The Irish Economic Update

Growth Slowing as Brexit Looms

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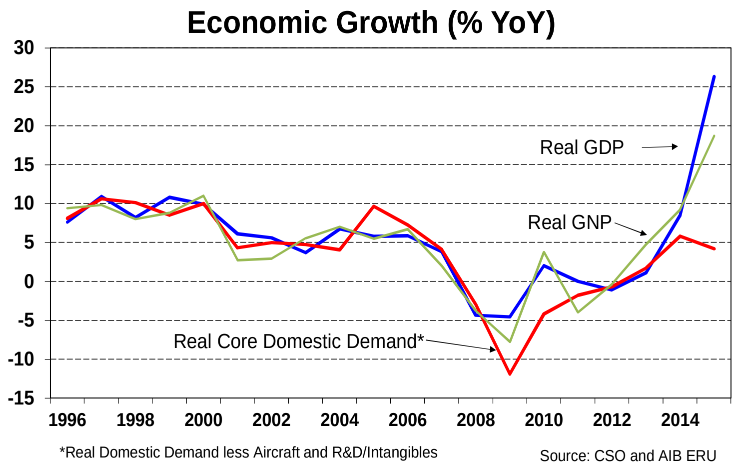
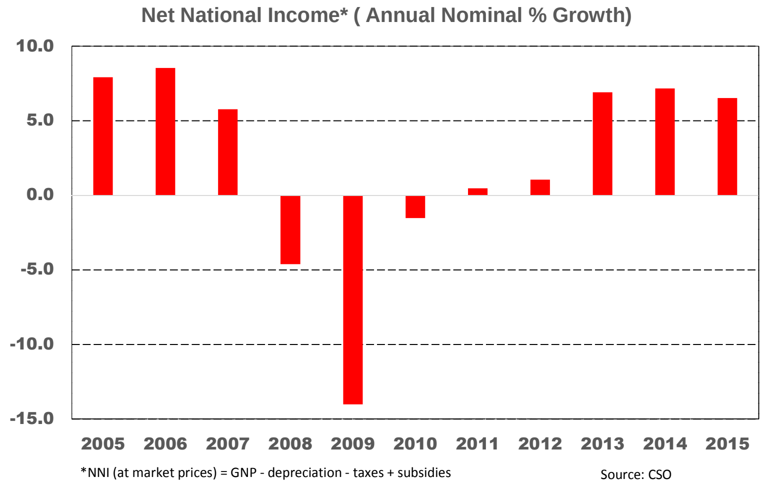
Strong recovery by Irish economy since 2013

- 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 7.7% in late 2016
- Budget deficit has declined at quicker than expected pace. Circa 1% of GDP in 2016

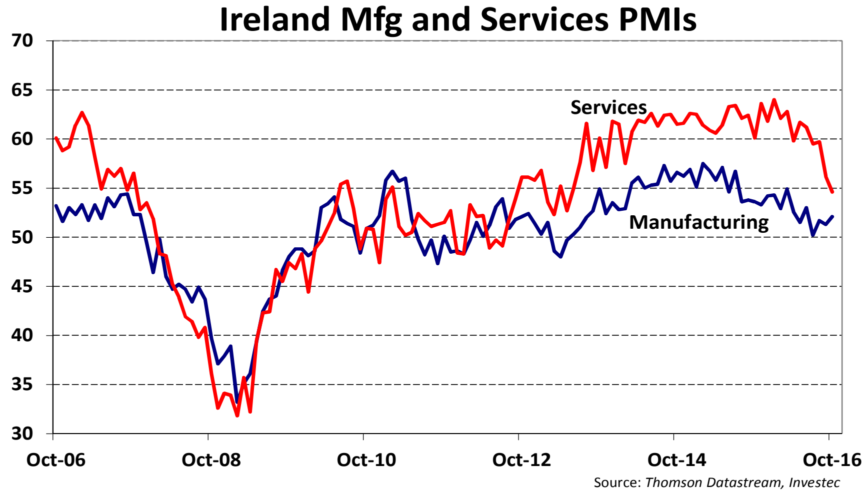
Huge distortions inflate Irish GDP/GNP figures

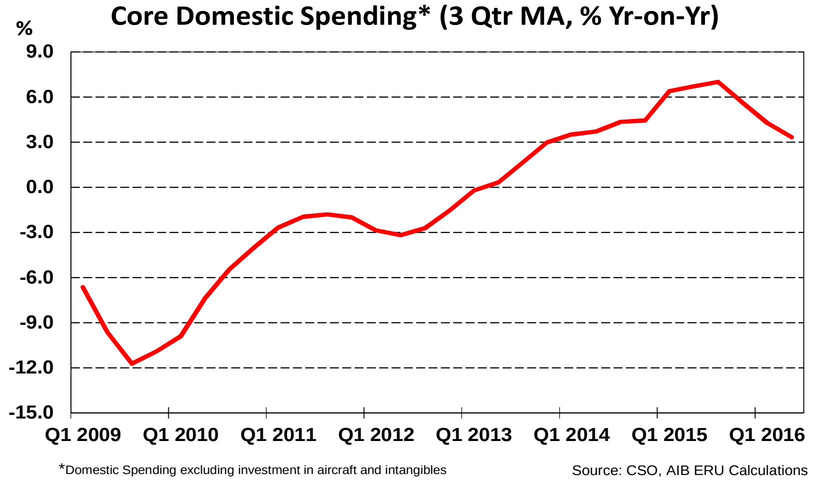
- GDP/GNP no longer reliable measures of output in Ireland. Review underway of National A\Cs
- Exports, imports, industrial production, investment, BoP distorted by activities of some multi-nationals
- Contract manufacturing also distorting trade data
- Aircraft leasing, R&D and intangibles such as patents, distorting investment figures
- Better measures of economic activity required that strip out distorting effects of multi-nationals
- We focus on core domestic demand/spending. Net national income/product also useful
- Growth in core domestic spending averaged around 5% in 2014-15
- Signs of a slowdown in growth this year, notably consumer spending and business investment

