Address by Minister for Finance Michael McGrath TD Irish Association of Pension Funds Annual Dinner

23 February 2023

Introduction

I am delighted to be able to join you for this evening's event and to acknowledge, on behalf of the government, the hugely important contribution the pensions industry makes to the Irish economy and wider society.

Over the last 50 years, the Irish Association of Pension Funds has played a pivotal role in bringing our pensions industry to where it is today, accounting for almost €130 billion in retirement savings.

You are an organisation that brings a strong practitioner-level insight on pension developments, providing education, training and development opportunities to your members. As Minister for Finance, I want to assure you that I share your goal in ensuring we improve retirement provision in Ireland.

I would like to pay tribute to your Chief Executive Jerry Moriarty, your Chairperson Ann, Council members - both past and present - for your advocacy and engagement on important policy issues affecting your members and the people who depend on your services.

We should never lose sight of what the sector is ultimately all about, the provision of a good standard of living for people in their retirement. This is the purpose – the very essence – the objective of all that you do. It is therefore meaningful, impactful and adds real value to society.

To achieve this on as wide a basis as possible takes the collaboration of many stakeholders. The role of trustees, both professional and member representatives, is central to the overall wellbeing of pension schemes and I want to acknowledge their contribution. In addition, investment managers, investment consultants, actuaries, regulators, professional services firms, public servants, and many others play a vital role in the success of the sector and I join Ann in thanking you for all your hard work.

The Economic Outlook

Before speaking about pension specific matters, I would like to say a few words first about the economic outlook and the public finances. The current economic and interest rate climate has certainly helped benefit our defined benefit pension schemes, improving their funding position but challenges remain.

The invasion of Ukraine unleashed appalling destruction and loss of life and triggered massive upheaval in the global economy. Russia's weaponisation of gas supplies left global energy markets in flux with almost every advanced economy grappling with multi-decade high inflation rates in the past year.

Ireland is no exception with annual average inflation of just over 8 per cent recorded last year. Last September, when we announced Budget 2023, wholesale gas prices were trading at around eight times their long-term average.

Thankfully, headline inflation appears to have passed its peak and is now on a downward trajectory.

Indeed, the January harmonised inflation reading of 7.5 per cent is two percentage points below the peak recorded last summer. We had positive news yesterday that wholesale electricity prices fell 40% in December and are now 15% below this time last year, and I am hopeful that this will be reflected shortly in retail prices.

However, it is no surprise that given the elevated and broad based nature of inflationary pressures over the past year, central banks have brought the era of cheap money to a close. In the euro area, the ECB has raised interest rates by 3 percentage points since last July - the fastest pace of tightening in the history of the currency.

Unfortunately, this has raised the debt service costs for both households and businesses, although rising rates do benefit others such as savers as well as changing the narrative on the "search for yield" that so many long term investors, such as your industry, have been facing for so long.

Of course, rising consumer prices over the past year has also had knock-on effects on the domestic economy, by eroding household incomes and weighing on consumer spending. At the same time, SME's have been faced with the simultaneous headwinds of slowing domestic demand, tightening financing conditions and continued economic uncertainty.

Against this backdrop, my Department expects the domestic economy to effectively move sideways over the coming months, before returning to growth in the second half of the year.

For the year as a whole, we are forecasting growth in modified domestic demand – which provides the best measure of our domestic economic activity

- of 1¼ per cent. In effect, this represents a short and shallow downturn. However, in an increasingly volatile world and when compared to our nearest neighbour and European counterparts it represents a good position.

Overall the economy has proven remarkably resilient in the face of many challenges.

This is particularly so within our labour market. Today the CSO published very encouraging new data showing that there is now close to 2.6 million people in employment – higher than at any point in our nation's history, and some 220,000 higher than the pre pandemic peak. We have seen strong employment performance across the regions.

Public Finances

Earlier this week, along with my colleagues, I announced a new suite of Cost of Living measures worth €1¼ billion. This means that, since Budget 2022, we have provided approx.. €12 billion in direct relief to households and businesses to help ease the burden of inflation. That is almost 4½ per cent of national income.

We have been forceful and decisive in our fiscal response to the Cost of Living challenge, and, crucially, we have ensured that measures are carefully crafted. In an inflationary economic environment, hastily designed or excessive fiscal interventions by Government would backfire, adding to inflationary pressures.

We have to recognise that there remain real vulnerabilities in our public finances. Last year, we recorded an estimated headline surplus of over €5 billion, or around 2 per cent of national income. This was, of course, very welcome news, and is an indicator of the strength of our economic recovery from the pandemic.

However, the true picture is not so unambiguously positive.

An overreliance on corporation tax is something which this Government has frequently highlighted as a key risk to the Irish public finances, and we are acting to mitigate this risk.

Earlier this month, I announced that €4 billion in excess corporate tax has now been transferred to the National Reserve Fund, building on an earlier transfer last year, this amounts to €6 billion in receipts that we have set aside to rebuild our fiscal buffers.

Ultimately, the best way we can circumvent the risks around corporation tax and ensure the long-term resilience of our public finances is by adhering to the fiscal parameters set out in the budgetary framework and keeping public expenditure growth at sustainable rates and that is what I as Minister for Finance intend to do.

Sustainable Finance

I would like to turn now to the topical issue of Sustainable Finance encompassing the Sustainable Finance Disclosure Regulation, the Taxonomy for sustainable activities, and the Corporate Sustainability Reporting Directive, which have imposed obligations for asset managers and other financial markets participants.

