

# The Irish Economic Update:

*Growth remains solid, though some soft spots emerge in economy*

January 2020

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# Strong growth by Irish economy over 2013-2019

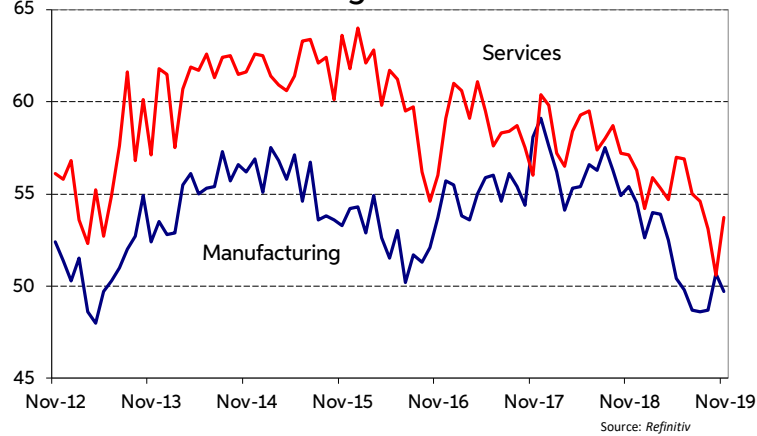


- Irish economy boomed from 1993 to 2007 with GDP up by over 250% – Celtic Tiger
- Very severe recession in Ireland in 2008-2009. GDP fell by 8.5% and GNP down 11%
- Collapse in construction activity and banking system, severe fiscal tightening, high unemployment. Ireland entered a 3 year EU/IMF assistance programme from 2010-2013
- GDP at end of 2008-09 recession was still over 25% higher than in 2001, highlighting that the economic crash came after a long period of very strong growth
- Ireland tackled its problems aggressively in the public finances, banking sector and property market. Imbalances in economy unwound – housing, debt levels, competitiveness, BoP
- Ireland focused on generating growth via its large export base and FDI as the route to recovery
- Domestic economy has recovered strongly, led by rebound in investment and retail spending
- Strong jobs growth. Unemployment rate fell from 16% in early 2012 to below 5% by Q3 2019
- Budget deficit eliminated at a quicker than expected pace. Public finances now in surplus
- Major deleveraging by private sector, including households, in past decade
- Balance of payments in surplus

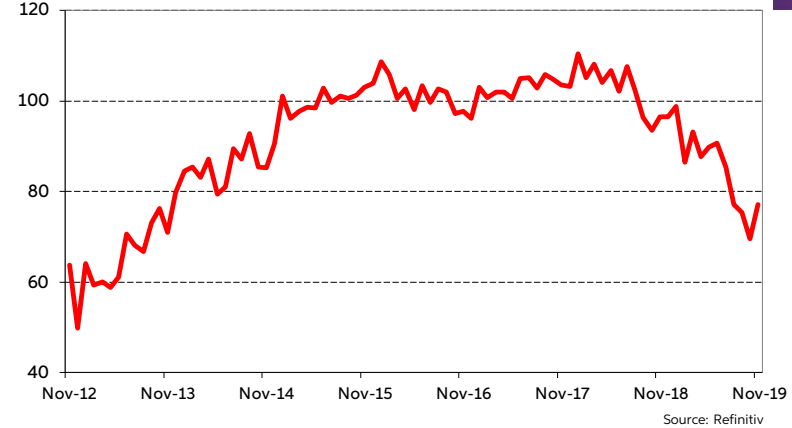
# Survey data weaken in 2019, but growth remains solid



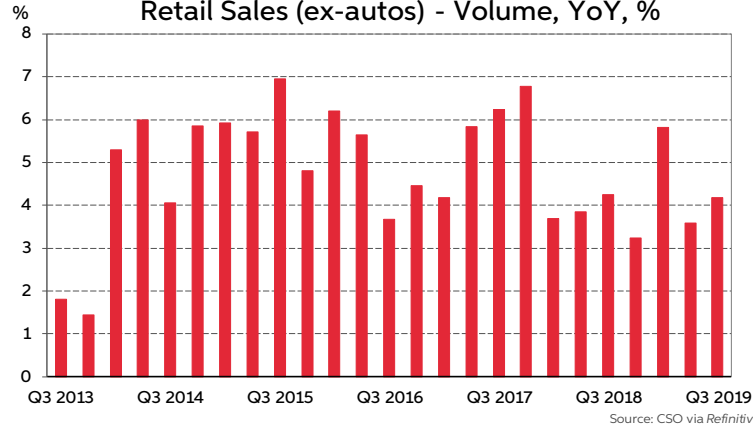
## AIB Irish Mfg and Services PMIs



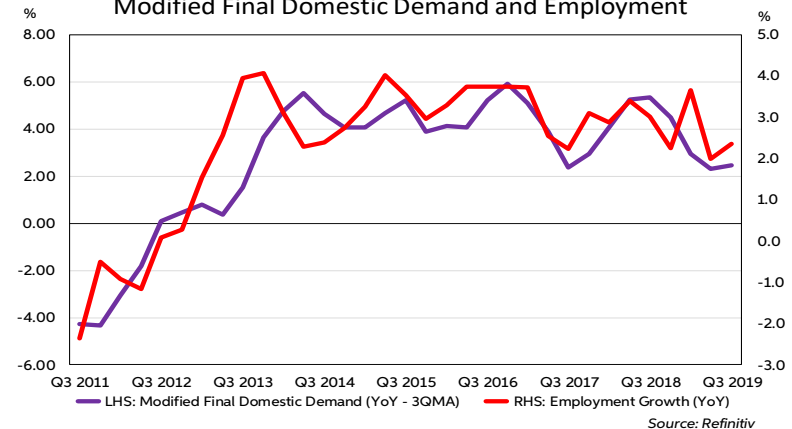
## Consumer Confidence (ESRI - KBC)