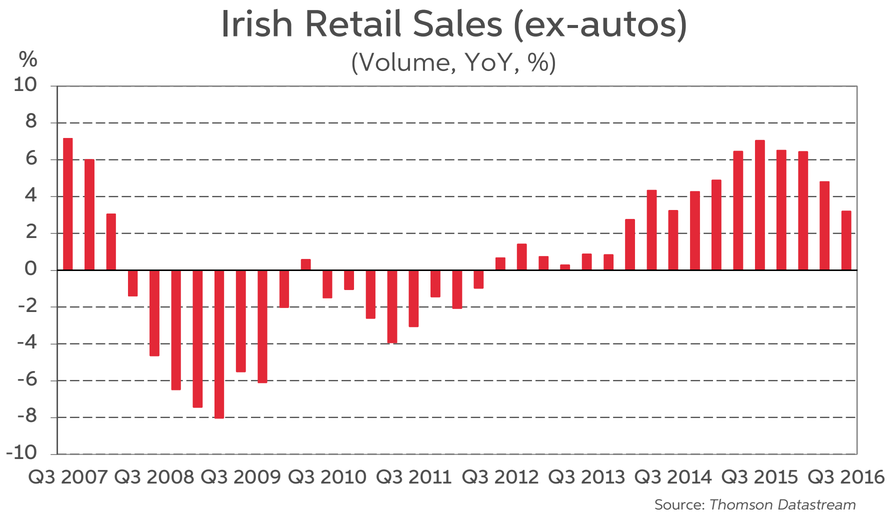


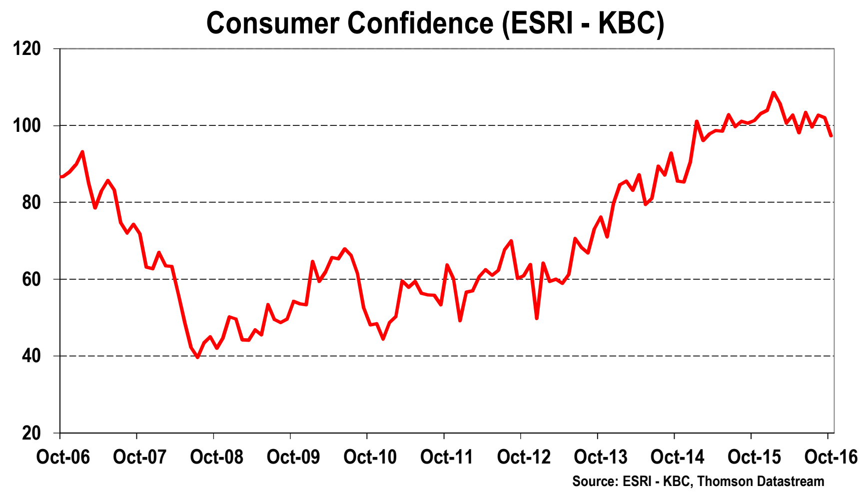


Signs that Irish economy slowed during 2016









Mixed tone to recent data

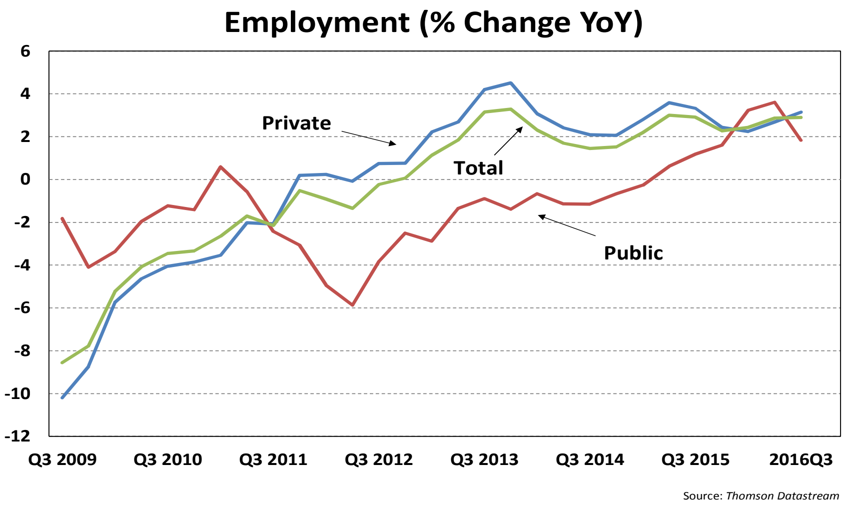
- GDP growth averaged solid 4% year-on-year in H1 2016
- Good manufacturing PMI data in Q1 2016 but at lower levels since then – 52 in October
- Very robust services PMI in H1 2016 but falls sharply in H2 – hits 4 year low in October
- Slower growth in service exports of 5.8% yoy in H1 2016 after a big rise in 2015
- Construction PMI performing strongly – averaged over 60 in H1 2016. Close to 60 in Q3
- Consumer confidence remains strong but has fallen back from 15 year highs hit in Q1
- Core retail sales (ex motor trade) decline in Q3 after strong growth in 2015 & H1 2016
- Growth in car sales slows since the spring after 30% jump in both 2014 and 2015
- Housing completions up by 18% yoy in first nine 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 7.3% in November – peaked at 15.1%
- Slower growth in tax receipts since early summer but still ahead of target in 2016

