



The Irish Economic Update:

Deep COVID-19 recession, but resilient Irish economy can bounce back

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Oliver Mangan
Chief Economist
AIB

Coronavirus pandemic triggers deep H1 2020 recession

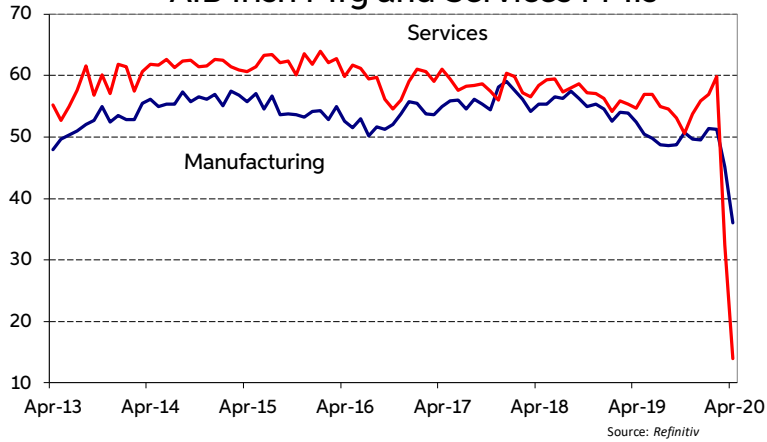


- Ireland hit by deep recession in H1 2020 as economy put into lockdown to contain coronavirus
- Some 1.25 million or 50% of labour force enrolled on various State income support schemes
- Jobless rate soars in March-April; COVID-19 adjusted unemployment rate hits 28% in April
- PMIs in April sink to 36.5 for manufacturing, 13.9 for Services and 4.5 for Construction
- Big fall in GDP will be seen in Ireland, as elsewhere, in H1 2020
- Activity expected to rebound in H2 2020 as virus abates and restrictions on activity are lifted
- Government plan is to ease most restrictions gradually in stages from mid-May to mid-August
- Nonetheless, IMF, ESRI, EC and Central Bank still expect that GDP will fall by circa 7-8% in 2020
- Strong growth expected in 2021 given depressed base for this year – growth of over 6% per IMF
- Broad range of government supports announced to help household incomes and businesses
- Blow-out in public finances, with budget deficit likely to hit 7-9% of GDP in 2020

