The Irish Economic Update

Growth should remain impressive, but may not be as strong as in recent years

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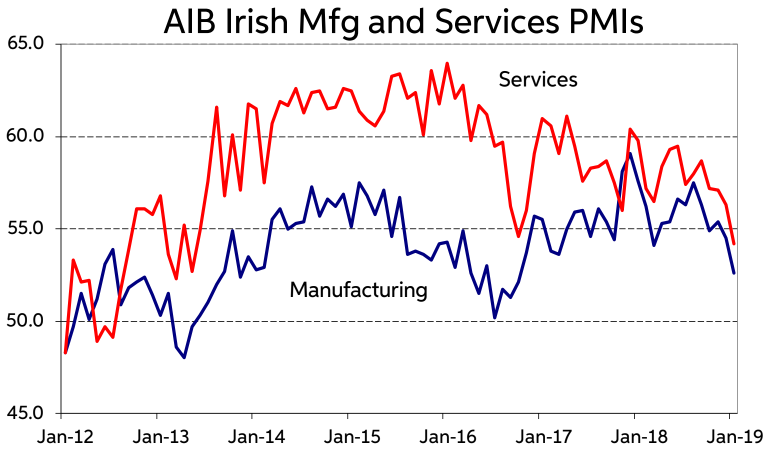
Oliver Mangan
Chief Economist
AIB

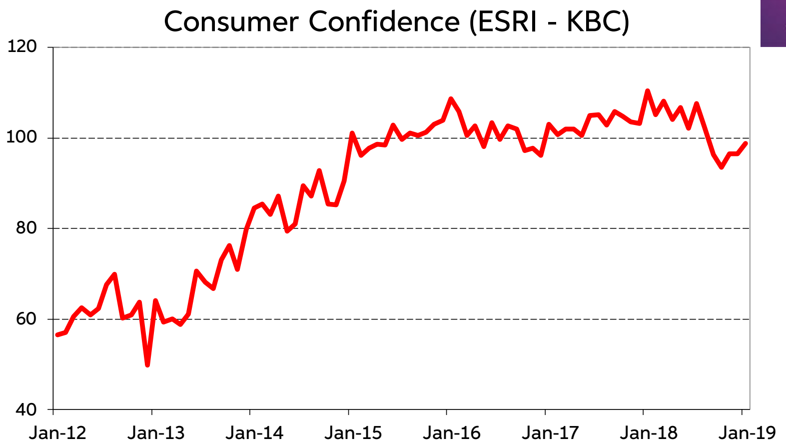
Strong growth by Irish economy in 2013-2018 period

- 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 grew very strongly over 2013-18 – underlying growth averaged 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 5.7% in H2 2018
- Budget deficit eliminated at a quicker than expected pace. Small surplus recorded in 2018

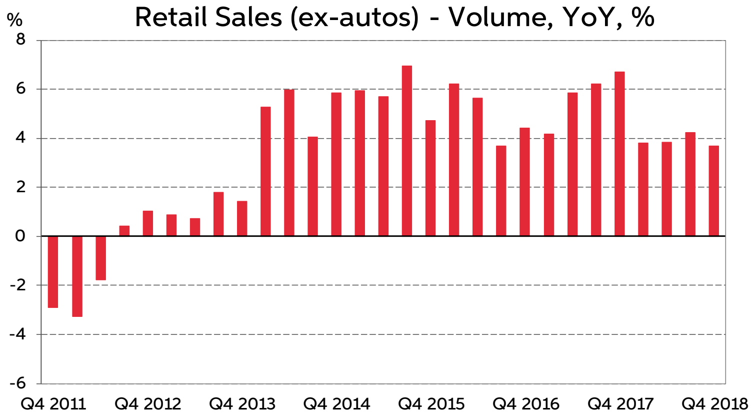
Survey indicators suggest growth may have peaked



Source: *Thomson Datastream, Investec*



Source: ESRI - KBC, Thomson Datastream



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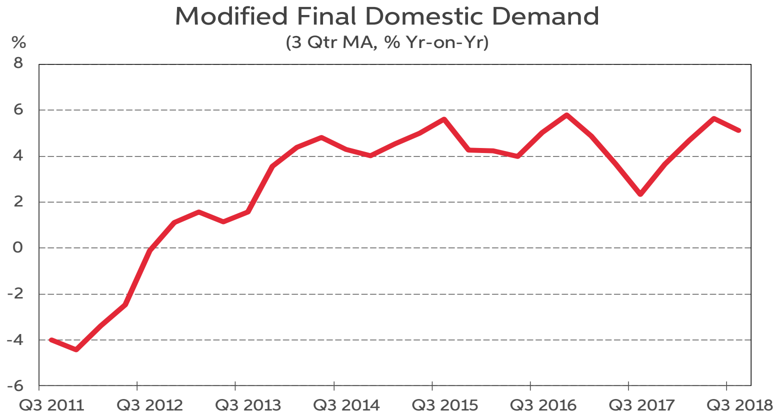


