Banc Ceannais na hÉireann
Central Bank of Ireland
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Box B: QB 4 – December 2024

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Developments in Private Sector Debt

By John Andreuccetti and Daniel Martin (Statistics Division)

This *Box* describes developments in Irish private sector debt, which stood at 146 per cent of GDP on a consolidated basis in Q2 2024. Private sector debt refers to the total debt securities and loan liabilities of Irish non-financial corporations (NFCs) and households. Private sector indebtedness forms part of the European Commission's macroeconomic imbalances procedure (MIP), which aims to identify risks and trends that could adversely affect member state economies[1]. Consolidated debt, which eliminates inter-sectoral transactions and positions[2], is the preferred debt measure for MIP analysis.

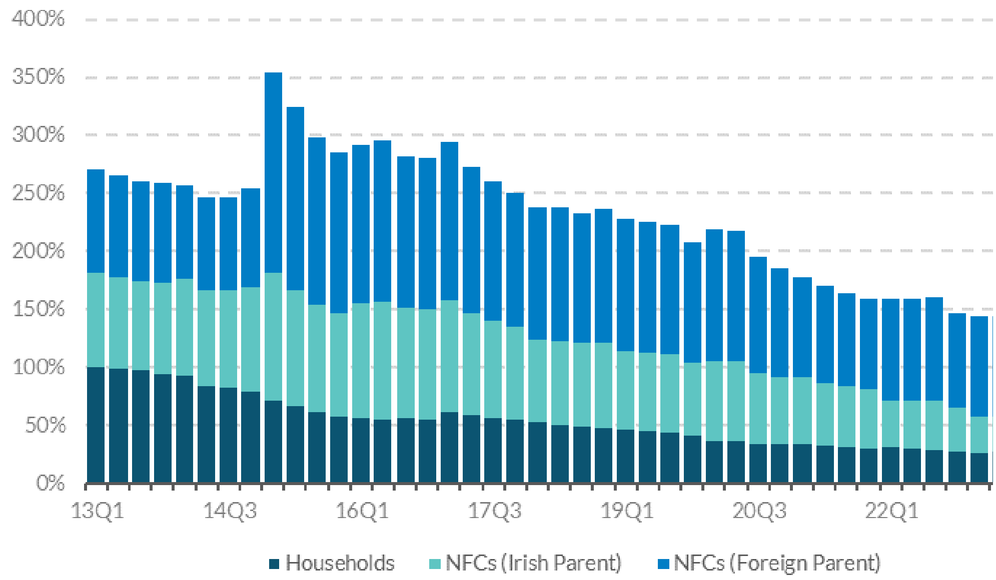
[1] Macroeconomic Imbalances Procedure Introduced from Eurostat and Eurostat's Alert Mechanism Report (2024)

[2] Private sector debt is shown on an unconsolidated basis within Quarterly Financial Accounts (QFA) and totalled €832.7bn in Q2 2024. For more details on consolidation see Eurostat's methodology.

Private Sector Debt has been on a downward trajectory

Figure 1

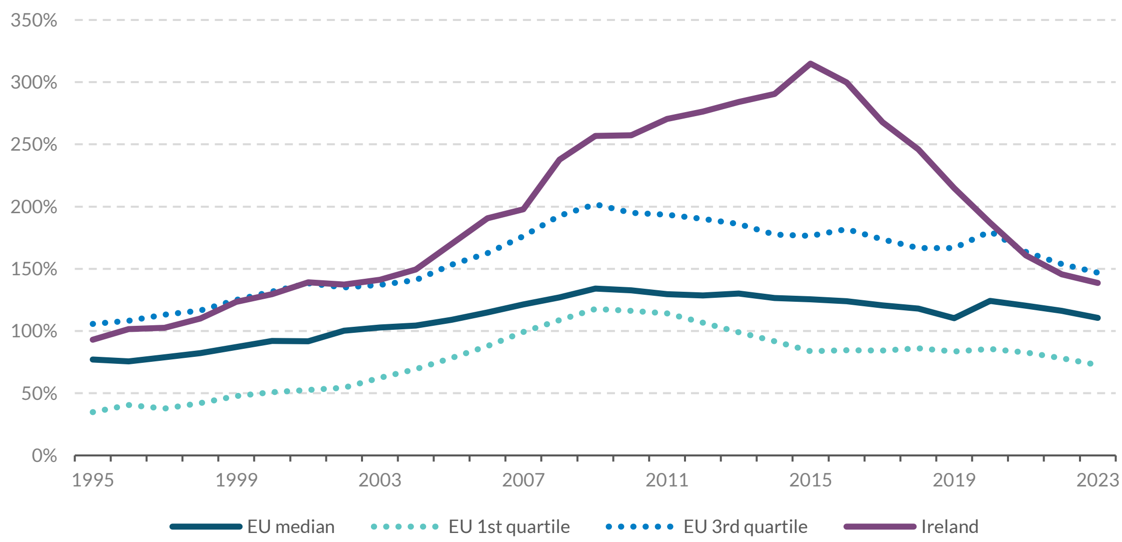
Consolidated Private Sector Debt to GDP (%), Ireland