## Retail Sales (ex-autos) - Volume, YoY, %



## Modified Final Domestic Demand and Employment



# Real indicators hold up, despite weaker survey data



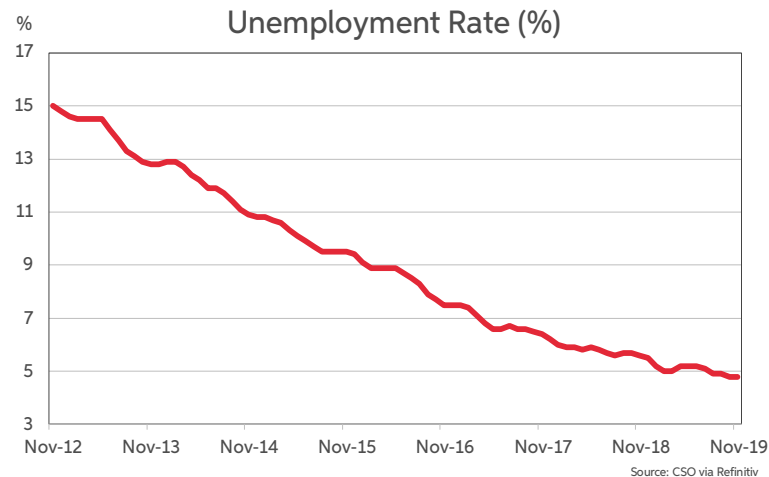
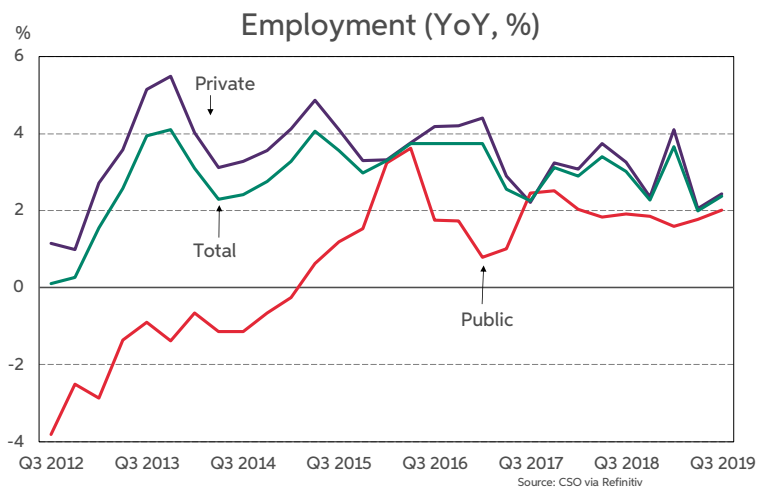
- Still strong jobs growth – employment rose by 2.4% yoy in Q3 2019, but slower than in previous years
- Downtrend in unemployment rate continues, as it drops below 5% in H2 2019
- Housing completions up strong 18% yoy to end Q3 2019, though slower growth than in 2018
- Rising housing commencements – up 25% yoy to Sept 2019, close to robust 2018 growth rate
- Mortgage lending growth slows to 11% yoy in Q1-Q3 2019 – flattening house prices a factor
- Construction PMI at 48.2 in November. Third sub-50 reading in a row. Housing PMI declines to 47.7
- Retail sales (ex-motor trade) up a robust 4.5% yoy in Jan-Sept 2019, after 3.7% growth in 2018
- Total car registrations (new + second hand imports) unchanged in 2019 – remained at very high level
- Manufacturing PMI weakened markedly during 2019. At 49.7 in November, above Q3 levels.
- Services PMI has slipped in 2019, but still pointing to good growth – at 53.7 in November
- Consumer confidence drops sharply to 6 year lows as Brexit fears weigh on sentiment
- Good growth of 6.7% yoy in tax receipts to Nov 2019. Budget surplus to exceed target in 2019

# Jobs growth still solid, unemployment rate drops below 5%



Year Average	2016	2017	2018	2019(f)	2020(f)	2021(f)
<b>Unemployment Rate %</b>	8.4	6.8	5.8	5.0	4.8	4.7
<b>Labour Force Growth %</b>	1.9	1.1	1.8	1.8	1.6	1.8
<b>Employment Growth %</b>	3.7	2.9	2.9	2.6	1.8	1.9
<b>Net Migration : Year to April ('000)</b>	16.2	19.8	34.0	34.0	35.0	35.0

