The Irish Economic Update:

Tough start to 2021, but prospects brighten as vaccine rollout sees economy reopening

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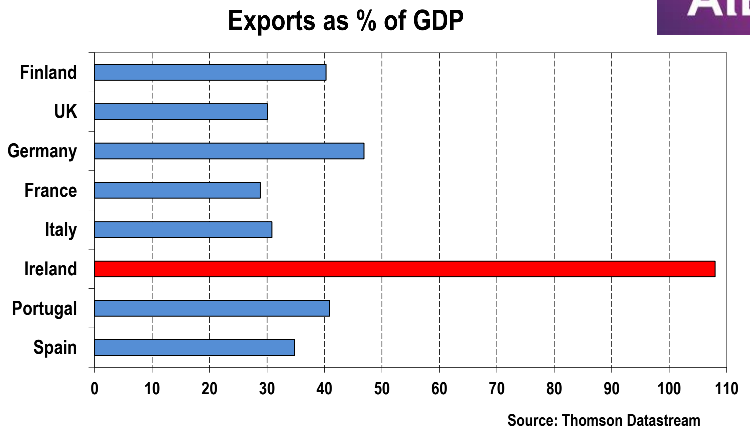
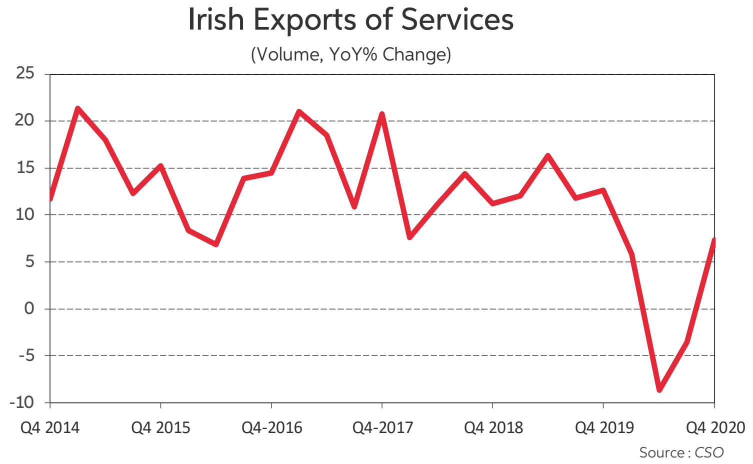
Economy starts reopening from long third lockdown

- Irish GDP grew by 3.4% in 2020, with GNP up 0.6%, as exports increased by 6.2%
- Domestic economy contracted by 5.4%, with consumer spending down 9% and fixed investment falling by 8.5%, partially offset by 9.8% rise in government expenditure
- Long third lockdown imposed since Xmas, with restrictions only being lifted during Q2
- Sharp fall in construction & services PMIs in early 2021, decline in consumer spending
- Economic contraction not as severe as last spring – more activity and spending this time
- More modest decline in retail sales in Q1, down 4% yoy, versus 12% yoy fall in Q2 2020
- Mfg PMI rises during Q1, hits 57.1 in March. Services PMI jumps from 41.2 to 54.6 in March
- Vaccination programme ramping up considerably in Q2, restrictions start to be eased
- Growth prospects improve for H2 2021 and 2022, following economy reopening during Q2
- DoF sees GDP growth of 4.5% in 2021, 5.0% in 2022. ESRI at 4.4% and 5.2%
- CBI has higher GDP f'cast in 2021 of 5.9%, but IMF and EC at 4.2% and 3.4%, respectively

Goods exports up strongly last year, services exports flat

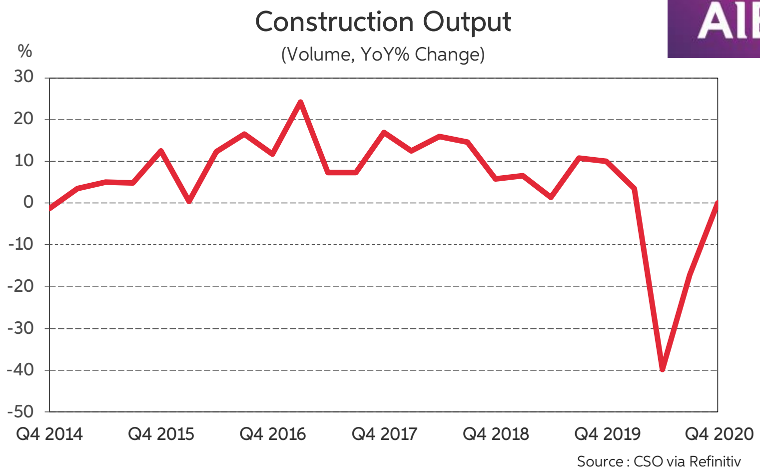
- Ireland a very open economy – exports, driven by large scale FDI, are a huge part of economy
- Exports rise strongly in recent years, helped by large FDI inflows
- Total exports rose 10.4% in 2018, 11.1% in 2019
- Pharma, medical care products, IT equipment, and food & drink are main goods exports
- IT, business, financial and tourism are the main service exports
- Total exports rise 6.2% in 2020
- Goods exports up 11.8% last year, fuelled by very big jump in pharma exports
- Service exports flat in 2020 – fell sharply in H1 but strong rebound in second half of year
- Collapse in earnings from tourism & travel, but computer service exports showed strong growth