Source: CSO, Central Bank and Author Calculations

Figure 2

Consolidated Private Sector Debt to GDP, EU Comparison



Source: Eurostat and Author Calculations

Irish private sector debt was 146 per cent of GDP in Q2 2024 under the consolidated measure, as shown in Figure 1. The Irish private sector debt to GDP ratio has been decreasing and ranked ninth highest among European Union (EU) countries in 2023, an improvement by historical standards, as highlighted in Figure 2, but it remains above the EU median.

Consolidated NFC debt, stood at 115 per cent of GDP in Q2 2024 and movements in NFC debt have consistently driven changes in total private sector debt given their large share of the total. This creates a risk that focusing on overall private sector debt measures could overlook important movements in Irish-controlled NFC debt and household debt.

Large multinational enterprises (MNEs) activity and the globalised nature of the Irish economy distort measures of private sector debt for Ireland. GNI* attempts to more accurately capture domestic economic activity (see Byrne et al, 2021) and indicates a higher level of consolidated private sector indebtedness, 250 per cent of GNI*, as of Q4 2023[3], when used as a benchmark.

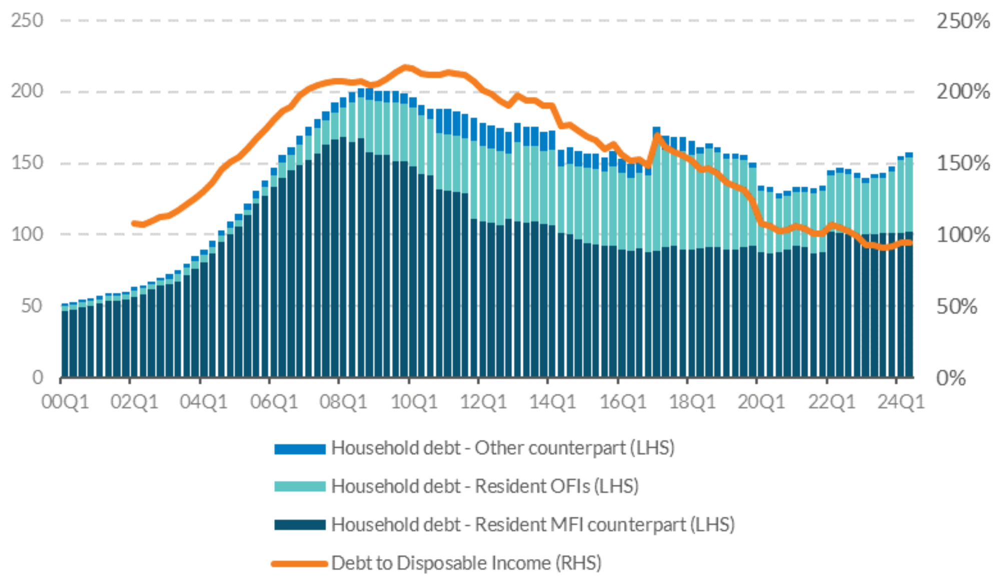
Debt held by MNEs in Ireland may be decoupled from their Irish economic activity and more reflective of their global activity. Consequently, it is useful to analyse households, Irish-controlled NFCs, and foreign-controlled NFCs[4] separately. Households and Irish-controlled NFCs debt was each equivalent to approximately 50 per cent of GNI* in Q4 2023, with the remaining 150 per cent accounted for by foreign-controlled NFCs. Prior to Q4 2021, the path of foreign-controlled debt was similar to that of household and Irish-controlled NFC debt. Since then, foreign-controlled NFC debt and household debt have increased by 18 per cent and 17 per cent respectively but Irish-controlled NFC debt has decreased by 26 per cent. Decreasing loan liabilities have driven this decline for Irish controlled NFCs, with contractions in lending to certain sectors of the real economy in this period such as Hotels and Restaurants, and Manufacturing (Ó Cléirigh & Kaiser, 2024).

