the national accounts. This will support development of a measure for underlying investment in the economy which can then be used for economic modelling. The new details will relate to IP product relocations, aircraft leasing, re-domiciled firms and contract manufacturing in exports and imports.

Box 1.2 Earnings, Labour Costs and Standard of Living in the Republic of Ireland

The Republic is a Small Open Economy (SOE) with a development model based on attracting and retaining FDI. Wages and competitiveness are therefore constant topics of discussion. One striking feature of the most 'competitive' economies according to two prominent international indices is that many of the highest-wage economies in the world feature on both lists

IMD (2016)	1	Hong Kong	**WEF (2016)**	1	Switzerland
	2	Switzerland		2	Singapore
	3	USA		3	USA
	4	Singapore		4	Netherlands
	5	Sweden		5	Germany
	6	Denmark		6	Sweden
	7	Rep Ireland		7	UK
	8	Netherlands		8	Japan
	9	Norway		9	Hong Kong
	10	Canada		10	Finland

According to IMD, the Republic's ranking has improved from 24th position in 2011 to 7th in 2016, the highest in the euro area and well ahead of the UK in 18th position. These competitiveness indices are aggregated using dozens of indicators from the *effectiveness of institutions* to *innovation* to *third level education*. The Republic is ahead of the UK in *prices*, *the labour market* and *management practices* whilst it lags behind in *employment*, *basic infrastructure*, *scientific infrastructure* and *technological infrastructure*.

Labour costs include compulsory employer social contributions and employment taxes. Relative to other EU member states these costs are low in the Republic translating relatively high hourly earnings into average or even lower than average **hourly labour costs**. In the *business economy*, the Republic at €28.70 is slightly lower than euro area (€29.50) and UK (€29.00) averages *in total hourly labour costs*. This is well below other SOEs like Belgium (€41.10) and Austria (€32.20).

Wages are also often used as a metric for living standards ignoring the impact of employers' social contributions. In other European countries these contributions are used to provide supports of different kinds such as GP visits, unemployment or illness relief as well as subsidies for maternity leave. The extra amount Irish workers have to pay from their hourly wages to avail of these services is not captured by a simple hourly income rate. Eurostat's preferred metric is ***Actual Individual Consumption***. This is a per capita measurement where everything consumed in an economy, including services such as health and education is measured regardless of whether they were paid for out-of-pocket or provided by the state. Ireland's *AIC* is in the bottom half of the Eurozone table sitting just above Spain and Portugal and is one of the only countries in the EU in which the level has declined since 2008. Ireland's 2015 standard of living as measured by *AIC* was €19,200 compared to Germany's €24,500 and Italy's €19,700.

Outlook

While acknowledging the current difficulties related to interpretation of the national accounts, and therefore, to the estimation of the cyclical position of the economy, our baseline projection for the Republic's economy remains highly favourable (see Table 1.3), albeit with downside risks (see Box 1.3). Our baseline assumption is that the economy is not yet overheating and that there remains some limited scope for above trend growth and the working through of pent-up demand. We expect GDP to increase by 3.8% in real terms in 2017 before slowing to 3.0% growth in 2018.

Domestic demand will drive the bulk of real GDP growth in 2017 and 2018. Personal consumption should grow strongly on the back of very robust employment growth and increasing wage and income levels, along with continued improvements in household wealth and debt dynamics. There is significant scope for above-trend catch-up growth in underlying investment given the persistently low underlying investment ratio in recent years and the expected increase in housing output.

Table 1.3 Macroeconomic performance & projection, Republic of Ireland

	2015	2015	2016	2017	2018
Real Output		*Percentage real change over previous year*			
Gross Domestic Product	€255.8bn	26.3	5.2	3.8	3.0
Personal Consumption	€92.4bn	4.5	3.0	3.4	2.3
Government Consumption	€27.0bn	1.2	5.3	2.0	1.8
Investment	€54.1bn*	32.7	45.5	5.8	4.0
Exports	€317.2bn	34.4	2.4	4.3	3.9
Imports	€236.0bn	21.7	10.3	4.7	4.0
Earnings		*Percentage nominal change over previous year*			
Average Hourly Earnings	€21.91	0.2	0.7	2.2	2.7
Government Finances		*Percentage of GDP*			
General Government Balance	-€4.8bn	-1.9	-0.9	-0.3	-0.1
Gross Debt	€201.3bn	78.6	75.2	71.7	69.9
Labour Force		*Percentage change over previous year*			
Employment	1,963,550	2.6	2.9	2.8	1.6
		Percentage of labour force			
Unemployment	203,625	9.4	7.9	6.3	5.8

Notes: Projections for *Gross Domestic Product* and components refer to real economic activity; *Investment* refers to Gross Fixed Capital Formation; *Employment*, *Unemployment* and *Earnings* all represent the average value over the four quarters.
*Gross Fixed Capital Formation excluding intangibles was €30.6 billion in 2015.

Sources: NERI estimates for 2016-2018; 2015 data is from CSO *National Income and Expenditure*, CSO *Earnings and Labour Costs Survey*, CSO *Government Finance Statistics* and CSO *Quarterly National Household Survey*.

Box 1.3 Macroeconomic Risks and Uncertainties: Republic of Ireland

There are always major uncertainties inherent to our projection. For example **labour productivity is notoriously volatile** and difficult to project as it is dependent on hard to track processes such as the diffusion of innovation and the changing composition of inter and intra sector employment. A further uncertainty relates to the amount of damage done to the quality of labour supply due to the prolonged unemployment crisis. If the structural damage done is greater than assumed the potential for above trend growth over our forecast horizon, as well as our **assumption of a negative output gap, may well be wrong**.

Recent political developments in the US and the UK have added to the **uncertainty surrounding economic policy** and economic prospects in these countries. Upcoming elections in a number of European countries have the potential to produce similar shocks. The impact of a **Trump presidency** on the Republic's economy is difficult to assess. Fiscal stimulus will boost growth in the US as well as demand for imports. However, tightening US monetary policy should dampen demand and could lead to capital flight and a tightening of credit in a number of emerging markets. In addition, a move towards protectionism and/or a significant change in corporation tax policy both represent significant downside risks to the Irish economy.

