The Irish Economic Update

Performing well, but risks rising

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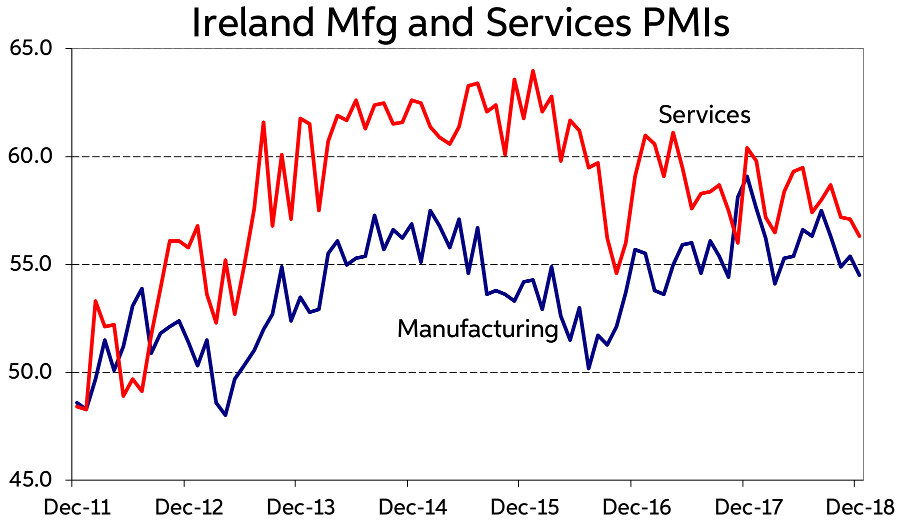
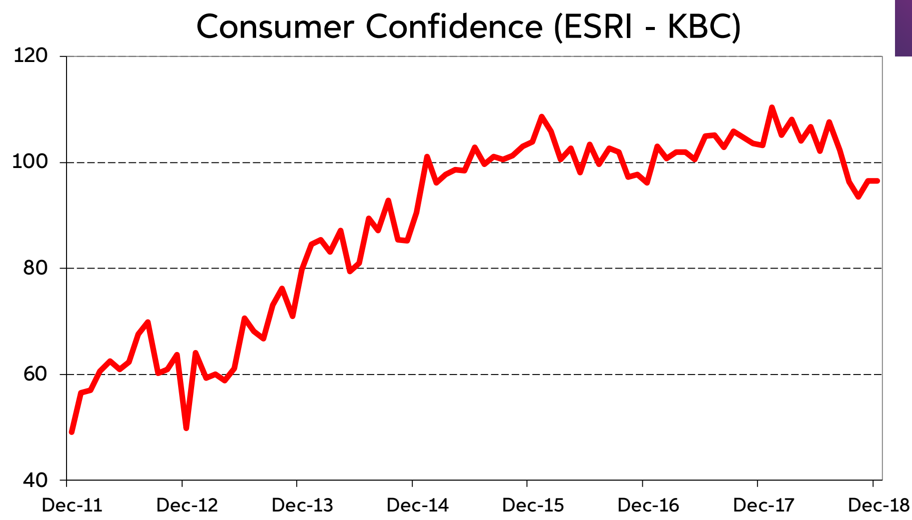
Strong growth by Irish economy over past 6 years

- 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, unlike in other countries
- 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 as the route to recovery
- Economy grows very strongly over 2013-18 – underlying growth averages 4.5% for the period
- 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 5.3% in December 2018
- Budget deficit eliminated at a quicker than expected pace. Small surplus recorded in 2018

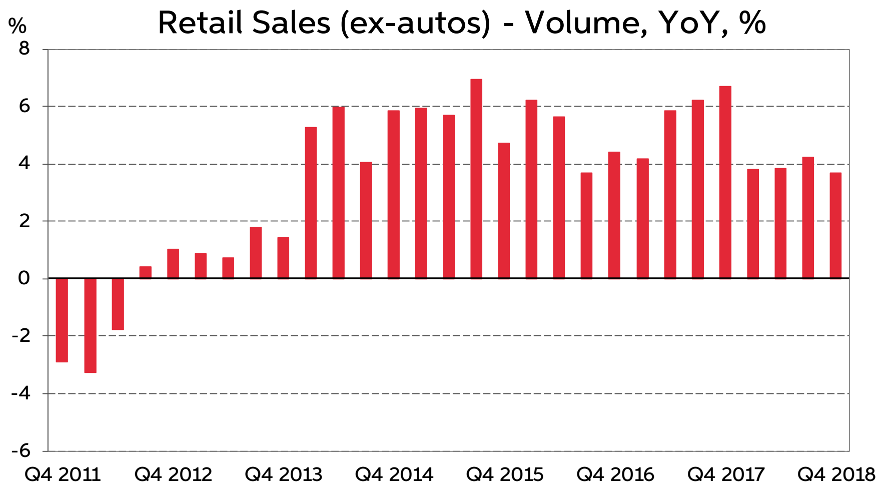
Economic indicators remained upbeat in 2018



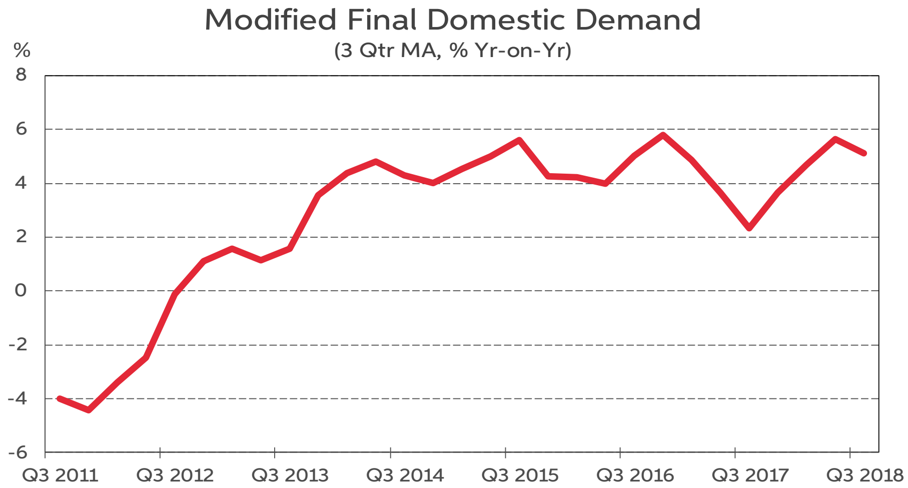
Source: *Thomson Datastream, Investec*



Source: ESRI - KBC, Thomson Datastream



Source: *Thomson Datastream*



Source: CSO, (Excludes I.P. imports & Aircraft Leasing)