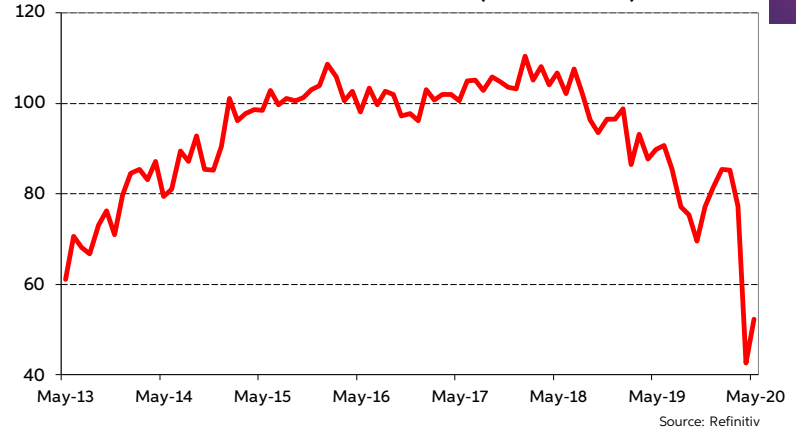


Data slump as COVID-19 lockdown restrictions bite hard

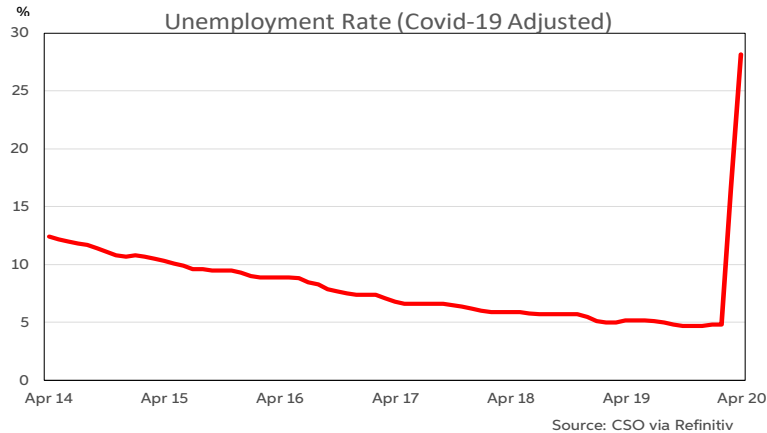
AIB Irish Mfg and Services PMIs



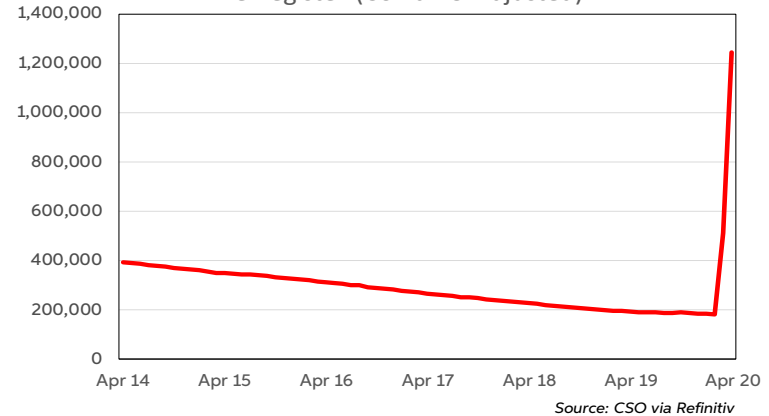
Consumer Confidence (ESRI - KBC)



Unemployment Rate (Covid-19 Adjusted)



Live Register (Covid-19 Adjusted)



Activity data weaken sharply with economy in cold-storage

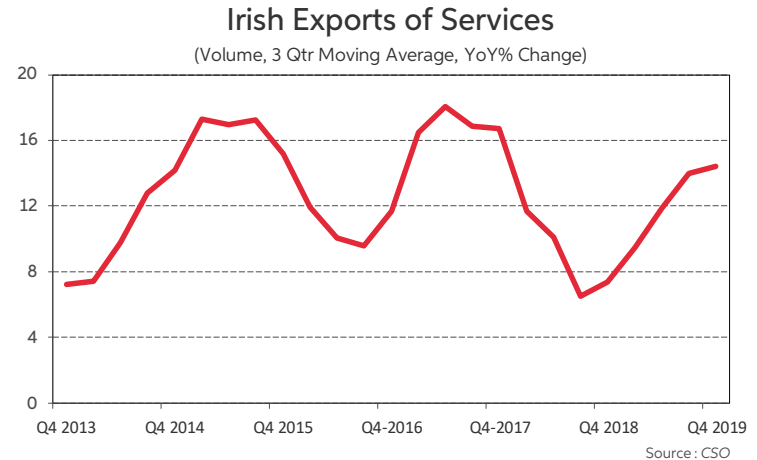
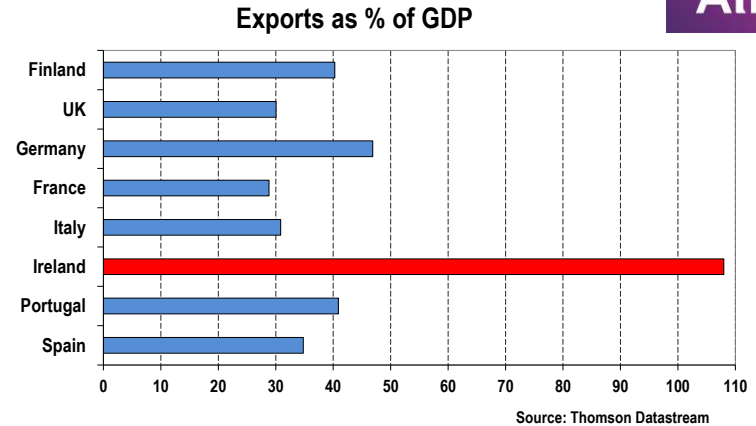