Source: CSO, (Excludes I.P. imports & Aircraft Leasing)

Signs recently that growth is starting to moderate

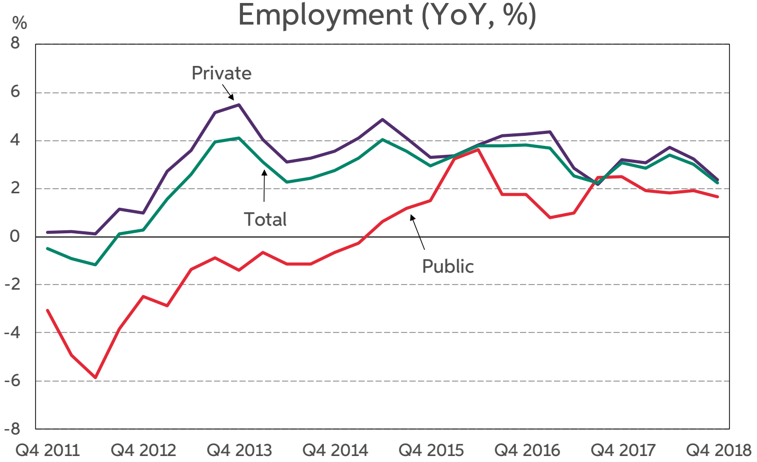
- Modified final domestic demand grew by 5% yoy in Q1-Q3 2018
- Continuing strong job growth last year – employment rose by 2.9% in 2018, but slowed in H2
- Further strong rise in housing completions in 2018– increased by 25% to over 18,000 units
- Mortgage lending up by 20% to €8.7bn in 2018, after rising by 29% in 2017
- Retail sales (ex-motor trade) rose strongly again last year, increasing by 3.9%
- Total car sales (new + second hand imports) fell 10% yoy in Jan 2019 from 2017-18 high levels
- Mfg PMI declined in closing months of 2018 and fell further to 52.6 January, an over 2-year low
- Services PMI also weakened in late 2018, and hit a near 6-year low in January of 54.2
- Construction PMI down too in recent months from last summer's high levels – at 54.6 in January
- Consumer confidence also falls back from summer highs, though still at strong level in January
- Unemployment rate unchanged at 5.7% since August, though Live Register has continued to fall
- Strong growth in tax receipts in January – up 7% yoy – with budget surplus virtually unchanged

Strong jobs growth; unemployment rate down to 5.7%

Year Average	2015	2016	2017	2018(f)	2019(f)	2020(f)
Unemployment Rate %	10.0	8.4	6.8	5.8	5.3	5.1
Labour Force Growth %	1.2	1.9	1.1	1.8	1.9	1.7
Employment Growth %	3.5	3.7	2.9	2.9	2.3	2.0
Net Migration : Year to April ('000)	5.9	16.2	19.8	34.0	38.0	40.0

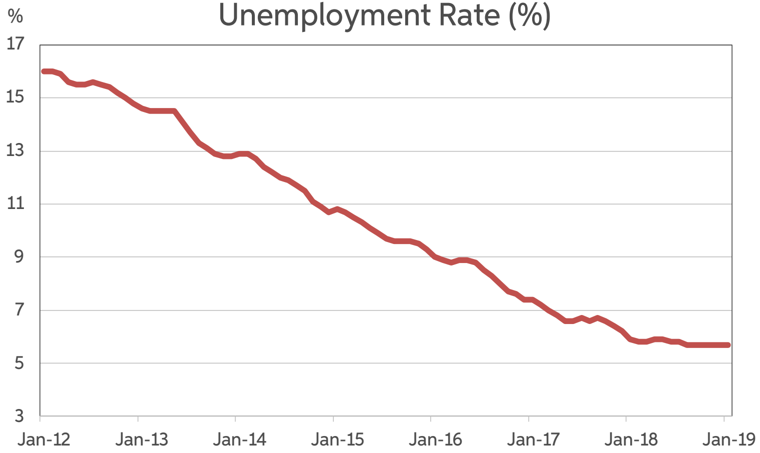
Source: CSO and AIB ERU forecasts

Employment (YoY, %)