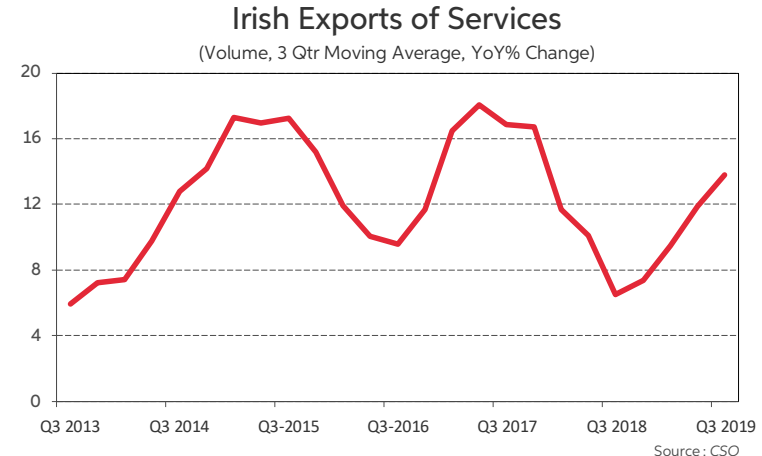
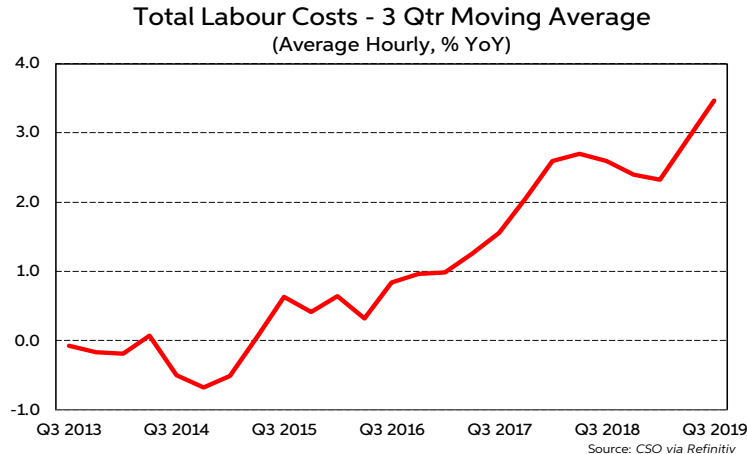
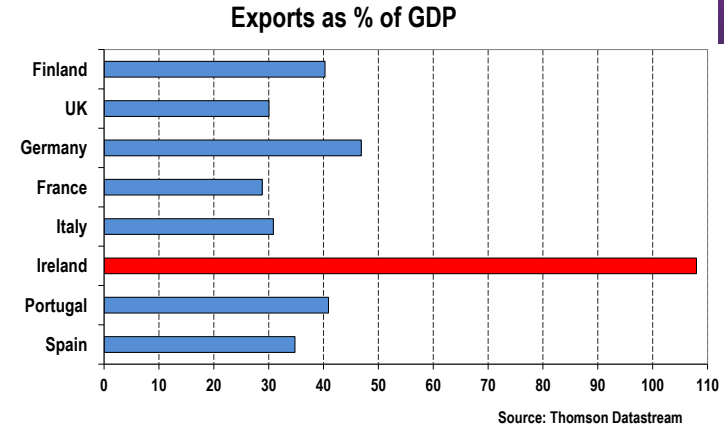
Source: CSO and AIB ERU forecasts



# Large Irish export base performing very well



- Ireland a very open economy – exports, driven by enormous FDI, equate to well over 100% of GDP
- Major gains in Irish competitiveness earlier in decade – though wage growth now picking up
- Exports rise strongly, helped by large FDI inflows
- Total exports up by 10.4% in 2018, with a further strong rise of 12.1% yoy in Q1-Q3 2019



# FDI and the Irish economy



## WHAT ATTRACTS FDI TO IRELAND?

- Access to European markets
- Low corporate tax rate of 12.5%
- English speaking country
- Well educated, flexible workforce
- Common law legal system
- Stable political framework
- Long history of successful FDI
- Access to decision makers

## KEY FDI IMPACTS ON THE IRISH ECONOMY

- Some 1,200 multinational companies
- €189bn in Exports
- 230,000 Jobs in FDI, 390,000 in total
- €7bn in Corporation Tax ( 67% of total )
- 33% of State's income tax/PRSI/USC
- €13.2bn Spending on Irish services/materials
- €11.7bn in Payroll
- 67% of Business R&D expenditure

## WORLD LEADERS CHOOSE IRELAND

- 17 of the top 20 in ICT
- 10 of the top 10 in Pharmaceuticals
- 14 of the top 15 in Medical Devices
- 8 of the top 10 Industrial Automation
- 10 of the 'top born on the Internet' firms
- 20 of the top 25 Financial Services firms
- UK becoming less attractive for FDI owing to Brexit

## US TAX CHANGES HAVE NOT HIT FDI

- US firms have well established operations here
- Need highly skilled, multi-lingual workforce
- Firms do not move to Ireland to avoid US tax
- Ireland is base to service their European markets
- Easier to operate in local rather than US time zone
- Still wide gap between US & Irish corporate tax rates
- Very strong year for FDI in 2018

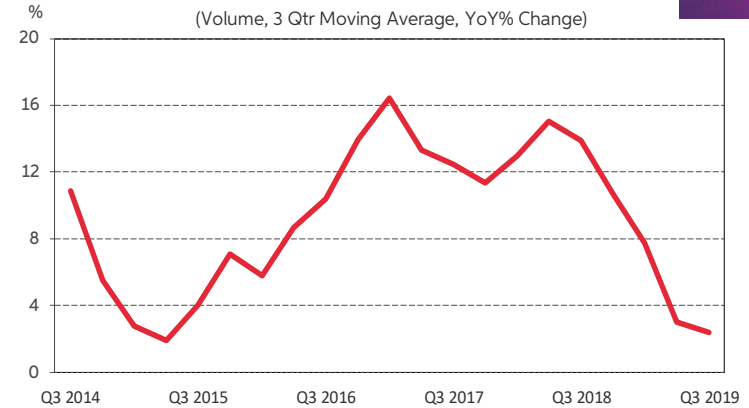
# Domestic economy has rebounded strongly



