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# PANEL RESPONSE: FINANCIAL SECTOR POLICY

# Delivering Long Term Resilience – Savings And Investment Dynamics in Ireland

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## I INTRODUCTION

Dia dhaoibh a cháirde go léir. Is mór an onóir a bheith anseo inniu, in Acadamh Ríoga na hÉireann i mBaile Átha Cliath, chun aitheantas a thabhairt do Patrick Honohan.

Le linn a shaol oibre, mar fhostaí sa tseirbhís phoiblí, mar ollamh le clú agus cáil domhanda air agus mar Gobharnóir an Bhainc Cheannais, chuir sé go mór le cur chuige na tíre ó thaobh cursaí shoisialta agus eacnamaíóchta.

Many thanks. I am delighted to be here at this conference in honour of Patrick Honohan who, through his incredible career as a professor and public servant, has contributed so much in both thought and action to Irish, European and Global economic stability and well-being.

Before I begin, let me just share some personal reflections about Patrick, who to me will always be Governor Honohan. I worked for Patrick throughout his time as Governor of the Central Bank from 2009 to 2015. It always struck me that Patrick had what might be considered the “holy trinity” of attributes needed for a Governor at that time:

- a deep understanding of the Irish economy and financial system as well as a knowledge of how to manage economies and banking systems which are in crisis;

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- the leadership qualities needed to guide the Central Bank through a period of rebuilding and reform (bearing in mind that failures in the Central Bank had been part of systemic failures that caused the crisis, but also that the Bank was central to rebuilding the banking system and supporting economic recovery); and
- the communication skills needed to be trusted by the public as well as to engage with the wide range of stakeholders at both domestic and international level.

The esteem in which he is held in the Bank is evident today given former Governor Lane's involvement in organising the event, but also by the attendance of current Governor Makhlouf, no less than five current or former deputy governors and a number of current and retired Bank staff.

Patrick was the right person for the right job at the right time. I am immensely proud to have worked for him and grateful for all the personal support and advice he has given me over the years since.

Many thanks too to my colleagues for their interesting paper[1] – setting out the data in terms of savings and investment landscape for households and businesses in Ireland – as well as some of the policy changes that could enhance that landscape.

For my part, I thought I would ground and contrast this research with some of the big challenges we are thinking about currently at the Central Bank of Ireland, including:

- the changing nature of our financial system;
- geo-economic fragmentation;
- and structural changes underway, including demographics.

Underpinning all of these challenges is something that is always at the forefront of our considerations; namely resilience – of households, the financial sector, the economy, and the public finances.

As Patrick has said in a recent IMF/CEPR address:

> *…key among the characteristics needed to prosper in what seems to be a rapidly changing and increasingly unpredictable global economic environment are resilience and the adaptability to take advantage of new opportunities and trends.*[2]

Therefore, I will use my remarks to discuss the current structure of savings and investment behaviour in light of these big issues, including the implications the dynamics may have for Ireland's future.

[1] Laura Boyd, Niall McGeever, Fergal McCann, Tara McIndoe-Calder: "Saving to invest? Financial Intermediation in Ireland since the GFC".
[2] See Honohan: "Some Lessons Learnt from the EU-IMF Programme", January 2025. Available at: www.centralbank.ie

## II BETTING THE HOUSE ON HOUSING

One thing you will know is on our mind at Central Bank of Ireland is the evolving financial services landscape in Ireland, which has grown and changed significantly in recent years, becoming more international and more complex:

- While there has been some consolidation in the number of retail banks, total assets are still growing. We have also seen a five-fold increase in the assets held by investment banks, with two additional Globally Systemically Important Banks making Ireland their European HQ;
- The number of Payment and E-Money Institutions regulated by the Central Bank of Ireland has tripled in the last seven years, with a more than ten-fold increase in safeguarded funds;
- We have gone from having just two international trading venues to now having seven; and the number of complex trading firms has tripled to nine, with the size of that sector in terms of assets having grown more than 500 per cent since 2016;
- And the vast majority of assets and liabilities of the Irish financial Sector are cross-border – and have been for a long time. In 2022, around 85 per cent of the assets of the financial sector in Ireland were cross-border in nature.