Source: CSO via Thomson Datastream

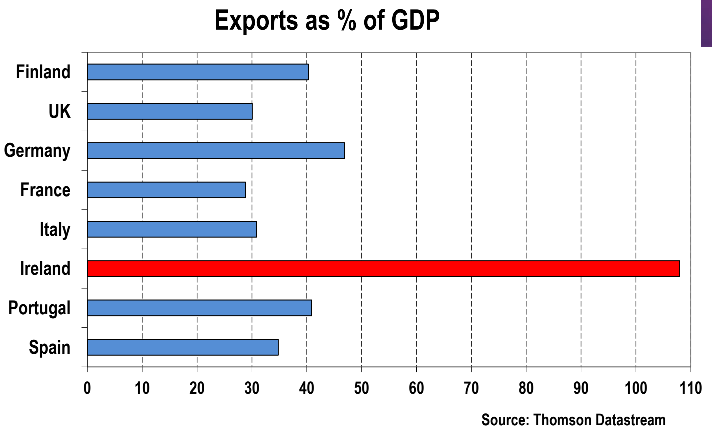
Unemployment Rate (%)

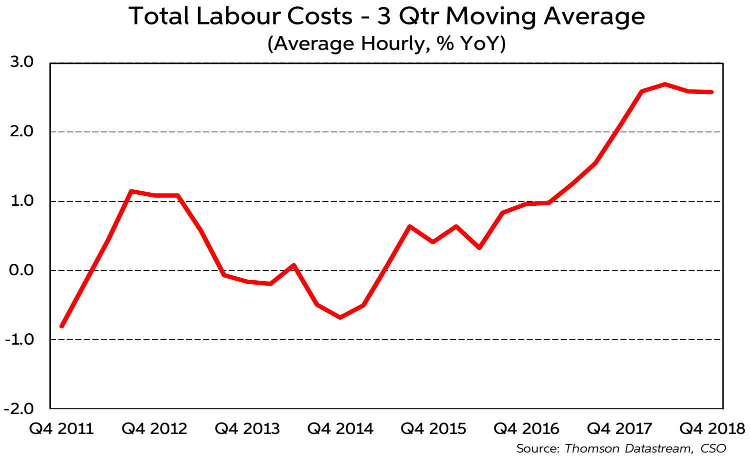


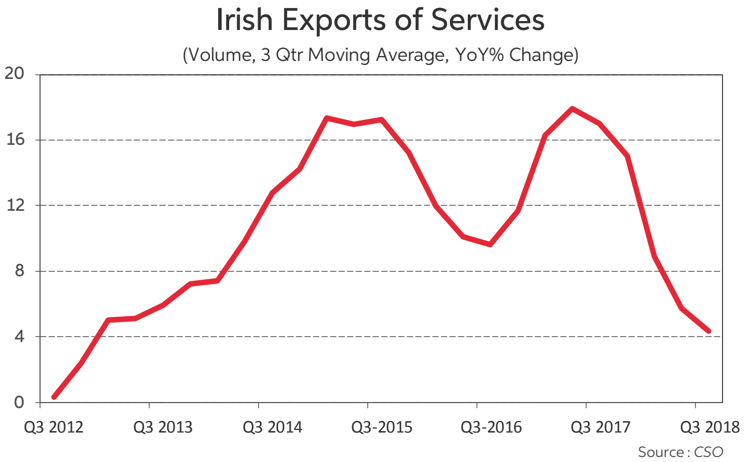
Source: CSO via Thomson Datastream

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 - 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

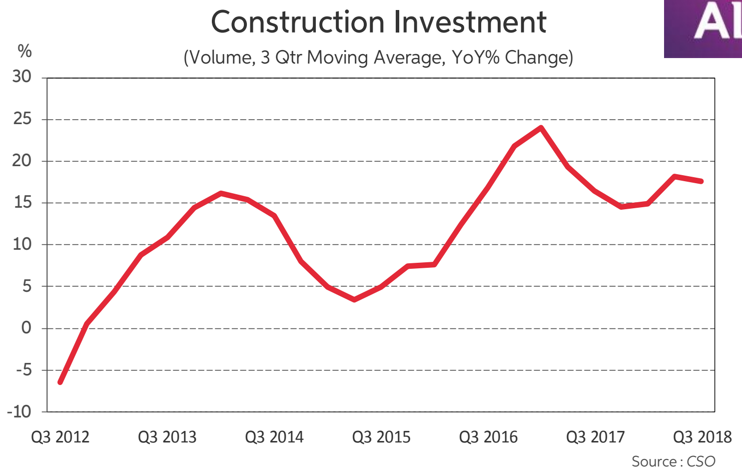
- US firms have well established operations here
- Need highly skilled, multi-lingual workforce
- Firms do not move Ireland to avoid US tax
- Ireland is base to service their European markets
- Easier to operate in local rather than US time zone
- Still wide gap between US & Irish corporate tax rates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