The Republic's tax and regulatory advantages in securing FDI may come under pressure from **corporate tax reduction in the UK**, or from a greater willingness of the EU to punish aggressive tax avoidance or increase **momentum toward a Common Consolidated Corporate Tax Base**.

Brexit, on the whole, is very likely to exert a negative effect on the economy. However, the scale of this effect is impossible to quantify as it is an historical evident without clear precedent. In any event we expect the bulk of the negative impact on the Republic to manifest in 2019 and 2020 reflecting the worsened trade relationship. In the interim we anticipate that some investment decisions will be delayed reflecting increased uncertainty. A **weakening of Sterling relative to the euro** would damage Irish exports and negatively impact on retail sales in the Border counties. Sterling is likely to weaken if the probability of a hard or contentious Brexit is seen to increase. At any rate the fluctuations in the Brexit process should manifest as increased exchange rate volatility.

A **tightening of euro area monetary policy** would reduce internal and external demand and could be particularly problematic for the Irish economy given the still-high private and public debt overhangs. Monetary tightening seems unlikely in the short-term despite the improving outlook for the euro area economy. The Republic is an energy importer and a faster than expected **rebound in energy prices** would negatively impact on corporate balance sheets and investment as well as on real household disposable incomes and personal consumption.

The outlook for trade is highly uncertain given the volatile policy environment and the outsize impact of a small number of multinationals. Brexit effects could manifest as weaker foreign demand while changes to US policy could affect the scale and type of economic activity undertaken by US multinationals in the Republic. We project that net exports will make a positive contribution to growth in 2017, albeit with imports growing at a faster rate than exports. The higher rate of import growth will partially be driven by the growth in real disposable income, personal consumption and investment.

Total employment should continue to grow strongly for the rest of 2017 before slowing in 2018. We project that unemployment will fall to 5.8% by the middle of 2018 as cyclical unemployment disappears. Growth in average hourly earnings should accelerate, albeit with sectoral variation, in response to the tightening labour market. Prices should start to increase in response to growing wage pressure, strengthening domestic demand, and a medium-term normalisation of oil prices. Finally, assuming no major negative shocks, the public finances look set to improve on the back of the strengthening labour market with the government deficit improving to 0.3% of GDP in 2017 and 0.1% of GDP in 2018.

1.3 Northern Ireland

Almost nine months on from the BREXIT referendum in June 2016 there has been some indication of how that event has impacted on the Northern Ireland economy. However, whilst the data in question do cover the months following the referendum it would be unwise to make definitive pronouncements about the economic impact of BREXIT at this stage. Firstly, data from one quarter can only give an initial indication of any such impact and initial estimates of output are oftentimes revised, occasionally substantially. Moreover, the economy is still dealing with a political event (the referendum result), the economic event (actually leaving the EU) is still several years away.

We may begin to assess the impact of BREXIT as an economic event now that the UK parliament has given consent for the government to invoke Article 50 of the Lisbon Treaty. Previous NERI research has outlined how new agreements on issues such as tariffs, regulations and immigration controls could affect the Northern Ireland economy. As these negotiations get underway this analysis will provide the basis on which we assess the future prospects for the Northern Ireland economy, post-BREXIT.

As Table 1.4 shows however, the early indications of economic growth since June 2016 are not encouraging. The Northern Ireland Composite Economic Index (NICEI) declined by almost 1% in the third quarter of 2016, its first such decline in over a year. By comparison UK GDP grew by 0.6% and the Scottish GDP Index grew by 0.2% in the third quarter of 2016. The reduction in public sector employment in Northern Ireland of almost 10,000 jobs since December 2014, explains much of this decline in public sector output. While public expenditure accounts for almost 60% of GVA, this does not equate with the size of the public sector which accounts for only 24% of total employment. The decline in the private sector appears to be directly related to a contraction in the services sector in Q3 2016. The production industries have been in decline since the beginning of the year, however growth in the services sector to date has been able to absorb this loss. Wholesale & Retail and Accommodation & Food were the only sectors to post any positive growth in Q3 of 2016, with all other sectors experiencing a decline. Some of this performance may be a positive impact on cross-border trade from a reduced Sterling exchange rate. Early indicators from the tourism sector do point to a significant upturn in sales in the latter half of 2016. Hotel room sales in the 12 months to the end of June 2016 were down 2% on the previous 12 months, by December these room sales were up by over 6%.

Table 1.4 Dashboard of Macroeconomic Indicators (Northern Ireland)

	2011	2012	2013	2014	2015	Latest
	Percentage volume change over previous year					
Gross Value Added	-0.9	1.1	1.1	0.2	1.6	1.6 *(2015)*
NICEI	-1.6	-1.4	0.0	0.7	1.5	-0.9 *(Q3 2016)*
Index of Services	-2.7	-1.4	0.5	1.24	1.3	-0.5 *(Q3 2016)*
Index of Production	7	-1.4	1	2.3	2.0	-1.8 *(Q3 2016)*
	Percentage annual average rate of change					
Employment Rate	2	-0.3	-0.6	1.8	0.3	-0.1 *(M11'16-M1 '17)*
Ave. Hourly Earnings	1.7	1.5	2.5	-1.3	4.2	4.2 *(2016)*
Price Inflation (UK)	4.5	2.8	2.6	1.5	0	2.3 *(M2'17)*
	Percentage of GVA					
Exports	29.0	28.9	30.0	28.4	26.5	26.5 *(2015)*
Government Spending	61.7	61.6	60.2	60.6	-	60.6 *(2014)*
	Percentage of labour force					
Unemployment	7.2	7.5	7.5	6.4	6.1	5.7*(M11'16-M1'17)*
Youth Unemployment	18.2	20.1	22.5	19	19.3	14.4 *(M11'16-M1 '17)*
Long-term Unemployment	3.2	3.8	4	3.4	3.6	2.5*(M11'16-M1'17)*
	Percentage of households					
Relative Poverty	21	19	21	22	-	21 *(2014)*

Notes: Employment Rate refers to all persons in employment (ILO definition) aged 16-64 as proportion of all persons 16-64. GVA is deflated using UK GDP deflator. NI Exports refer to sales outside the UK. Exports refers to both goods and services sold from NI beyond the UK. Government Spending refers to Total identifiable expenditure on services apportioned to NI.