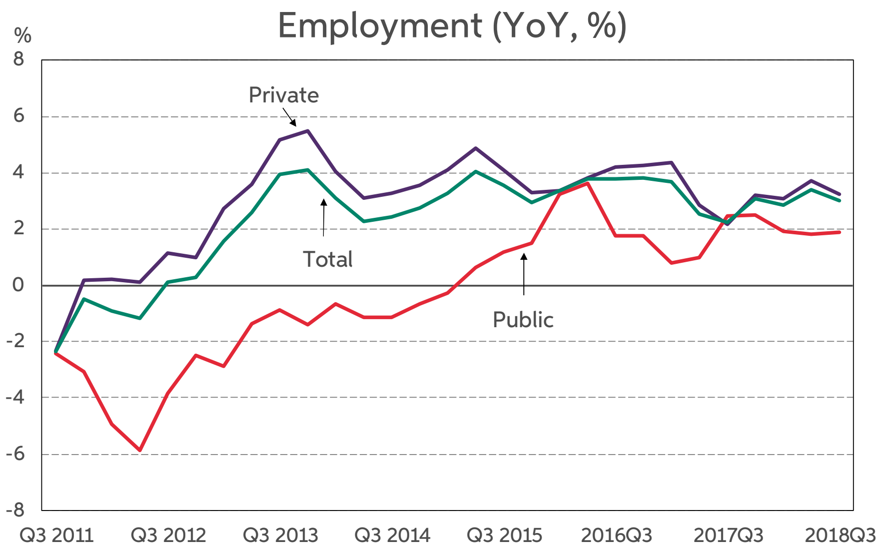
Economy continued to perform strongly in 2018

- Modified final domestic demand grew by 5% yoy in Q1-Q3 2018
- Mfg PMI remained high through out 2018 – at 55.4 in November and 54.5 in December
- Services PMI also very strong in 2018 – at 57.1 in November and 56.3 in December
- Construction PMI at strong levels throughout 2018 – at 55.5 in November, 56.3 in December
- Consumer confidence remained high in 2018 but dipped in closing months on Brexit concerns
- Retail sales (ex-motor trade) rose strongly again last year, increasing by 3.9%
- Total car regs (new + used imports) steady at very high level in 2018 – surged over 2014-17
- Further strong rise in housing completions – up 28% yoy to September
- Mortgage lending up by 20% in 2018, after rising by 29% in 2017
- Continuing strong job growth – employment rose by over 3% yoy in Q1-Q3 2018
- Live Register continued its sharp decline in 2018. Jobless rate down to 5.3% in December 2018
- Budget moved into small surplus in 2018. Tax receipts up 8.3% in the year, well ahead of target

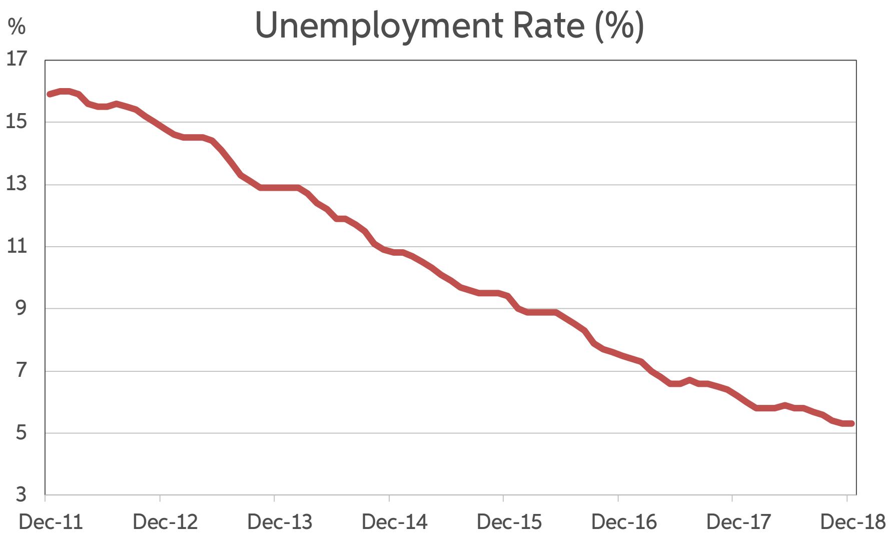
Robust jobs growth; unemployment rate falls to 5.3%

Year Average	2015	2016	2017	2018(f)	2019(f)	2020(f)
Unemployment Rate %	10.0	8.4	6.8	5.7	5.2	5.0
Labour Force Growth %	1.2	1.9	1.1	1.8	2.0	1.8
Employment Growth %	3.5	3.7	2.9	3.0	2.5	2.0
Net Migration : Year to April ('000)	5.9	16.2	19.8	34.0	38.0	40.0