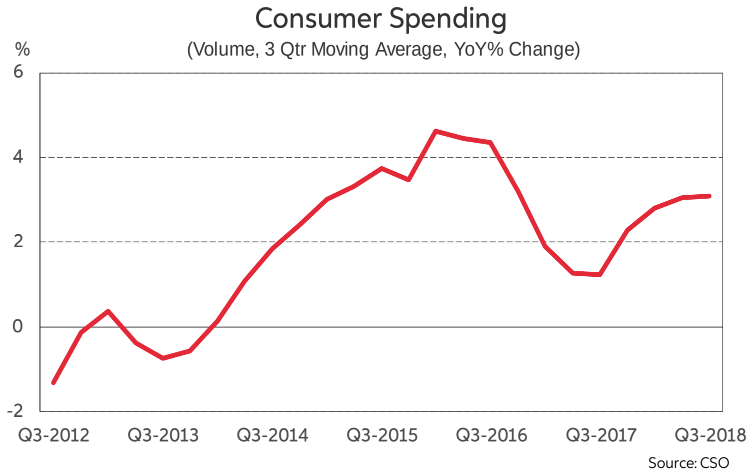
Many top global companies have big operations in Ireland

eBay
Abbott
Pfizer
Boston Scientific
Google
gsk GlaxoSmithKline
citi
ZURICH
BNY MELLON
DELL EMC
IBM
intel
ANALOG DEVICES
SAP
NOVARTIS
Microsoft
SIEMENS
accenture
Johnson & Johnson
STATE STREET

Strong performance by domestic economy since 2013

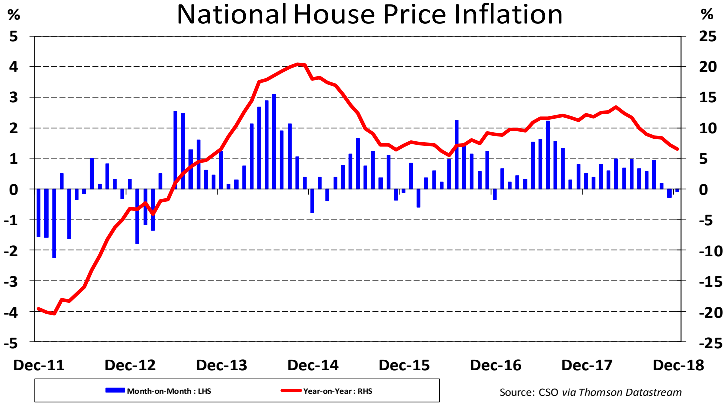
- Domestic economy contracted by 20% in period from 2008-2012, with particularly big fall in construction
- Construction sees strong recovery since 2013. Output up by 15% in 2016 & 2017 and 17% in Q1-Q3 2018
- Difficult year for agricultural sector in 2018, but comes after very strong growth in 2014-17 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, but fell by 10% yoy in January 2019

