Economic Research Unit

Bank of Ireland

Ireland Outlook

February 2016

Strong Growth Continuing

2016

GDP	EMPLOYMENT	UNEMPLOYMENT	INFLATION
5.0%	2.5%	8.2%	0.7%

Exports at record high

Business conditions improving

Low oil prices a tailwind

Unemployment below 7% by end 2017

> "Net migration is expected to turn positive this year on the back of sustained economic growth and job creation"

Loretta O'Sullivan
Group Chief Economist

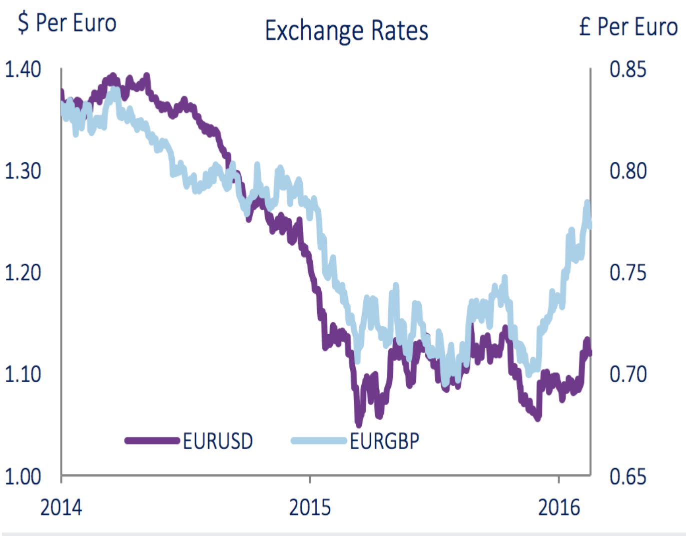
Overview The Irish economy was the fastest growing economy in Europe in 2014, a feat that it looks to have repeated for a second year running in 2015. While the CSO has not yet published official data for the final quarter of last year, strong numbers for the first three quarters and positive high frequency indicators since point to GDP growth in the region of 6.8% in 2015. Robust exports and investment, employment growth and sustained consumer spending saw economic activity last year expand at its fastest pace in fifteen years. The underlying picture at the start of this year is also upbeat and we are forecasting GDP growth of 5% in 2016 (revised up from 4.8% in our previous Outlook), while GNP is projected to increase by 4.6%. This means that Ireland will outperform its European counterparts yet again. Another year of solid growth and further job gains should take the unemployment rate down below 8% by year-end. And with the recovery becoming embedded, we see net migration moving back into positive territory, for the first time since 2009. Looking further ahead, GDP is expected to grow by 4% next year (GNP by 3.7%), with the unemployment rate falling to under 7% by end-2017. As always, there are risks to these forecasts. Potential headwinds include uncertainty about the global economy and the outlook for sterling, though on the upside, housing construction could respond more rapidly to meet demand than currently assumed.

Outlook

	2015 (f)	2016 (f)	2017 (f)
Personal Consumption	3.5%	3.4%	3.0%
Government Consumption	2.4%	2.0%	2.0%
Investment	24.0%	12.0%	7.5%
Exports	12.5%	8.0%	6.0%
Imports	15.4%	9.0%	6.4%
GDP	6.8%	5.0%	4.0%
GNP	5.8%	4.6%	3.7%
Employment	2.8%	2.5%	2.2%
Unemployment Rate (Average)	9.4%	8.2%	7.4%
CPI	-0.3%	0.7%	1.6%

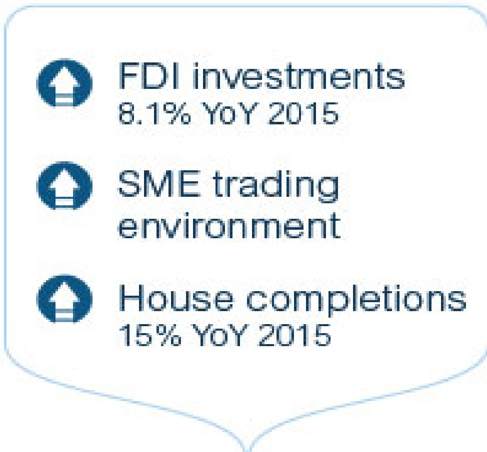
Exports at record high

Exports grew strongly during 2015, increasing by over 13% year-on-year in the first three quarters of the year. Growth in our key trading partners, exchange rate movements and sector-specific developments translated into a robust goods performance and healthy services activity. With high frequency indicators for the fourth quarter also broadly positive, export growth in the region of 12.5% is expected for 2015 as a whole. Exports are forecast to increase this year too, albeit the pace of expansion is set to ease. While the IMF has marginally revised up its GDP growth forecast for the euro area and low oil prices are providing support, concerns about the global outlook have increased of late and activity in the US and UK has softened a little. The euro has also strengthened against the dollar and sterling. Trading partner demand remains positive though and sectoral conditions continue to be favourable, underpinning our export growth forecast of 8% for this year. Next year, exports are projected to increase by 6%. Turning to imports, solid growth is expected over the forecast horizon, reflecting the export outlook and domestic activity.