Reading the paper here though, from a household and SME perspective, despite this changing financial services sector, the data paint a pretty static picture in terms of savings and investment decisions and preferences – aside from the level shift in the savings *rate* post-pandemic.

Such decisions for households remain simple – still primarily bank deposits and housing – with the data showing little impact of the increasingly sophisticated international financial sector we regulate on the real economy of citizens and businesses.

And while not surprising given current challenges facing the country, it is striking what a dominant role housing still plays in domestic finances. With the exception of the forced savings of the pandemic period, around half the stock of savings flow into housing; houses also account for large shares of household wealth; and in one area of financial evolution, in terms of financing to SMEs from the non-bank lenders, almost half this lending goes to real estate SMEs.

Again, as I said, given current housing situation in the country this concentration is not a surprise. But, in light of the boom bust cycle we have experienced in housing this century, and the long tail of the financial crisis in this regard – and how in many ways we are socially and economically still paying the price – I think this concentration is still something worth considering.

For me it reinforces the importance of the post-crisis measures we introduced to embed resilience in our economy; and point to the fact that as we rightly seek to make up lost ground, we do not lose sight of the importance of resilience – and ensure long term stability is not sacrificed for short term catch up.

For these reasons, maintaining the bank capital framework, our macro prudential rules (both of which Patrick contributed to significantly), and building resilience in the non-bank sector should remain key priorities for the Central Bank. And indeed in a monetary union, I would say that domestic macro policy tools – in particular fiscal policy and macroprudential policy – become all the more important.

And from a broader policy point of view, such concentration also suggests we should encourage a diversification in investment and wealth, given diversification is the cornerstone of portfolio resilience, with some worthwhile policy measures proposed by the paper.

This point brings me to two issues I want to discuss, in terms of behaviours and dual economies in Ireland, at the household and business level. Both of which are important from a forward-looking policy perspective, as we seek to ensure long term micro and macro resilience for our citizens and the State.

## III DUAL ECONOMY 1: HOUSEHOLD WEALTH

Firstly at the household level, the paper touches on the very different investment behaviours depending on the income distribution.

Looking ahead at challenges, I want to tie this to household wealth and a potential wealth gap that could significantly open up in the future.

As Boyd says:

> *the highest income households are not only more likely to save and build up wealth, but they are also more likely to diversify their portfolio and invest their savings. This gives them access to potentially higher returns and larger wealth gains, which in turn, further concentrates the stock of savings.*[3]

While speaking of financial assets, this dynamic also extends to non-financial assets and housing – considering its dominant role in wealth in Ireland.

Ireland has a very progressive tax rate, which significantly reduces inequality of incomes. As noted by the Commission on Taxation and Welfare:

> *while the distribution of market incomes [in Ireland] has been and remains highly unequal compared to other advanced economies, the distribution of disposable incomes is closer to European norms.*[4]

[3] Boyd (2025) "Saving to Invest? Financial Intermediation in Ireland Since the GFC" Section 2.4.
[4] *Foundations for the Future: Report of the Commission on Taxation and Welfare* pg. 30.

In terms of household wealth, however, while Ireland has historically had low levels of wealth, this has changed in modern times, with net wealth in particular having grown across the distribution over the last decade.[5]

In line with other countries, however, that growth has not been evenly spread across the distribution, with the top 10 per cent accounting for almost 50 per cent of growth. Absent a change in policy or behaviours, it is hard not to see this wealth gap widening in future decades.

Add this to our housing challenges – with homeownership potentially in structural decline,[6] and the fact that one-third of Irish workers are currently without any supplemental coverage outside of their future State pension,[7] there is a significant risk on the horizon where a material proportion of households would have neither housing nor private pension as a form of wealth for their old age.

This is even without considering the demographic challenges ahead – with the old age dependency ratio expected to increase from around 25 per cent in 2022 to close to 50 per cent in 2050 – and the stresses that will put on our public finances, meaning the extent of government intervention or transfers in future to advert this risk may be restricted.