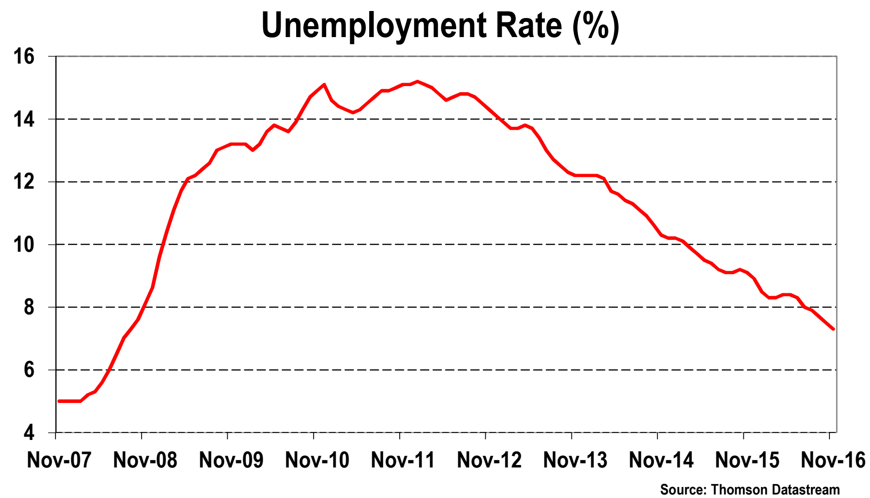
Strong jobs growth continues; unemployment falls

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

** Employment ex Agriculture +1.3% in 2013*

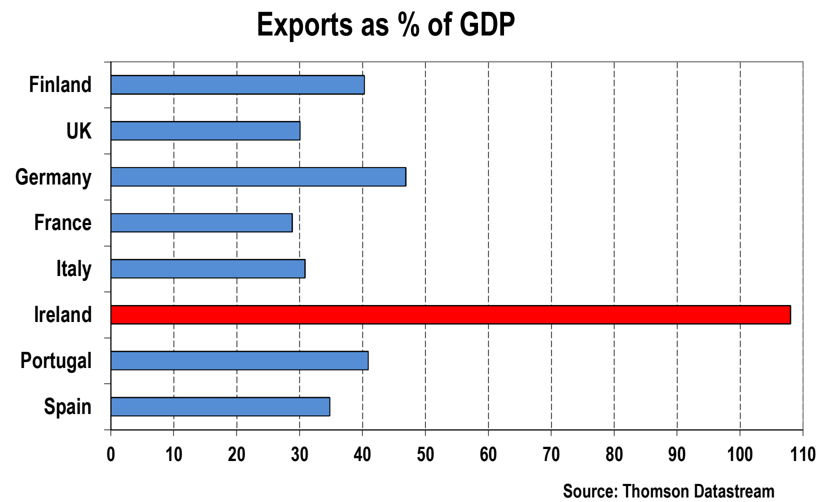
Source: CSO and AIB ERU forecasts

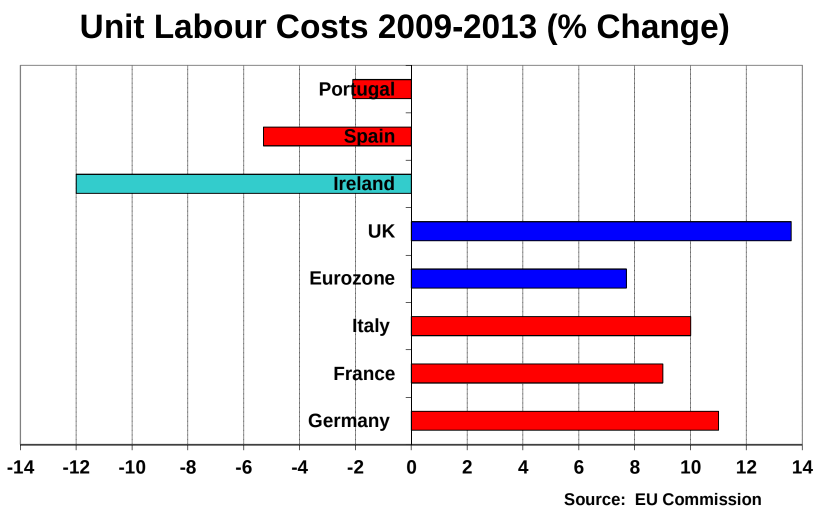


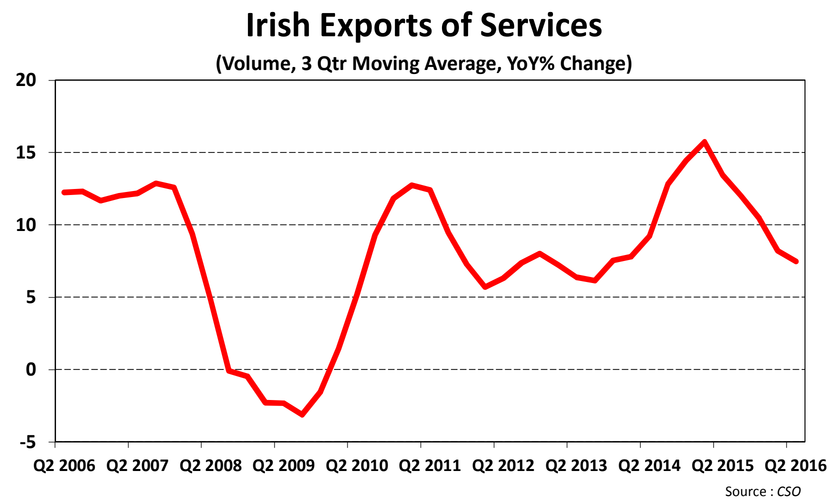


Large Irish export base performs strongly

- 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







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 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
- €125bn Exports (70% of Irish exports)
- 175,000 Jobs in FDI, 290,000 in total
- 70% of Corporation Tax
- €13.5bn Spending on services/materials
- €8.5bn 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 appealing to repatriate profits if US taxes cut