Source: ONS *Regional Gross Value Added (Income Approach)*; HMT *GDP Deflators*; NISRA *Northern Ireland Composite Economic Index*; NISRA *Index of Production*; NISRA *Index of Services;* NISRA *Labour Force Survey*; NISRA *Annual Survey of Hours and Earning*; ONS *Consumer Price Inflation*; HMT *Public Expenditure Statistical Analyses*; NISRA *Households Below Average Income*

For the production sector, this most recent contraction fits with a trend of decline that began in early 2015. Manufacturing, which constitutes 82% of production industries has led this decline. The largest component of manufacturing, Food and Drink, has been in decline for the last three years, losing 14% of value since Q3 of 2013. However, the second largest component of manufacturing, Engineering & Allied Industries, has lost 9% of value since Q3 2015. Pharmaceuticals & Chemicals experienced something of a mini-boom in 2015, gaining over 25% in output from Q1 2015 to Q1 2016, however the sector lost 9% of output in the second and third quarters of 2016. Whilst the weak sterling may have given a short-term boost to consumer orientated services, it is quite clear that no such impact is discernible for the production industries. Northern Ireland's manufacturing base, beyond food and drink, relies on imports and it is likely that the depreciation of Sterling has given as much to industry as it has taken away. These recent trends in the manufacturing sector compound longer term concerns particularly regarding employment levels. Whilst the sector lost 1400 jobs in during the 8 years since the onset of the crisis in 2008, it lost almost 19,000 jobs in 8 years which preceded it.

This leaves the Northern Ireland economy with a considerable vulnerability. As Table 1.4 shows inflation has begun to increase significantly, reaching 2.3% in February of this year, with most forecasters expecting it to exceed 3% by the middle of 2017. In addition to the hit on real wages, inflation will also begin to erode the competitive edge of both Retail and Hospitality in Northern Ireland. For economic growth to be so dependent on consumer activity at a time of resurgent inflation is unwise and calls into question the sustainability of growth over the medium term.

There are also longer-term issues of concern for growth in the Northern Ireland economy. As table 1.4 shows, Gross Value Added in Northern Ireland increased in real terms by 1.6% in 2015. This represents a welcome upswing following less impressive results in 2014. However, the data on GVA also contained more concerning trends regarding productivity. Output per head of population in Northern Ireland as a percentage of the UK average fell from 73.8% in 2014 to 73.3% in 2015, the second lowest after Wales. This latest contraction follows a trend of decline which began in 2008 during which time Northern Ireland fell a further 10% behind the UK average. A recent NERI working paper outlines the scale of the challenge that these trends pose for Northern Ireland's economy and policy areas which need to be addressed.

Box 1.4 Improving job quality in Northern Ireland

The recently published draft industrial strategy document for Northern Ireland 'Economy 2030' includes as a key priority the importance of increasing the proportion of people working in good jobs. This commitment to a focus on job quality marks a fundamental shift away from the traditional focus in Northern Ireland on the numbers of jobs being created, and the numbers of people employed, unemployed and economically active. This is notable and hints a recognition from the Department for the Economy that in efforts to strengthen the labour market and improve economic performance both the quantity and the quality of jobs need to be on the agenda. The quality of available jobs has been shown to be an important driver of labour force participation influencing decisions such as whether to work and the number of hours to work. Job quality has also been shown to be related to aggregate economic performance, with those working in higher quality jobs shown to be more productive, more loyal, and absent from work less often.

Whilst a monthly report is published detailing employment figures there is little empirical evidence on the quality of jobs in Northern Ireland. However, it is worth pointing out that a 'Better Jobs' Index is currently under development. In the absence of official statistics, the results of a recent NERI working paper which employs the OECD's conceptualisation of job quality to assess the quality of jobs in Northern Ireland are summarised. The OECD's conceptualisation builds on the extensive efforts of the ILO-UNECE-Eurostat taskforce by linking conceptual frameworks on job quality with recent OECD work on well-being. The OECD identifies three dimensions for a job quality framework: quality of earnings; labour market security; and quality of the working environment.

Drawing on data for Northern Ireland from the recent UK Poverty and Social Exclusion Survey, quality of earnings is assessed using three partly overlapping measures of poverty. The first is a 'low-income poverty' measure; the second is a 'deprivation poverty' measure; the third is the PSE poverty measure. The results show that at a conservative estimate, over 1 in 6 employees live with a standard of living that can be described as 'income poor' or 'PSE poor'. This figure rises to just over 1 in 4 for the deprivation measure. A subjective measure capturing whether employees perceive their job to be secure shows that over 1 in 3 were either not sure if their job was secure or perceived their job to be insecure. Quality of the working environment is assessed using four measures: satisfaction; stress; control/flexibility; and quality of the physical environment. The results show that the majority (74%) are satisfied with their job, yet a substantial proportion have jobs that are either stressful (66%); have little control in terms of their working arrangements (49%); or work in a poor physical environment (45%). Critically, 1 in 3 have poor job quality on one of these three dimensions.

Together these findings emphasise the logic of policy aimed at creating good quality jobs and point toward the need for a broad policy agenda. This needs to cover the material rewards of work. It should also extend beyond this and include policies to improve job security and quality of the working environment. Thus, whilst there is much to be welcomed in 'Economy 2030' in terms of commitments to the creation of more jobs, it includes no milestones in terms of increasing the number of good quality jobs. The strategy needs to provide more details on the manner in which the Better Jobs Index will be used to inform policy. It also needs to be more explicit in terms of milestones for the improvement of job quality, as without this, business as usual and a sole focus on the number of jobs will continue.