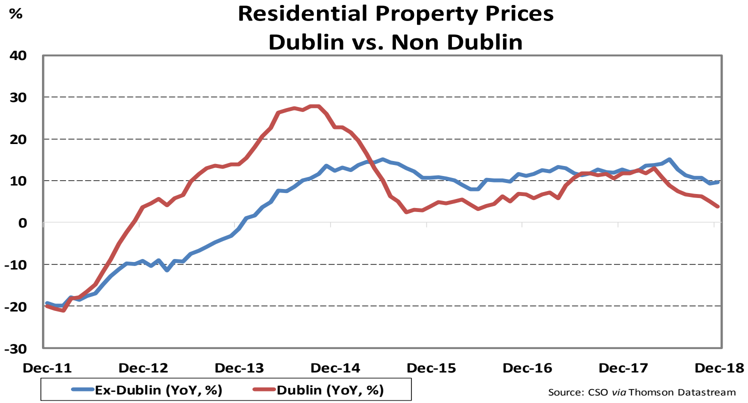




High house price inflation slowed during 2018

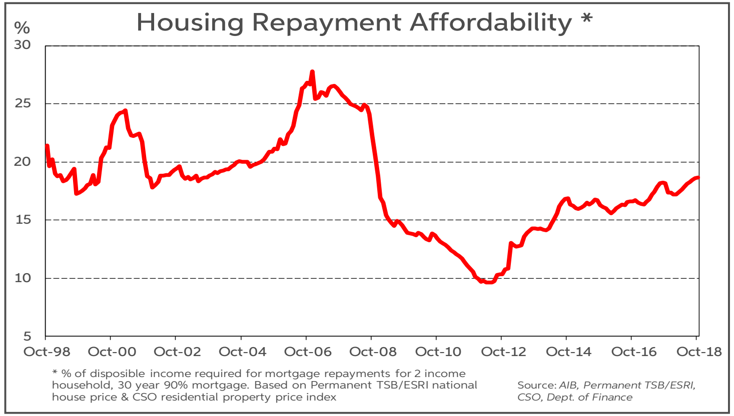
- House prices declined by a very sharp 55% between their peak in late 2007 and early 2013
- House prices have since rebounded as big housing shortage emerged after 90% fall in house building
- Small stock for sale, house building still at low level
- Prices up 83% by December from low in March 2013 –Dublin prices up by 95%, non-Dublin rise 80%
- House prices nationally still 18% below 2007 peak
- House price inflation moderated last year as Central Bank lending rules and affordability impacted
- Prices up 6.5% yoy nationally in December 2018, down from recent high of 13.3% in April
- Dublin up 3.8% yoy, down from 14% in April, while non-Dublin slows from 15.4% in June to 9.6% yoy
- Rents have also rebounded strongly – now over 26% above previous peak reached in 2008 per CSO data





House building rising steadily, but still at quite low level

- Housing completions rose by 25% to over 18,000 in 2018, having increased by 45% to 14,400 in 2017
- Housing commencements on rising trend: up by 33% in 2017 to 17,500 and by 29% to 22,500 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 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 last year
- 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



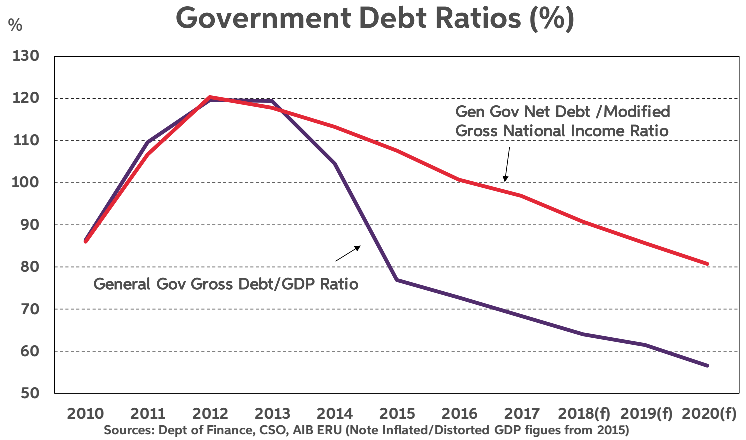
AIB Model of Estimated Housing Demand

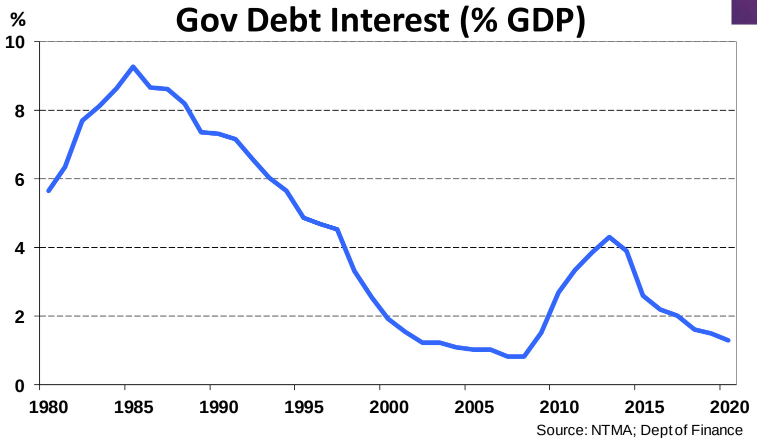
- Rising headship rates added circa 8,000 per year to housing demand in 2002-2011 period
- Shortage of housing, high rents, tighter lending rules saw average household size rise in 2011-16. Thus, headship fell – was a drag of circa 10,000 p.a. on housing demand
- Assume no change in headship in 2016-2020 – 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