Source: CSO and AIB ERU forecasts



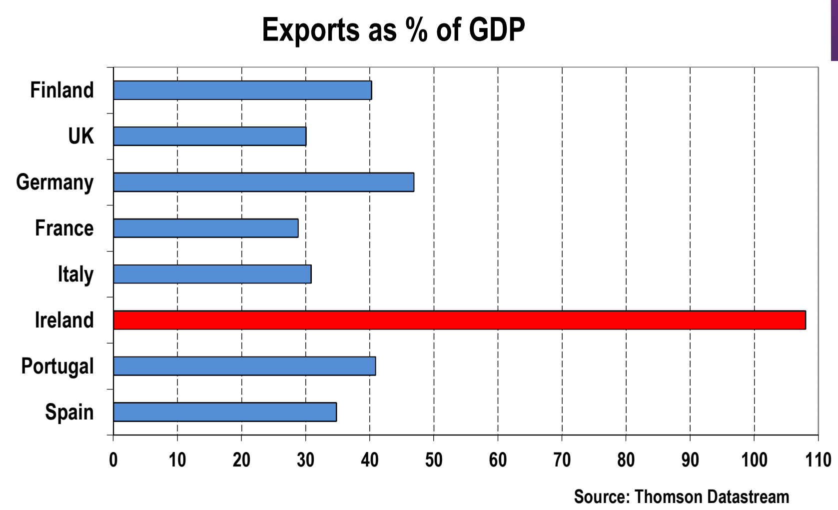
Source: *Thomson Datastream, CSO*

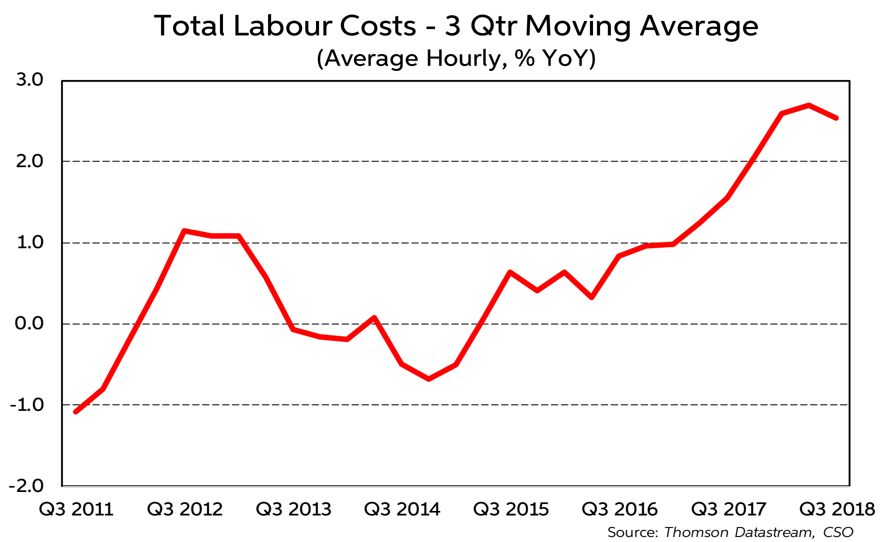


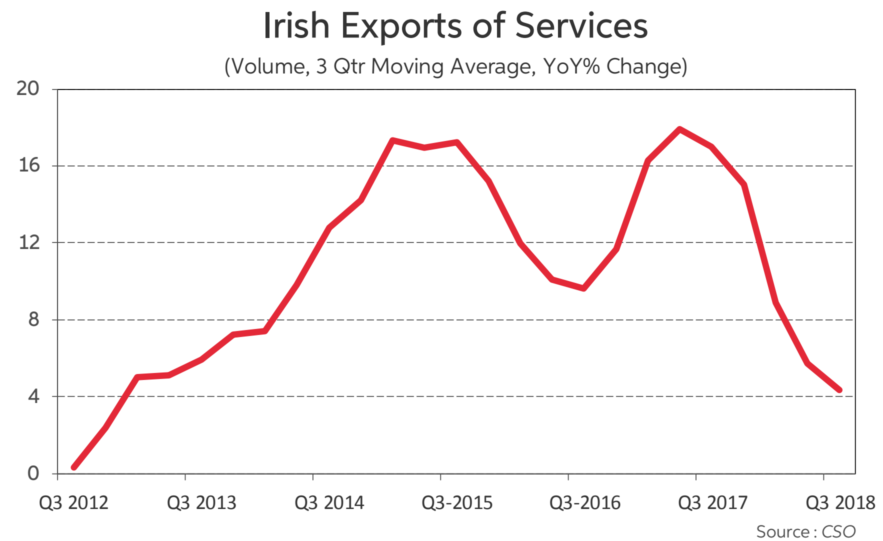
Source: Thomson Datastream

Large Irish export base performing very well

- Ireland a very open economy – exports, driven by huge FDI, equate to well over 100% of GDP
- Major gains in Irish competitiveness in past decade - weakening of euro in 2014/15 helpful
- Exports have risen strongly, helped by large FDI inflows and recovery in global economy
- Weak sterling a challenge for exports to UK, but total exports still up 9% yoy in Q1-Q3 2018







