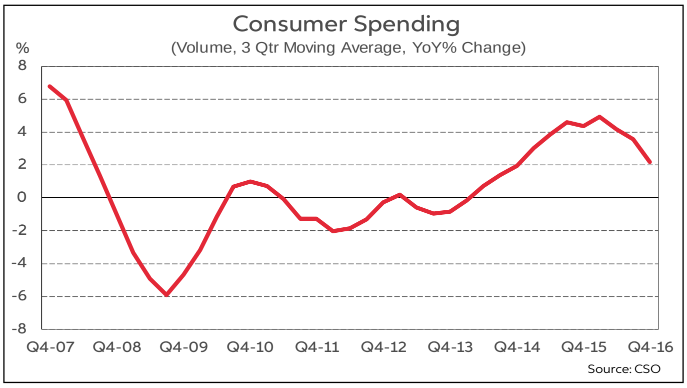
Irish Economy Update

AIB Treasury Economic Research Unit

March 2017

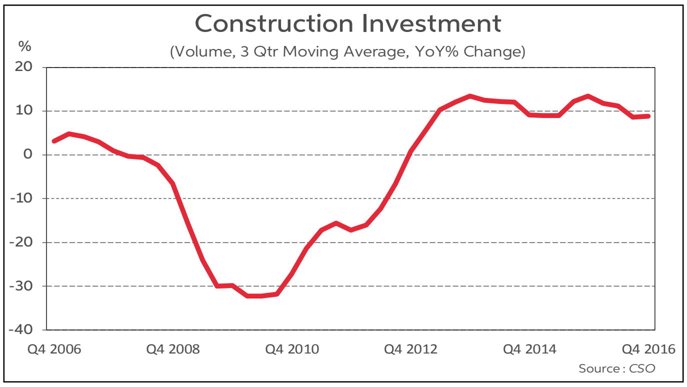
National Accounts not fit for purpose

The recently published CSO National Accounts for 2016 show that **GDP grew by 5.2% last year**, which was stronger than expected. Meanwhile, **GNP is estimated to have grown by 9%**, having been boosted by a decline in profit repatriations by multi-national companies. Hence, it does not provide a true reflection of the real performance of the economy.



Irish National Accounts have become badly distorted by the activities of multi-national companies in the past couple of years and this is again reflected in the data for last year. The figures show that GDP flat lined in the first half of the year and then grew by 6% in the second half, which clearly did not happen. **Contract manufacturing, transfers of intellectual property rights and companies re-domiciling to Ireland are all distorting the data.** This has given rise to some rather **bizarre figures**, such as growth rates of 45% and 33% in fixed investment in 2016 and 2015, export growth slowing from 34.5% in 2015 to 2.4% last year, as well as the infamous 26.3% rise in GDP in 2015.

We have great sympathy for the CSO in trying to compile the National Accounts as it is required to follow Eurostat conventions and U.N. rules and so is unable to adjust Irish data to allow for distortions and produce meaningful measures of GDP, GNP and other figures. In the past, the CSO published detailed data that allowed economists to derive the underlying growth rate of the domestic economy. However, these **detailed figures had to be suppressed** for the final quarter of 2016 and in the annual data for 2016 due to confidentiality reasons—another constraint on the CSO in terms of what it can publish. This has reduced even further the usefulness of the National Accounts data as a barometer of economic activity.



The National Accounts do show **a slowdown in the growth in consumer spending to 3% last year** from 4.5% in 2015, although we suspect this figure could be revised up when final data are published in the summer. They also show growth of 5.3% in net government spending on goods and services last year, which would not seem to tie in with reality.

Output from the construction sector rose by 11.4% in 2016 as it continues its steady, albeit moderate, recovery. Meanwhile, agricultural output rose by 6%, continuing to grow at a strong rate following the lifting of EU quota restrictions on milk production. The data also show **continuing strong growth in output from a broad range of service sectors,** including transport, communications, software, business and hospitality services.

Beyond that, there is not much to be gleaned from the detailed National Accounts, with external trade and manufacturing output figures, as well as investment data, all badly distorted. **The CSO hopes to publish a new metric this summer called GNI*, or adjusted Gross National Income, which will provide an alternative measure of Irish growth that will exclude much of the distortionary effects caused by re-domiciled firms and relocation of intellectual property rights. This is badly required as the Irish National Accounts are not fit for purpose** and give rise to critical commentary about 'leprechaun economics' and 'fake news' that is doing Ireland and its reputation no favours. We also need to look at other data to get a clearer picture on how the economy is performing.