- Unemployment rate spikes from 4.8% in Feb to COVID-19 adjusted figure of 28.2% in April
- Some 1.25 million workers either in receipt of Pandemic Unemployment Benefit / standard unemployment benefit or enrolled on State's temporary wage subsidy scheme by end April
- Retail sales (ex-motor trade) fell by 0.7% in Q1, with sales down by 1.9% in March
- Consumer confidence collapses to near record low in April, but recovers somewhat in May
- Drop of 90% yoy in total number of cars licensed for first time (new + second-hand imports) in April
- Manufacturing PMI falls sharply in April to 36.0 as virus outbreak hits output and orders hard
- Services PMI plummets to record low of 13.9 in April, with many sectors shut down
- Construction PMI slumps to just 4.5 in April, with sector in full lockdown
- Tax receipts fall sharply March-April; government spending rises. Big budget deficit on cards in 2020
- But goods export soar in March as the large pharma sector sees surge in output

But Ireland's Pharma exports surge on COVID-19 outbreak



- Ireland a very open economy – exports, driven by large scale FDI, are a huge part of economy
- Exports rise strongly in recent years, helped by large FDI inflows
- Total exports rose by 10.4% in 2018 and 11.1% in 2019.
- Pharma, medical care products, IT equipment, and food & drink are main goods exports
- IT, business, financial and tourism are the main service exports
- Goods exports rise 13% yoy in Q1 2020. Surge by 40% yoy in March to record high level
- Pharma exports (36% of good exports) up 60% yoy in March due to COVID-19 pandemic
- Organic chemicals (27% of good exports) jump by 121% yoy in March

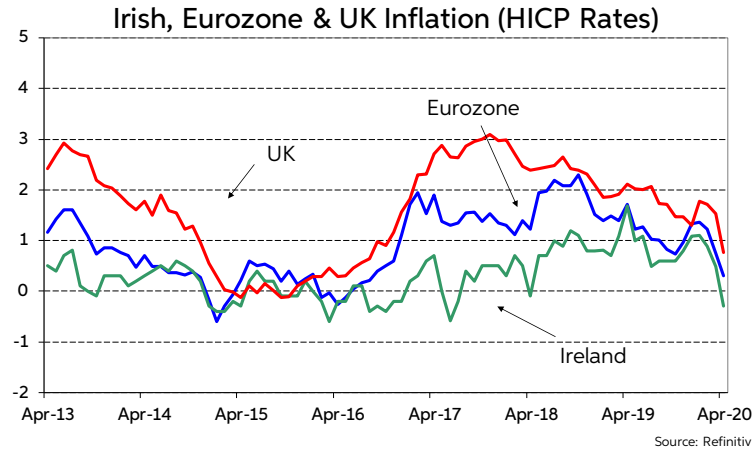
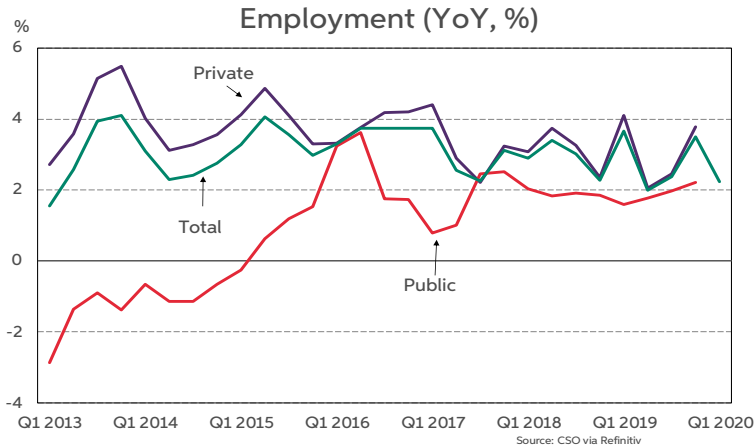
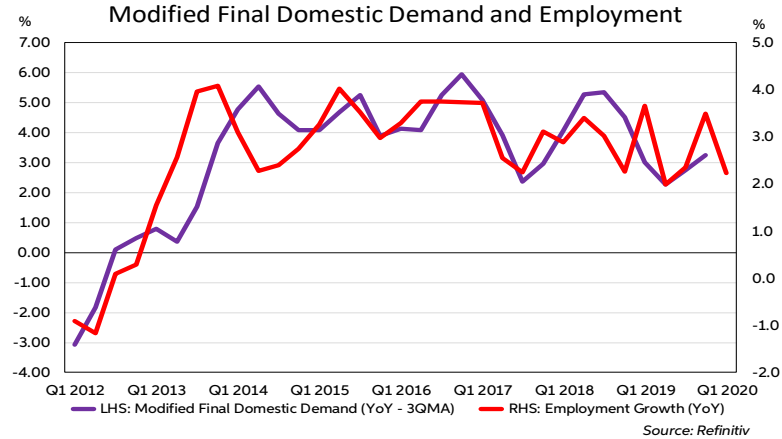
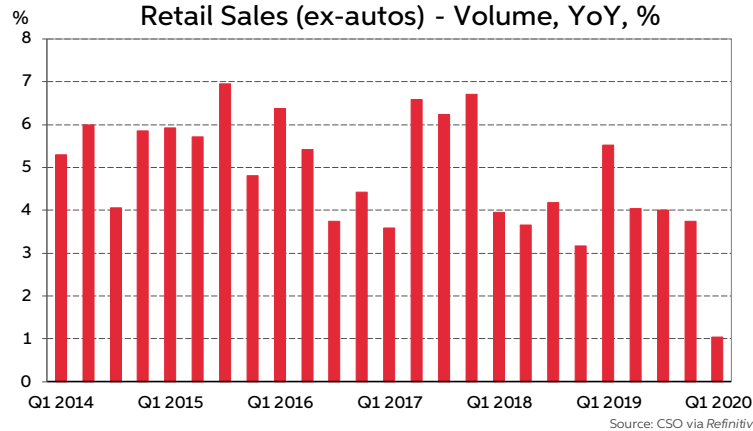


