



# The Irish Economic Update

*Economy Continues To Perform  
Well Despite Concerns Over Brexit*

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## Strong recovery by Irish economy since 2013



- 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% and GNP down 10%
- 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 still over 25% higher than in 2001, highlighting that the economic crash came after a very strong period of 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 rebounds strongly in 2013-16 period. (Note 2015 GDP/GNP data distorted)
- Domestic economy has recovered strongly, led by rebound in investment and retail spending
- Core domestic demand averaged growth of 4% in the period 2013-15
- Strong jobs growth. Unemployment rate fallen from 15% in 2012 to 7.3% in late 2016
- Budget deficit has declined at quicker than expected pace. Circa 1% of GDP in 2016

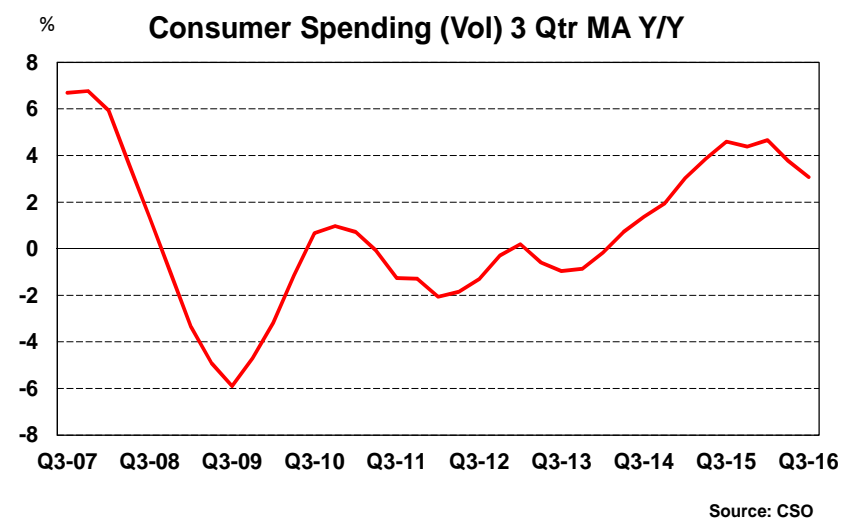
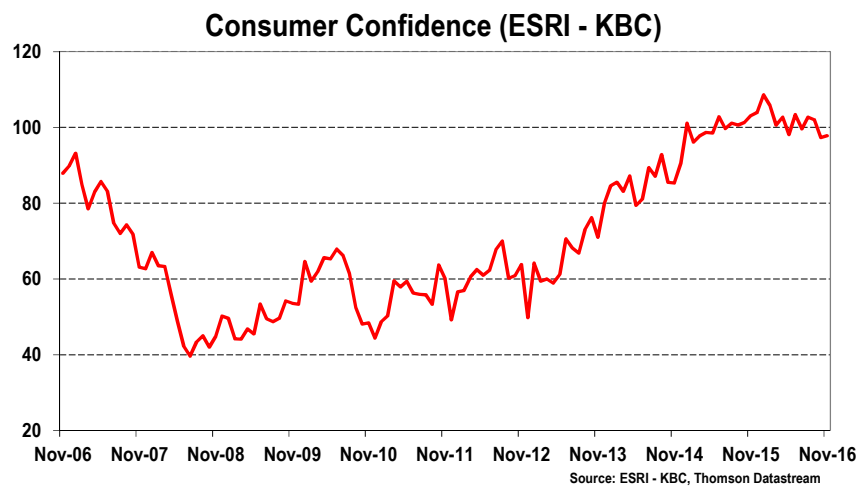
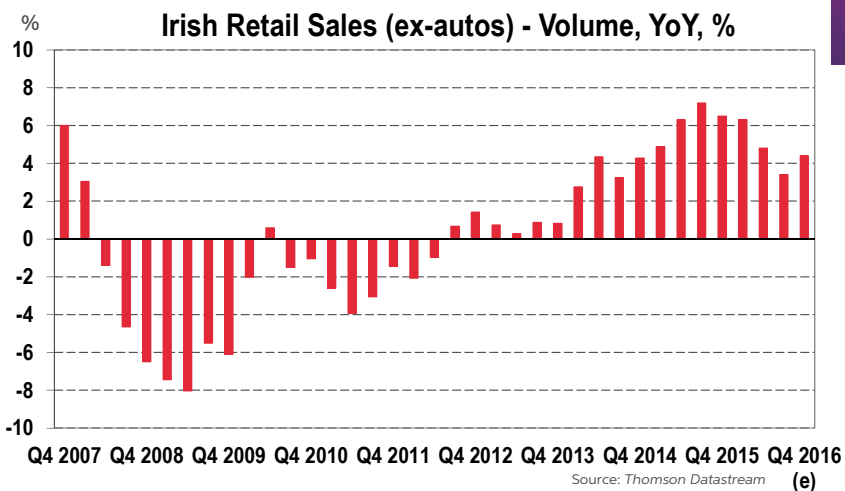
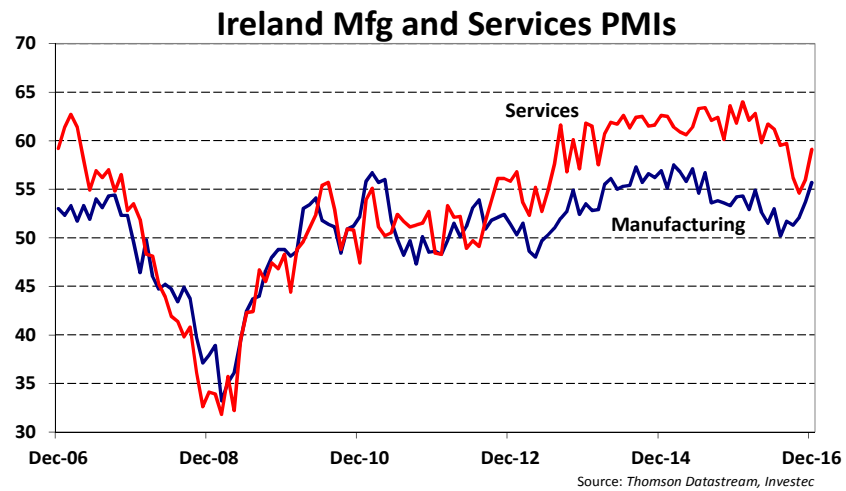
## Economy performed well again in 2016