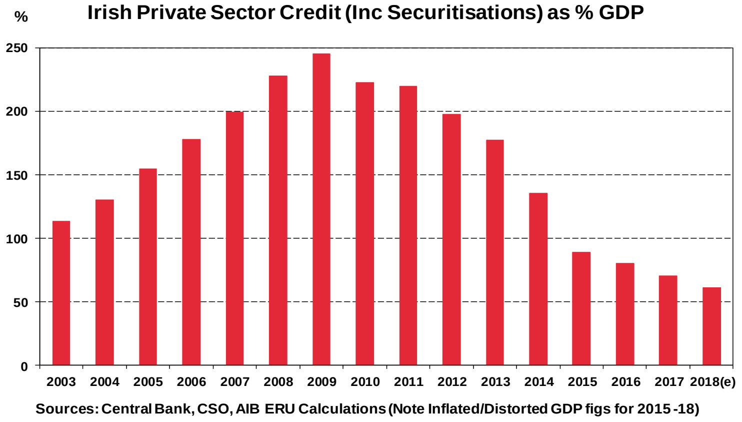
Calendar Year	2016	2017	2018	2019	2020
Household Formation	26,500	26,500	26,500	27,500	27,500
of which					
Indigenous Population Growth	*18,000*	*18,500*	*17,500*	*16,500*	*14,500*
Migration Flows	*8,500*	*9,500*	*12,000*	*13,000*	*13,000*
Headship Change*	*0*	*0*	*0*	*0*	*0*
Second Homes	500	500	500	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**	**14,400**	**18,100**	**22,500**	**27,000**
Shortfall in Supply	***-22,100***	***-19,100***	***-16,900***	***-12,500***	***-6,000***

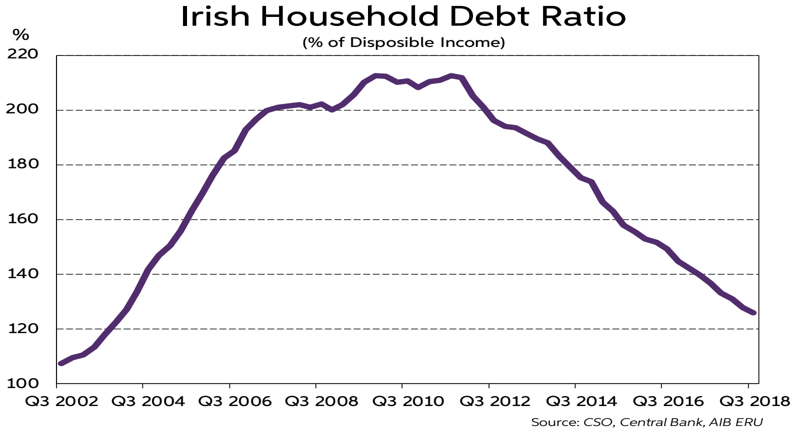
**Headship is % of population that are heads of households.* *Sources: CSO, DoECLG, AIB ERU*