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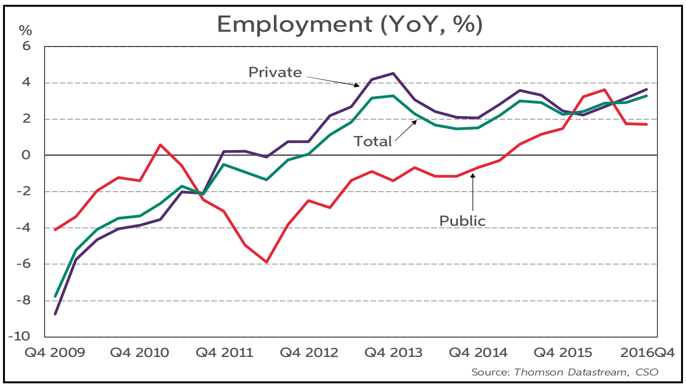
Economy performing well despite Brexit concerns

All the evidence is that the Irish economy finished 2016 on a very strong note and has sustained this momentum in early 2017, despite the concerns about Brexit and weakness of sterling. Data on the Irish labour market for the fourth quarter of 2016 were exceptionally strong and reminiscent of figures from the Celtic Tiger era. They rounded off a very strong year for the Irish jobs market. Employment rose 16,700 in Q4 over the previous quarter to give an increase of 65,000 over the year as a whole. **Employment grew by 2.9% in 2016 after increasing by 2.6% in 2015. These figures would suggest that the real growth rate of the Irish economy may have been in the range of 4.0-4.5% in the last couple of years.**

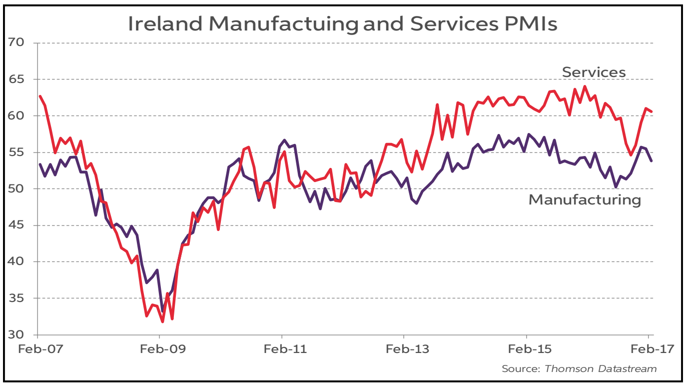
The strong job growth is making major inroads into the level of unemployment, which fell by 40,000 to 151,700 over the course of last year. The jobless rate had dropped to 6.9% by December, down from 8.9% at end 2015. This was the lowest rate since mid-2008. It had fallen even further to 6.6% by February this year, with the level of unemployment declining to 145,000. On the basis of these trends, the **unemployment rate will drop below 6% during the course of 2017.**



The robust labour market data point to a strongly performing economy and suggest that it has entered 2017 with a good deal of momentum. This is borne out by other recent data. **Consumer confidence figures were strong in January and February. Meanwhile, PMI survey data for the same months show high levels of activity** in the services and manufacturing sectors, as well as an ongoing recovery in construction.

Tax receipts were also solid in the first two months on the year, with a further improvement in the budget balance. **Car purchases also continue to rise.** While new car sales fell back in January and February, this has been more than offset by much higher imports of second-hand cars from the UK. Thus, CSO data show that the number of cars licensed for the first time rose by 4% in January/February from already high levels in the same two months last year. Meanwhile, retail sales, excluding the motor trade, rose by 1.5% in January following strong growth of 1.9% in the final quarter of last year.

There is little sign, then, that uncertainty around Brexit and the sharp fall in the value of sterling are having much of an impact on the Irish economy, which continues to power ahead. Nonetheless, **both the Dept. of Finance and the ESRI are projecting that GDP growth will slow to 3.5% this year as Brexit starts to impact the economy.** A recent Bloomberg poll of 22 economists also forecast growth at 3.5% this year, and 3% in 2018. These projections are in line with AIB's forecasts.



However, we have to say **there is little sign yet of growth slowing in the Irish economy** as it benefits from a pick-up in the global economy, low interest rates and a looser fiscal stance. Further out, **Brexit remains a serious event risk for the economy**. Much will depend on the nature of the exit deal reached between the UK and EU, probably towards end 2018. This will shape how the Irish economy performs in 2019 and beyond.

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