- GDP growth averaged strong 4.5% year-on-year in Q1-Q3 2016
- Manufacturing PMI weakened appreciably around mid-year but rebounded strongly in Q4'16
- Strong rebound by services PMI at end 2016 after marked decline post Brexit vote in UK
- Slower growth in service exports of 6.5% yoy in Q1-Q3 2016 after a big rise in 2015
- Construction PMI performed strongly in 2016 – averaged around 60.
- Consumer confidence strong but has fallen back somewhat from 15 year highs hit in Q1'16
- Consumer spending up 3.2% yoy in Q1-Q3 2016 – strong retail spending last year
- New car sales rose by 17.5% in 2016 after 30% jump in both 2014 and 2015
- Housing completions up by 17% yoy in first ten months of 2016
- Mortgage lending picks up strongly in 2016 after slowing in 2015 on new CB lending rules
- Strong employment growth in 2016 – up 2.9% yoy in both Q2 and Q3
- Live Register continues to fall. Jobless rate down to 7.2% in December – peaked at 15.1%
- Slower growth in tax receipts since early summer but finished well ahead of target in 2016



# UK Brexit vote had limited impact on Irish data



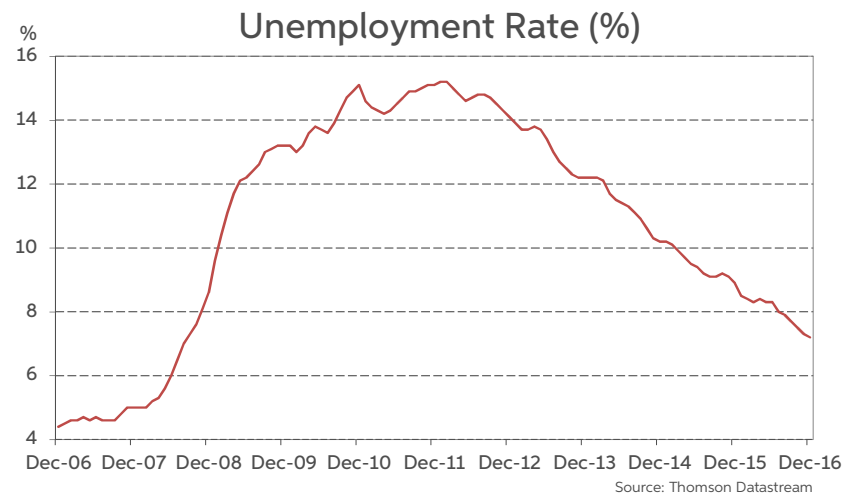
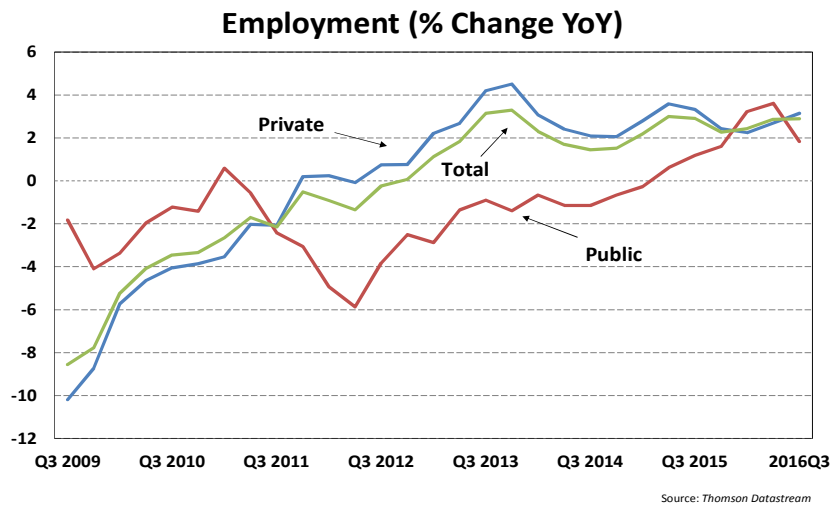
# Strong jobs growth continues; unemployment falls



Year Average	2013	2014	2015	2016(f)	2017(f)	2018(f)
<b>Unemployment Rate %</b>	13.1	11.3	9.5	8.1	7.2	6.6
<b>Labour Force Growth %</b>	0.4	-0.3	0.5	1.2	1.2	1.1
<b>Employment Growth %</b>	2.4*	1.7	2.6	2.8	2.1	1.7
<b>Net Migration : Year to April ('000)</b>	-33.1	-21.4	-11.6	3.0	10.0	15.0