Govt debt ratios fall, private sector deleverages



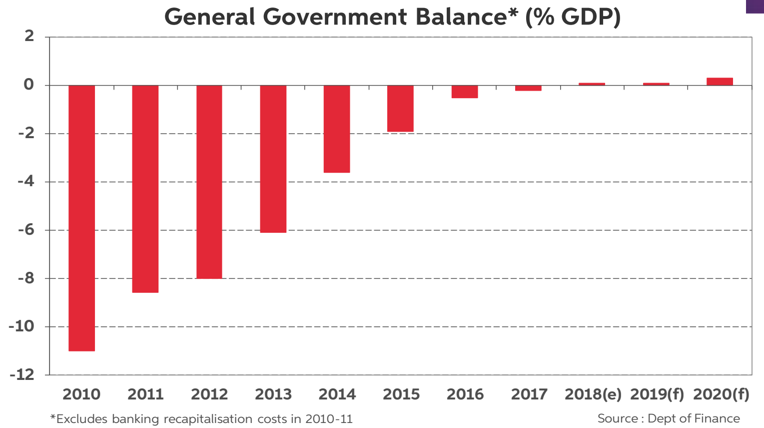


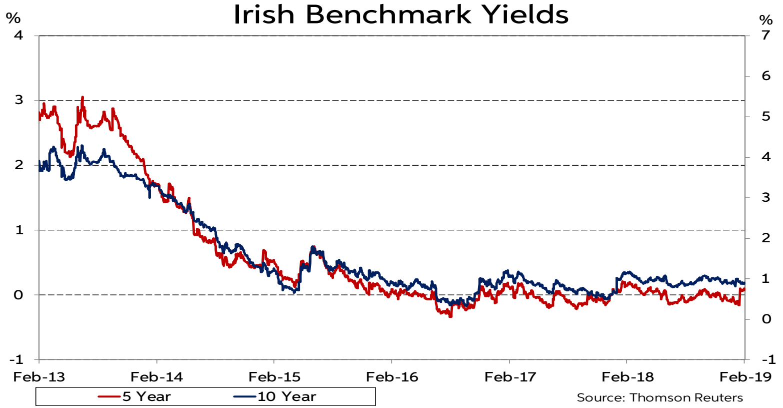




Budget returned to surplus in 2018

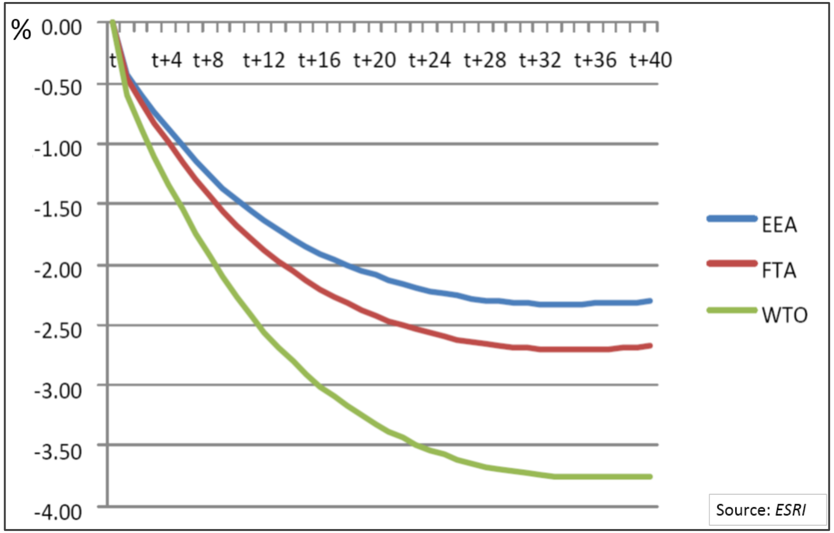
- Some €30bn (18% of GDP) of fiscal tightening implemented in 2008-2014 period
- Budget deficit has fallen sharply over past decade. Fell to 0.2% of GDP in 2017
- A small surplus was recorded in 2018, estimated at 0.1% of GDP
- Primary budget surplus (i.e. excluding debt interest) of 1.5% of GDP in 2018
- 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)*



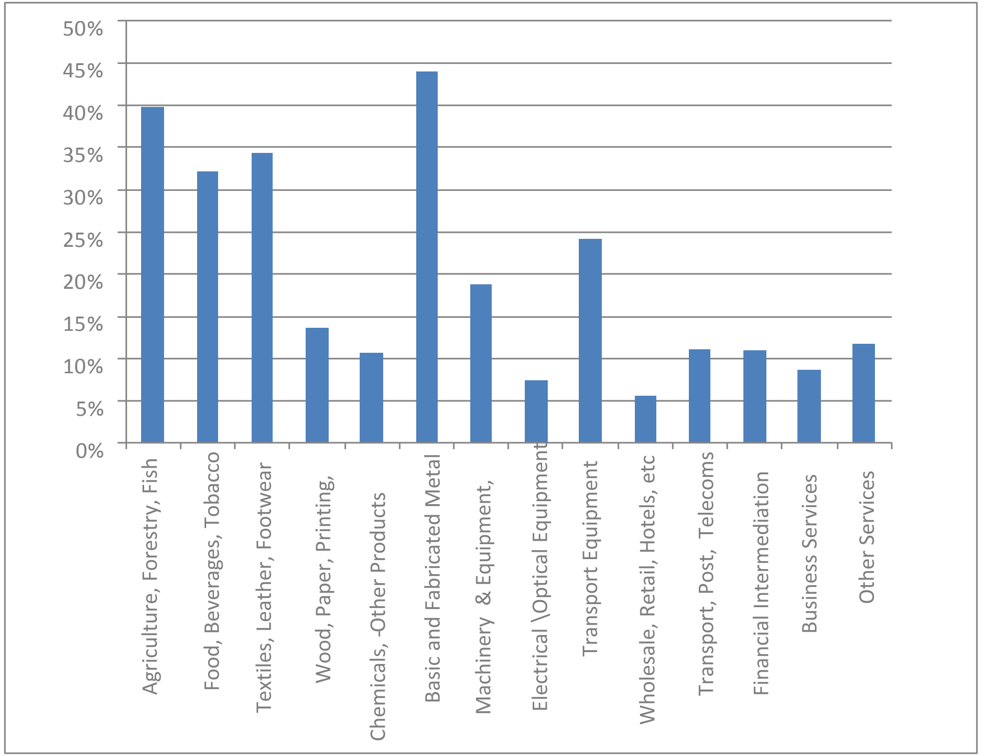
- **ESRI** estimate that Irish output would be reduced over time by 2-2.5% on a soft Brexit
- Sharp fall-off in trade with UK likely on a no-deal, hard Brexit
- Output almost 4.0 % lower over time if there is hard Brexit and a fall back on WTO rules and tariffs
- **Central Bank** say a disorderly hard 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 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 – Q4 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.

