Can We Afford the Costs of the Covid-19 Crisis?

Donal de Buitléir

It is now clear that the costs of the Covid 19 crisis will be very high perhaps up to €30 billion or almost 10% of GDP. How can we pay for this?

In its latest Quarterly Bulletin the Central Bank projected that the general government balance will move from an estimated surplus of 0.7 per cent of GNI* in 2019 to a deficit of over 10 per cent of GNI* this year (or from 0.4 per cent of GDP to -6 per cent of GDP). In terms of general government debt, the projection is for an increase in the ratio from an estimated 97 per cent of GNI* in 2019 to 112 per cent of GNI* (or from 58 to 66 per cent of GDP).

Debt Burden

The size of the public debt burden is usually measured as the stock of debt as a percentage of GDP. However, this measure is no longer a useful guide for Ireland and does not take account of the rate of interest countries are charged on their debt. The debt burden may be better expressed in terms of debt servicing costs which are a function of the size of the debt stock as well as the interest rate.

For example**,** in the 1987 Ireland's debt/GDP ratio reached 119 per cent. While the Debt/GNP ratio in the 1980's is broadly similar to that which we may now face, the burden of servicing that debt is lower because the interest rate on that debt is now much lower. Interest payments by general government reached 10.3 per cent of GDP in 1985. This compares with about 2 per cent of GNP now.

This year we are fortunate in that two big bonds are due for redemption in April and October amounting to €17 billon at an average interest rate of 4.7 per cent. If these were replaced at an average interest rate of 2 per cent the saving would amount to €460 million a year. We refinanced €17.6 billion of debt in 2018 at an average interest rate of 1.08 per cent. If the maturing bonds were replaced at an average interest rate of 2 per cent (a conservative assumption) the saving would amount to €460 million a year. This saving would finance €30 billion of borrowing at an interest rate of 1.53 per cent.

My conclusion is that the costs of the additional borrowing necessitated by the crisis are affordable. Notwithstanding this, it is desirable that additional borrowing has extended maturity dates and that the funds are spent in a targeted and efficient way.