These regulatory and supervisory frameworks will allow companies, products, and financial services firms to meet objective, scientifically based, standards and will also help influence investor and consumer behaviour to drive the sustainable transition.

It is imperative that participants such as you, the pension industry, help guide the necessary investments to decarbonise the economy, and drive energy efficiency, and renewable options. We also need you to help support the mainstreaming of sustainable practises across our entire economy and society.

This transition to a climate neutral economy has significant potential to create sustainable employment and enterprise opportunities and in turn a more productive, stable and resilient, economy.

It is recognised that there are challenges in making this transition. However, in identifying and meeting the demand for sustainable products and investments you will help ensure that the common ambition of a net zero transformation can be met and ultimately a better future for us all.

Automatic Enrolment Pension System

The Roadmap for Pensions Reform set out a number of crucial areas to address the changes needed in our pension system.

Introducing an Automatic Enrolment Retirement Saving System represents a key policy goal, as reflected through our Programme for Government objectives. In March last year, the Government approved the final design principles for the new auto-enrolment (AE) retirement savings system.

This is expected to become operational in 2024. Within scope are employees who are aged between 23 and 60 years, earning over €20,000 across all their employments, and who are not already enrolled in an occupational pension scheme.

AE will be gradually phased in over a decade, with both employer and employee contributions starting at 1.5 per cent of gross salary, and rising every three years, until reaching the maximum contribution rate of 6 per cent from Year 10 onwards with the State also making a contribution at a rate of €1 for every €3 saved by the employee.

While participants will have the freedom of choice to opt-out under certain conditions I am hopeful that the benefits of long term saving will result in high retention rates in the scheme.

The principle underlying the scheme is to increase supplementary pension coverage, especially amongst those who have not joined a pension scheme due to inertia rather than unaffordability. The CSO published some new data today on pension coverage indicating two-thirds of people aged between 20 and 69 have some form of private pension on top of the state pension.

However, there is wide variation in coverage. 90% of employees in Financial Service have a private pension whereas it is just 24% in the Accommodation and Food Services Sector.

When implemented, Auto Enrolment will enable people to save and accumulate sufficient resources to maintain a good standard of living in their retirement. In this way, the AE System will increase the wellbeing, financial security and independence of our future retirees.

I am pleased to say that implementation is well underway, with a project team in the Department of Social Protection progressing a range of elements. The General Scheme of the Bill has been published and the Joint Oireachtas Committee on Social Protection has been meeting key stakeholders over the last few weeks.

While I accept that views differ amongst some key stakeholders on aspects of the design of Automatic Enrolment, I think that we can all agree the positive, transformative effect that this major public policy initiative will have for future generations of pension savers, retirees and their families.

Interdepartmental Pensions and Taxation Reform Group

Another area the Roadmap for Pensions Reform prioritised is a workstream to help simplify and harmonise the supplemental pension system. Chaired by my Department, the Interdepartmental Pensions and Taxation Reform Group prepared a Report containing a number of practical, focussed recommendations to help deliver this commitment.

I am pleased that equalising the funding treatment of the PRSA with Occupational Pensions Schemes was enacted in the 2022 Finance Act. A number of further proposals from the report are currently being examined to form the work programme for the Group in 2023 and they are also looking at pension-specific recommendations from the Commission on Taxation and Welfare Report.

In tandem with this, the EU Pan-European Personal Pension Product (PEPP) regulation was also transposed into Irish law last year, with the Finance Bill granting it similar tax treatment to other pension products in the State.

Other important work remains. The gender pension gap is an important point to consider in the ongoing reform process. The combination of reduced working hours and breaks in employment due to caring roles can have significant implications for women’s duration of working life and lifetime earnings. This impacts directly on their pension adequacy and bridging this gap is an important policy objective.

IORP II

As you will all be aware, under IORP II new regulations for trustees and the Pensions Authority have been introduced. Ireland has been an outlier in the EU in terms of the number of occupational pension schemes we have, many of which are single member schemes. There was a need to address this situation for consumer protection, simplification and to allow for appropriate regulation.

With the establishment of more Master Trusts we have begun to see consolidation emerge in the marketplace. The next few years will see further significant changes in pension funds and I look forward to working together on our shared vision of achieving secure, fair and simplified retirement provision.

Pension Commission

Before I conclude, I will very briefly mention the Government's response to the Pension Commission recommendations. As the bedrock of the pension system in Ireland, the State Pension is very effective at ensuring that our pensioners do not experience poverty.

This Government is committed to ensuring that this remains the case for current pensioners, those nearing State Pension age and today's young workers.

A series of proposals are currently being examined by my colleague Minister Humphreys. Amongst other things this will reflect: changes in the workplace where some may choose to work longer; the important contribution made by carers; and the critical need to place our State Pension system on a sustainable footing.

Minister Humphreys will bring forward a recommended response and implementation plan to the Pensions Commission's recommendations as soon as possible

Conclusion

To finish, I would like again thank the IAPF for the invitation to speak to you this evening. The sector that you all work makes a positive and important contribution to the lives of our citizens, society and wider economy.

As Minister for Finance I wish to acknowledge this, and the role of the industry in assisting Government in delivering many public policy objectives.

It remains to me to wish you all an enjoyable evening. Thank you.

Michael McGrath TD

Minister for Finance