Irish Economy Update

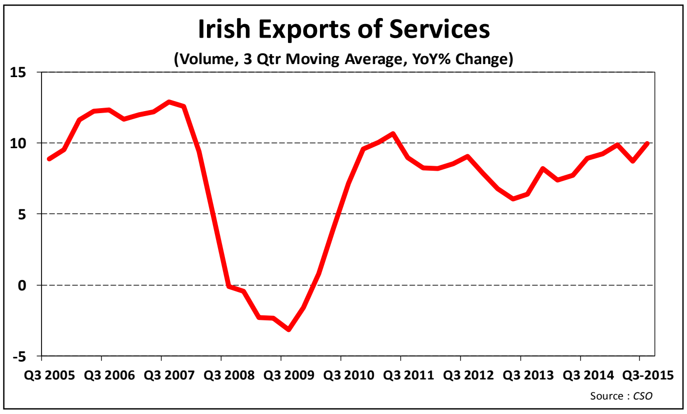
December 2015

AIB Treasury Economic Research Unit

Irish economy rebounds strongly

The surprisingly strong rebound of the Irish economy over the past two years has been much commented on at home and abroad. We have official National Accounts data from the CSO for the first three quarters of 2015. These show that Irish GDP grew at a steady pace of 7% year-on-year over this period. This follows the rise of 5.2% recorded for Irish GDP in 2014. These are exceptionally strong growth rates.

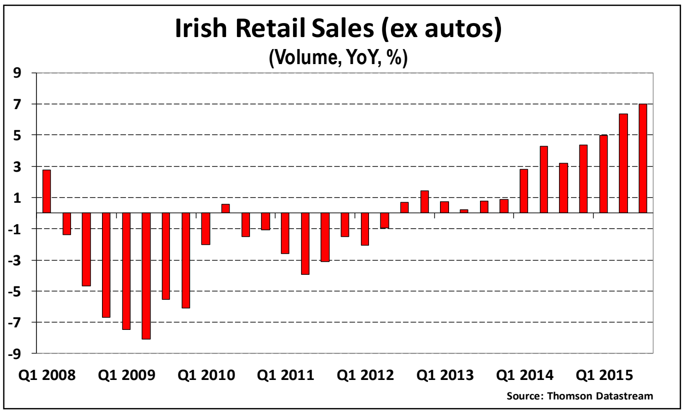
What is particularly impressive is that on a quarterly basis, the economy has expanded by between 1.1% and 2.2% for seven consecutive quarters, stretching all the way back to the opening three months of 2014. Thus, continuous robust growth has been evident in Ireland for two years now.



A cornerstone of this impressive performance has been the strong growth in exports, which have increased at a double-digit rate over the past two years. This reflects the recovery in activity in our main export markets, the significant gains made in Irish competitiveness, very favourable movements in exchange rates with the marked weakening of the euro, as well as the expansion in the export base due to the large inflow of FDI into Ireland in recent years.

However, the domestic sector of the economy is also recovering strongly. Domestic spending, excluding some elements associated with the multi-national sector, rose by 4.5% year-on-year in the opening three quarters of 2015, thereby maintaining the rate of growth seen in 2014. Importantly, consumer spending rose by 3.5% in the first three quarters of the year, following the rise of 2% recorded in 2014.

Consumer spending had contracted over the previous six years, so this rebound marks an important turning point for the domestic economy. Notably, car sales increased by 30% in both 2014 and 2015. Retail spending has also risen strongly in both years. However, spending on services has yet to recover, with on-going deleveraging still acting as a restraint on household expenditure.



Meanwhile, there has been a particularly strong rebound in business investment, albeit from a very low base. It grew by 25% in the opening three quarters of 2015, following a rise of 33% in 2014. Government spending has also risen in the past two years.

There are always doubts about the validity of strong Irish growth rates given the presence of a very large number of multi-national companies, which can at times have a distortionary impact on economic data, especially trade figures. However, the buoyant National Accounts statistics are in line with a broad range of other data. The PMI for the services sector hit a fifteen year high of 63.6 in November. Output from indigenous manufacturing firms rose by 10% in the first three quarters of the year. Agricultural output has risen very sharply in the past two years. Meanwhile, tourism numbers hit record levels this year.