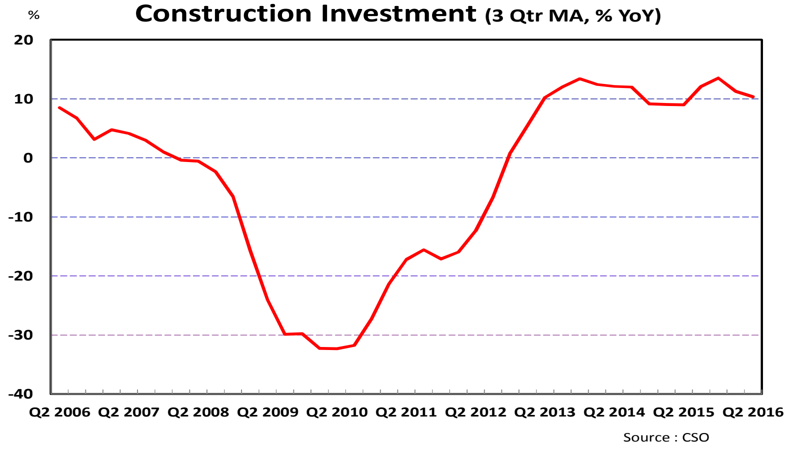
Many top global companies have big operations in Ireland

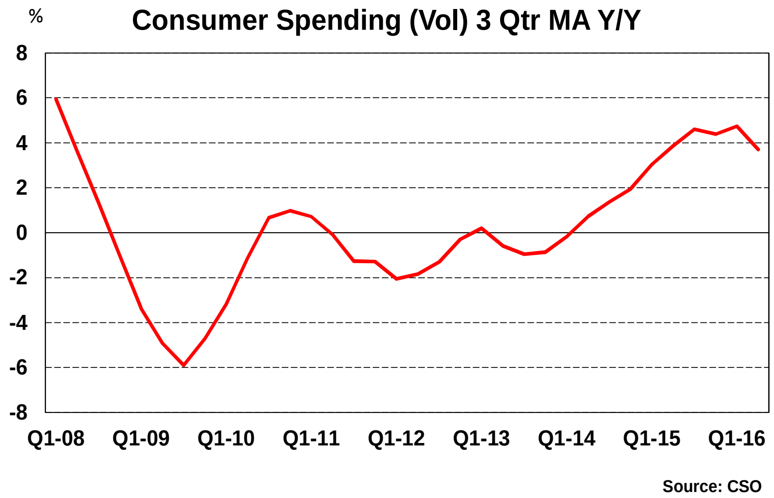
AIB

ebay
facebook
Abbott
Pfizer
Boston Scientific
gsk GlaxoSmithKline
BNY MELLON
Google
citi
ZURICH
EMC2 where information lives
DELL
IBM
intel
ANALOG DEVICES
SAP
NOVARTIS
Microsoft
SIEMENS
accenture
Johnson & Johnson
STATE STREET

Slower growth in domestic economy this year

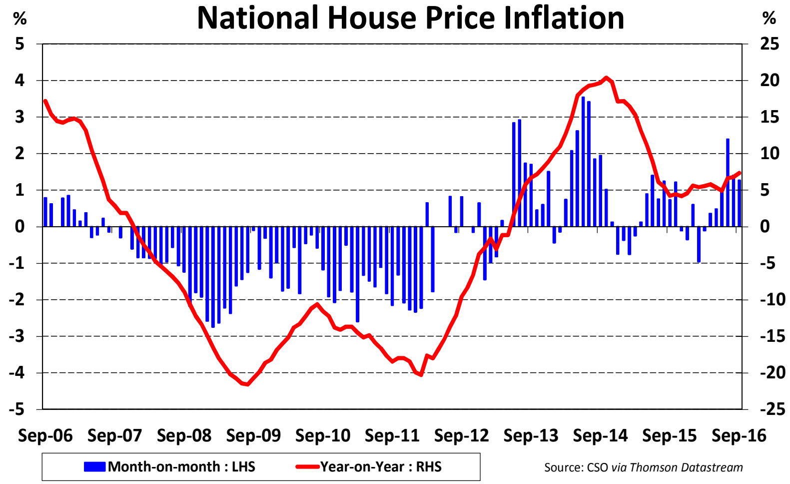
- Domestic economy contracted by 20% from 2008-12
- Collapse in construction was big drag on GDP - fell from 13.5% of GDP in 2005-07 to 5.3% by 2012
- Construction has seen steady growth since 2013 – output rose by over 10% in each of last three years
- Business investment (ex planes/R&D) more than doubled in 2013-2015 but falls back in H1 2016
- Consumer spending grew by 1.7% in 2014, 4.5% in 2015 and 3.5% yoy in H1 2016
- Core domestic spending (ex aircraft, R&D, Intangibles) averaged growth of 4.4% in 2013-2015
- Slower growth of 2.4% yoy in core domestic spending in H1 2016 as business investment falls
- Decline in retail sales in Q3 with new car sales also losing some momentum during the year