[3] GNI* is an annual measure and available to reference period 2023.
[4] Note, this is based on CSO annual shares of foreign-controlled NFCs available as part of their institutional sector accounts applied to Central Bank QFA data.

Household debt has increased in recent quarters but income growth has limited the change in debt to disposable income

Figure 3

Household Debt (€ Billion) and Household Debt to Disposable Income Ratio (%)



Source: Central Bank and Author Calculations

The stock of household debt has increased in each of the last five quarters, reaching €157.6bn (Figure 3), the highest household debt level since Q4 2018[5]. Income growth has largely matched the rise in household debt meaning that the debt to disposable income ratio has been relatively stable even as the stock of debt rose. At 95 per cent in Q2 2024, debt to disposable income was low by Irish historical standards but remained above the euro area average of 85 per cent.

Beyond incomes, household deposits are also relevant when considering the resilience of household balance sheets and debt sustainability more generally. The accumulation of excess savings during the pandemic has been well documented (Byrne, McIndoe-Calder & Wu, 2023). The latest Money and Banking Statistics show that, although the rate of growth in household deposits has declined, it remains positive and broadly in line with pre-pandemic levels. In the year to end-September 2024, household deposits increased by 3.1 per cent to stand at €157.5bn.

Figure 3 also shows that loans to households from domestic other financial institutions (OFIs) have been the main driver of household debt growth in recent quarters. However, domestic monetary

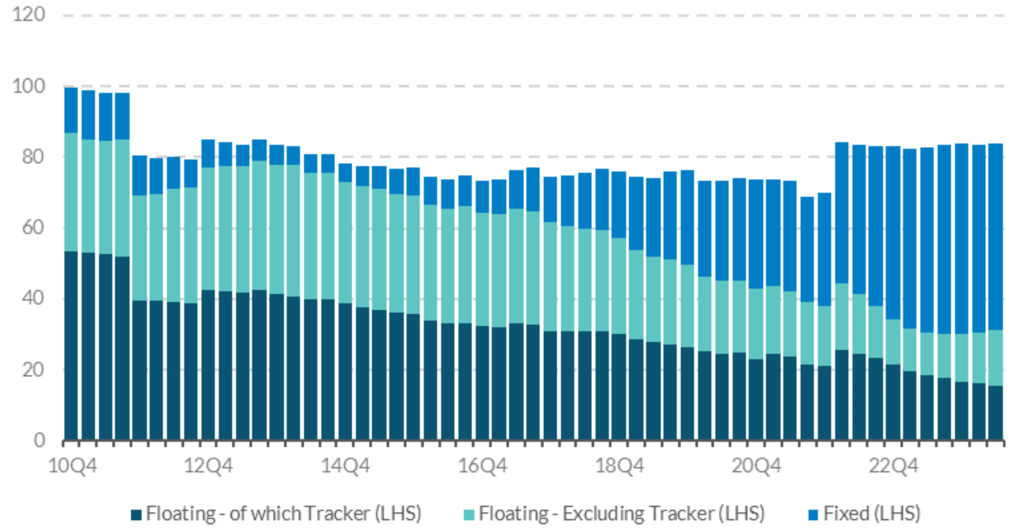
[5] This does not take account of differences in debt across the wealth distribution (see Moreno, 2024).

financial institutions (MFIs) continue to account for the largest share of the total, accounting for around two thirds of total household debt in Q2 2024.