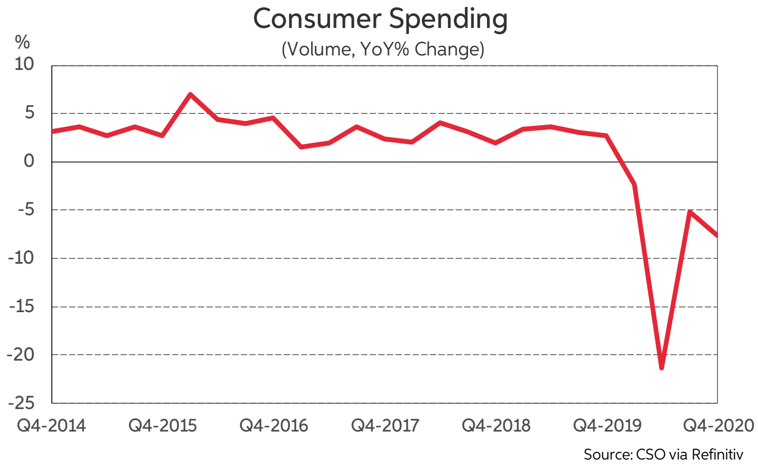




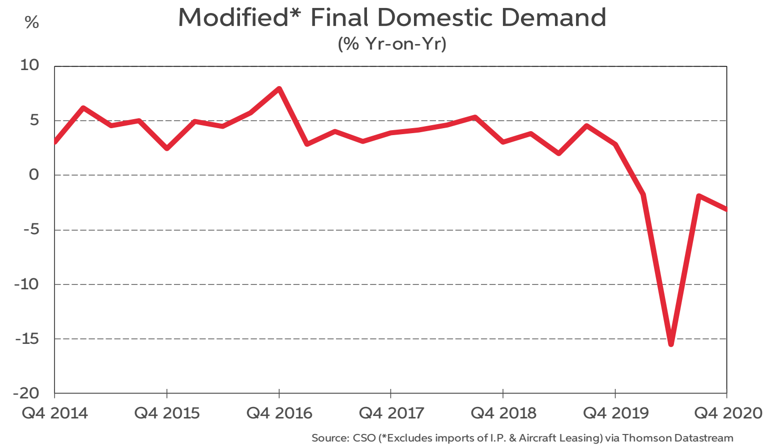
Strong economic rebound followed big Covid hit in H1'20

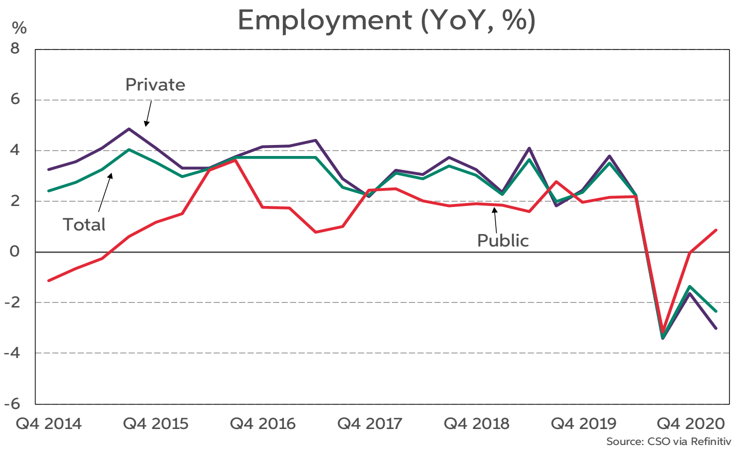
- Modified final domestic demand up by 18.8% in Q3, with small fall of 2.2% in Q4, after big H1'20 decline
- Overall, modified domestic demand contracted by 5.4% in 2020. It was running at -3% yoy by Q4
- Consumer spending fell by 2.9% in Q1, 19.6% in Q2. Rebounded by 21% in Q3. Fell by 2.2% in Q4,
- Domestic fixed investment fell by 25% in Q2. Up by 35% in Q3. Fell by 4% in Q4 and down 3.4% yoy
- Construction investment fell by 9% in 2020, though new housing output was down by just 2.3%
- GDP rose by 3.4% in 2020, boosted by strong performance of net trade, with exports up 6.2%
- GNP up 0.6% in 2020 – takes account of big rise in profits outflows from multi-nationals last year