*\* Employment ex Agriculture +1.3% in 2013*

Source: CSO and AIB ERU forecasts

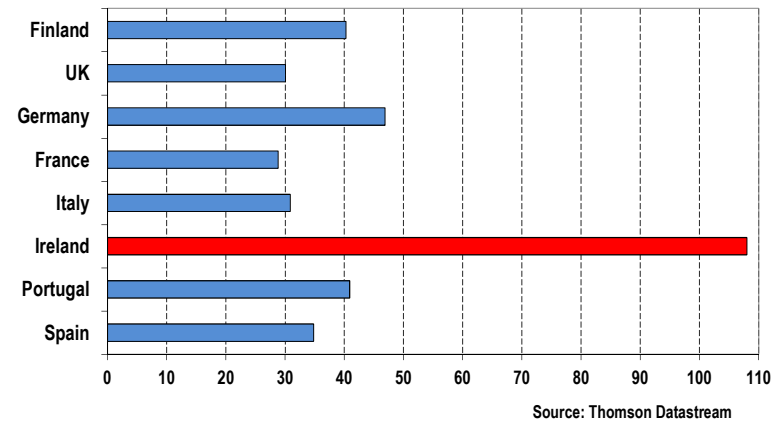


# Large Irish export base performs well

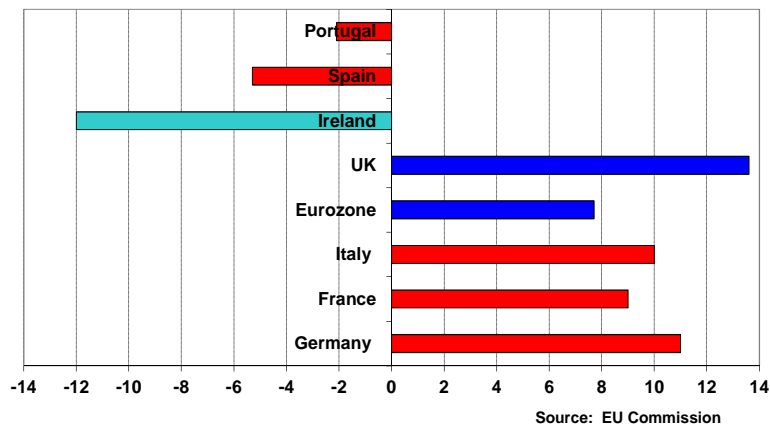


- Ireland a very open economy – exports, driven by huge FDI, equate to well over 100% of GDP
- Major gains in Irish competitiveness since 2009, with weakening of euro also helpful
- Exports have risen strongly, helped by large FDI inflows and recovery in global economy
- Sterling’s sharp fall a challenge for exports to UK

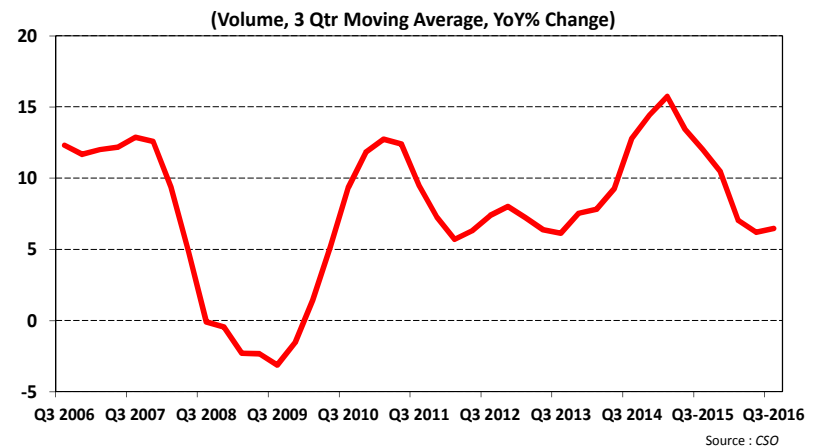
Exports as % of GDP



Unit Labour Costs 2009-2013 (% Change)



Irish Exports of Services



# 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
- Easy access to decision makers

## KEY FDI IMPACTS ON THE IRISH ECONOMY

- 1,200 multinational companies
- €150bn Exports (64% of Irish exports)
- 200,000 Jobs in FDI, 340,000 in total
- 70% of Corporation Tax
- €8.7bn Spending on Irish services/materials
- €10bn in Payroll
- 67% of Business R&D expenditure

## WORLD LEADERS CHOOSE IRELAND

- 8 of the top 10 in ICT
- 9 of the top 10 in Pharmaceuticals
- 17 of the top 25 in Medical Devices
- 3 of the top 5 Games companies
- 10 of the 'top born on the Internet' firms
- More than 50% of the world's leading Financial firms

## TRUMP 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
- Risk of protectionism means need bases abroad
- No certainty about future US tax policy
- More likely to repatriate profits if US taxes cut

# Many top global companies have big operations in Ireland

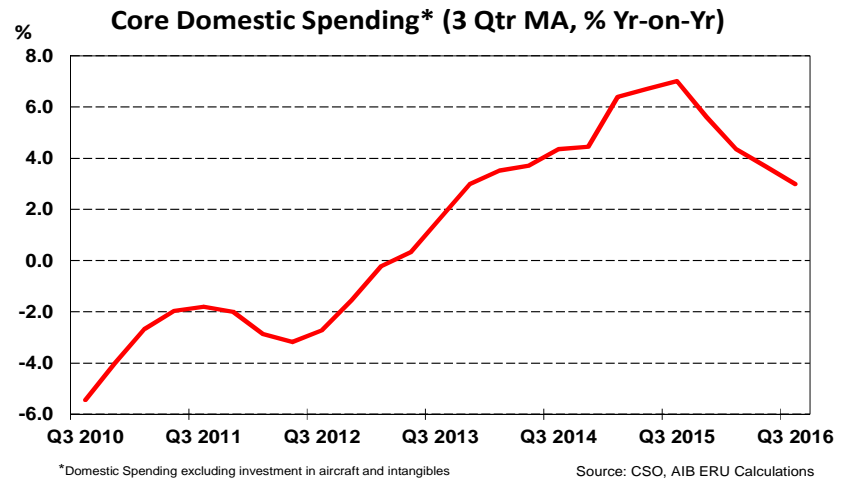
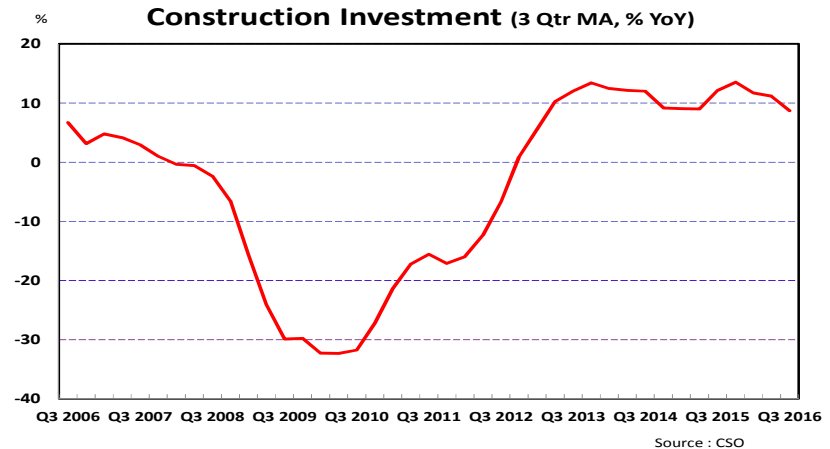