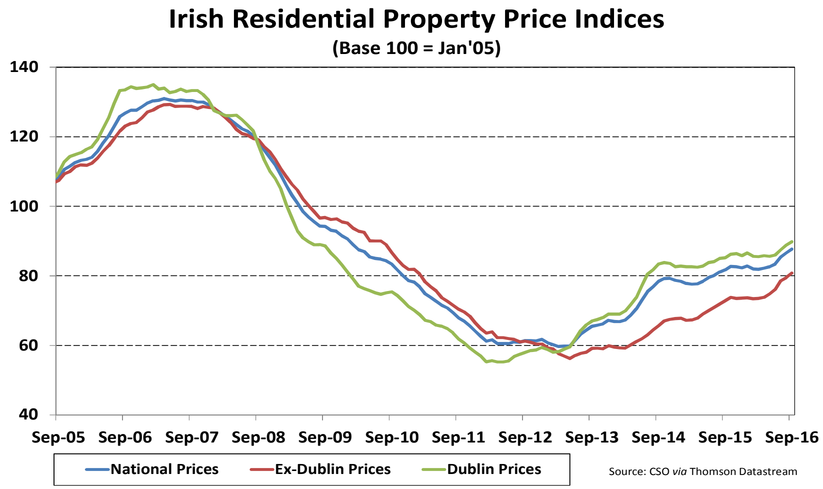




Prices rebound as major housing shortage emerges

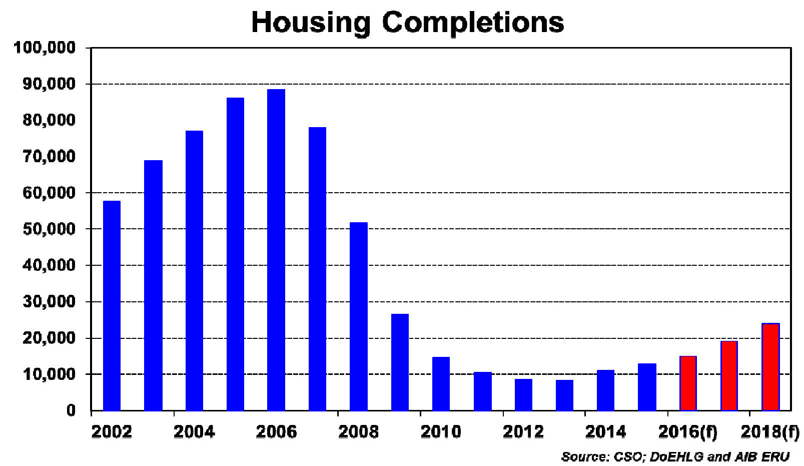
- Housing output fell by 90% but now past trough
- Bulk of the new housing stock overhang eliminated
- House prices declined sharply – fell by almost 55% between their peak in late 2007 and early 2013
- House prices rebound: up 47% by Sept 2016 from low in early 2013 as housing shortage emerges
- Dublin prices up by 63% from trough with non-Dublin prices up by 44%
- House prices, though, including in Dublin, are still some 33% below peak levels hit in 2007
- Central Bank mortgage rules cooled Dublin house price inflation – fell from 25% to circa 5% yoy
- Strong house price rises over the summer. Prices up 7.3% yoy nationally in September
- Rents have rebounded – now 11.5 % above previous peak reached in 2008

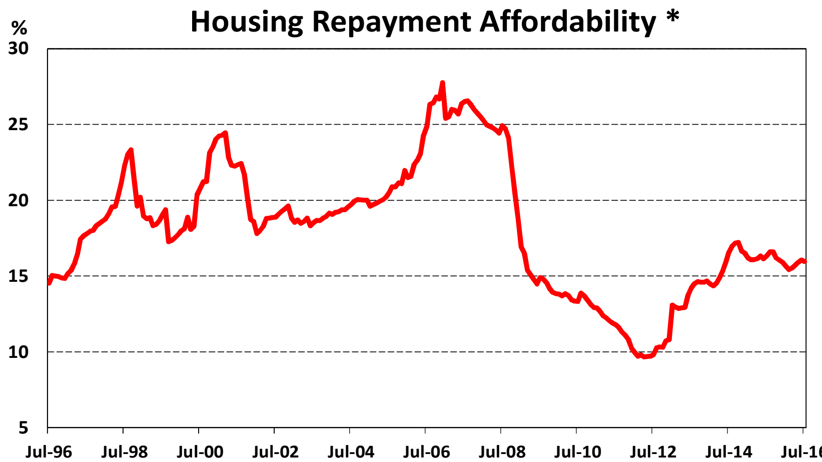




House building rising slowly from very low levels

- Housing completions at 12,700 in 2015, up from 11,000 in 2014 and 8,300 in 2013
- Completions up 18% to Sept 2016. Should reach 15,000 units this year but still at very low levels
- 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 to be relaxed while tax rebates introduced 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