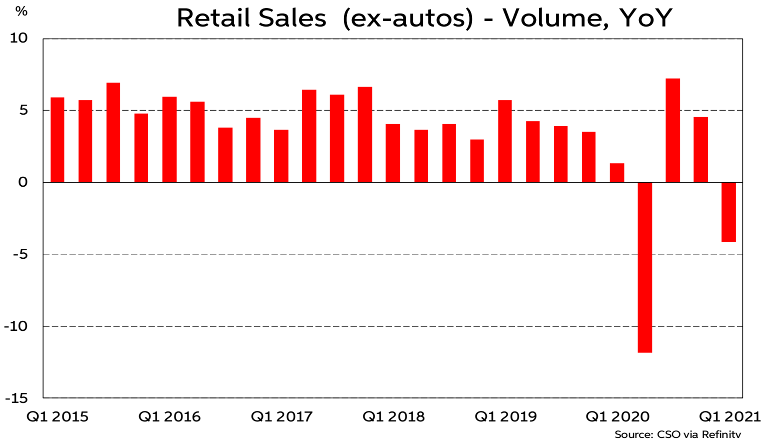


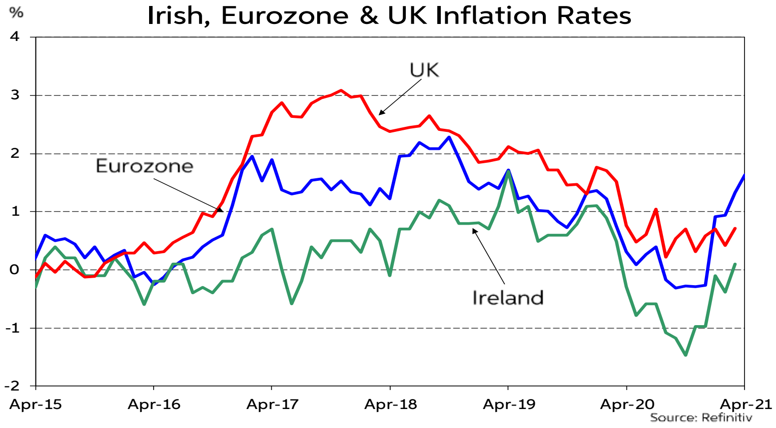


But domestic recovery interrupted by new lockdowns

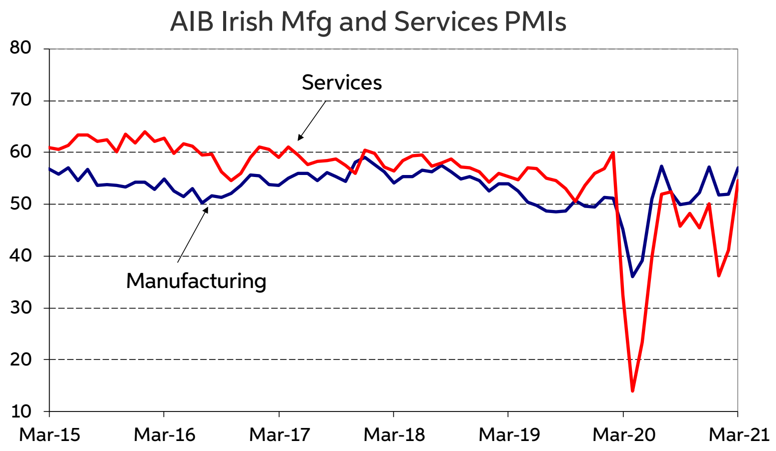




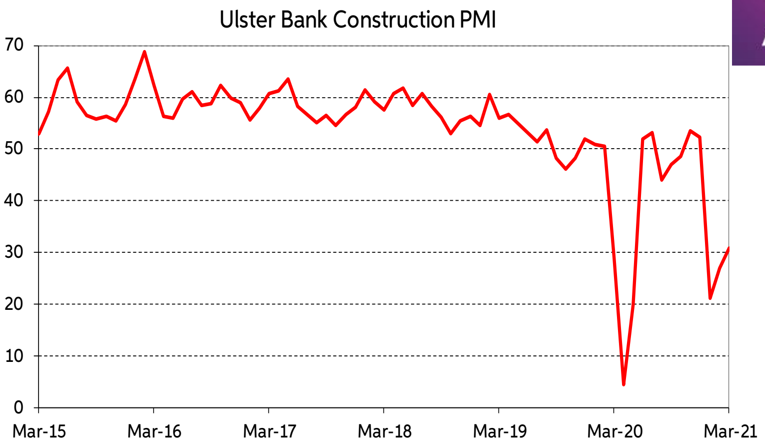




Weak start to 2021, but lead indices now starting to pick up



Source: *Refinitiv*



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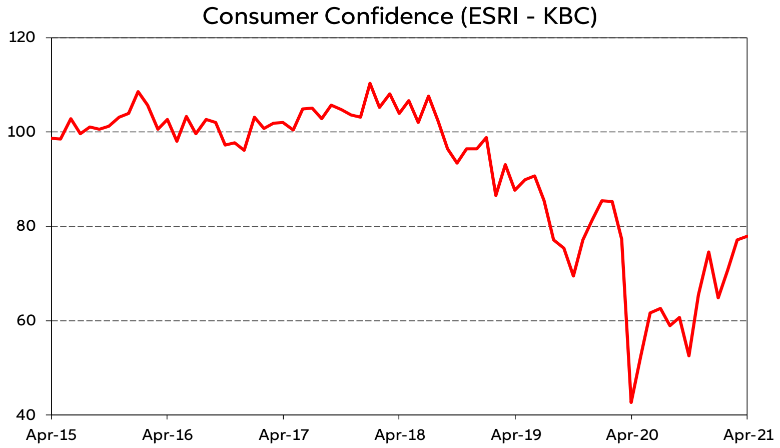
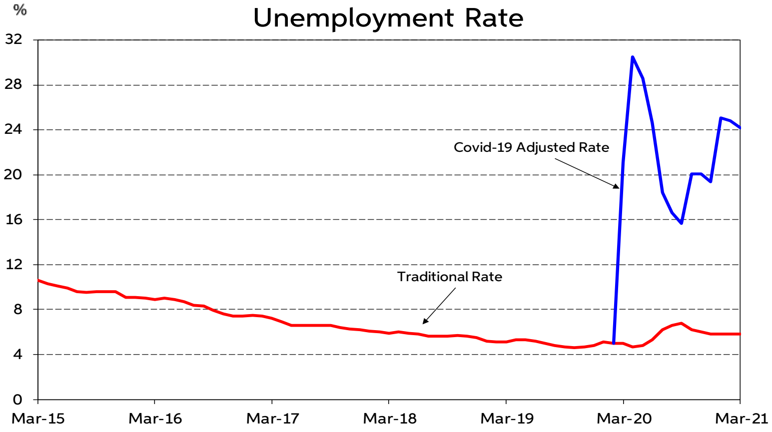


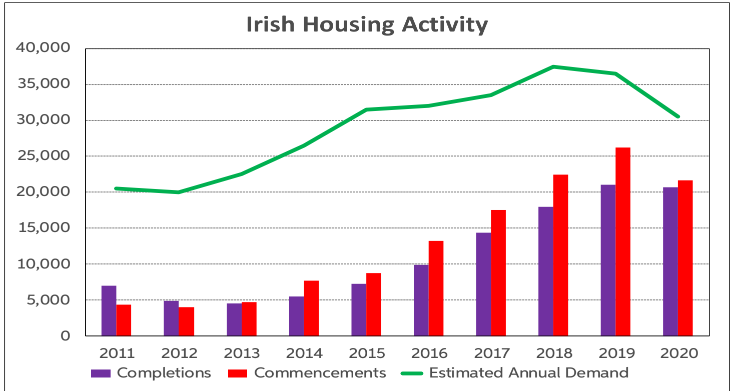
Source: ESRI via Refinitiv



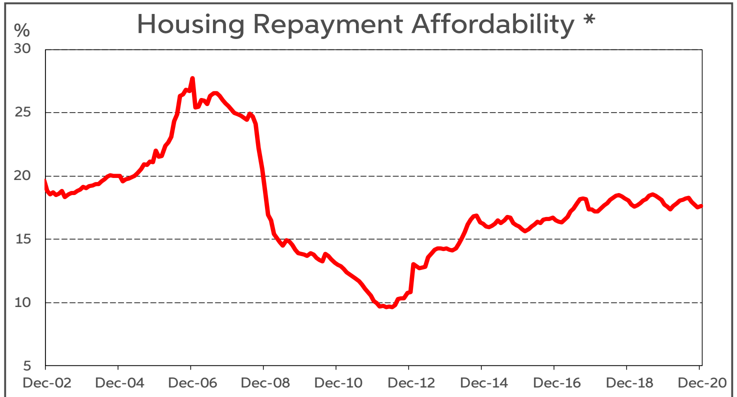
Source: CSO via Refinitiv

House building likely to fall back given big decline in starts

- Total completions amounted to 20,676 in 2020, just 2% down on 2019 level despite a 6-week lockdown
- Commencements fell by over 17% to 21,700 in 2020 from 26,240 in 2019. Further big fall at start of 2021
- Planning permissions jumped sharply last year – up 13.5% as apartments surged for second year
- Housing output likely to be less than 20,000 this year, given long lockdown & fall in commencements\starts
- Thus shortfall in supply could worsen, with annual housing demand estimated at circa 30k
- Mortgage lending rose by 9.5% to €9.5bn in 2019, but Covid saw it fall by 12% to €8.4bn in 2020
- However, mortgage approvals surged in H2 2020 and rose by 7.3% yoy in Q1 2021
- Market forecasts are for €9.5-10.0bn market in 2021
- Housing affordability metrics remain quite stable