## Slower growth by domestic economy last year



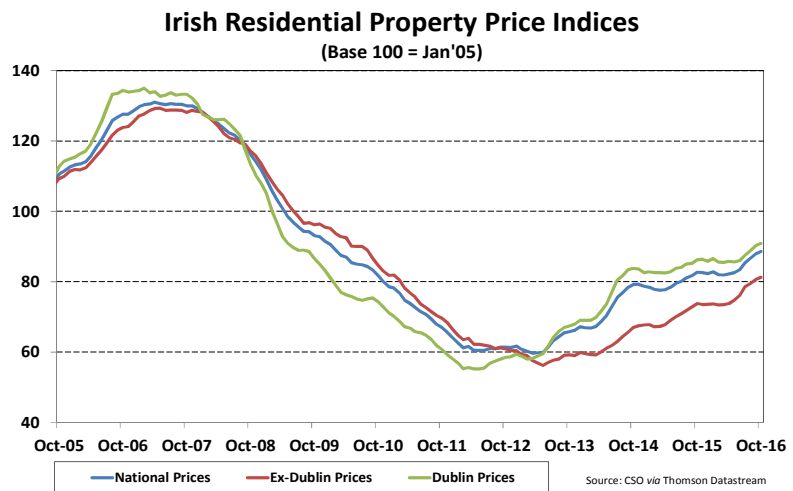
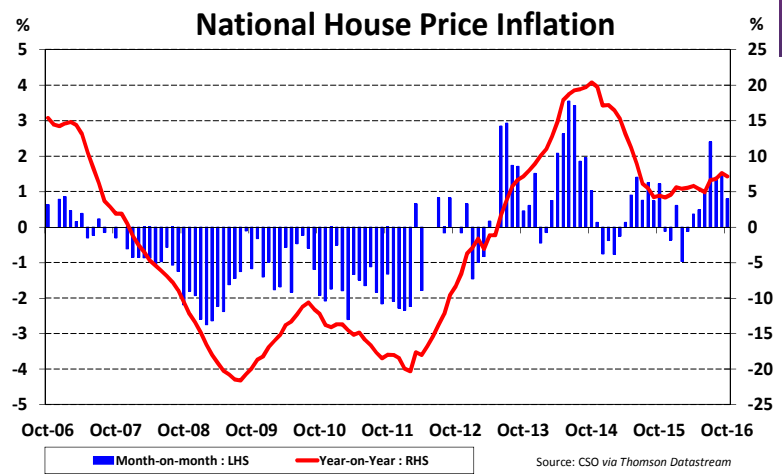
- Domestic economy contracted by 20% from 2008-12
- Collapse in construction was big drag on GDP - fell from 13.5% of GDP in 2005-07 to 5.3% by 2012
- Construction has seen steady growth since 2013 of circa 10% per annum – continued in 2016
- Business investment (ex planes/R&D) more than doubled in 2013-2015 but fell back in 2016
- Consumer spending grew by 1.7% in 2014, 4.5% in 2015 and 3.2% yoy in Q1-Q3 2016
- Core domestic spending (ex aircraft, R&D, Intangibles) averaged growth of 4.4% in 2013-2015
- Slower growth of 3% yoy in core domestic spending in Q1-Q3 2016 as business investment declined
- Core retail sales rising strongly again towards end 2016 after slowing on Brexit vote around mid-year