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

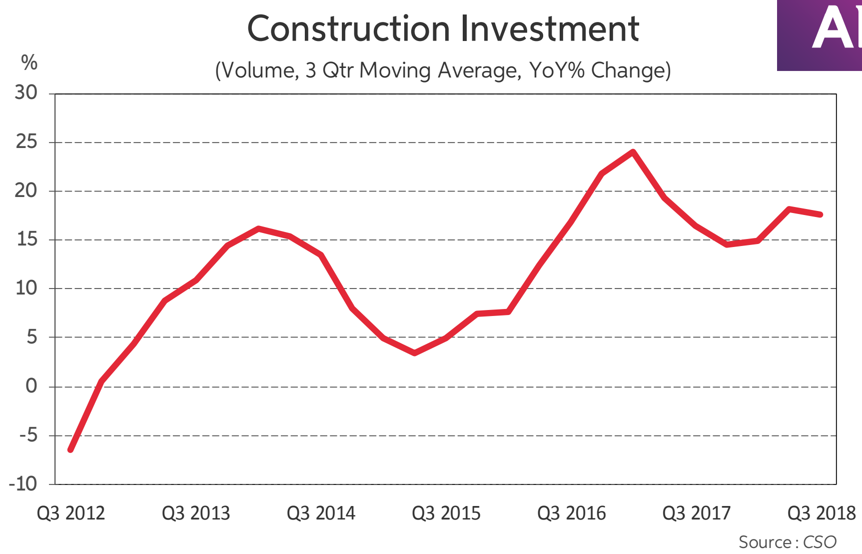
US TAX CHANGES SHOULD NOT HIT FDI

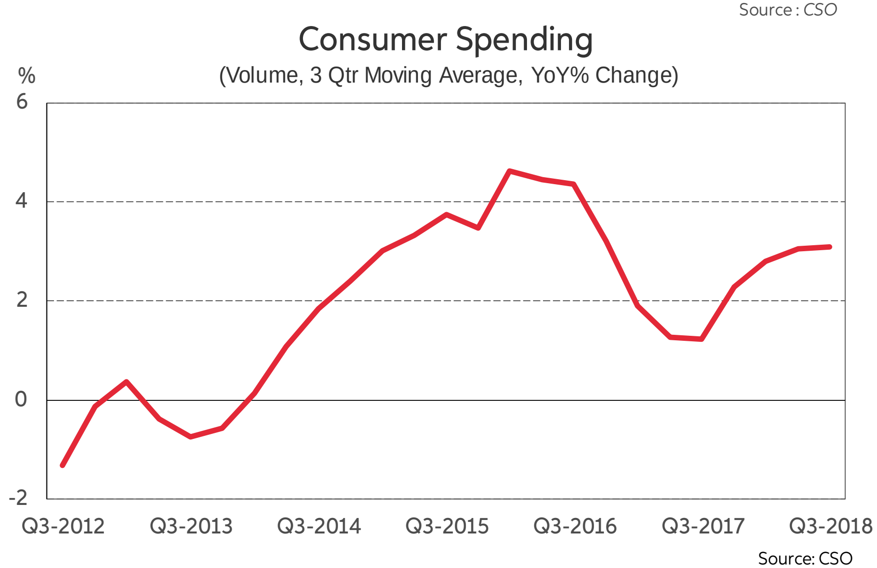
- US firms have well established operations here
- Need highly skilled, multi-lingual workforce
- Firms do not move Ireland to avoid US tax
- Ireland is base to service their European markets
- Easier to operate in local rather than US time zone
- Still wide gap between US & Irish corporate tax rates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

Many top global companies have big operations in Ireland

Strong recovery by domestic economy in place since 2013

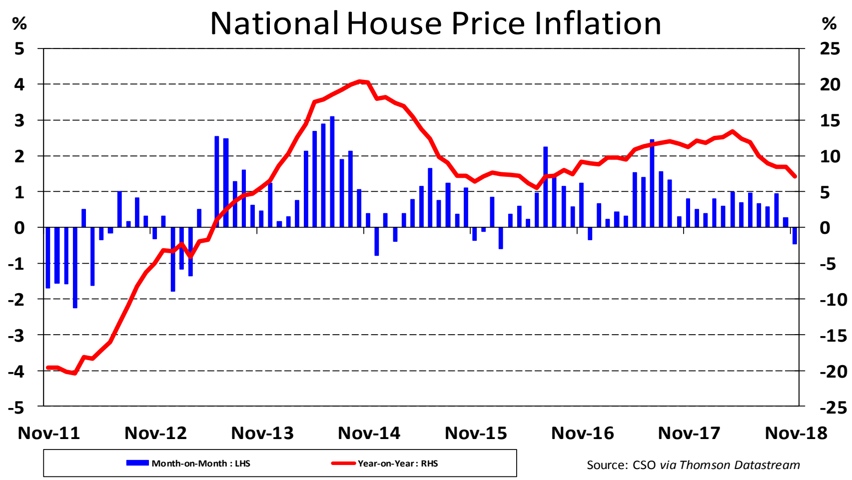
- Domestic economy contracted by 20% in period from 2008-2012, with particularly big fall in construction
- Construction sees strong recovery since 2013. Output up by 15% in 2016 & 2017 and 17% in Q1-Q3 2018
- Difficult year for agricultural sector in 2018, but comes after very strong growth in 2014-17 period
- Modified final domestic demand up 5% yoy in Q1-Q3 2018, after averaging growth of 4.4% in 2014-17
- Core business investment (ex aircraft/intangibles) has rebounded since 2013. Rose by 18.5% in Q1-Q3 2018
- Consumer spending grew by close to 3% on average over 2014-2017 period. Up 3% yoy in Q1-Q3 2018
- Core retail sales rose by a strong 3.9% in 2018
- Total car regs (new + used imports) remained at very high level in 2018, having surged over 2014-17 period

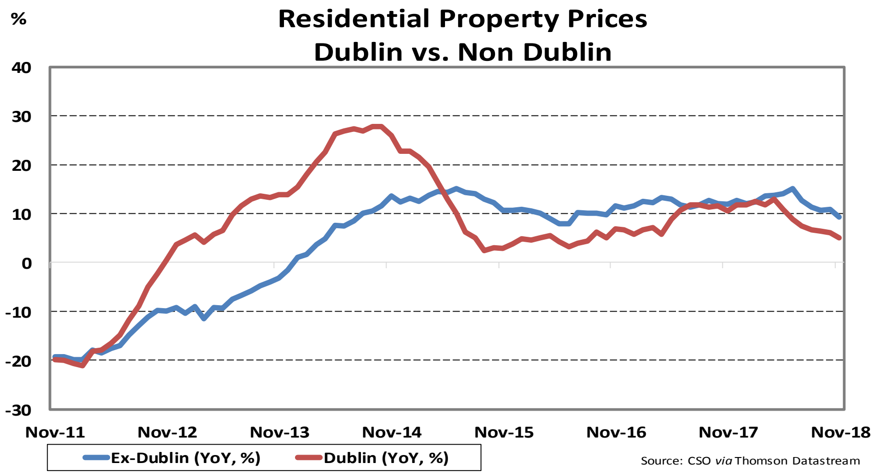




High house price inflation slowed during 2018

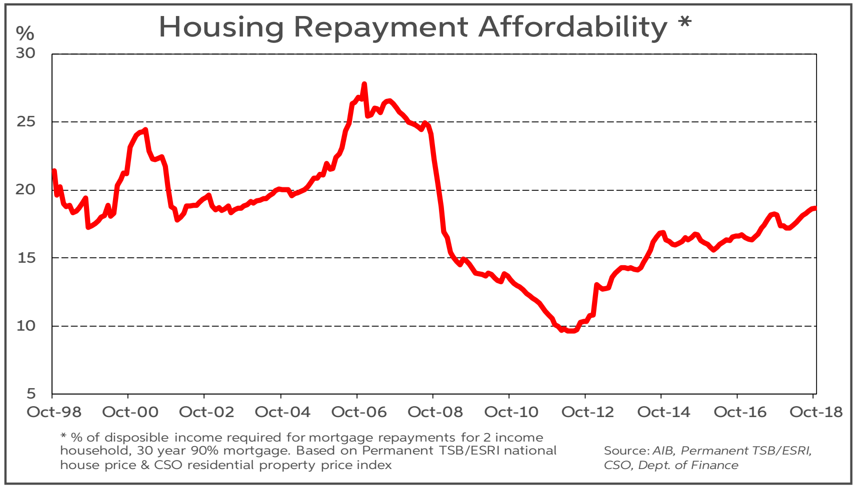
- House prices declined by a very sharp 55% between their peak in late 2007 and early 2013
- House prices have since rebounded as big housing shortage emerged after 90% fall in house building
- Little stock for sale, house building still at low level
- Prices up 83% by November from low in March 2013 –Dublin prices up by 96%, non-Dublin rise 78%
- House prices nationally still 18% below 2007 peak
- House price inflation moderated last year as Central Bank lending rules and affordability impacted
- Prices up 7% yoy nationally in November 2018, down from their peak of 13.3% in April
- Dublin up 5% vs their peak of 13% in April, while non-Dublin slows from 15.4% in June to 9.3% yoy
- Rents have also rebounded strongly – now over 26% above previous peak reached in 2008 per CSO data