Source: CSO, Dept. of Housing, AIB ERU Calculations

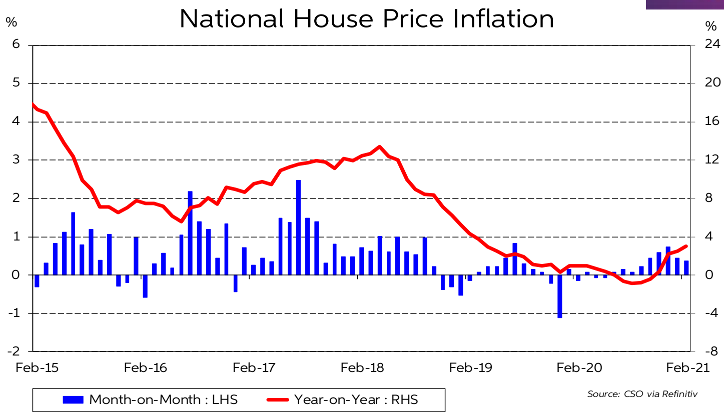


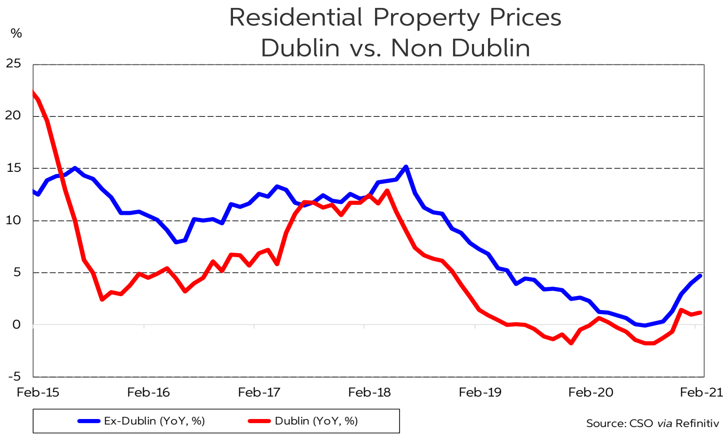
* % of disposible income required for mortgage repayments for 2 average income household, 30 year, 90% LTV, AIB variable mortgage rate. Based on Permanent TSB/ESRI national house price & CSO residential property price index

Source: *AIB, Permanent TSB/ESRI, CSO, Dept. of Finance*

House price inflation up to 3% in early 2021 and rising

- House prices declined by very sharp 55% over 2007-13
- Prices have recovered strongly; 88.5% above trough by Feb’21, but still some 15.5% below 2007 peak
- CSO data show house prices little changed over 2019-20, until moving much higher in Q4 last year
- Further rise in house prices in early 2021, with Feb yoy at 3%. Prices rise at 5.5% annualised rate since autumn
- Non-Dublin prices up 4.7% yoy in February, well above Dublin rate of 1.2% yoy
- Property websites show big jump in asking prices since mid-2020. Running at 7.5% yoy in Q1 2021
- Low supply, remote working, strong public/institutional demand, enhanced help-to-buy scheme, rising personal savings are all supporting house prices
- Marked fall in rents in H1 2O2O during first lockdown
- Rents recovering well in recent months, but still down 1.4% yoy at March 2021





Source: CSO *via* Refinitiv

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 2016-2021 – 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 2016-21

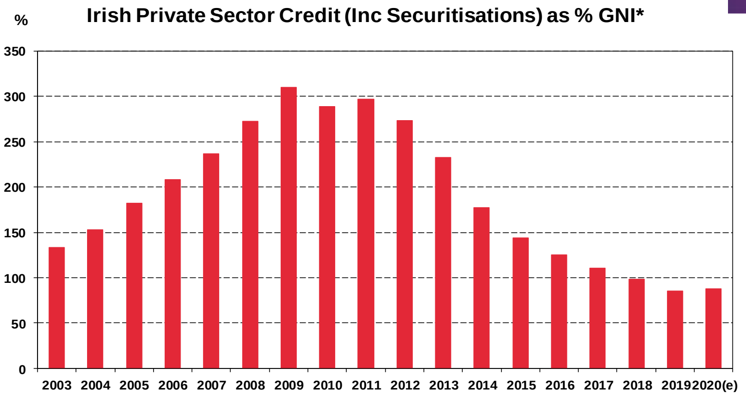
Calendar Year	2017	2018	2019	2020	2021
Household Formation	28,000	32,000	31,000	25,000	25,000
of which					
Indigenous Population Growth	*18,500*	*21,000*	*21,000*	*17,500*	*16,000*
Migration Flows	*9,500*	*11,000*	*10,000*	*7,500*	*9,000*
Headship Change*	*0*	*0*	*0*	*0*	*0*
Second Homes	500	500	500	500	500
Replacement of Obsolete Units	5,000	5,000	5,000	5,000	5,000
Estimated Demand	**33,500**	**37,500**	**36,500**	**30,500**	**30,500**
Completions	**14,400**	**18,100**	**21,100**	**20,700**	**17,500**
Shortfall in Supply	***-19,100***	***-19,400***	***-15,400***	***-9,800***	***-13,000***