- Construction sees strong recovery since 2013. Output up nearly 12% on average in 2016-18 period
- Slowdown in non-residential construction activity this year – construction output up 4% yoy in Q1-Q3 2019
- Business investment (ex aircraft/intangibles) has picked up strongly since 2013
- However, Brexit uncertainty saw decline in business investment in 2019
- Consumer spending grew by 3.5% on average over 2014-2018 period. Up by 3.4% yoy in Q1-Q3 2019
- Core retail sales rose by a strong 3.9% in 2018, and were up 4.5% yoy in Jan-Sept 2019
- Total car regs (new + used imports) rose to high levels in 2017-18. Remained at this high level in 2019
- Modified final domestic demand grew at 4.4% rate in 2014-2018 period. Up 3.5% yoy in Q3 2019

## Construction Output

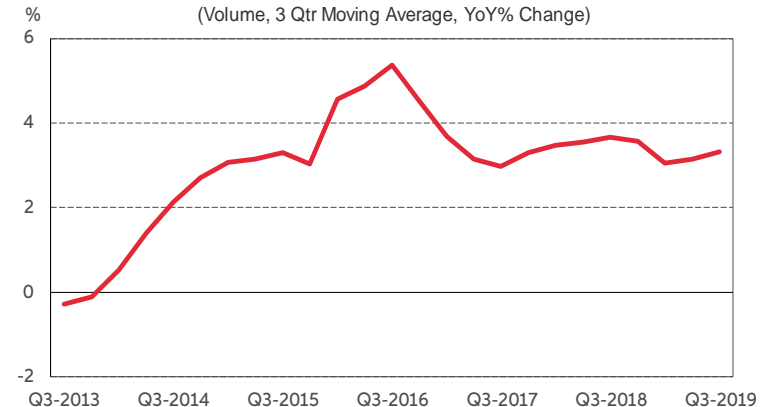
(Volume, 3 Qtr Moving Average, YoY% Change)



Source: CSO via Refinitiv

## Consumer Spending

(Volume, 3 Qtr Moving Average, YoY% Change)



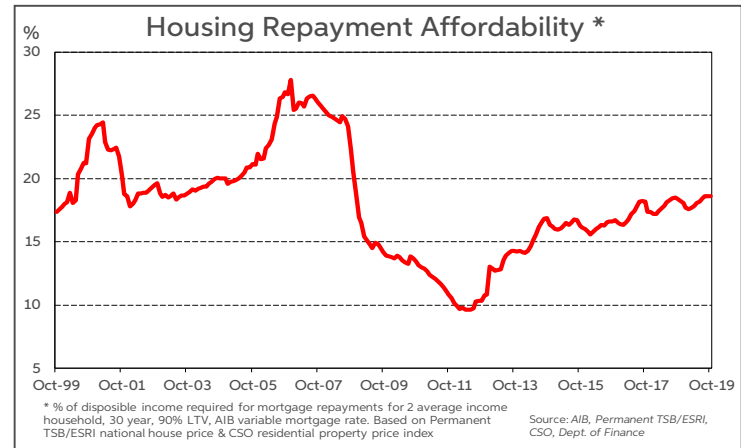
Source: CSO via Refinitiv



# House building on the rise, but still at quite a low level



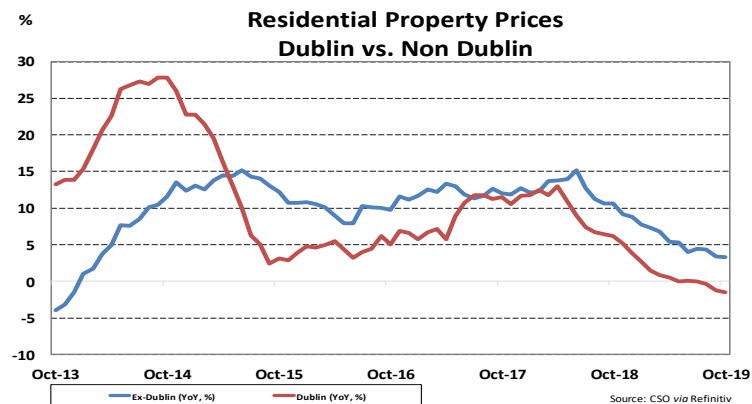
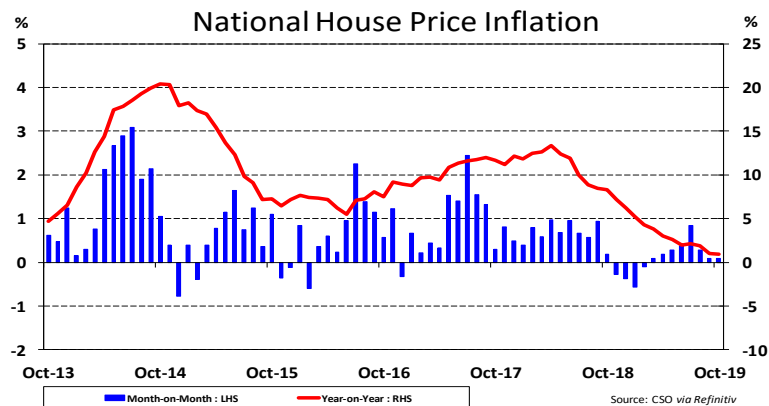
- Housing completions up 18% yoy in Q1-Q3 2019 after rising by 25% to over 18,000 in 2018
- Housing commencements rose 25% yoy to end Q3 2019 following a 28% increase in 2018
- Planning permissions up 23% yoy in Q1-Q3 2019, with 12 month running total now above 34,000
- Measures put in place to boost new house building. More NAMA activity, apartment planning rules relaxed
- Housing output still running well below annual new housing demand, estimated at 35,000 units
- Completions of 21.5k likely this year; forecast at circa 25k in 2020
- Mortgage lending +20% in 2018, but slowed to 11% in Q1-Q3 2019. Mortgage approvals pick up this year
- Rising house prices have impacted affordability, but it remains at a relatively accommodative level