House building rising slowly from very low levels

- Housing completions increased by 45% to 14,500 in 2017. Expected to have surpassed 18,000 in 2018
- Housing commencements rose by 33% in 2017 to 17,500. Could have risen to near 23,000 in 2018
- Very big jump in planning permissions in 2018. Up 70% year-on-year in Q3
- Housing output still running well below annual new housing demand, estimated at circa 35,000 units
- Measures put in place to boost new house building. More Local Authority and NAMA building
- Mortgage lending up by 20% in 2018, though rise in mortgage approvals slowed
- Housing affordability hit by rising house prices, especially Dublin, but helped by low mortgage rates
- Could be 2022 before housing output rises to 35,000 units – around level of estimated annual demand



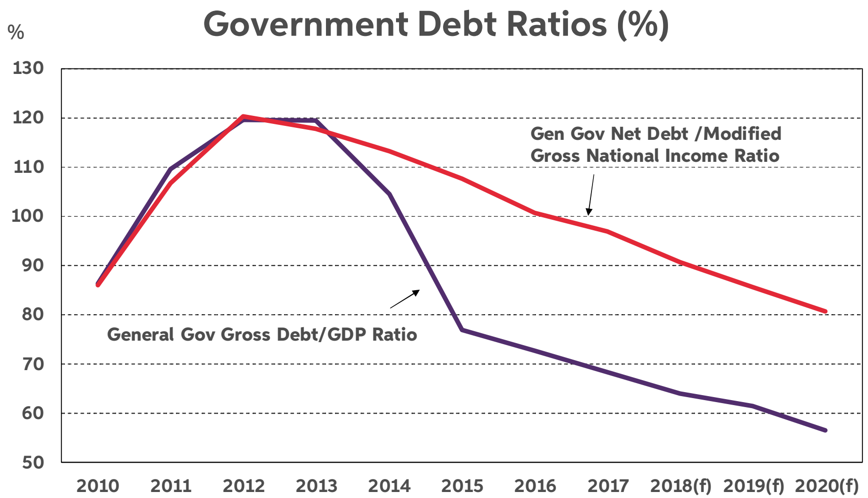
AIB Model of Estimated Housing Demand

- 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

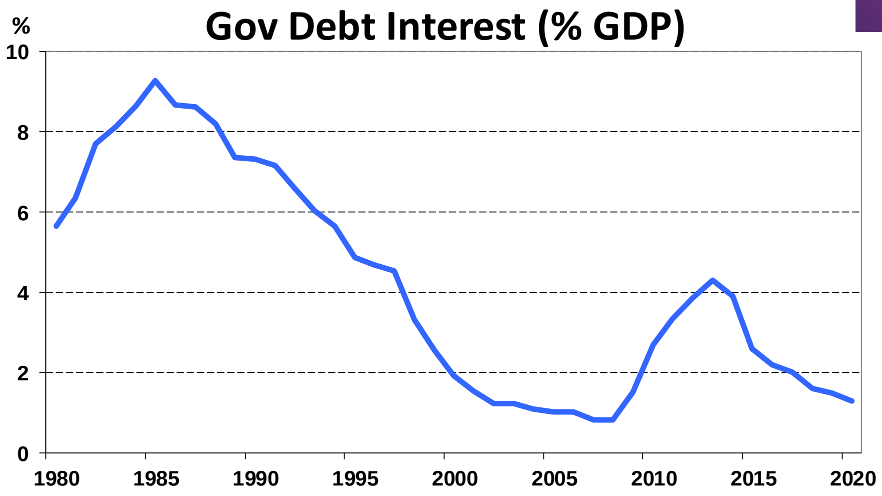
Calendar Year	2016	2017	2018	2019	2020
Household Formation	26,500	26,500	26,500	27,500	27,500
of which					
Indigenous Population Growth	*18,000*	*18,500*	*17,500*	*16,500*	*14,500*
Migration Flows	*8,500*	*9,500*	*12,000*	*13,000*	*13,000*
Headship Change*	*0*	*0*	*0*	*0*	*0*
Second Homes	500	500	500	500	500
Replacement of Obsolete Units	5,000	5,000	5,000	5,000	5,000
Estimated Demand	**32,000**	**33,500**	**35,000**	**35,000**	**33,000**
Completions	**9,900**	**14,500**	**18,500**	**23,000**	**27,000**
Shortfall in Supply	***-22,100***	***-19,000***	***-16,500***	***-12,000***	***-6,000***

*Headship is % of population that are heads of households. Sources: CSO, DoECLG, AIB ERU

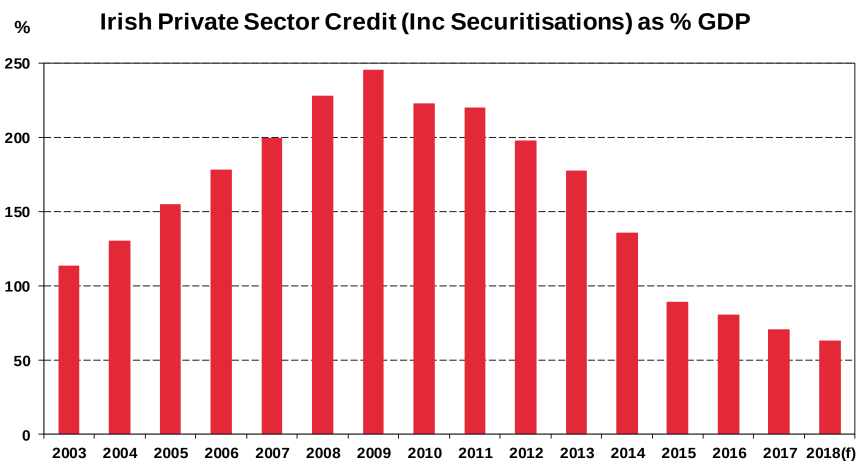
Govt debt ratios fall, private sector deleverages