This calls for action now, and why the Government's introduction of auto-enrolment is so important; why work to increase supply and affordability of housing is critical, as are cultural and financial literacy initiatives to increase retail investor participation.

As outlined in the paper, tax policy has a potential role to make it easier for households to invest. Industry has a role too, in creating better retail products, better value for money and better channels for investment.

All of this would increase the future well-being of our citizens, and the long-term resilience of households, the economy and the State.

## IV DUAL ECONOMY 2: MNE VS DOMESTIC PRODUCTIVITY

Finally, at the business level, the paper illustrates the very different financing behaviours in our dual economy – with domestic businesses much less likely to seek investment. Part of this is perhaps another long tail of the Global Financial Crisis in terms of an aversion from businesses to take on debt.

[5] Daly, 2022. *The Evolution of Irish Household Wealth Inequality Since 2013: Insights from new Distributional Wealth Accounts November 2022.*

[6] See for example *Foundations for the Future: Report of the Commission on Taxation and Welfare* pg. 34: "Over 60 per cent of those born in the 1960s lived in a home they or their partner owned by the age of 30, whereas the comparable figure for those born in the 1970s was 39 per cent and, for those born in the early 1980s, 32 per cent".

[7] See *CSO Pension Coverage 2023.*

While the paper observes that domestic firms are satisfied with structurally lower investment rates, I wonder if policymakers should be satisfied with that?

And although it is rare for a central banker to be asking people to take on more leverage, Central Bank of Ireland analysis puts annual productivity growth of domestic-dominated sectors of the Irish economy at just 0.7 per cent on average between 2011 and 2023,[8] demonstrating how much of our productivity growth is driven by our MNEs.

This would suggest the domestic economy needs to significantly increase its productivity, with a potential role for increased investment. And so, while conservative borrowing at a firm level in the short term may look resilient, there are risks in a dual economy context that it may ultimately compromise the long run resilience of the country.

For while openness will, and should, remain fundamental to Ireland's economic model, increasing reliance on our MNE sector in recent years, allied with potential geopolitical shifts and geo-economic fragmentation, would suggest that diversification would again lead to better resilience here.

In line with retail investment for households there is likely something cultural to tackle, including hangovers from previous excess credit cycles. As the paper recognises, the system of financial intermediation in Ireland appears to meet the credit demand needs of the economy appropriately.

The important question is if that demand is appropriate. If not, then a question arises as to whether policymakers should encourage a more dynamic, innovative, and entrepreneurial domestic sector, which leverages productivity spill-overs from our MNEs and uses the access to international capital our financial sector provides.

Needless to say the objective of this should be increasing the long-term resilience of our economy, and so achieving it should be done in a way that does not sacrifice stability for growth.

## V CONCLUSION

To conclude, the world is changing rapidly – with significant challenges on the horizon. But the current savings and investment dynamics in Ireland may not set us up well to meet those challenges:

- Households may not be able to meet their future needs, and our society may become more unequal than it has previously been. And without diversification of investment they may not be resilient to shocks;
- Our domestic firms may be missing an opportunity for productivity growth, meaning Ireland is missing an opportunity to broaden and strengthen its economy – in particular in an increasingly uncertain global economy, and potential geo-economic fragmentation.

[8] Central Bank of Ireland staff calculations from CSO Data.

These are not challenges we face alone, and indeed in an European context developing a savings and investment union in the EU, ensuring we have the financing for the huge structural transitions ahead, and increasing our productivity and firms in the key sectors of the future are all likely to be the Economic priorities of the next Commission and beyond.

In this context, I would say that these are all important priorities. But the pursuit of them should avoid an inappropriate rowing back of the post-Global Financial Crisis regulatory reforms, and should be cognisant of the importance of maintaining the resilience we have built across the euro area economy.

As we move forward, and Europe looks to embrace competitiveness, to quote Patrick writing on the occasion of the 20th anniversary of the euro "policy needs the balanced economic pragmatism that has increasingly characterised euro area decision-makers since 2012."[9]

Comhghairdeachas arís Patrick agus go raibh maith agat.

[9] Honohan, 2019. "The euro at 20: pragmatism underpins success of single currency", *Irish Times* January 2019.