There were 210 confirmed redundancies in Northern Ireland in January 2017, with 176 of these occurring in the manufacturing sector. 2016 was the worst year for redundancies in Northern Ireland since 2009, with a total of 3,653 confirmed cases, almost half of which came from the manufacturing sector. BREXIT poses challenges for all sectors of the economy, but as recent evidence to the House of Commons Northern Ireland Affairs select Committee has shown, the manufacturing sector is particularly vulnerable specifically regarding membership of the EU Customs Union. Unless a compromise can be found which secures much of the existing arrangements on the border between Northern Ireland and the Republic of Ireland, further redundancies in the manufacturing sector are to be expected.

Unemployment in Northern Ireland remained static at 5.7% in the three months ending in January 2017. There was a slight increase of up to 1,000 in the number of persons unemployed but in reality, the rate has been stable at an average of 5.7% for almost a year. There was a small increase in employment and no increase in economic inactivity but once again fundamental indicators within the labour market appear to be broadly stable. There was also a small decrease in youth unemployment coupled with a small increase in long-term unemployment. Whilst the unemployment rate in Northern Ireland remains persistently 1% above the UK average, the current rates of employment and economic activity in Northern Ireland are amongst the highest on record.

2 Ireland's housing emergency: Time for a game-changer

2.1 Introduction

The greatest social crisis impacting on workers, families and communities in the Republic of Ireland is the lack of affordable quality homes. A key part of the response to this crisis, we propose, is the careful design, planning and establishment of an entirely new *European Cost Rental Model* (ECRM). In this Section, we draw on a recent NERI Working paper (Healy and Goldrick-Kelly, 2017).

A crisis in housing is characterised by an acute and enduring shortage of appropriate housing given current and emerging patterns of demand for accommodation. The evidence reviewed elsewhere points to a systematic imbalance in housing supply and demand with rising levels of homelessness coupled with a rising crisis of affordability for individuals and households.

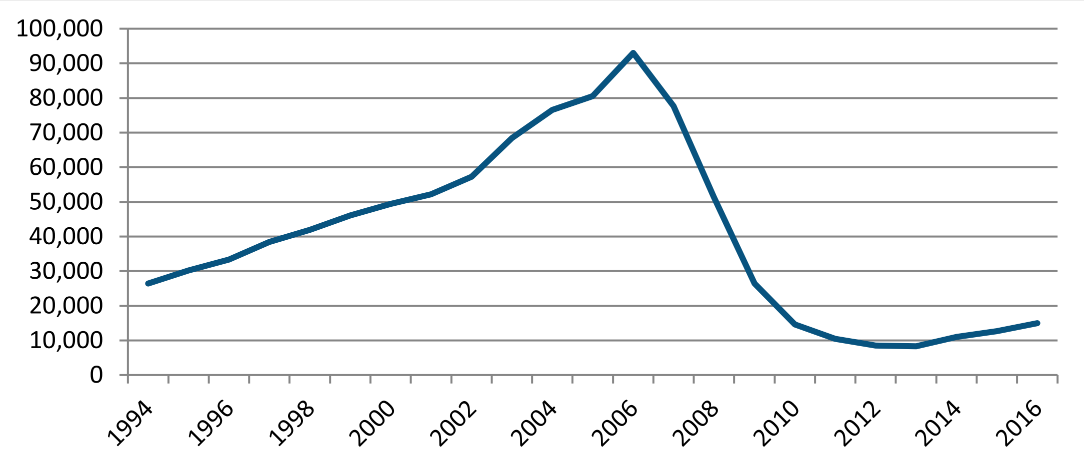
The main thrust of public policy on housing in the Republic of Ireland has been a marked reliance on the private sector. House building and development has been led, in the main, by private developers. Land speculation – notwithstanding much analysis, recommendation and feeble public interventions – has been a feature of the housing market for decades. There is no evidence that recent statements of public policy as outlined in in *Rebuilding Ireland* (Government of Ireland, 2016) or in *Construction 2020* (Government of Ireland, 2014) has departed from the traditional reliance on the private sector and market incentives. Policy has placed the emphasis on public subsidies to private landlords and plans to leave the lead role to the private sector in building the houses when and where markets dictate (albeit influenced by regulatory and planning restrictions).

2.2 Housing supply and demand

Figure 1 shows reported construction activity between 1994 and 2016. According to these statistics, building activity peaked in 2006 at over 93,000 units and fell back sharply to around 8,300 units per annum in 2013 (Department of Housing, Planning Community and Local Government, 2017). The data shown in Figure 1 represent completions of dwellings including an unknown number of older dwellings reconnected to the electricity grid for whatever reason.

Net changes in the housing stock reflect changes that augment the existing stock. This corresponds to the difference between additions to habitable stock in the form of new buildings, conversions of existing buildings not currently in residential use and, retrofitting and restoring of buildings that have fallen out of residential use, on the one hand, and residential obsolescence flows as a result of dwellings becoming uninhabitable, on the other.