Total mortgage debt has been stable but the concentration of fixed rate loans has increased

Figure 4

Volume of Total Household Mortgage Debt by Type (€ Billion)



Source: Central Bank and Author Calculation

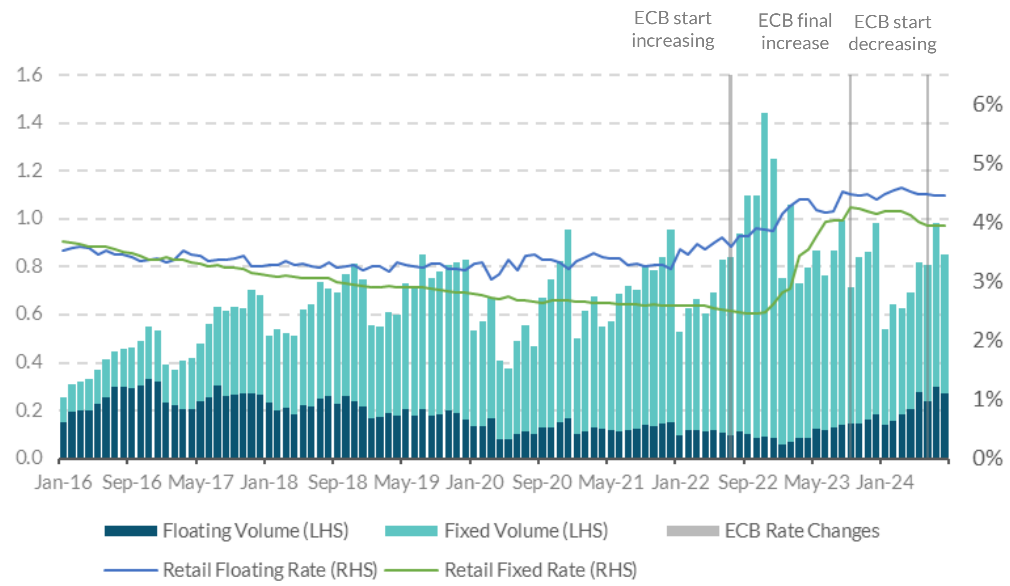
Mortgage loans remain the key determinant of household debt, accounting for around 83 per cent of household loans from MFIs and over 50 per cent of total household debt in Q2 2024. Central Bank Mortgage arrears statistics show that in addition to this MFI mortgage debt, non-banks held around €25bn of Irish household mortgage debt at the end of Q2 2024 (also see Gaffney et al, 2022).

While the share of household debt with domestic banks accounted for by mortgage loans has been relatively stable, the type of mortgages making up this debt has changed in recent years. Figure 4 shows that total household mortgage debt has been relatively stable since Q1 2022 but fixed rate mortgages have increased their share of total mortgage debt from 47 per cent in Q1 2022 to 63 per cent in Q2 2024.

New lending at fixed rates peaks before ECB rate changes pass through to retail rates

Figure 5

New mortgage lending by type (€ Billion) and retail interest rates (%)



Source: Central Bank

Figure 5 shows new mortgage lending to households from Central Bank retail interest rate statistics. The share of new lending accounted for by fixed rate mortgages has been increasing, in line with the discussion on total outstanding mortgage debt above. Fixed rate mortgages accounted for over 50 per cent of all new mortgage lending for the first time in 2017 and peaked at over 90 per cent in late 2022, coinciding with the first ECB rate increase of the current cycle in July 2022. Although remaining elevated by long-term historical standards, the share of fixed rate loans within new mortgage lending has steadily decreased since then. This decrease in the fixed rate share coincided with the ECB moving from interest rate increases towards their first rate reduction of the current cycle. Therefore, the change may reflect household expectations around future interest rate movements and the perceived benefit of opting for a fixed rate. Previous Central Bank research (Byrne and Foster, 2023) highlighted that the pass-through of ECB base rate increases to retail mortgage rates has been uneven across Europe. In June 2022, prior to the interest rate increases, retail mortgage rates in Ireland were the second highest in Europe but Irish rates ranked sixth as of September 2024. As mortgage loans account for over half of total household debt, the interest households pay on these loans is of particular importance for total household debt and ultimately private sector debt.

In conclusion, the globalised nature of the Irish economy creates challenges interpreting standard international measures such as private sector debt to GDP. Comparisons to GNI* are more informative and enhanced further by considering Irish-controlled NFCs, foreign-controlled NFCs, and

households individually. Prior to Q4 2021, the trends were similar but since then foreign-controlled NFCs and households have increased their debt levels while Irish-controlled NFC debt has decreased. Irish-controlled NFC debt may have been impacted by negative lending to certain sectors of the real economy while foreign-controlled NFC debt is impacted by the global activity of MNEs based in Ireland. Mortgage loans are the key component of household debt and fixed rate loans account for a larger share of this debt than the historic norm, which could have implications for future interest payments by households.