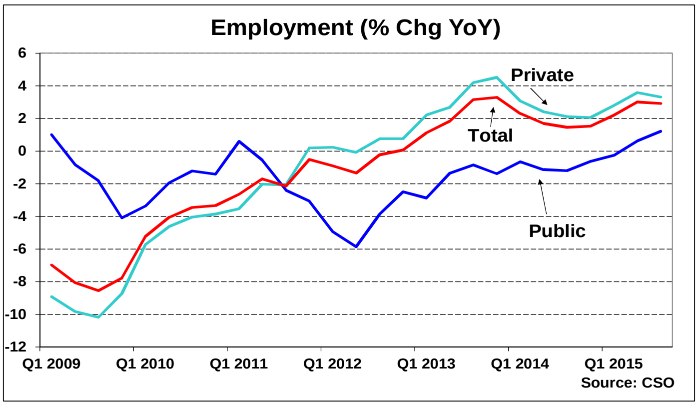
Oliver Mangan
Chief Economist
oliver.n.mangan@aib.ie

John Fahey
Senior Economist
john.j.fahey@aib.ie

Dara Turnbull
Economist
dara.c.turnbull@aib.ie

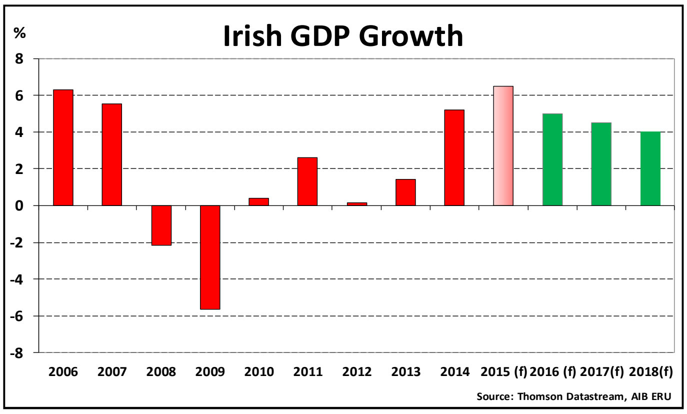
Robust growth can be sustained

The impact of the strong economic rebound can also be seen in many other indicators. The budget deficit is falling rapidly, helped by buoyant tax receipts, which are on course for a 10% rise this year. Exchequer figures, due in early January, are expected to show that the budget deficit fell to close on 1.5% of GDP in 2015. The deficit stood at 8% of GDP as recently as 2012.



Employment is growing at a rate of 3%, with the economy likely to have added around 60,000 full-time jobs in 2015. The unemployment rate has fallen to under 9% from 15% in 2012. Consumer confidence has risen to its best level in over ten years. Meanwhile, the balance of payments has returned to a very strong surplus in the past couple of years.

Two things are remarkable about the strong rebound of the Irish economy. First, the world economy is enjoying just modest growth as it continues to struggle to recover from the financial crisis of 2008-09. Indeed, global growth slowed to its weakest pace in five years in 2015. Even better performing economies, like the US and UK, are growing at around one-third the rate of the Irish economy. Eurozone growth is running at just 1.5%. Thus, Ireland has been a stand-out performer in terms of its economic growth over the past two years.



Second, the strong rebound in the domestic economy has occurred in the absence of any real recovery in the key construction sector, which has yet to spring back into life. CSO data show a rise of just 3% in construction output in the first three quarters of this year. House building remains at very depressed levels, while public capital spending is running at about half the level in other developed economies.

The key question as we enter 2016 is whether the economy can sustain its strong growth performance going forward. The outlook is promising, given that there are a number of favourable tailwinds at work. The global recovery is expected to continue at a modest pace over the next couple of years, although there are some downside risks, most notably from the slowdown in emerging economies.

Eurozone interest rates are set to remain at their current exceptionally low levels for a number of years, so monetary conditions will remain very accommodative. Meantime, Irish fiscal policy should be slightly expansionary in the coming years, supporting growth. Inflation is likely to remain low, helped by very weak commodity prices. Wage inflation is picking up, which combined with tax cuts and low inflation, points to good growth in real disposable income, boosting spending power.

Construction should also emerge from the doldrums, with some signs already of pick-up in private non-residential building activity, as well as a rise in housing starts. However, we are far from a construction boom. Instead, the Irish economic recovery is being built around exports, business investment and consumer spending. Overall, while there may not be a repeat of the 7% rise in GDP seen in 2015, the economy looks capable of expanding by 4-5% in the next couple of years, assuming that the global economy can maintain its current moderate rate of growth.

This publication 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 publication 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.

AIB Bankcentre, Ballsbridge, Dublin 4 Tel: 353-1-6600311 www.aibeconomicresearch.com