Figure 1 Output of completed dwellings over time



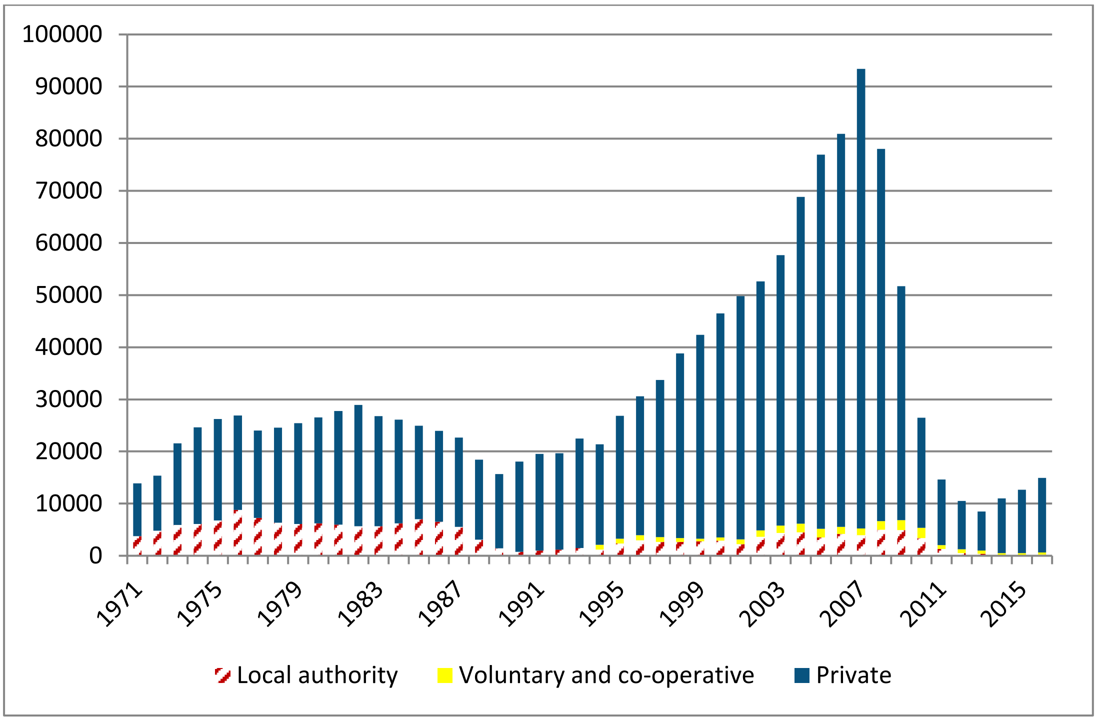
Note: These data are based upon new electricity connections recorded monthly and include reconnection of buildings that were not connected for two years or more. The rate of house completions as proxied by ESB new connections or reconnections is likely to flatter estimates of newly built units.

Sources: Source: **National New House Completions by month (Table A1)** (Department of Housing, Planning Community and Local Government, 2017)

Based on Census of Population data, total habitable housing stock increased by just under 19,000 between 2011 and 2016 – indicating an annual average increase of just under 4,000 over that period. What is remarkable about the supply of new dwellings over recent decades has been the collapse in 'social housing' whether built in the traditional way by local authorities, or in more recent decades, by voluntary not-for-profit housing associations or bodies. Figure 2 (on the following page) shows the composition of total new completions. Social housing output virtually collapsed in 2010 and, as of early 2017, there is no evidence that it has recovered to any significant degree since then.

One of the striking features of Figure 2 is the highly 'pro-cyclical' nature of building activity up to 2012. The output of new houses is very much in step with economic activity as noted by Norris and Byrne (2016). The fortunes and behaviour of the building industry serve to magnify the impact of boom or recession. The experience since 2012 is unusual because the recovery in building output is nowhere at the pace of general recovery in the economy. There has been a modest recovery in output but, notwithstanding various tax incentives and announcement of Government plans in 2014, officially counted new completions in 2016 were little more than they were in 2010.

Figure 2 Composition of 'house completions' over time



Note: The 2016 figures are imputed such that they are consistent with overall completion statistics for 2016 given proportions consistent with 2015 sectoral data.

Sources: Completions by Type Annually (Table A5) (Department of Housing, Planning Community and Local Government, 2017) Completions by Sector Quarterly (Table A10) (Department of Housing, Planning Community and Local Government, 2017a).

A key driver of the recent acute crisis in homelessness or threat of homelessness for many more struggling with high rents is the sharp pro-cyclical drop in public investment in social housing. Within the overall total the component of local authority social housing sharply contracted to such an extent that a total of just 75 were built in the year 2015. This corresponds to a little over one new dwelling per week for the entire jurisdiction. In the first three quarters of 2016 a total of 161 new social housing units were built by local authorities. The final figure for 2016 is unlikely to be much more than 200. In real terms, using Eurostat data, total capital spending by public authorities on housing and associated community amenities peaked at almost €2.5 billion in 2007 and fell back to a little over €600million in 2015 (Healy and Goldrick-Kelly, 2017).

Norris and Byrne (2016) have also noted the impact of a centralisation of public funding for local authority housing since the 1980s. This impact along with the absence of a significant recovery of costs via rental income to local authorities has been to render the full upfront cost of all spending on social housing a charge to General Government spending. Funding for social housing became more vulnerable to fiscal shocks, especially as capital funding is typically the first casualty of a cut-back in government spending. More recently, the application of EU fiscal rules including expenditure ceilings has served to further tighten the potential funding space for local authorities.