# House price inflation slows sharply



- House prices declined by a very sharp 55% between their peak in late 2007 and early 2013
- House prices have since rebounded as big housing shortage emerged after 90% fall in home building
- Prices up 85% by Oct 2019 from low in March 2013 – Dublin prices up by 95%, non-Dublin rise 84%
- But house prices still some 17% below 2007 peak
- House price inflation slows sharply reflecting Central Bank rules, though signs recently may be stabilising
- Prices up 0.9% yoy nationally in October 2019, down from high of 13.3% in April 2018
- Dublin prices fall 1.5% yoy in Oct, down from +13% in Apr '18; non-Dublin slows to 3.3% from 15% last year
- Rents have also rebounded strongly – now 31.5% above previous peak reached in 2008, per CSO data



# AIB Model of Estimated Housing Demand



- Rising headship rates added circa 8,000 per year to housing demand in 2002-2011 period
- Shortage of housing, high rents, tighter lending rules saw average household size rise in 2011-16. Thus, headship fell – was a drag of circa 10,000 p.a. on housing demand
- Assume no change in headship in 2016-2020 – note long-term trend is upwards, adding to demand
- Pent-up demand has also built up in recent years from lack of supply
- Thus, forecast table may be under-estimating actual real level of housing demand
- Shortfall in supply met from run down of vacant stock and demand being reduced by fall in headship rate. Both factors very evident in 2011-16 and most likely in 2016-20

Calendar Year	2016	2017	2018	2019	2020
<b>Household Formation</b>	26,500	26,500	26,500	27,500	27,500
<i>of which</i>					
<b>Indigenous Population Growth</b>	18,000	18,500	17,500	16,500	14,500
<b>Migration Flows</b>	8,500	9,500	12,000	13,000	13,000
<b>Headship Change*</b>	0	0	0	0	0
<b>Second Homes</b>	500	500	500	500	500
<b>Replacement of Obsolete Units</b>	5,000	5,000	5,000	5,000	5,000
<b>Estimated Demand</b>	<b>32,000</b>	<b>33,500</b>	<b>35,000</b>	<b>35,000</b>	<b>33,000</b>
<b>Completions</b>	<b>9,900</b>	<b>14,400</b>	<b>18,100</b>	<b>21,500</b>	<b>25,000</b>
<b>Shortfall in Supply</b>	<b>-22,100</b>	<b>-19,100</b>	<b>-16,900</b>	<b>-13,500</b>	<b>-8,000</b>

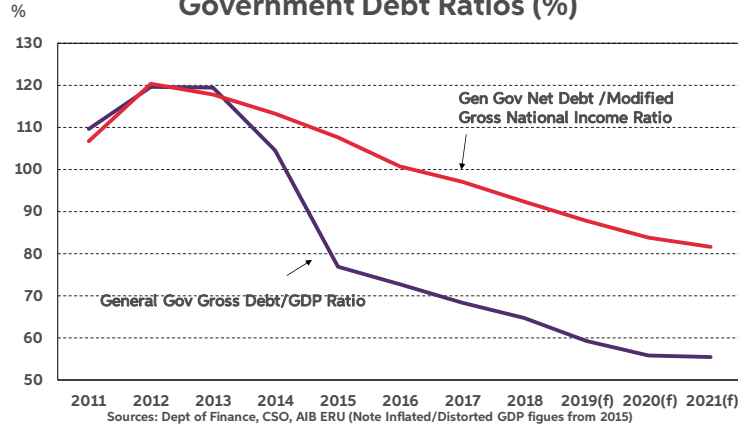
\*Headship is % of population that are heads of households.

Sources: CSO, DoECLG, AIB ERU

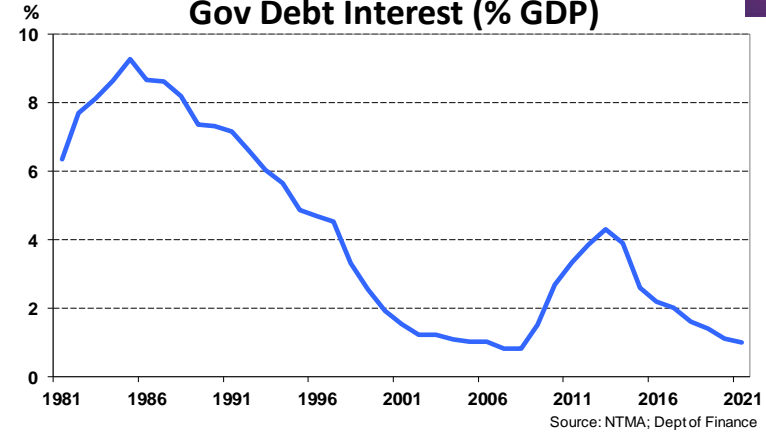
# Govt debt ratios fall, private sector deleverages



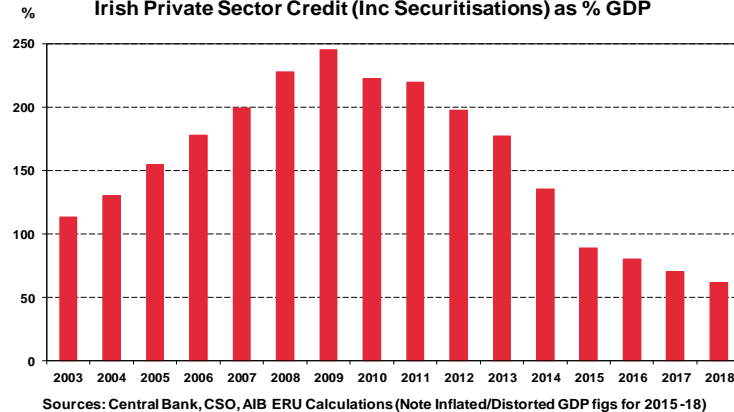
## Government Debt Ratios (%)



