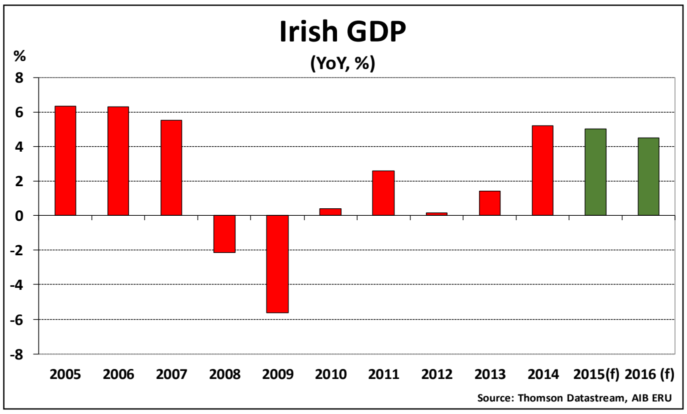
Irish Economy Update

August 2015

AIB Treasury Economic Research Unit

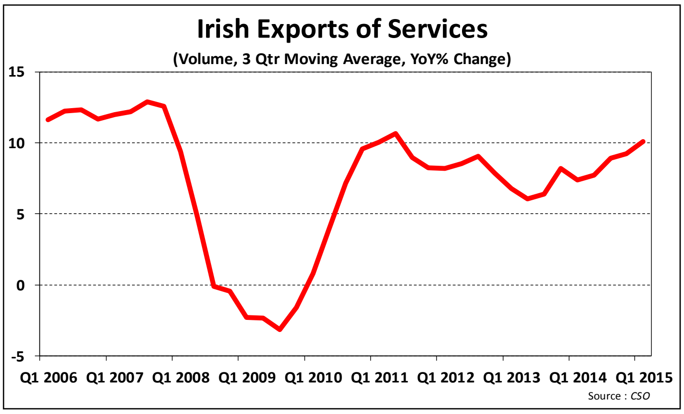
Irish economy to grow by 5% again this year

National Accounts data published recently by the CSO for the first quarter of 2015, together with revisions to previous years, confirm that the Irish economy is performing very strongly. They show that GDP rose by 1.4% in Q1 for a year-on-year gain of 6.5%. This follows growth of 5.2% last year, up from 1.4% in 2013. GDP growth for the period 2010-12 averaged 1% per annum.



All the expenditure components of GDP showed good growth last year. Consumer spending rose by 2%, while government expenditure also increased. Core business investment was very robust, increasing by 33%, while construction spending rose by 9%. Notably, there was a big jump in new housing output, which was up by over 25%, although in absolute terms, it remains at very subdued levels. Overall domestic spending, excluding investment in transport equipment (mainly planes and aircraft leasing), rose by 4.7% last year. This is particularly encouraging as it shows that the recovery in activity has spread to the domestic sector of the economy.

Meanwhile, exports which have been the main engine of growth in the economy in recent years, continued to perform strongly in 2014. Service exports rose by 8% last year, in line with the trend over the previous four years. There was a strong rebound in goods exports but these have been distorted by various factors in recent times.



The GDP data for Q1 2015 show a continuation of these trends. Most encouraging has been the further strengthening in consumer spending, which rose by a 1.2% in the quarter for a year-on-year gain of 3.8%. Output from the building and construction sector rose by almost 5% in the quarter, while exports were up by 2.3%.

These data are in line with the strong labour market figures published for the first quarter. Employment rose by 0.6% for a year-on-year gain of 2.2%. The gains in jobs were broadly based and concentrated in full-time positions. The number unemployed continued to fall, with the jobless rate declining to 9.9% from 10.4% in the final quarter of last year. Other indicators for the early months of the year, such as buoyant tax receipts, car sales and core retail sales figures, as well as robust PMI readings, are all consistent with the strong GDP growth recorded for Q1.