# House prices rebound as big housing shortage emerges



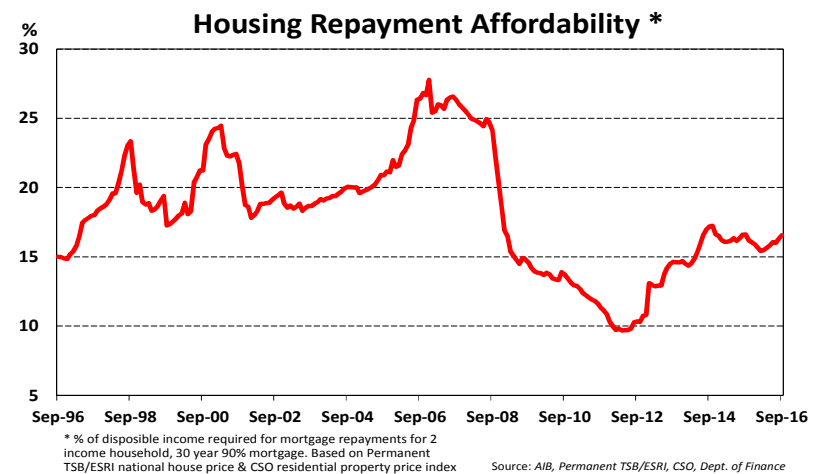
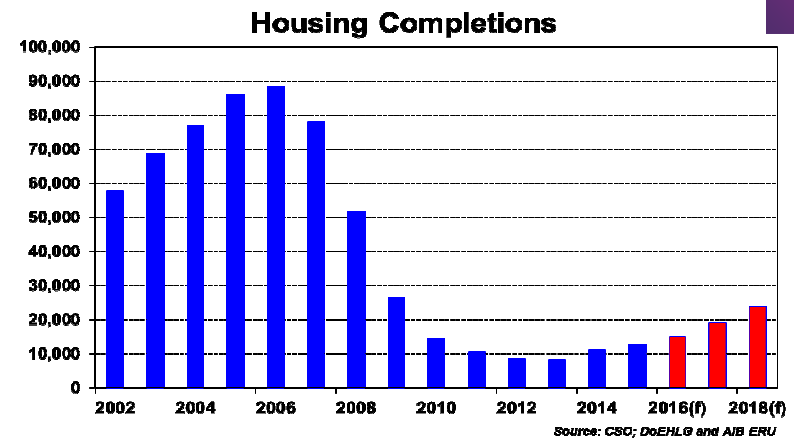
- House prices declined by a very sharp 55% between their peak in late 2007 and early 2013
- House prices rebound: up 48.5% by Oct 2016 from low in early 2013 as big housing shortage emerges
- 90% decline in housing output. Supply overhang eliminated and low level of stock for sale now
- Dublin prices up by 65% from trough, with non-Dublin prices up by 45%
- House prices, though, including in Dublin, are still some 32% below peak levels hit in 2007
- Central Bank mortgage rules cooled Dublin house price inflation in 2015– fell from 25% to 3% yoy
- House prices inflation picked up somewhat in 2016. Prices up 7% yoy nationally in October, Dublin 5.5%
- Rents have also rebounded strongly – now 11.5 % above previous peak reached in 2008



# House building rising only slowly from very low levels



- Housing completions at 12,700 in 2015, up from 11,000 in 2014 and 8,300 in 2013
- Completions up 17% to Oct 2016. Should reach 15,000 units last year but still at low level
- Annual demand estimated at 25,000-30,000 units
- Measures being put in place to boost new house building. More Local Authority and NAMA building
- Central bank lending rules relaxed while tax rebates introduced in budget to help fund deposits for FTB
- Mortgage lending has picked up after slowing in 2015/early 2016 on introduction of CB rules
- Housing affordability helped by low mortgage rates
- Improving trend in new housing starts a positive sign that housing completions will continue rising
- However, likely to be 2018/19 before housing output rises to 25,000 units or above



# AIB Model of Potential Housing Demand



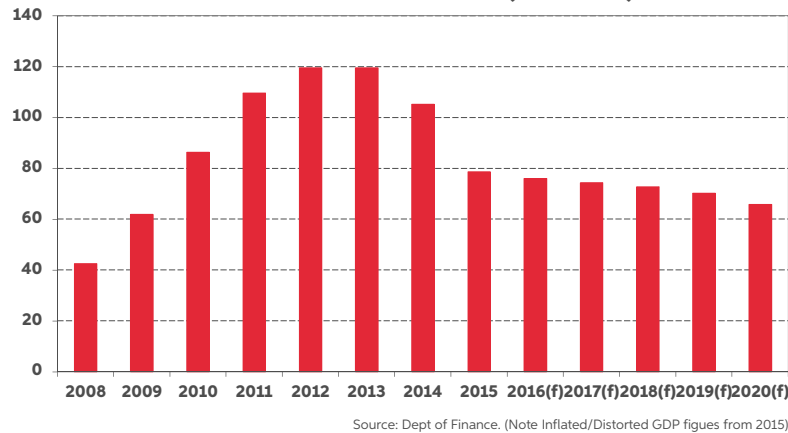
Calendar Year	2012	2013	2014	2015	2016	2017	2018
<b>Household Formation</b>	14,000	15,000	16,500	19,500	21,500	22,000	23,000
<i>of which</i>							
<b>Indigenous Population Growth</b>	20,000	17,500	17,000	17,500	17,000	16,000	15,500
<b>Migration Flows</b>	-9,000	-5,500	-3,500	-1,500	1,000	2,500	3,500
<b>Increased Headship</b>	3,000	3,000	3,000	3,500	3,500	3,500	4,000
<b>Second Homes</b>	1,000	1,000	1,000	1,000	1,000	1,500	1,500
<b>Replacement of Obsolete Units</b>	4,000	4,000	4,500	4,500	4,500	5,000	5,500
<b>Total POTENTIAL Demand</b>	<b>19,000</b>	<b>20,000</b>	<b>22,000</b>	<b>25,000</b>	<b>27,000</b>	<b>28,500</b>	<b>30,000</b>
<b>Completions</b>	<b>8,500</b>	<b>8,300</b>	<b>11,000</b>	<b>12,700</b>	<b>15,000</b>	<b>19,000</b>	<b>24,000</b>
<b>POTENTIAL Impact on Vacant Stock</b>	<b>-10,500</b>	<b>-11,700</b>	<b>-11,000</b>	<b>-12,300</b>	<b>-12,000</b>	<b>-9,500</b>	<b>-6,000</b>