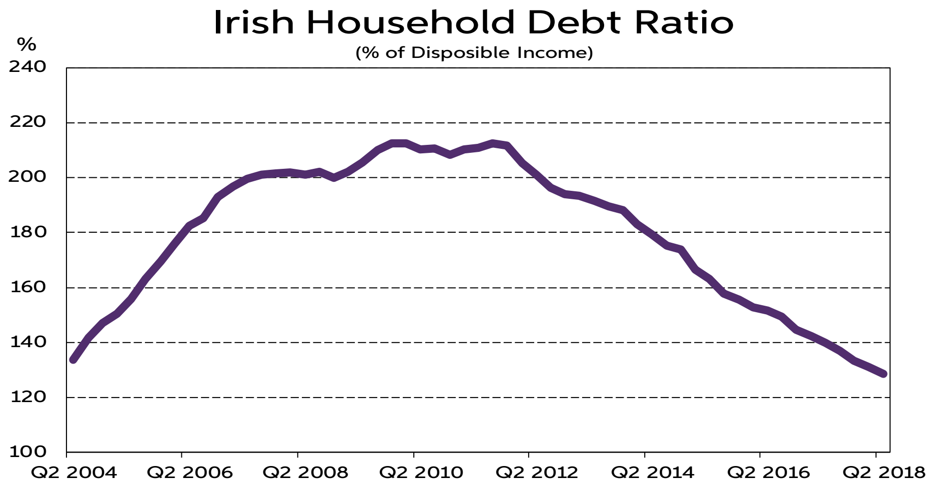
Sources: Dept of Finance, CSO, AIB ERU (Note Inflated/Distorted GDP figues from 2015)



Source: NTMA; Dept of Finance



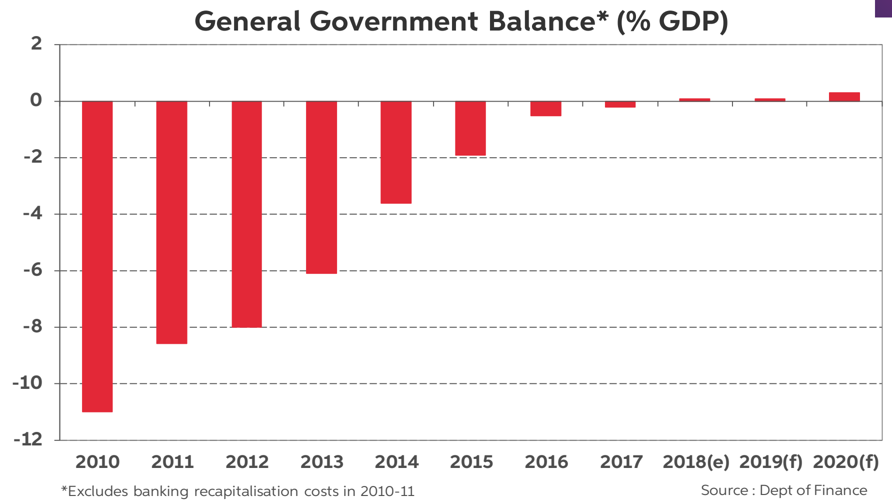
Sources: Central Bank, CSO, AIB ERU Calculations (Note Inflated/Distorted GDP figs for 2015-17)