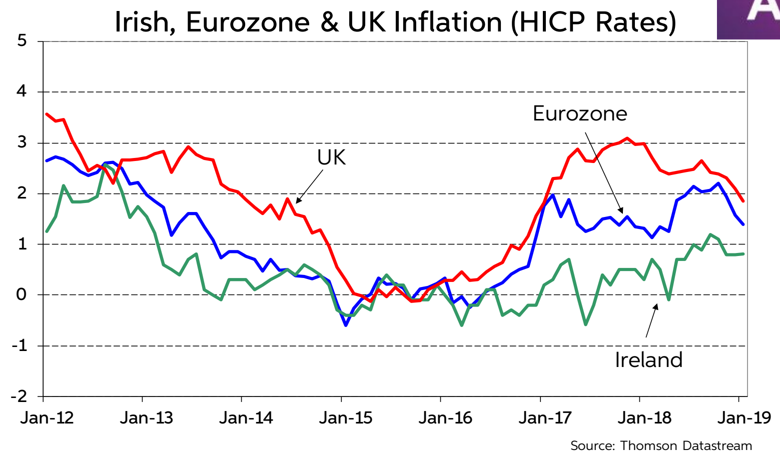
- **Consistent very negative sentiment readings, though firms say Brexit is having little impact to date on their businesses**
- **SMEs are very concerned about its impact in the future, both on their own business & the wider economy**
- **35% of RoI and 40% of NI firms who had investment plans say they have been cancelled or postponed owing to Brexit**
- **Food & Drink, Tourism and Retail are the sectors most concerned about Brexit**

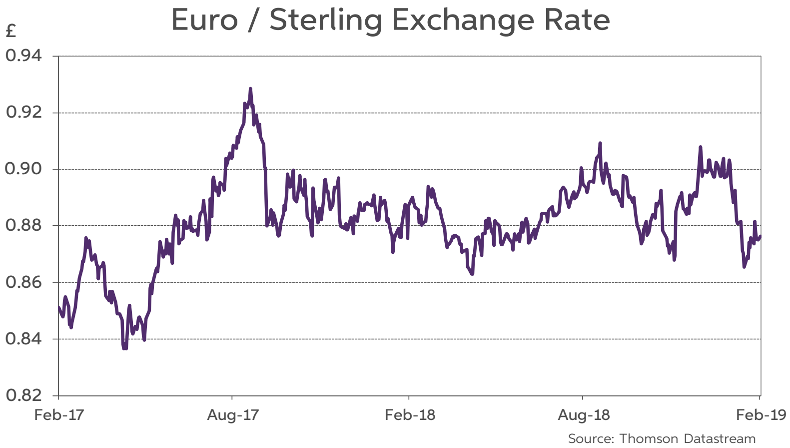
Still much uncertainty about Brexit

- UK wants 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 EU. UK looking to re-negotiate the backstop. EU rules this out
- PM has said she will bring WA back to Parliament for a fresh vote by March 12th. If WA is still not passed by Parliament, votes to follow to have a no deal hard Brexit or seek delay to Brexit
- Delay to Brexit will need extension to Article 50. Likely to be for 2-3 months period only
- Still a lot of uncertainty about Brexit. Likely to be delayed if WA not ratified by March 12th
- Could still be a hard Brexit if WA is not ratified by end of any extended period. Difficult EU-UK trade talks also in prospect post Brexit, even if WA eventually ratified. Customs still big issue

Good Irish growth to continue if external risks avoided

- Irish economy should continue to grow at impressive pace, but not as strongly as in recent years
- Construction picking up from still low output levels
- Public spending on the rise
- Activity supported by low interest rate environment
- Continuing strong inflows of FDI
- 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 avoids downturn given importance of exports to Ireland
- GDP growth forecast at 4.0% for 2019 and 3.5% in 2020, assuming hard Brexit/global downturn avoided
- 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 (e)	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	1.3
Unemployment Rate (%)	8.4	6.8	5.8	5.3	5.1
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
- Slowing external environment with growing downside risks to global growth from increasing protectionism/tariffs, tighter 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