Sources: CSO, DoECLG, AIB ERU

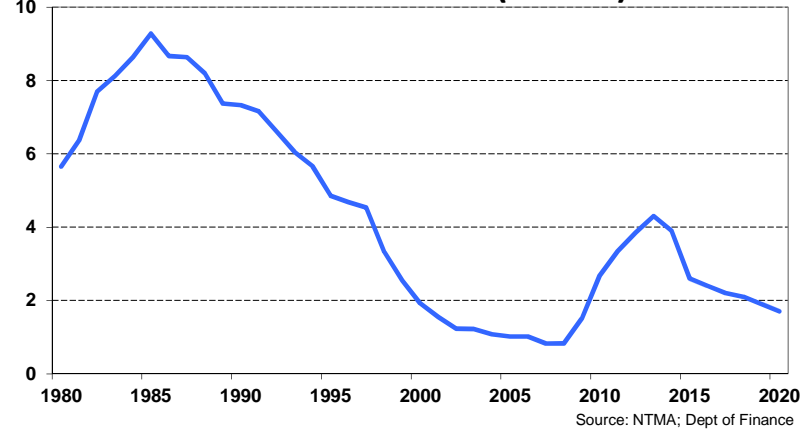
# Gov debt ratio falling, private sector deleveraging



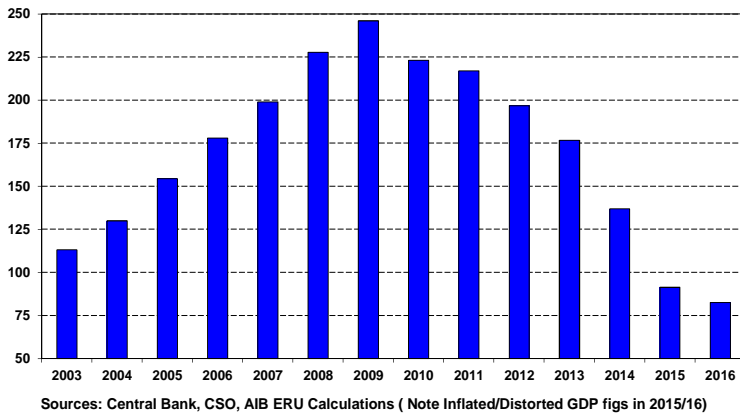
**Gross Gen Gov Debt (% GDP)**



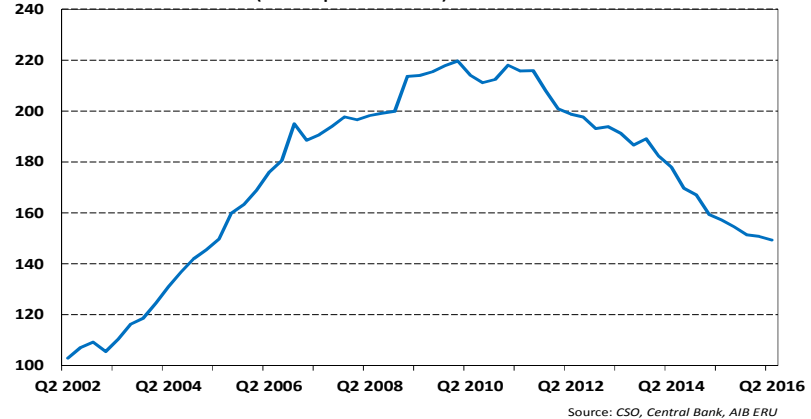
**Gov Debt Interest (% GDP)**



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



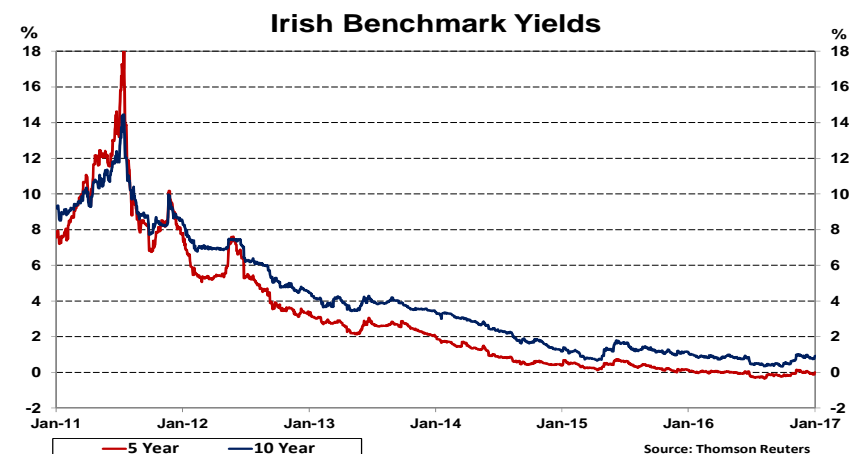
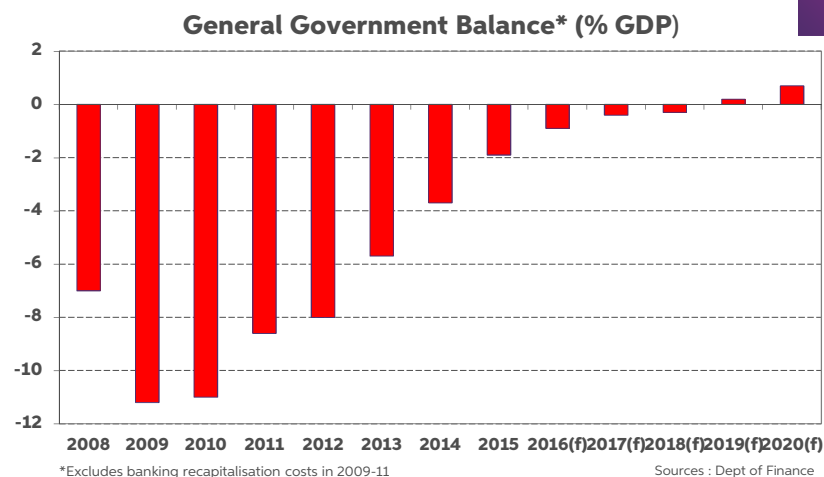
**Irish Household Debt (% of Disposable Income)**