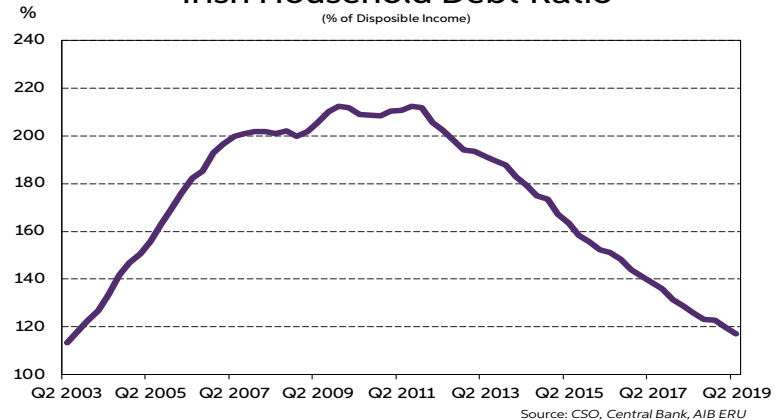
## Gov Debt Interest (% GDP)



## Irish Private Sector Credit (Inc Securitisations) as % GDP



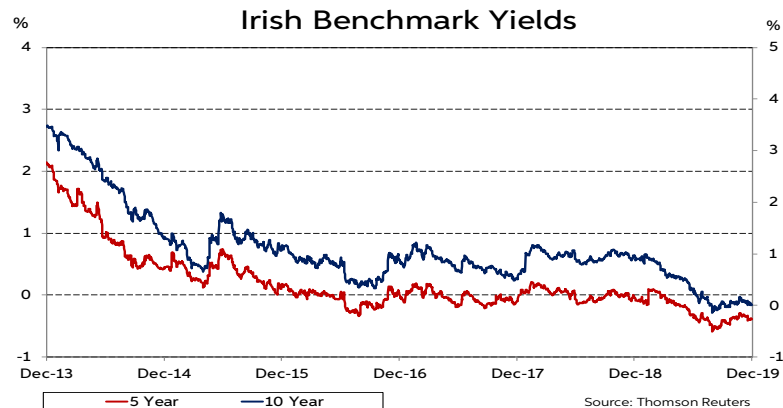
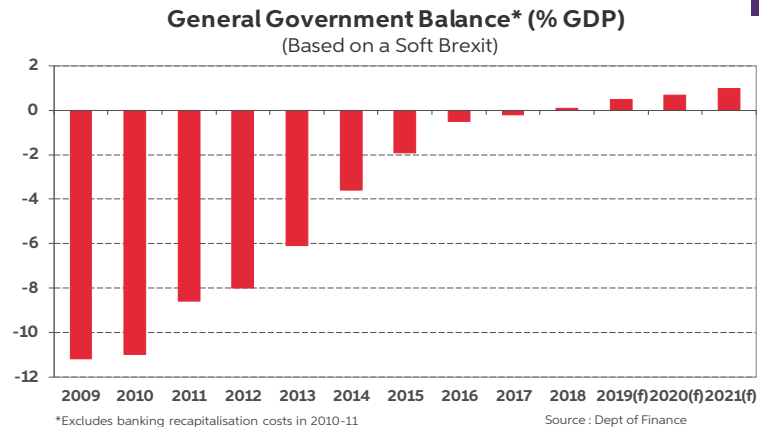
## Irish Household Debt Ratio



# Government finances return to surplus in 2018/19



- Budget deficit has fallen sharply in past decade. Declined to 0.2% of GDP in 2017
- A small surplus of €170m was recorded in 2018
- Public finances ahead of target this year – strong tax receipts, up 6.7% yoy to end Nov
- Budget surplus to exceed target in 2019. Could rise to near 0.5% of GDP
- Primary budget surplus (i.e. excluding debt interest) of near 2% of GDP in 2019
- Debt interest costs very low – at 1.4% of GDP
- Budget surplus to rise further in 2020 – Finance Minister wants to get surplus up to 1% of GDP
- Gross Gov Debt/GDP ratio has fallen sharply
- Irish bonds yields negative out to 10 years
- Sovereign debt ratings upgraded in recent years; S&P at AA-, Fitch at A+, Moody's A2 for Ireland



# Brexit: Difficult trade talks lie ahead in 2020

- EU and UK agree on revised Brexit deal at mid-October Heads of State Summit
- NI to remain within Single Market for goods and have dual EU-UK customs system
- Revised deal did not get through the UK Parliament in October
- Further extension to Article 50 to 31 January 2020 granted by EU to avoid hard Brexit
- UK held election on 12<sup>th</sup> December. Conservative party won, gaining big majority
- Withdrawal Agreement now set to be ratified by UK and EU Parliaments
- UK will leave the EU on Jan 31<sup>st</sup> 2020 in orderly exit. Transition period to last to end 2020
- UK government rules out extending transition period beyond this date
- EU-UK trade talks next year will determine final shape of Brexit. Likely to prove difficult
- Risk of minimal trade deal if Conservative Gov. puts focus on 'taking back control' in talks
- Indeed, UK could opt for no deal - fall back on WTO rules from 2021- i.e. a hard Brexit