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

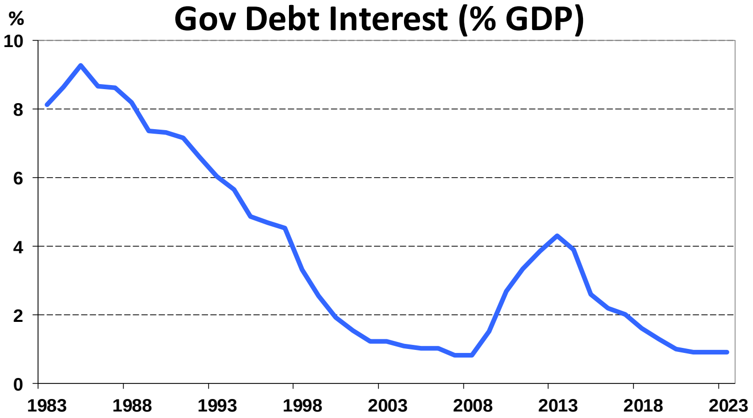
Sources: CSO, DoECLG, AIB ERU.

Private sector deleverages, Gov. debt ratios move higher

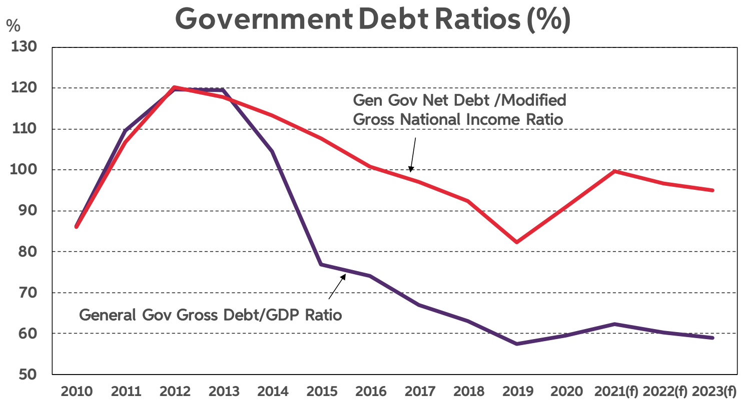
Source: CSO, Central Bank, AIB ERU



Sources: Central Bank, CSO, AIB ERU Calculations



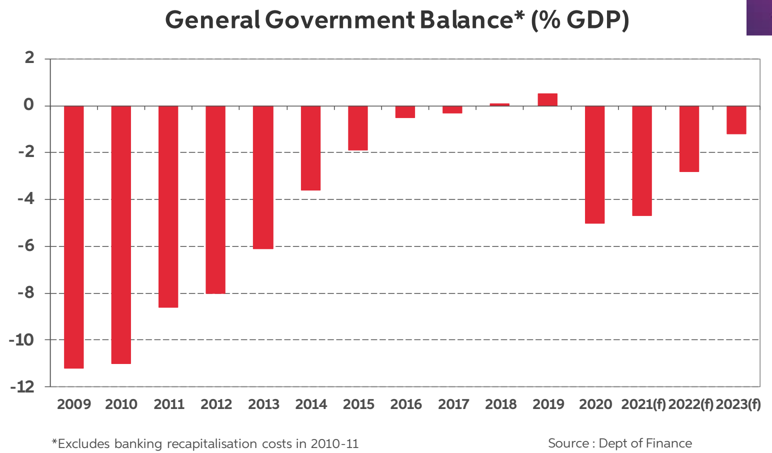
Source: NTMA; Dept of Finance

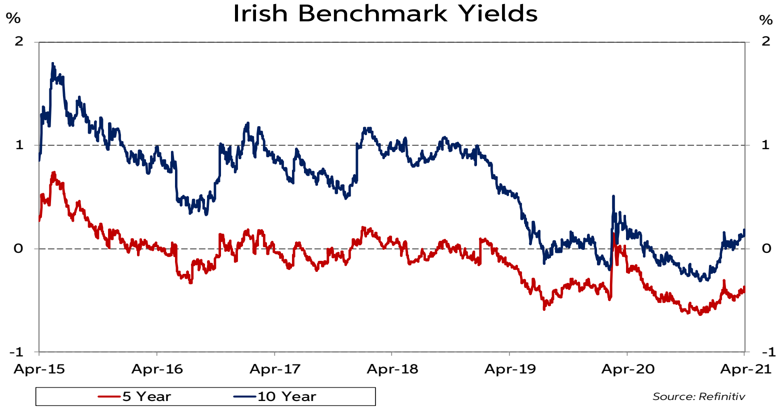


Sources: Dept of Finance, CSO, AIB ERU (Inflated/Distorted GDP figues from 2015)