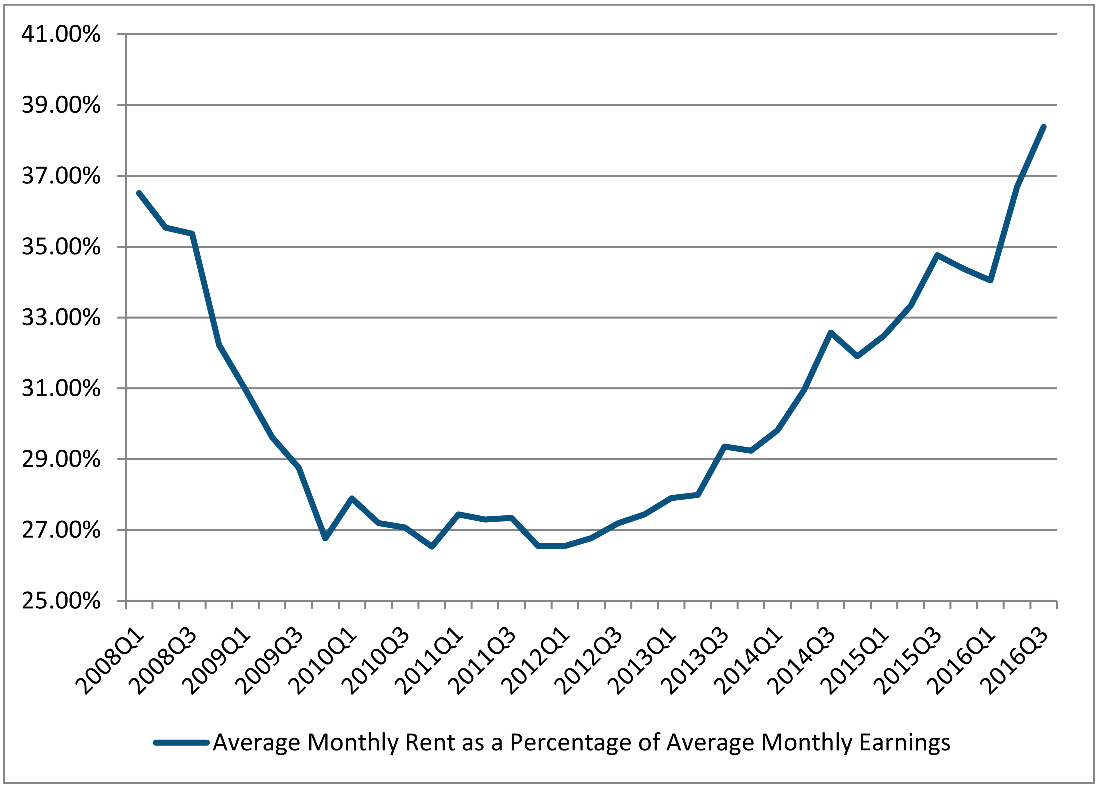
Various stop-gap measures were introduced or greatly expanded to meet the shortfall in social housing provision as well as address affordability concerns. Hence, *Rent Supplement* expenditure (and more recently the *Housing Assistance Payment*, or HAP, designed to replace Rent Supplement for those in long-term need) have increased since the onset of the crisis. However, these measures – while blunting some of the worst impacts of accommodation affordability, do not address the fundamental problem, which is that of supply. As the fiscal crisis deepened in 2010-2011 and the housing crisis worsened, total public spending on financial assistance to households increased in response to the emergency just as housing-related capital spending via the local authorities dried up.

The Housing Agency (2014) has undertaken a projection of future housing demand based on population projections published by the Central Statistics Office in 2013. The analysis took account of the stock of residential housing, obsolescence and household composition. The Agency, in line with the view of other analysts, assumed an annual obsolescence rate of 0.5% of total housing stock. The analysis did not take account of 'pent-up' demand resulting from shortage of supply in years prior to 2014. It should also be noted that realised estimated net immigration has proven substantially higher than that implied by the projections produced by the Central Statistics Office in 2013.

Pressures in the housing market may delay household formation to some extent but growth within the 20 to 40 age-cohort will exert significant additional pressures on house supply over the coming years (Byrne, Duffy and FitzGerald, 2014). Furthermore, unexpected increases in net inward migration (above those assumed in any of the scenarios by the Central Statistics Office in 2013 and more recently by the ESRI) is likely to add to the estimated formation rate. Duffy, et al. (2016:49) have projected a matching of supply and demand around 2018 consistent with a flow of 27,000 new builds in that year (up from just under 15,000 in 2016). Supply shortages are particularly acute in the greater Dublin catchment area. Shortages coupled with rising demand has triggered rising rents across the country especially in the greater Dublin area.

Figure 3 shows quarterly data on the ratio of average national rents (Daft, 2017) to average gross monthly earnings. The graph shows a fall in average rents consistent with depressed conditions in residential markets in the immediate aftermath of the economic collapse. Relative to average earning, rents now exceed 2008 levels. The latest data for the last quarter of 2016 indicate that rents were, on average, 38% of individual average gross monthly earnings.

Figure 3 Average Monthly Rent as a Percentage of Average Monthly Earnings



Sources: Irish Rental Report- Q4 2016 Daft (Daft, 2017), Earnings, Hours and Employment Costs Survey (Central Statistics Office, 2017) and Author's calculations.

Some sense of the social crisis in accommodation is given by the most recent data on rental accommodation. According to DAFT (2017:6), just under 4,000 dwellings were available for rent in February 2017 compared to 23,000 in 2009.

It is likely that a long period of time will elapse before order and balance is restored to the housing market. In the meantime, a much stronger, more ambitious and better-funded public agency led intervention is required to break the back of the supply shortage.

2.3 A European Cost Rental Model is required

The supply shortage is associated with a range of problems – fiscal, financial and market related. Decades of social policy entailing a developer led model of housing and significant speculation in land provided a basis for an acute housing crisis just as economic activity began to recover from 2013 onwards.

As described in Healy and Goldrick-Kelly (2017), the common thread in social policy failure in the area of housing is:

- Over-reliance on profit-seeking enterprises to provide the optimal level of housing including social.
- Use of passive tax reliefs to stimulate construction activity
- Use of scarce public funds to, effectively, subsidise private landlords through Rent Supplement and Housing Assistance Payments.

Restoring activity in the sector will be particularly challenging in the current period given a large overhang of public and private debt as well as evidence of a lack of coordination and leadership from Government. Typically, a lead-in time is required to restore building activity following a major shock such as was experienced in recent years. Clearly, a crisis of housing and accommodation will not be fixed in one year or even five years. Coordination of planning, land management, site development and mobilisation of skills, finance and other resources will take time.

A pro-active role by public agencies and local public authorities in regards to acquisition of land and use of integrated planning to ensure balance, inclusive and sustainable supply of accommodation linked to public services is needed.

While difficulties persist in a range of areas from planning to coordination, it is clear that the problem is mainly one of supply. The answer to the problem of supply is to build more houses. Unfortunately, the response of the private sector has been slow, uneven and well short of what is needed. While public expenditure remains constrained by a very rigid and conservative interpretation of EU fiscal rules there is scope for Government to significantly expand funding for housing by adopting a very different approach. We propose the development of what we term the *European Cost Rental Model*.

The *European Cost Rental Model* (ECRM) would distribute the cost of new homes over a long period of time and would socialise the costs of constructing and renting high quality accommodation. A key feature of this model is the development of a much stronger rental sector availed of by a mix of household types and incomes. To be effective and sustainable, the model would have to be self-financing in the medium term following an initial start-up phase where exchequer funding or injections of public and private capital would be necessary.

We propose a single, unitary, mixed-income rental model operated by a commercial publicly owned company and operating on a full cost-recovery basis. To that end, we propose the establishment of The *Housing Company of Ireland (HCI)*.