# Brexit expected to lower growth rate of Irish economy

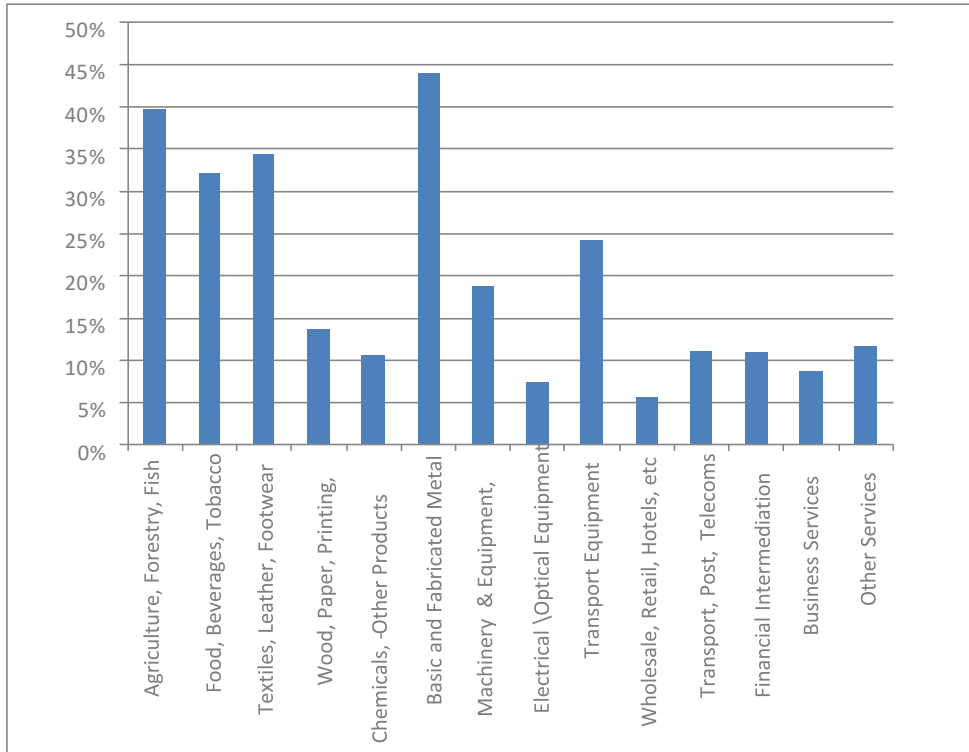


- **ESRI** estimate that Irish output would be reduced over time by **2.6% under a benign 'deal' scenario** in the long run (i.e. after 10 years). Unemployment rate is 1% higher
  - **Multiple hits to the Irish economy from a no-deal Brexit:** further collapse in sterling, recession in UK, disruption to trade/supply lines, tariffs, new adm. and regulatory costs
  - Sharp fall-off in trade with UK likely on a no-deal Brexit, with this **shock front loaded** - around half of the impact on trade would take place in the first two years, per ESRI
  - In a **'disorderly no deal'** scenario, ESRI estimates that GDP would be **5% lower** after 10 years. Unemployment rate would be 2 percentage points higher
  - **Central Bank** say a disorderly hard Brexit could reduce Irish growth by 4% in first year and 6% in long run
- **Copenhagen Economics** Report considered costs of regulatory divergence for goods and services and of border checks, as well as tariffs in assessing impact of Brexit
  - Estimates impact by 2030 is to **reduce Irish GDP by 2.8%** under a soft Brexit (EEA), **4.3% in a FTA** and 7% in a no-deal, hard Brexit WTO scenario

# Agri. sector would be severely impacted by hard Brexit

- Main EU tariffs relate to food products, keeping prices high. UK may also impose tariffs on all food imports post Brexit
- Food and Beverages account for 25% of total Irish exports to UK
- Around 40% of Irish food exports go to the UK – key market for beef and cheese
- Other sectors very dependent on UK market include machinery and transport, metal products, textiles
- Some 40% of indigenous Irish exports go to UK compared to 10% for foreign owned companies

Share of Exports by Industry Destined for the UK (ESRI)





# AIB Brexit Sentiment Index – Q3 2019



- A total of **700 SME's (with up to 250 employees)** across the island of Ireland



Source: Ipsos MRBI

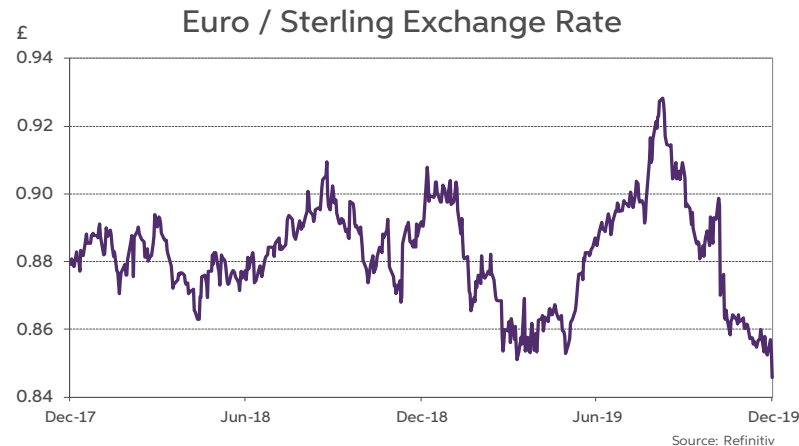
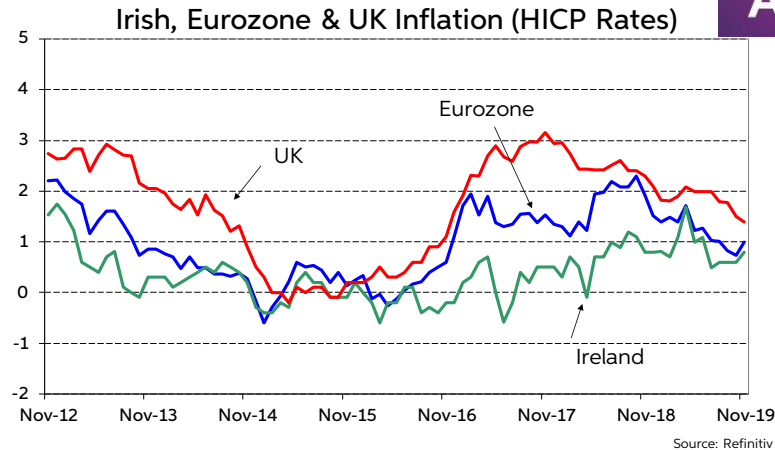
\*The Index reflects and measures the sentiment of Irish SMEs in the Republic of Ireland and Northern Ireland towards Brexit, summarised as a single number, with a potential range from +100 to -100. It takes the difference between the positive and negative responses across four key measures: Impact on business now, Impact on future business (next 5 years), Level of visibility and, finally, the Wider economic impact of Brexit.