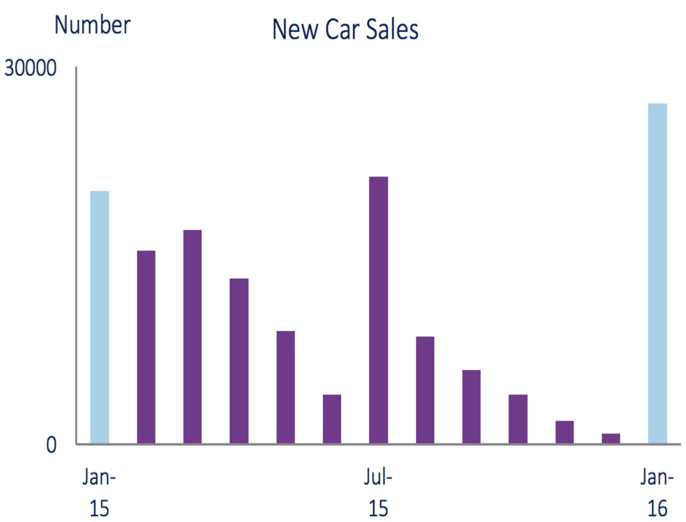
Business conditions improving

Headline investment put in a strong performance last year, helped by a sharp annual increase in the intangibles component (e.g. R&D, patents) in both the second and third quarters. On the business side, improving sentiment and a better trading environment for firms supported 'core' machinery and equipment investment (i.e. excluding the volatile planes category). Moreover, some 60% of small and medium sized enterprises (SMEs) see activity increasing over the next 3 months, which also bodes well for business investment this year. On the construction side, we saw a pick up in residential and other building last year. House completions came in at 12,666 units for the full year - a 15% increase, but off a low base – and are expected to rise again this year and next. Taking these various components together, total investment growth is now forecast at 24% for 2015, with healthy growth of 12% projected for 2016 and 7.5% for 2017.



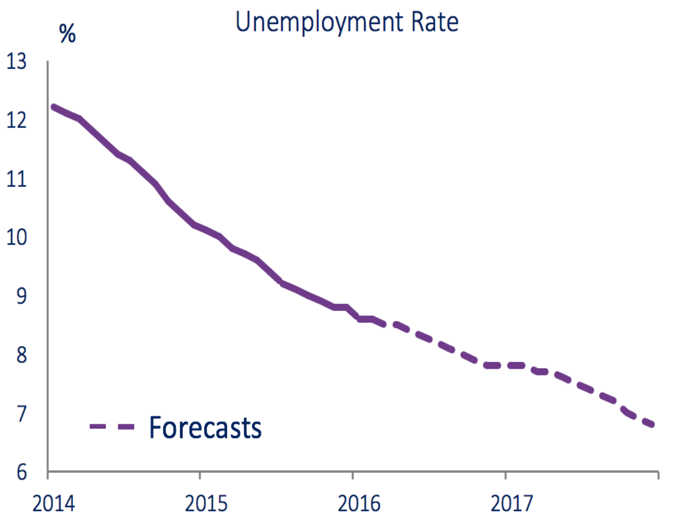
Low oil prices a tailwind for consumer spending

Consumer spending gained ground in 2015, with growth averaging 3.5% in the first three quarters of the year and available indicators pointing to continuing positive momentum. The core retail sales index (excluding cars) rose further in the fourth quarter of last year and car sales – which increased by over 30% to 121,110 in 2015 – posted a similarly strong increase in January of this year. While deleveraging remains a headwind, low oil prices are a tailwind and with more people in work, earnings growing and budget measures starting to feed through, consumer confidence is high and spending prospects bright. Back in October, we noted that there was some upside risk to the consumer spending numbers we published at that time. As this now looks to be materialising, we have revised up our forecasts for personal consumption in this Outlook (by ¼ percentage point) to 3.5% last year and 3.4% this year, and are projecting growth of 3.0% in 2017. On the Government side, spending is forecast to increase by 2% in 2016 and 2017.



Unemployment below 7% by end 2017

The steady rise in employment which began in late 2012 has continued through 2015. The number of people in work is heading towards the 2 million mark and the latest data show that jobs gains have been broad based across sectors and regions. This trend is expected to continue and employment growth of 2.5% is projected for this year (c. 50,000 new jobs) and 2.2% for next year. Developments on the unemployment front have also been positive, with the unemployment rate down to 8.6% in January, a seven year low. Solid job creation should see the rate continue to fall – even with the labour force rising modestly – to under 8% by end-2016 and below 7% by end-2017. With the economic recovery becoming embedded, employment opportunities increasing and indications of skill shortages in some areas, our expectation is that net migration will move back into positive territory this year. This would make 2016 the first year that the number of people coming into the country exceeded the number leaving since 2009.