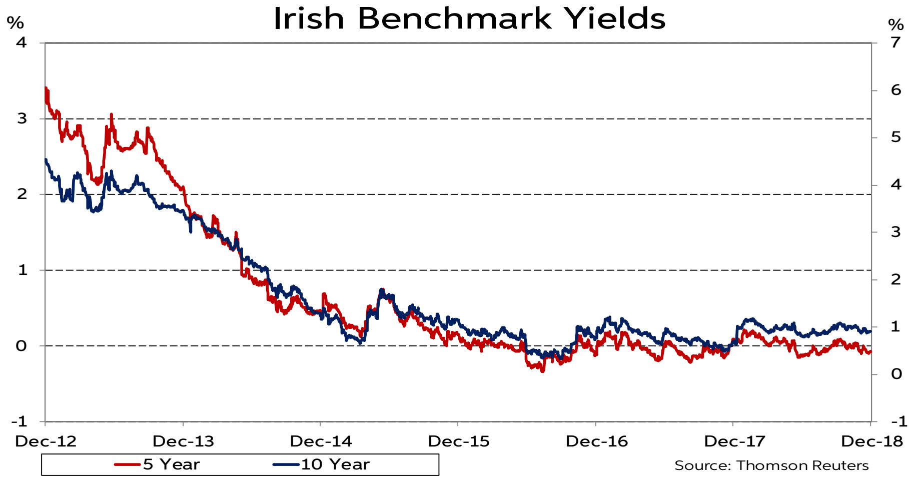


Source: CSO, Central Bank, AIB ERU

Budget returns to surplus in 2018

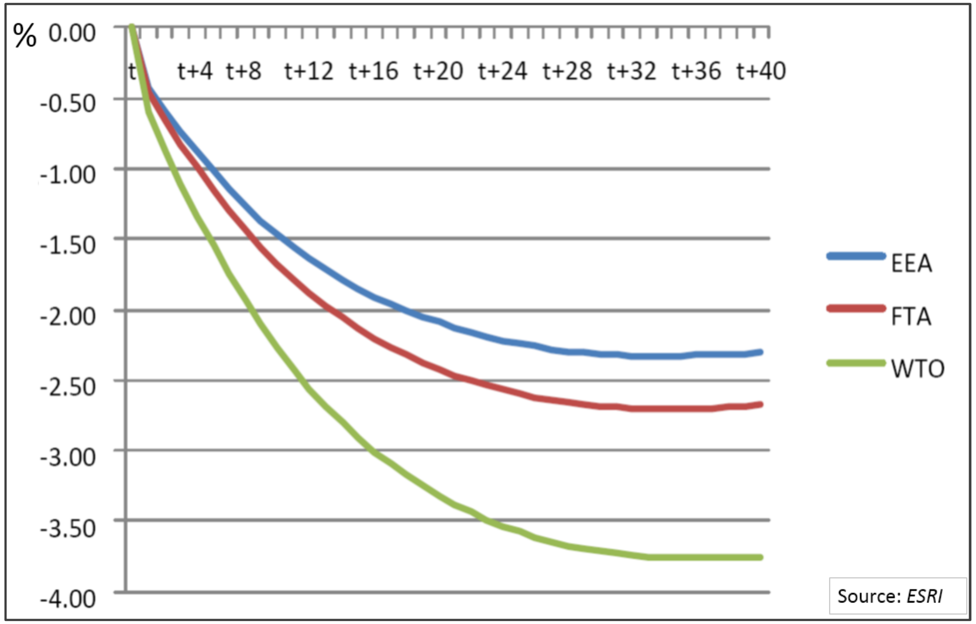
- Some €30bn (18% of GDP) of fiscal tightening implemented in 2008-2014 period
- Budget deficit has fallen sharply over past decade. Fell to 0.2% of GDP in 2017
- A small surplus was recorded in 2018, estimated at 0.1% of GDP
- Primary budget surplus (i.e. excluding debt interest) of 1.5% of GDP in 2018
- Debt interest costs low – at 1.5% of GDP
- Government aims to maintain the budget in surplus in coming years
- Gross Gov Debt/GDP ratio has fallen sharply
- Irish bonds yields at very low levels
- Sovereign debt ratings upgraded; S&P have Ireland at A+, Fitch at A+, Moody's A2





Brexit expected to lower growth rate of Irish economy

Impact of Brexit on Output *(% deviation from base)*



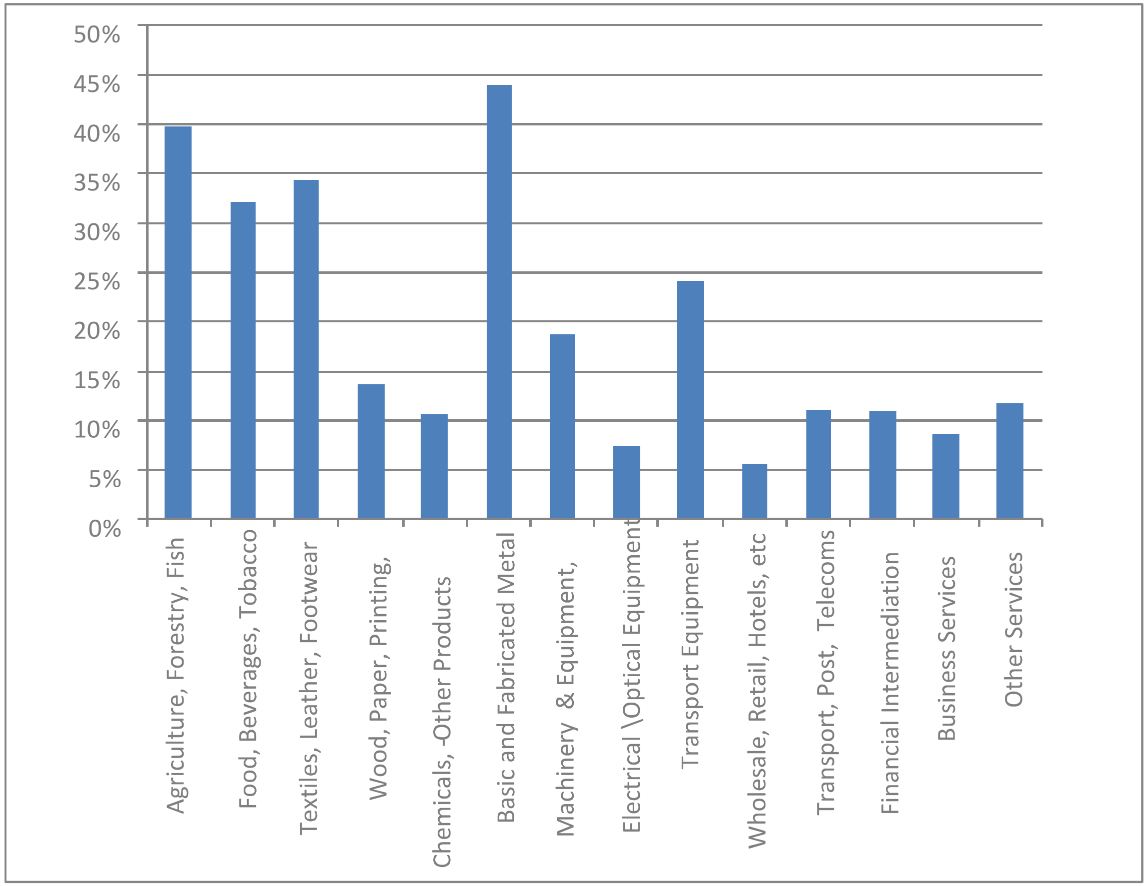
- ESRI estimate that Irish output would be reduced over time by 2-2.5% on a soft Brexit
- Sharp fall-off in trade with UK likely on a no-deal, hard Brexit
- Output almost 4.0 % lower over time if there is hard Brexit and a fall back on WTO rules and tariffs
- Employment 2% lower and unemployment rate nearly 2% higher in hard Brexit

- Copenhagen Economics Report considers 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 up. UK may not maintain these post Brexit
- Food and Beverages account for 25% of total Irish exports to UK
- Around 40% of Irish food exports go to the UK
- 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 2018

- 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.