- Headline index **weak again** in Q3. One of the most notable features of the survey this year is the number of firms that say Brexit is having a negative impact on their business now
- Manufacturing, Food & Drink, Transport, Tourism and Retail sectors **most concerned** about Brexit
- 50% of ROI and 66% of NI firms who had investment plans say they have been **cancelled or postponed** owing to Brexit.
- Big jump in expectations of a **hard Brexit** to 59% in ROI and 32% in NI

# Good Irish growth can continue if external risks avoided



- Irish economy should continue to grow at impressive pace, but not as strongly as in recent years
- House building picking up from still low output levels
- Public spending on the rise
- Activity supported by low interest rate environment
- Strong growth in household incomes
- Continuing good inflows of FDI
- Irish inflation still very low
- However, Brexit is a real challenge for the economy
- Important also that global economy avoids downturn
- GDP growth forecast at 3.25% in 2020 & 3% in 2021, assuming hard Brexit/global downturn avoided
- ESRI has estimated medium-term growth rate of economy at around 3.25% in the period 2020-2025



# AIB Irish Economic Forecasts



<i>% change in real terms unless stated</i>	2017	2018	2019 (f)	2020 (f)	2021 (f)
<b>GDP</b>	<b>8.1</b>	<b>8.2</b>	<b>5.5</b>	<b>3.25</b>	<b>3.0</b>
<b>GNP</b>	5.1	6.5	3.0	3.0	2.75
<b>Personal Consumption</b>	3.0	3.4	3.5	2.5	2.2
<b>Government Spending</b>	3.9	4.4	4.0	3.0	3.0
<b>Fixed Investment</b>	-6.6	-21.1	48.0	6.0	5.0
<b>Core Fixed Investment*</b>	4.0	13.0	2.0	5.0	5.0
<b>Exports</b>	9.2	10.4	11.0	7.0	5.0
<b>Imports</b>	1.1	-2.9	24.0	8.0	5.5
<b>HICP Inflation (%)</b>	0.3	0.7	0.9	1.1	1.3
<b>Unemployment Rate (%)</b>	6.8	5.8	5.0	4.8	4.7
<b>Budget Balance (% GDP)</b>	-0.2	0.1	0.4	0.7	1.0
<b>Gross General Gov Debt (% GDP)</b>	68.0	63.5	59.3	55.5	55.0

\*Excludes investment in aircraft and intangibles

Source: CSO, D/Finance; AIB ERU Forecasts

# Risks to the Irish economy



- Main near-term risks to the Irish economy are external
- Brexit still major concern for Ireland given its strong trading links with UK and impact on sterling
- Weaker external environment, with growing downside risks to global growth from increasing protectionism/tariffs, declining world trade/manufacturing activity, weak European economy
- Questions around Ireland's corporation tax regime (Apple ruling, moves on tax harmonisation in EU, cuts in US/UK rates, OECD tax reform proposals) could impact FDI
- Supply constraints in new house building activity, which is recovering at a slow pace with output still at low levels
- Competitiveness issues - high Dublin house prices, high rents, high personal taxes, rising wages
- Credit constraints – tightening of lending rules, on-going deleveraging, weak credit demand

Note: All Irish data in tables are sourced from the CSO unless otherwise stated. Non-Irish data are from the IMF, OECD and Thomson Financial. Irish forecasts are from AIB Economic Research Unit. This presentation is for information purposes and is not an invitation to deal. The information is believed to be reliable but is not guaranteed. Any expressions of opinions are subject to change without notice. This presentation is not to be reproduced in whole or in part without prior permission. In the Republic of Ireland it is distributed by Allied Irish Banks, p.l.c. In the UK it is distributed by Allied Irish Banks, plc and Allied Irish Banks (GB). In Northern Ireland it is distributed by First Trust Bank. In the United States of America it is distributed by Allied Irish Banks, plc. Allied Irish Banks, p.l.c. is regulated by the Central Bank of Ireland. Allied Irish Bank (GB) and First Trust Bank are trade marks used under licence by AIB Group (UK) p.l.c. (a wholly owned subsidiary of Allied Irish Banks, p.l.c.), incorporated in Northern Ireland. Registered Office: 92 Ann Street, Belfast BT1 3HH. Registered Number NI 018800. Authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority. In the United States of America, Allied Irish Banks, p.l.c., New York Branch, is a branch licensed by the New York State Department of Financial Services. Deposits and other investment products are not FDIC insured, they are not guaranteed by any bank and they may lose value. Please note that telephone calls may be recorded in line with market practice.