Big 2020-21 budget deficits to decline sharply over 2022-23

- Budget deficit fell sharply in last decade, with small surpluses recorded in 2018 and 2019
- However, Covid-19 and efforts to mitigate it saw the public finances deteriorate during 2020
- Tax receipts were down 3.5% last year, while net voted government spending soared by 25%
- General Government budget deficit of €18.5bn in 2020, or 5% of GDP
- Dept. of Finance forecasting another large deficit of €18bn in 2021, 4.7% of GDP
- Deficit then forecast to fall sharply to 2.8% in 2022 and 1.2% in 2023 as economy recovers
- Gov. Debt ratios had fallen in past decade, but move higher in 2020 and 2021
- Bond yields low and stable despite big jump in budget deficit and large rise in debt issuance
- Ireland's sovereign debt ratings hold steady; S&P at AA-, Fitch at A+, Moody's A2





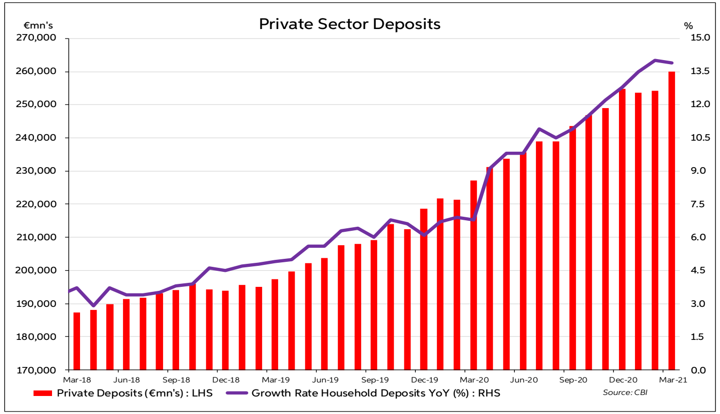
Economy was in very strong shape ahead of Covid shock

- Economy was in very strong shape ahead of being hit by very deep 2020 Covid recession
- Well balanced, robust underlying growth of circa 5% per annum over 2013-19 period
- Large inflows of FDI and strong export growth remain key features of the economy
- Strong jobs growth, averaging over 3% per annum during the period 2013-19
- Unemployment rate fell from 16% in early 2012 to below 5% in H2 2019
- Budget deficit eliminated quicker than expected. Public finances in surplus in 2018/19
- Major deleveraging by private sector, including households, during the past decade
- Sound financial system, with well capitalised banks
- Stable housing market - house price inflation at 1%, moderate growth in mortgage market
- Very low, stable CPI inflation of below 1% over 2013-19 period
- Balance of payments returned to large surplus

Factors in place for a strong rebound by Irish economy

- Key ingredients for a strong rebound by Irish economy from mid-2021 onwards moving into place
- Rollout of vaccines gathering momentum, which should allow big reopening of economy by summer
- World economy rebounding strongly, which augurs well for export orientated countries like Ireland
- House building to pick up from still low output levels – big focus of government policy
- Government policy can remain supportive of growth - DoF forecasts provide for increased core spending
- Activity to be aided by continuing very low interest rate environment
- Economy has deleveraged; low private sector debt
- Large build-up in private savings in 2020-H1'21 will unwind, fuelling strong growth in domestic spending
- GDP to rise by cumulative 13% over 2021-23 period

IMF GDP Forecasts (April 2021)			
% Vol	2020	2021	2022
World	-3.3	6.0	4.4
OECD	-4.7	5.1	3.6
US	-3.5	6.4	3.5
Eurozone	-6.6	4.4	3.8
UK	-9.9	5.3	5.1
Japan	-4.8	3.3	2.5



AIB Irish Economic Forecasts

% change in real terms unless stated	2019	2020	2021 (f)	2022 (f)	2023 (f)
GDP	**5.6**	**3.4**	**3.0**	**5.5**	**4.0**
GNP	3.4	0.6	2.5	5.0	3.5
Modified Final Domestic Demand	**3.3**	**-5.4**	**2.8**	**5.5**	**3.5**
Personal Consumption	3.2	-9.0	3.0	7.5	4.0
Government Spending	6.3	9.8	1.5	-3.0	1.0
Fixed Investment*	74.8	-32.3	-6.5	8.0	4.5
Exports	10.5	6.2	4.5	5.0	4.5
Imports*	32.4	-11.3	1.5	5.2	4.3
HICP Inflation (%)	0.9	-0.5	0.5	1.0	1.2
Unemployment Rate (Estimated %)	**5.0**	**10.4**	**11.0**	**8.2**	**6.9**
Budget Balance (% GDP)	0.5	-5.0	-4.7	-2.8	-1.2
Gross General Gov Debt (% GDP)	57.4	59.5	62.5	60.5	59.0