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

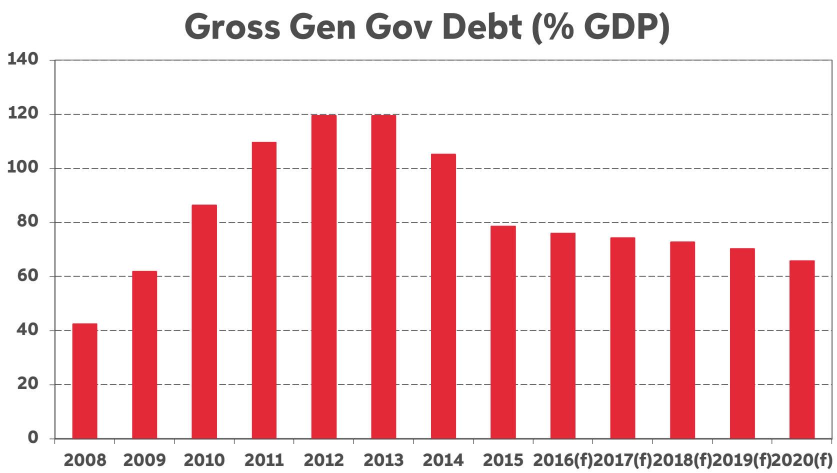
Source: *AIB, Permanent TSB/ESRI, CSO, Dept. of Finance*

AIB Model of Potential Housing Demand

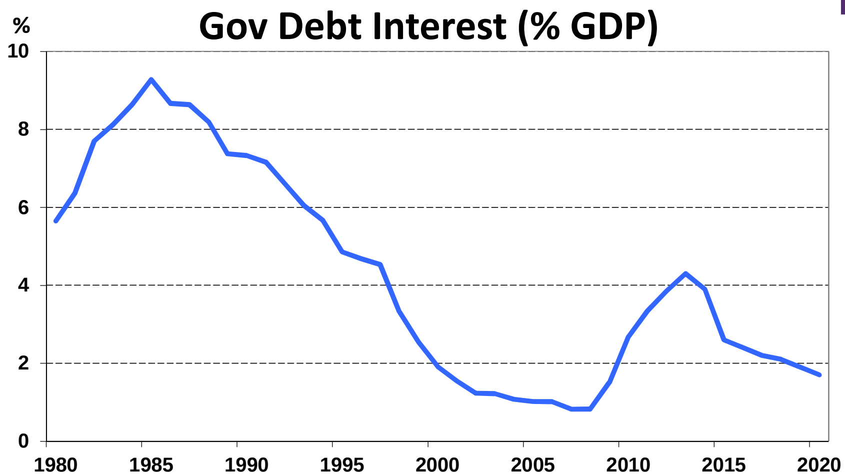
Calendar Year	2012	2013	2014	2015	2016	2017	2018
Household Formation	14,000	15,000	16,500	19,500	21,500	22,000	23,000
of which							
Indigenous Population Growth	*20,000*	*17,500*	*17,000*	*17,500*	*17,000*	*16,000*	*15,500*
Migration Flows	*-9,000*	*-5,500*	*-3,500*	*-1,500*	*1,000*	*2,500*	*3,500*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

Sources: CSO, DoECLG, AIB ERU

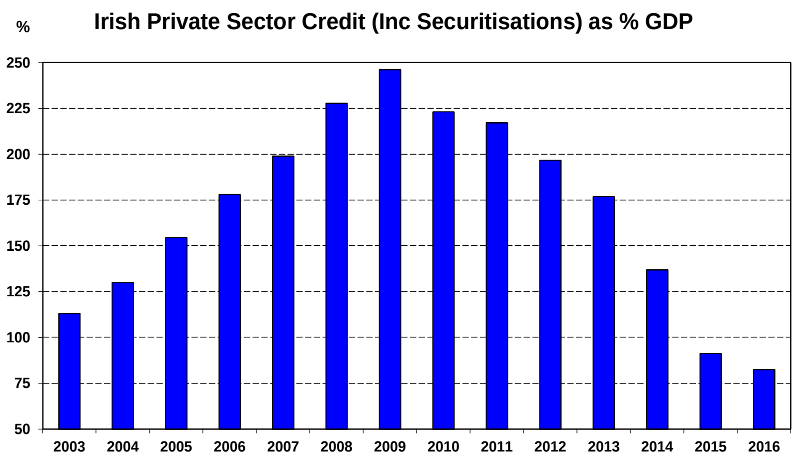
Gov debt ratio falling, private sector deleveraging



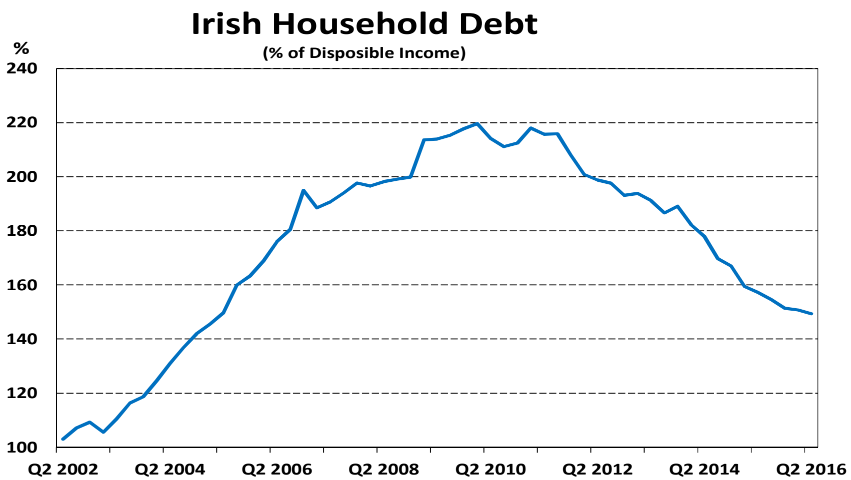
Source: Dept of Finance. (Note Inflated/Distorted GDP figues from 2015)