COVID recession comes after strong growth in 2013-2019



- Previous Irish recession of 2008-2009 also severe. GDP fell 9.5%, with GNP down 12%
- Collapse in construction activity and banking system, severe fiscal tightening, high unemployment
- GDP at end of 2008-09 recession was still almost 25% higher than in 2001, highlighting that economic crash came after a long period of very strong growth going back to 1993
- Ireland tackled its problems aggressively in the public finances, banking sector & property market. Imbalances in economy unwound – housing, debt levels, competitiveness, BoP
- Economy recovered strongly, with robust underlying growth of circa 5% in 2013-19 period
- Focus was on generating growth via the large export base and FDI as the route to recovery
- Recovery in domestic economy followed, led by rebound in investment & retail spending
- Strong jobs growth. Unemployment rate fell from 16% in early 2012 to below 5% in H2 2019
- Budget deficit eliminated quicker than expected. Public finances in surplus in 2018/19
- Major deleveraging by private sector, including households, during the last decade
- Balance of payments returned to large surplus

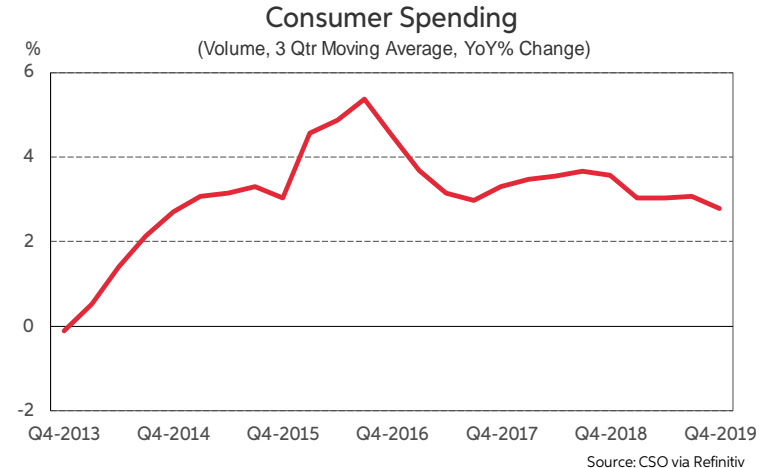
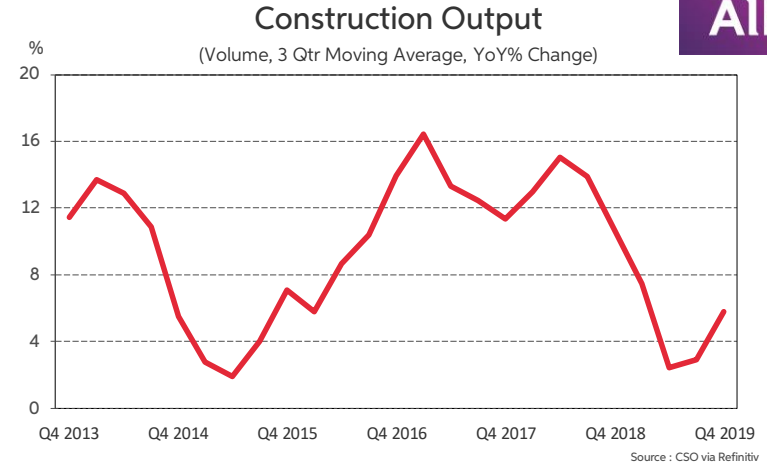
Economy was performing very well before virus struck



Domestic demand solid ahead of the pandemic



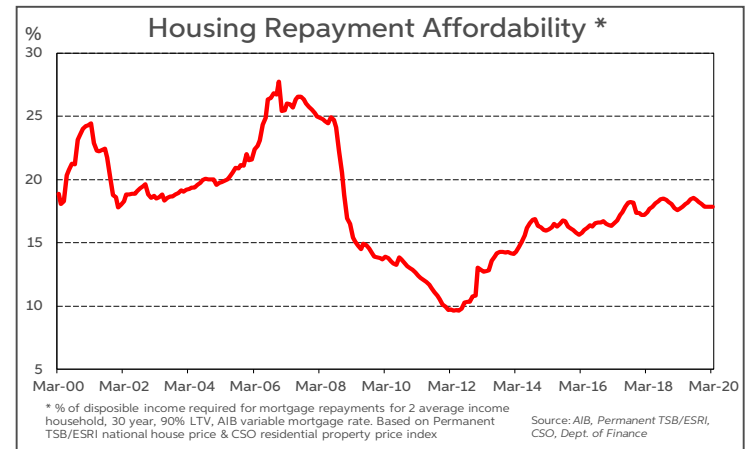
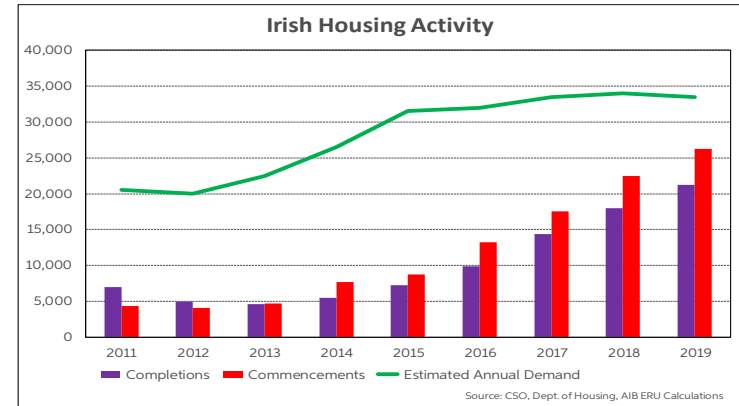
- Construction sees strong recovery since 2013. Output up nearly 12% on average in 2016-18 period
- Slowdown in non-residential construction activity last year – construction output up 5.8% in 2019
- Business investment (ex aircraft/intangibles) has recovered strongly since 2013
- However, Brexit uncertainty saw business investment flat-line in 2019
- Consumer spending grew by 3.5% on average over 2014-2018 period. Up by 2.8% in 2019
- Modified final domestic demand grew at 4.4% rate in 2014-2018 period. Rose by 3% in 2019
- Strong growth in core retail sales of circa 4-5% in recent years – rose by 4.4% in 2019
- Car sales returned to very high levels in 2018-19, with notable rise in direct imports from UK
- Good employment growth continued in Q1 2020