*Data very distorted by aircraft and intangibles (IP)

Source: CSO, D/Finance; AIB ERU Forecasts

Brexit: The EU-UK Trade & Cooperation Agreement

The Trade Deal:

- EU and UK finally agreed on a trade deal before end 2020, thereby allow for continuing tariff-free and quota-free trade in goods
- However, the FTA is much inferior to the EU Single Market, involves a lot of extra admin costs and delays at ports – it marks an end to frictionless UK-EU trade
- The FTA is unique in that it increases trade barriers– new customs procedures, compliance with onerous rules of origin requirements, documentary evidence needed to move goods
- Agri-food products may require export health certs and veterinary inspections at borders
- FTA does not extend to services. Financial services not given equivalence/passporting rights

The Fall-Out:

- Irish PMI surveys show firms reporting considerable import delays at ports, with longer supply chains and higher admin costs as a result of Brexit
- Estimated that higher trade costs will knock circa 0.5% off UK/RoI annual GDP growth rates
- UK not fully implementing all customs checks until 2022 when Irish exporters to GB will see impact
- Issues with NI protocol and GB-NI trade flows – Customs declarations, regulatory checks, political impact

Ireland's 12.5% Corporate Tax regime under threat

Importance of FDI:

- Some 1,600 multinational companies are based in Ireland, accounting for over 250,000 in direct employment or about 18% of total jobs in terms of direct and indirect employment.
- Corporation tax accounts for €12bn or circa 20% of total tax revenue... 80% of this comes from MNCs

Threats to Ireland's Corporate Tax Regime:

- Ireland's relatively low & stable 12.5% corporate tax rate has been seen as key cornerstone in attracting FDI
- President **Biden is proposing to increase global minimum tax rate for US companies from 10.5% to 21%.** This would mean US firms based here would have to pay top up rate in the US of 8.5%
- **OECD seeking to introduce a minimum global corporate tax rate.** This is being supported by larger EU economies. Not clear if US would align its proposed minimum global rate with OECD, or have higher rate
- **OECD also planning new digital sales tax** whereby multinationals would pay taxes on profits in countries where they make digital sales, rather than where they are based

Major Uncertainties Remain:

- DoF has allowed for a €2bn hit to Irish corporation tax receipts by 2025 from likely changes to tax system
- Huge uncertainty as (1) unclear what minimum global rate will be agreed by US Congress – may be less than proposed 21%; (2) OECD has not yet proposed a minimum global corporate tax – may not be that far above Irish 12.5% rate; and (3) unclear if will get agreement on digital sales tax if a minimum corporate tax rate introduced
- Big push to get reforms done, so new global corporate tax regime may be agreed by G2O Finance Ministers in July

Tax changes coming, but Ireland still has advantages

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Ireland will remain attractive FDI location:

- Big multinationals will still need to retain large global operations, whatever happens in the tax field
- US companies require employees with language skills to service European customers in European time zone
- English speaking country with common law system remains key attraction of Ireland for US companies
- Ireland's main competitor for FDI has been UK, but it is now out of EU, Single Market & Customs Union
- Strong talent pool of internationally mobile, highly skilled, well educated workers (17% of workforce is non-Irish)
- Key industries have large presence in Ireland, with its strong pro-enterprise culture, leading R&D and innovation

Change is coming, but FDI inflows continue:

- Irish Finance Minister has conceded that a "period of significant change is coming"
- Big rises in corporate tax rates in the pipeline for major economies (proposal to raise US rate from 21% to 28%; UK going from 19% to 25% in 2023). Thus, even if it is raised, Ireland's rate will likely remain comparatively low
- OECD changes may be phased in and MNCs unlikely to make any quick decisions on moving locations
- Strong inflow of FDI continues (Intel, Stripe) despite moves to change global corporate tax rules
- Of all the changes, US move to a higher global minimum corporate tax rate looks the biggest threat

Reprise of risks to the Irish economy

- Main near term risk is still Covid-19 – continues to weigh heavily on growth & employment
- Virus could leave lasting scarring effects – high business failures & bad debts, job losses
- Very open nature of Irish economy means it is exposed to any weakening in global trade
- Changed EU-UK trading relationship may yet negatively impact some Irish industries
- Questions around Ireland's corporation tax regime (pressure for tax harmonisation in EU, OECD digital tax/minimum tax rate proposals, changes to US overseas corporate tax rate)
- Supply constraints in new house building activity, with output still at very low levels
- Competitiveness issues - high house prices, high rents, high personal taxes, high wages
- Credit constrained – tight lending rules, on-going deleveraging, weak credit demand