# Budget deficit falls to very low level



- Some €30bn (18% of GDP) of fiscal tightening implemented in 2008-2014 period
- Fiscal policy now mildly expansionary
- Budget deficit falls sharply in recent years
- Deficit of some 1% of GDP in 2016
- Budget deficit forecast at below 0.5% of GDP for 2017 and 2018
- Primary budget (i.e. excluding debt interest) surplus of around 1.5% of GDP in 2016
- Debt interest costs low – circa 2.5% of GDP
- Gross Gov Debt/GDP ratio in marked decline
- Irish bonds yields have fallen to very low levels
- Sovereign debt ratings upgraded; S&P have Ireland at A+, Fitch at A, Moody's A3



# Brexit is a major headache for Ireland



- Brexit has serious implications given close economic/trade links with UK
- Trade with UK equates to **35% of Irish GDP**. Thus, it is a key trading partner
- UK takes **43% of Irish indigenous firm exports**, so very important trading partner
- Expected negative impact of Brexit on UK economy will have **knock-on effect** in Ireland
- Agri, tourism, energy, retailing, financial sector most likely to be impacted by Brexit

- Sterling has fallen sharply on Brexit concerns, which will hit **exports to UK**
- Also impacts Irish firms **competing with UK exports** to Ireland and third country markets
- **Cross border trade** picks up as shoppers head North following sterling's big fall
- **Sterling weakness** will also have a significant impact on cross-border businesses like hotels, restaurants

- **Higher trading costs** from more administration, differing trade rules and regulations, compliance costs, possible customs duties and tariffs when UK leaves EU
- Brexit could impact considerable **cross-country investment** between UK and Ireland.
- **Border** with Northern Ireland would become an external EU land border
- Ireland will **lose key ally** within EU when UK leaves as share similar views on taxation, regulation, state involvement in economy etc.

## Ireland hopes that hard Brexit will be avoided



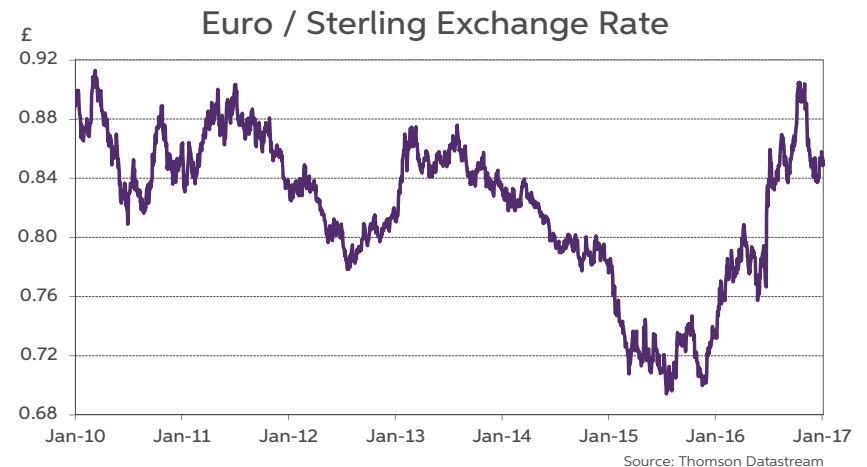
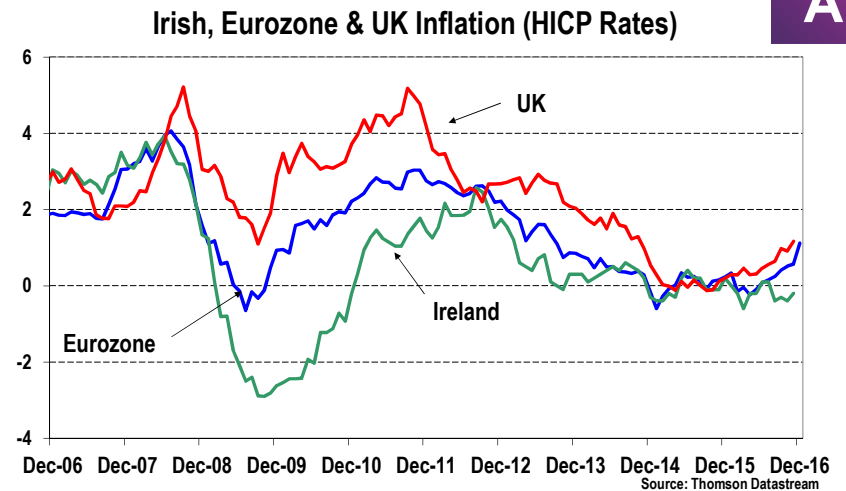
- Key will be the trade arrangements put in place between EU and UK post Brexit
- Ideally, UK would retain access to Single Market and UK/Irish common travel area remains
- Indications from EU that talks on new trade deal can only begin after UK leaves
- Thus, exit deal likely to contain only transition or interim arrangements on trade
- UK Government has put the emphasis on regaining control over immigration and return of full sovereignty and thus could lose access to Single Market – hard Brexit
- An interim/transitional trade deal will be difficult to conclude if UK continues to insist on regaining control over immigration and full independence for country
- Hard Brexit would see UK leaving the EU Customs Union and Single Market
- UK would have to fall back on WTO rules in a hard Brexit, which require a common set of tariff rates to be applied to all countries where no free trade deals exists
- This would be bad news for Irish/UK trade as could see imposition of tariffs, customs duties
- Main upside is that Brexit would make Ireland more attractive for FDI vis-à-vis the UK
- Lower Irish growth likely during 2016-19 in run-up to Brexit
- Long term impact will depend on the trade arrangements put in place post-Brexit