Source: NTMA; Dept of Finance



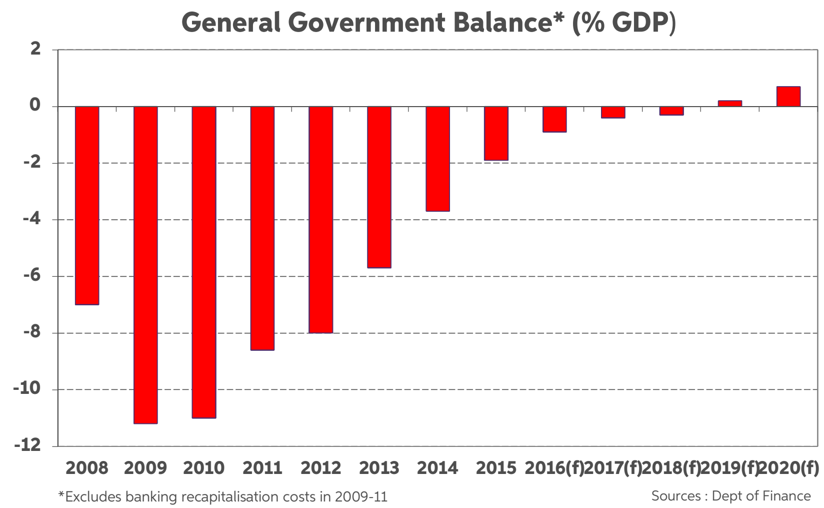
Sources: Central Bank, CSO, AIB ERU Calculations (Note Inflated/Distorted GDP figs in 2015/16)

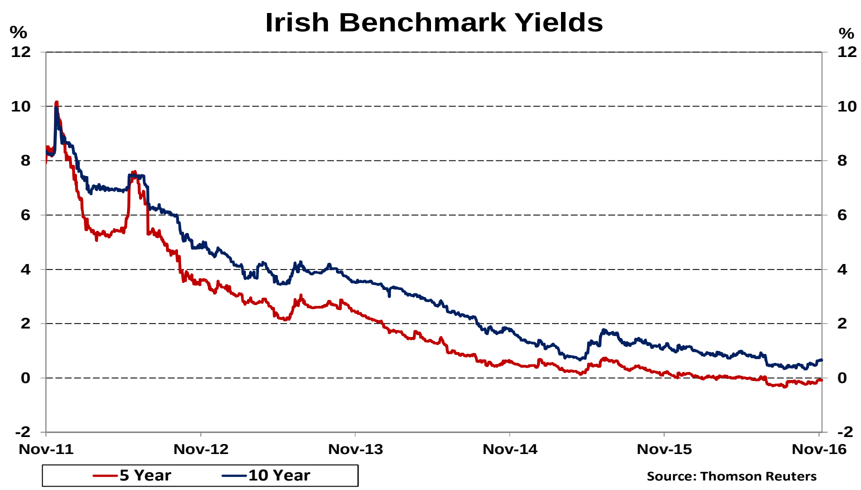


Source: *CSO, Central Bank, AIB ERU*

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 around 1% of GDP likely in 2016
- Budget deficit forecast at below 0.5% of GDP for 2017 and 2018
- Primary budget (i.e. excluding debt interest) surplus of circa 1.5% of GDP likely 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

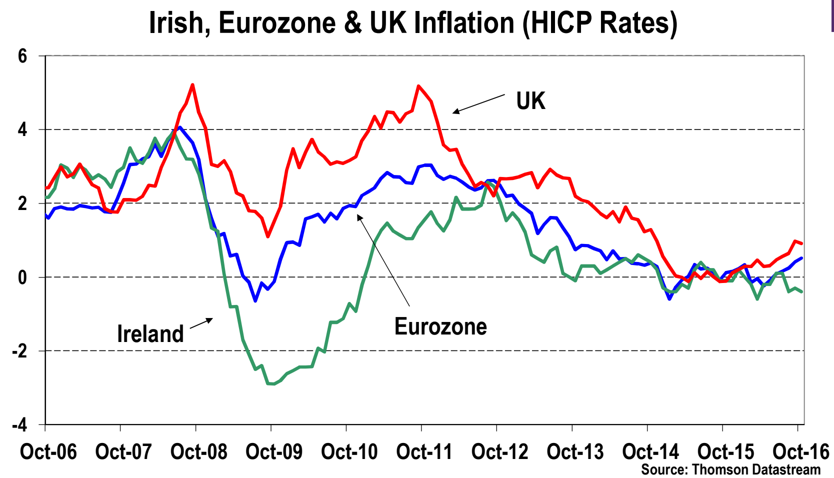
- **Higher trading costs** from more administration, differing trade rules and regulations, compliance costs, possible customs duties and tariffs when UK leaves EU
- Brexit could impact considerable **cross-country investment** between UK and Ireland.
- **Border** with Northern Ireland would become an 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.