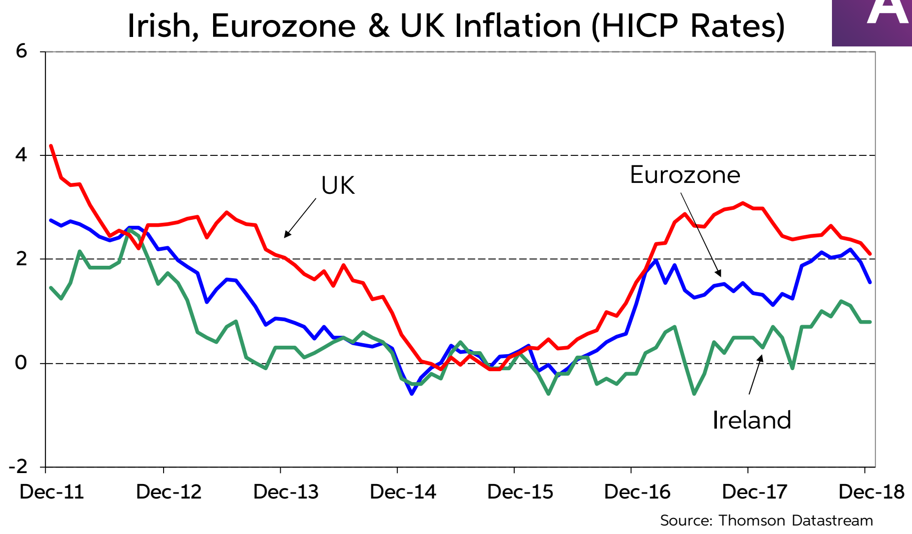
- **Very negative sentiment readings, but firms say Brexit is having little impact on businesses now**
- **SMEs surveyed are most concerned about its impact in the future, both on their own business and wider economy, as well as lack of clarity on Brexit**
- **Tourism, Manufacturing, Retail sectors most worried**

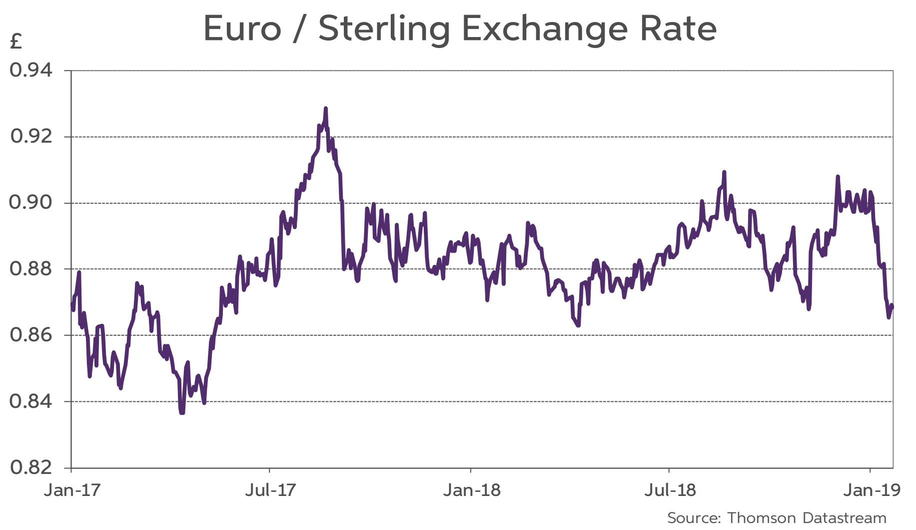
Still much uncertainty about Brexit

- UK plans to leave EU, Single Market & Customs Union on 29 March 2019. A no deal hard Brexit the default exit mechanism if no other option agreed, unless Article 50 is extended or revoked
- The Withdrawal Agreement reached between UK and EU allows for orderly UK departure from EU – includes transition period. However, it was voted down by the UK Parliament in January
- The WA provides for a backstop to be triggered if agreement cannot be reached on an EU-UK trade deal that would avoid a hard border in Ireland after the transition period expires
- The backstop is attracting strong opposition in Parliament as it could lock UK into a permanent common Customs territory with the EU. UK looking to re-negotiate the backstop
- UK Parliament wants to avoid the default no-deal hard Brexit, but likely in the end to face a choice between it and the Withdrawal Agreement as EU ruling out any changes
- UK likely to seek and get an extension to Article 50 to avoid a hard Brexit at end March, if it cannot get changes to the backstop in coming weeks
- Thus, still a lot of uncertainty about Brexit, when it will occur, and what form it takes

Irish growth to remain strong if external risks avoided

- Strong growth by Irish economy should continue
- Construction picking up from still low output levels
- Public spending on the rise
- Activity supported by low interest rate environment
- Continuing FDI despite concerns on corporate tax
- Low Irish inflation still low, well below that of the Eurozone, UK and US
- However, Brexit is a challenge for the economy
- Important also that global economy holds up given importance of exports to Ireland
- GDP growth forecast at 4.0%+ for 2019 and circa 3.5% in 2020, assuming a no-deal, hard Brexit is avoided and the global economy holds up
- ESRI estimates medium-term growth rate of economy at around 3.25% in the period 2020-2025





AIB Irish Economic Forecasts

% change in real terms unless stated	2016	2017	2018 (f)	2019 (f)	2020 (f)
GDP	**5.0**	**7.2**	**7.0**	**4.0**	**3.5**
GNP	11.5	4.4	7.0	3.7	3.2
Personal Consumption	4.0	1.6	3.0	2.5	2.5
Government Spending	3.5	3.9	4.8	3.0	3.0
Fixed Investment	51.7	-31.0	3.0	7.0	6.0
Modified Final Domestic Demand*	5.6	3.2	5.0	4.0	3.8
Exports	4.4	7.8	8.0	4.5	4.3
Imports	18.5	-9.4	4.0	4.5	4.5
HICP Inflation (%)	-0.2	0.3	0.7	1.0	1.5
Unemployment Rate (%)	8.4	6.8	5.7	5.2	5.0
Budget Balance (% GDP)	-0.5	-0.2	0.1	0.1	0.3
Gross General Gov Debt (% GDP)	72.8	68.0	64.0	61.0	56.5

*Excludes investment in aircraft and intangibles

Source: CSO, AIB ERU Forecasts

Risks to the Irish economy

- Main risks to Irish recovery no longer internal but external, in particular Brexit
- Brexit major issue for Ireland given its strong trading links with UK and sharp fall by sterling
- Uncertain external environment with growing downside risks to global growth from increasing protectionism/tariffs, tightening monetary conditions, problems in some emerging economies
- Questions around Irish corporation tax regime (Apple ruling, moves on tax harmonisation in EU, cuts in US/UK rates) could impact FDI. Note that Ireland has the right to set its own tax rates
- Supply constraints in new house building activity, which is recovering at a slow pace with output still at very low levels
- Competitiveness issues - high Dublin house prices, high rents, high personal taxes, rising wages
- Credit constraints – tightening of lending rules, on-going deleveraging