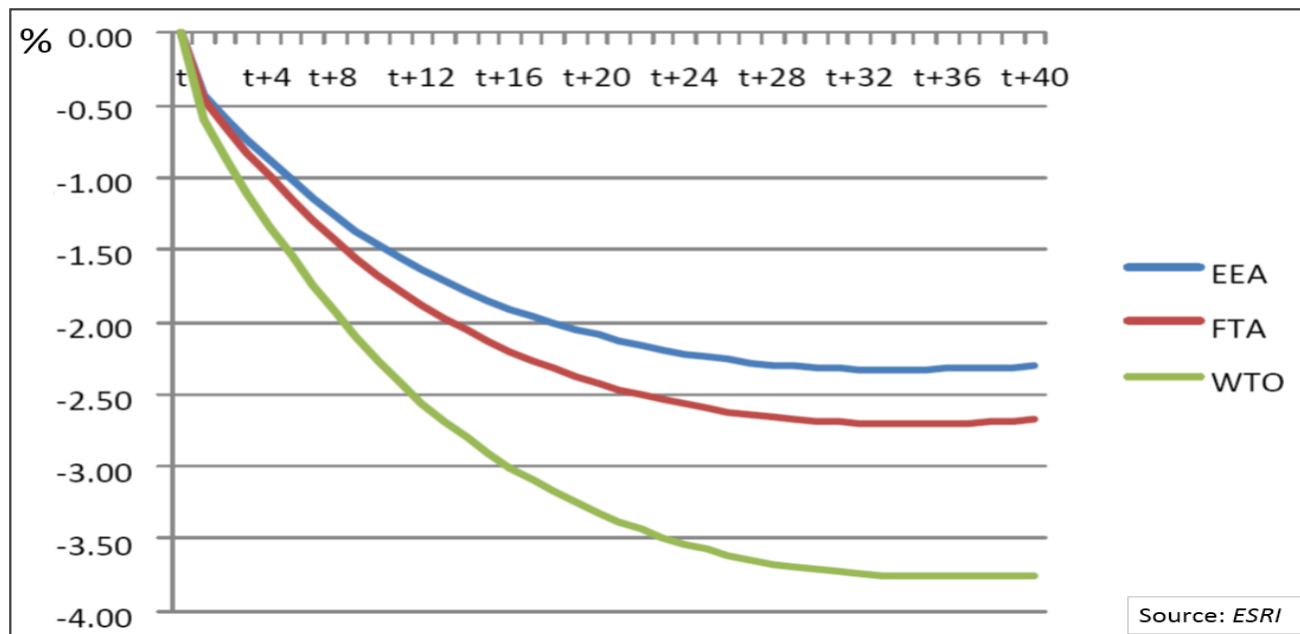
# Somewhat slower Irish growth likely ahead of Brexit



- Rebound by Irish economy should continue
- Construction picking up from still low output levels
- Budgetary policy turns mildly expansionary
- Activity supported by low interest rate environment
- FDI strong despite concerns on corporate tax
- Irish inflation remains very low, below that of the Eurozone and UK
- OECD and IMF forecasting that global growth will improve in 2017 and 2018
- However, Brexit is a major challenge for economy
- Sharp fall in sterling impacting exports to UK, tourism from UK, firms competing with UK imports
- Irish economy slowed somewhat in 2016 on weaker global activity, sterling's fall and Brexit uncertainty
- Irish GDP growth forecast to slow further to 3.0-3.5% in 2017-19 period as Brexit continues to impact



## Actual Brexit could have big impact on Irish economy



- ESRI-D/Finance estimate Irish output would be reduced by over 2% on a soft Brexit
- Sharp fall-off in trade with UK likely on a hard Brexit
- Output almost 4.0 % lower over time if there is hard Brexit and a fall back on WTO rules
- Employment 2% lower and unemployment nearly 2% higher

# AIB Irish Economic Forecasts



<i>% change in real terms unless stated</i>	2013	2014	2015	2016 (f)	2017 (f)	2018 (f)
<b>GDP</b>	<b>1.1</b>	<b>8.5</b>	<b>26.3</b>	<b>4.5</b>	<b>3.5</b>	<b>3.0</b>
GNP	4.7	9.2	18.7	8.0	3.5	3.0
Personal Consumption	-0.8	1.7	4.5	3.2	3.0	2.5
Government Spending	0.1	5.4	1.1	4.5	1.5	1.5
Fixed Investment	-5.4	18.2	32.7	6.0	6.0	5.5
Core Fixed Investment*	22.6	14.4	18.3	-1.0	6.0	5.5
<b>Core Domestic Spending*</b>	<b>2.3</b>	<b>4.2</b>	<b>6.6</b>	<b>3.0</b>	<b>3.7</b>	<b>3.3</b>
Exports	3.1	14.4	34.4	2.5	4.0	4.0
Imports	1.1	15.3	21.7	2.5	4.0	4.0
HICP Inflation (%)	0.5	0.3	0.0	-0.2	0.5	0.8
Unemployment Rate (%)	13.1	11.3	9.5	8.1	7.2	6.7
Budget Balance (% GDP)	-5.5	-3.7	-1.8	-0.9	-0.5	-0.3
Gross General Gov Debt (% GDP)	119.5	105.2	78.7	76	73	70

\*Excludes investment in aircraft and intangibles

Source: CSO, AIB ERU Forecasts

## Risks to the Irish economic recovery



- 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
- Recovery in the global economy still quite fragile, with on-going risks and headwinds, including weakness of emerging economies. Ireland vulnerable to any shocks that impacts its exports
- Possibility of reduced FDI from US if a new Trump administration slashes corporate taxes
- Questions around corporation tax regime (eg Apple ruling) could impact FDI but seems unlikely
- Supply constraints in the construction sector, especially new house building, which is recovering at a very slow pace and remains at depressed levels
- Competitiveness issues - high house prices, high rents, high personal taxes
- Continuing credit contraction – fewer banks, tighter credit conditions, on-going deleveraging

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.