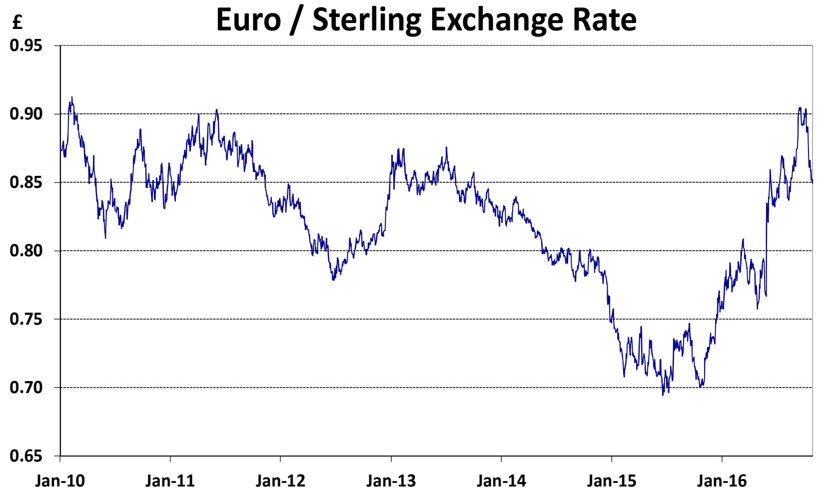
Ireland hopes that hard Brexit can be avoided

- 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 exits
- 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 during 2016-19 in run-up to Brexit on weak sterling and UK slowdown
- Long term impact will depend on the trade arrangements put in place post-Brexit

Irish economy already slowing on 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 below that of the Eurozone, UK and UK
- OECD and IMF forecasting that global growth will improve in 2017 and 2018
- However, Brexit is a major challenge for the economy
- Sharp fall in sterling to impact exports to UK, tourism from the UK, firms competing with UK imports
- Irish economy slows in 2016 on weaker global activity, sterling weakness and Brexit uncertainty
- Irish GDP growth forecast to moderate to 3.0-3.5% in 2016-19 period as Brexit concerns impact





Source: *Thomson Datastream*

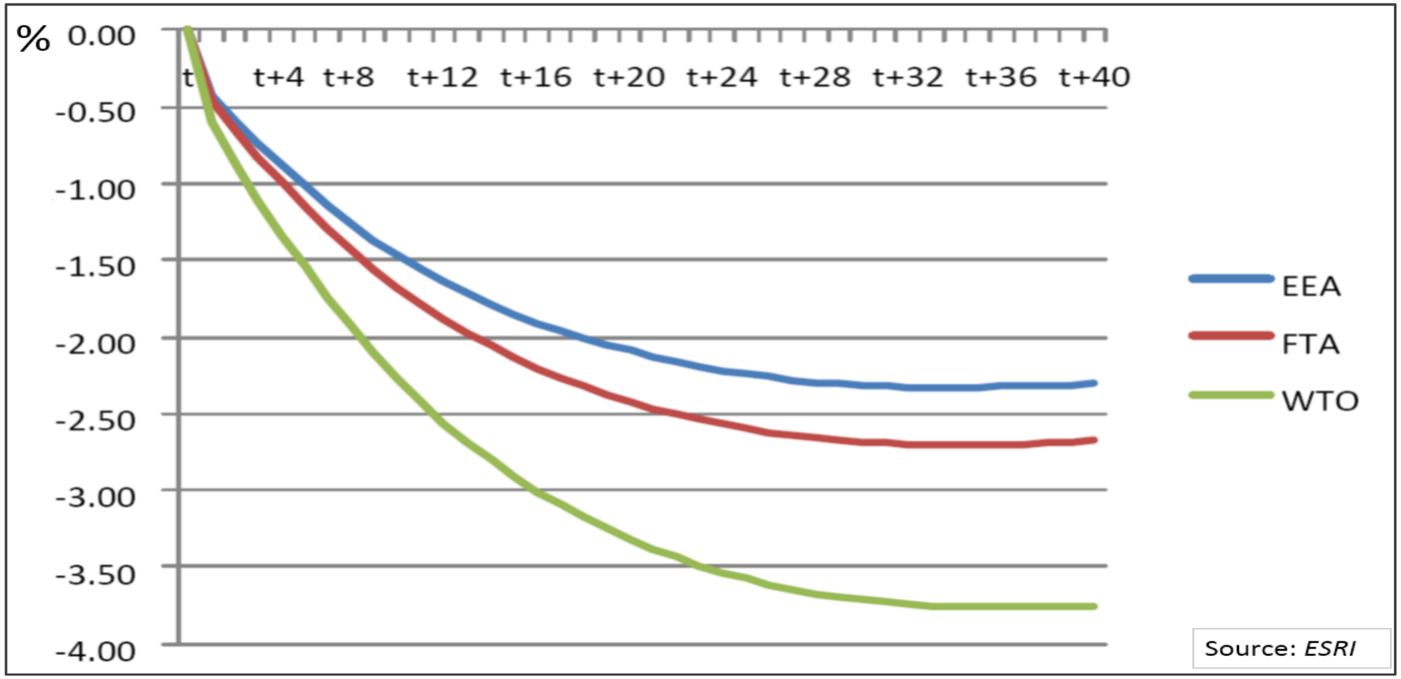
AIB Irish Economic Forecasts

% change in real terms unless stated	2013	2014	2015	2016 (f)	2017 (f)	2018 (f)
GDP	**1.1**	**8.5**	**26.3**	**3.5**	**3.5**	**3.0**
GNP	4.7	9.2	18.7	5.5	3.0	2.5
Personal Consumption	-0.8	1.7	4.5	3.0	3.0	2.5
Government Spending	0.1	5.4	1.1	3.0	1.0	1.0
Fixed Investment	-5.4	18.2	32.7	9.5	6.0	5.0
Core Fixed Investment*	22.6	14.4	18.3	3.0	6.0	5.0
Core Domestic Spending*	**2.3**	**4.2**	**6.6**	**3.0**	**3.7**	**3.1**
Exports	3.1	14.4	34.4	4.5	4.5	4.5
Imports	1.1	15.3	21.7	6.2	4.8	4.8
HICP Inflation (%)	0.5	0.3	0.0	-0.2	0.2	0.5
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

Brexit will impact Irish economy in coming decade



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

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