The State has an important role in not only providing quality social housing but setting the framework through planning and regulation to ensure a balance of provision and a better coordination of public services in new developments. Society needs to avoid a plan for social housing that, unintentionally or otherwise, reinforces social class segregation by place of residence, education and association in the community.

Strategically, we propose that public policy be re-orientated away from a limited social housing policy to a unitary publicly owned, but rented, housing system that ensures a mix of social and income groups in one location. From being a left over, public housing provision moves from social housing for the poor to support for a unitary rental market. By claiming a very significant place in the market, the HCI could help exert downward pressure on rent increases and, at the same time, contribute to higher supply. This would reap benefits by way of less strain on household finances, more options for temporary or migrant dwellers including high-skilled workers, students, etc.

2.4 How would a European Cost Rental Model be funded?

The HCI could draw on, and incorporate the staff and resources of the Housing Agency as well as resources and expertise in the local authorities in addition to the recruitment of the necessary expertise from the private sector and abroad. Such an approach would involve a relatively modest upfront 'on the books' injection of exchequer funds to get a new public commercial enterprise on the way and with a clear and ambitious business plan to operate on a medium-term full cost recovery basis. In other words, the undertaking would be self-financing in the medium-term on the strict condition that rental income would cover costs (which would include the servicing of debt attributed to the new entity). Whether or not the entity would be classified by Eurostat and the Central Statistics Office as 'on-the-books' or 'off-the-books' (circumventing EU fiscal rules in the latter case) is not central to the financial viability of our proposal. The development of a European Cost Rental Model would ensure a fully self-funded provision of high-quality rental accommodation with limited charge on exchequer resources.[1]

The new *The Housing Company of Ireland* would operate separately from the existing, but, reformed *Housing Finance Agency* which would provide funding mainly to The *Housing Company of Ireland* but also, where appropriate, to housing associations, local authorities, as well as municipal housing associations established by the latter. All lending would be undertaken according to sound and verifiable criteria taking advantage of exceptionally low current interest rates on capital markets and drawing on the considerable reserves of equity and cash at the National Treasury Management Agency as well as the international reputation and market access of the latter on international capital markets.

[1] The main charge would be our proposed enhanced Housing Assistance Payment mechanism to enable low-income households pay a below-market but full-cost rent

The funding base for *The Housing Company of Ireland* could be made up of a number of components including:

- Irish Exchequer
- *Ireland Strategic Investment Fund* including proceeds of the sale of Government shares in Allied Irish Banks.
- European Investment Bank and other EU funding institutions.
- National Asset Management Agency surplus funds expected from 2018 onwards.
- A new Irish Housing Solidarity Bond (e.g. for long-term pension investment).
- Domestic and international financial agencies including Trade unions, Credit Unions and other civic organisations with capital.
- Green Bonds issued as part of a European Investment Programme to invest in renewables and build new hyper insulated housing
- Private investment funds including pension funds as proposed by SIPTU (2014)

Were it possible to locate one billion euro, in the first instance, in additional funding over a period of 12 months it should be possible to put in place a building programme to construct just over 5,000 new dwellings at an average cost of €180,000 each.[2] This would be an ambitious but realistic start – albeit well short of what is needed in the medium-term to tackle the current crisis. Part of the upfront investment in this undertaking could be a free transfer of development land along with associated debt servicing costs from local authorities to The *Housing Company of Ireland*.

2.5 How would the ECRM be delivered and held to account?

In Figure 4, we outline a possible funding model with the aim of achieving an output of 70,000 new homes over a five-year period. We estimate that the total capital investment would be in the region of €12 billion over a five-year period.[3] This would include the cost of buying or acquiring 20,000 vacant but habitable houses over the same period. Some of these are currently in the possession of National Asset Management Agency and other agencies as well as private owners.

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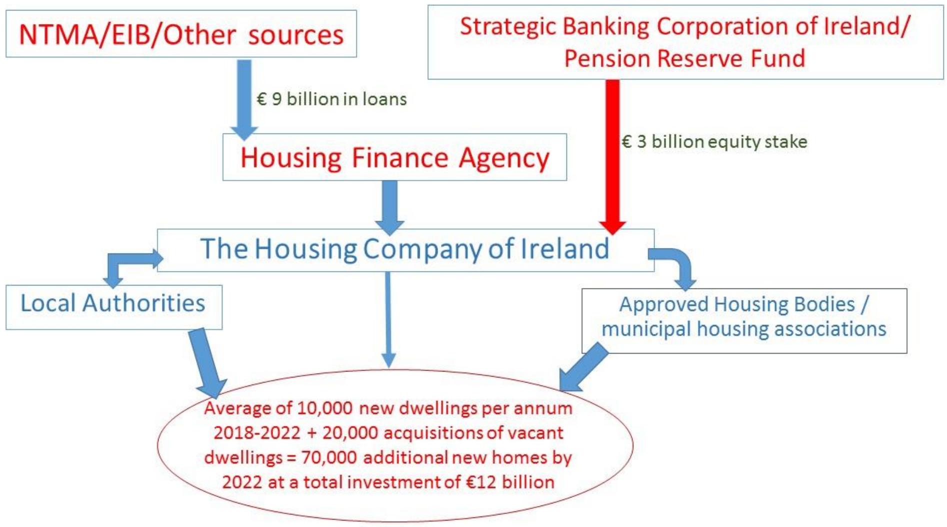
[2] Further detail is provided in Healy and Goldrick-Kelly (2017).

[3] This figure would be over and above what will be delivered by local authorities, housing associations and the private sector.

Figure 4 A self-funding European Cost Rental Model 2018-2022 (Healy and Goldrick-Kelly, 2017)



An injection of €3 billion in equity by the already existing *Strategic Banking Corporation of Ireland* (SBCI) would establish a strong, initial capital base for the Housing Company of Ireland. One option would be to re-structure state holdings of equity in Allied Irish Banks, Bank of Ireland and Permanent TSB and consolidate these into a new lending facility as part of the SBCI with a transfer of functions in order to strengthen the role of the SBCI. Switching equity by the state in these 'pillar' banks to the SBCI would represent a restoration of the National Pension Reserve Funds which were built up by payments from Irish tax payers over many years prior to 2009. Channelling this investment into long-term infrastructural projects such as the proposed *Housing Company of Ireland* would represent a good and safe investment backed by state guarantees.