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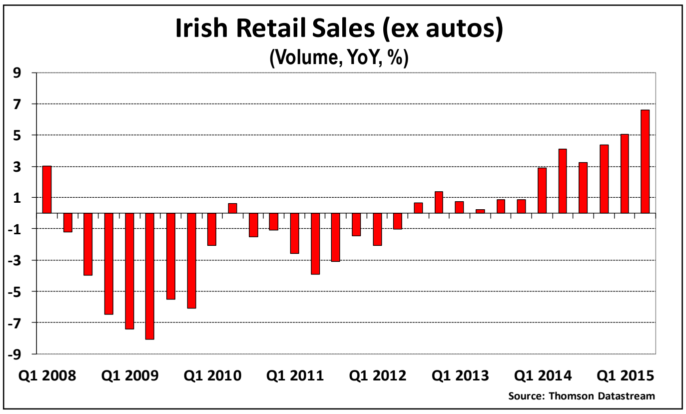
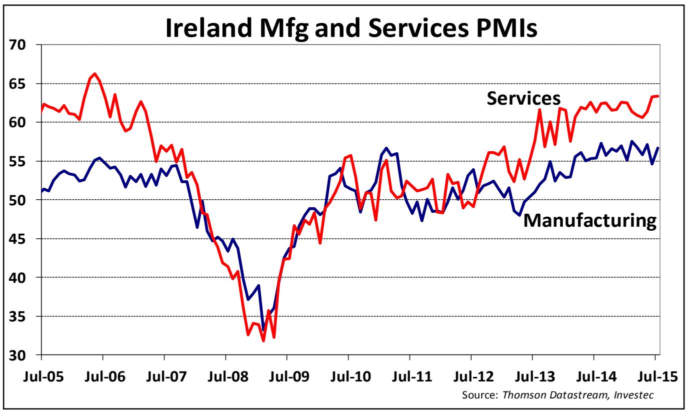
Lots of strong data pointing to robust growth

Figures released for more recent months point to a continuing strong performance by the economy in Q2 and into July. Retail sales, excluding the auto sector, rose by a very robust 2.5% in Q2 for a year-on-year gain of 6.6%. Meanwhile, new car sales which rose by 25% in the first half of the year, were up by almost 50% in July, a key month for the industry. Thus, consumer spending appears to be gaining even more momentum, helped by rising consumer confidence and improving labour market conditions. Consumer confidence has reached its best levels in nine years in recent months.



PMI data for Ireland, which are a good barometer of economic activity, have also been very strong in recent months. The services PMI climbed to a nine year high of 63.4 in July, up from 63.3 in June. Meanwhile, the manufacturing PMI stood at 56.7 in July, not far below its 15 year high of 57.5 posted in February. The construction PMI rose sharply in quarter two, hitting a nine year high of 65.7 in June.

Housing data have also continued to improve this year. Housing completions rose by a further 16% in H1 2015 and are on course to reach 13,000-14,000 this year. However, this is still well below estimated housing demand of close to 25,000 new units per year. Thus, the sector is still operating at very subdued levels of activity,



The strong performance of the economy is being reflected in the public finances. The latest Exchequer Returns are for end July. These show tax revenues over €1 billion ahead of target. There are big savings on debt interest payments also this year. Thus, a sub 2% budget deficit looks increasingly likely in 2015.

The strong data are not surprising as the backdrop for the economy has become increasingly favourable. Economic conditions in key export markets such as the UK and USA remain strong and have improved in the Eurozone. The traded sector of the economy is also benefitting from the sharp fall of the euro over the past year. On the domestic front, fiscal policy is now turning expansionary. Meanwhile, interest rates continue to fall and are set to remain very low for a prolonged period. The economy is also benefitting from the collapse in oil prices, with inflation running at around 0%.

Given the strong start to 2015 and recent upbeat data, we believe that the economy will grow by around 5% again this year. This strong growth is being built around exports, consumer spending and investment and not a construction boom as happened in the last decade. Thus, it should prove sustained. Hence, we forecast that GDP will grow by 4.5% next year and 4% in 2017 and 2018.

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