House price gains broaden out

The housing recovery continued in 2015, with activity and prices increasing year-on-year (by 10.8% and 10.6% respectively). House price gains have broadened out, with prices outside the capital rising at a faster pace than in Dublin last year. This is the opposite of what happened the year before, possibly reflecting in part the new CBI macro-prudential rules and also an element of catch up. Mortgage lending also grew in 2015, by some 26% in value terms to almost €4.9 billion. While both the housing and mortgage markets saw some easing during the year, underlying demand remains strong, with rising incomes and demographic factors providing support. On the supply side, shortages continue to be a feature and there is some way to go to meet estimated medium term demand (c. 25,000 units per annum).

Inflationary environment weak

Ireland, like many other countries, is going through a period of subdued inflation. CPI inflation was slightly negative in 2015, with low oil prices a key contributor to this - the headline rate of -0.3% would have been 0.9 percentage points higher had energy products been excluded from the basket of consumer goods and services. Rising domestic activity is set to put upward pressure on prices over the forecast horizon, although there is still some spare capacity in the economy which is likely to have a dampening effect. Recent oil price developments also imply a weaker starting point for 2016, and with this in mind, we have revised down our inflation forecasts for this year. CPI inflation is now projected to average 0.7% in 2016 (1.4% previously) and 1.6% in 2017. The corresponding HICP figures are 0.8% and 1.6%.

Debt ratio below 100%

The strong growth in tax revenues last year is a clear sign of the improving economy, with income tax, VAT and (in particular) corporation tax receipts all coming in ahead of profile. On the back of this, the Government had the fiscal room to increase spending towards the end of the year, while Budget 2016 provided for €1.5 billion in tax cuts / spending increases. The strength of the tax performance suggests that the General Government deficit may well come in below the official estimates of 2.1% of GDP in 2015 and 1.2% this year. Although still high, gross General Government debt as a percent of GDP is firmly on a downward trajectory, with data for the third quarter showing that the ratio has fallen below 100%.

Risks to the outlook

There are, as always, risks to the economic outlook. As a small, open economy, Ireland is particularly vulnerable to changes in the external environment and at the current juncture; risks on this front are to the downside. A pronounced slowdown in the global economy could dampen export growth, while uncertainty about the UK's continued membership of the EU may weigh on sterling and, in turn, the indigenous exporting sector. On the domestic front, upside risks include construction investment which might respond more rapidly than currently expected to meet demand, and earnings gains which may boost consumer spending by more than assumed.

THE IRISH ECONOMY

Strong Growth Continuing

Bank of Ireland

GDP

2015f	2016f	2017f
6.8%	5.0%	4.0%

EXPORTS

Supported by growing trading partners

US UK EA

Sectoral conditions also favourable

Potential headwind: Uncertain £ outlook

Exports	
2015f: 12.5%	
2016f: 8.0%	
2017f: 6.0%	

INVESTMENT

Business sentiment improving

FDI investments
8.1% YoY 2015

SME trading environment

Construction activity picking up

House completions
15% YoY 2015

Investment	
2015f: 24.0%	
2016f: 12.0%	
2017f: 7.5%	

EMPLOYMENT

Broadening out across sectors and regions

Earnings also

Unemployment rate falling

2015	2016f	2017f
9.4%	8.2%	7.4%

Employment	
2015f: 2.8%	
2016f: 2.5%	
2017f: 2.2%	

CONSUMER SPENDING

Confidence and income gains feeding through

121,110 new cars sold in 2015
34.8% YoY Jan 2016

Core retail sales
6.2%YoY 2015

Low oil prices and budget measures helping

Debt ongoing

Consumer Spending	
2015f: 3.5%	
2016f: 3.4%	
2017f: 3.0%	

60% of SMEs see activity increasing over the next 3 months

44% of consumers expect their household finances to improve this year; **42%** stay the same; **11%** deteriorate

Prepared by: Bank of Ireland Economic Research Unit
Sources: Bank of Ireland, IMF, Industrial Development Agency, Department of Finance, Department of Environment, Community and Local Government, Bloomberg, Central Bank of Ireland, ESRI

Contact us at:

economics@boi.com

Dr. Loretta O'Sullivan
Group Chief Economist
+353 (0) 766 244 267

Conn Creedon
Senior Economist
+353 (0) 766 235 134

Patrick Mullane
Senior Economist
+353 (0) 766 244 269

Mark Leech
Media Relations Manager
+353 (0) 766 234 773