In the long-term, the SBCI, which was established in 2014, could be developed into a national investment bank with a network of branches serving small and medium-sized businesses. The SBCI could invest in, or lend to, various infrastructural projects of which the activities of the proposed *Housing Company of Ireland* would be one. It could provide a major impetus to a pro-enterprise innovation programme to equip the Republic of Ireland to deal with the fall-out from Brexit (see McDonnell, 2017)

An initial injection of €3 billion directly from SBCI to HCI could be leveraged by a lending flow of €9 billion (three times the equity injection) through the existing *Housing Finance Agency* to the *Housing Company of Ireland*. The latter would commission new housing directly through existing approved housing bodies, municipal housing associations and local authorities (who should continue to have statutory responsibility for social housing). The aim is not to replace the existing building activity of the local authorities.

A crucial difference between ECRM and the current tiny level of local authority direct building of social housing is that the ECRM would be on a full cost recovery basis with very limited differentiation of rents by household income. Rents would be charged at full economic cost while the Housing Assistance Payment (HAP) would be expanded to ensure that low-income households have the option of paying full cost rent. The aim would be to set rent levels at full cost recovery but significantly below current market rates, which have become inflated due to a severe supply shortage.

An example of how a full cost recovery and partial cross-subsidisation model might work is provided by Healy and Goldrick-Kelly (2017). A number of scenarios are presented including varying rates of interest on long-term borrowing, mixed income profile of ECRM tenants and differentiation of rents around the average full economic cost level. We estimate that the required level of exchequer subsidy by way of HAP could be limited to around €50 million a year under the ECRM.

Cost rental accommodation is common in many European countries such as Austria and Netherlands. By anchoring rents in costs, it is possible to ensure stability in rental payments. Otherwise, cyclical changes in demand and supply as well as the possibility of excessive profiteering could jeopardise rent stability. Rental payments would service the cost of debt, construction, maintenance as well as provision for contingencies and upkeep.

A key feature of the housing crisis has been a slow, gradual and marked loss of necessary technical skills in the local authorities. Given the mixed history of public agency development in Ireland it is important that a new model for publicly managed house construction, financing and renting would be operated on a very different basis to that in other areas of public administration or commercial enterprise. A single commercial enterprise (The *Housing Company of Ireland*) would have the advantage of being able to pool particular resources and expertise from design to procurement to quality assurance.

The Company should be run at arms-length from Government but should, ultimately, be accountable to the public *Oireachtas* for monies spent and debt incurred. Consideration could also be given to giving legislative authority to the Minister in the relevant Department to make compulsory purchase orders as well as intervene by shortening and simplifying the process in particular planning disputes where there is a clear, undeniable and evidence-based case for a new development. A balance needs to be struck between the rights of private property, the common good, as well as the needs of all families and individuals where affordable quality housing is seen as a fundamental human right. We concur with the report of the *Oireachtas Committee on Housing and Homelessness* (Houses of the Oireachtas, 2016) which has urged for reform of the planning process and a review of the operations of *An Bord Pleanála,* as well as for a policy of making better use of Strategic Development Zones to bring forward social housing work.

Among the responsibilities of *The Housing Company of Ireland* could be the development of a comprehensive public register of land that has been rezoned for development. The public and policy makers have a right to know what land is available, who owns it, approximately how much it is worth at current market values and what evaluations have been undertaken with regards to the suitability of such land for building as well as relevant data on local public services (schools, health centres, transport, sports and other community facilities).

2.6 Other priority measures

The National Economic and Social Council (2015:20-21) has noted the in-built incentive for the National Asset Management Agency (NAMA) and developers still in ownership of land bought at pre-crash prices to ensure that a price floor is maintained at the level at which bad bank loans to developers were bought up (at a discount) by NAMA. There may even be an expectation on some owners or purchasers of lands to hold out for higher land prices (and associated rental or building profits) in the future. These factors do not help in regards to the supply of suitable land and associated housing supply in the short-term and may also serve to drive up, further, underlying construction and development costs.

We suggest that legislation governing the *National Asset Management Agency* (NAMA) be reviewed in order to facilitate rapid sale of lands on NAMA books without the constraint of a price floor. Freeing up land at a lower cost would help apply downward pressure on house prices and could help, in the medium-term, to constrain rent increases.

The *Housing Company of Ireland* would not be in a position to close down the deadly loop of land hoarding in expectation of price increases driving even more land hoarding without supplementary action by Government. Urgent action is needed at Government level to freeze the price of development land at a maximum level above agricultural land price. We recommend an active land management policy linked to taxes on vacant sites and a long-term strategic plan to develop and manage sites within an overall spatial and social plan for a county or larger unit.

In Budget 2015, the windfall profit tax of 80% on rezoned land for development, which was introduced in 2009, was abolished. The evidence that formed the basis for this decision in late 2014 has never been brought to light. It was claimed by the Minister for Finance, at the time, that the tax yielded little by way of revenue and may have become a barrier to a supply of land. However, it should be possible to combine a super tax on the profits or capital gains from a land sale for development with a substantial vacant site levy. A sufficiently high vacant site levy should be introduced without delay to prevent land hoarding.

2.7 Concluding remarks

Public policy needs to take the lead by investing in cost-rental, affordable and quality accommodation for its citizens. We concur with the views of the National Economic and Social Council (2015) that the hallmarks of a good societal housing policy is a social mixed economy that enables people to secure accommodation that is:

- Affordable
- Consistent with a sustainable community
- Inclusive of all

The main drawback with the current approach to public policy is that it is wasteful, costly and inefficient. Relying on the private sector, to the extent that has happened, to meet demand for social and affordable housing has not worked. A radical and realistic new departure is needed.

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