House building on steady rise before virus halted activity



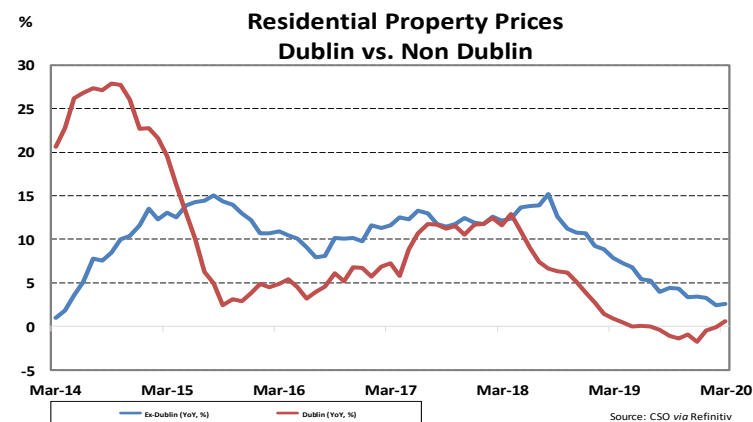
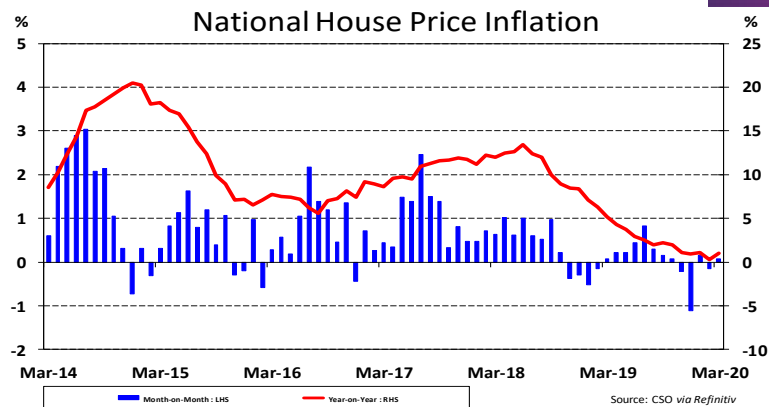
- Housing completions up 18% yoy to over 21,000 units in 2019, a moderation on 2018's 25% growth rate
- Housing commencements increase by further 17% in 2019 to 26,000 units
- Planning permissions jump by 38% YoY to over 40k in 2019, driven by a sharp rise in apartment applications
- Housing completions rose by 17% yoy in Q1 2020
- Completions were forecast at circa 24,500 for 2020
- Now expected to be down 15-25% at 16,000-18,000
- Housing output remains well below annual new housing demand, estimated at 30,000+ units
- Mortgage lending rose by 9.5% to €9.6bn in 2019, but big decline in store for 2020 after good start in Q1
- Housing affordability metrics stable ahead of crisis



House price inflation slows sharply



- 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 home building
- Prices up 83% by March 2020 from March 2013
- But house prices still some 18% below 2007 peak
- House price inflation slows sharply in 2018/19 reflecting tighter Central Bank lending rules
- Prices up 1% yoy nationally during Q1 2020, down from a high of 13.3% in April 2018
- Dublin prices up 0.6% in March, non-Dublin +1.5%
- Recession to see price falls, but may be limited if economic downturn short and given low supply
- Annual growth in rents had slowed before virus
- Rents now starting to fall as recession takes hold



AIB Model of Estimated Housing Demand



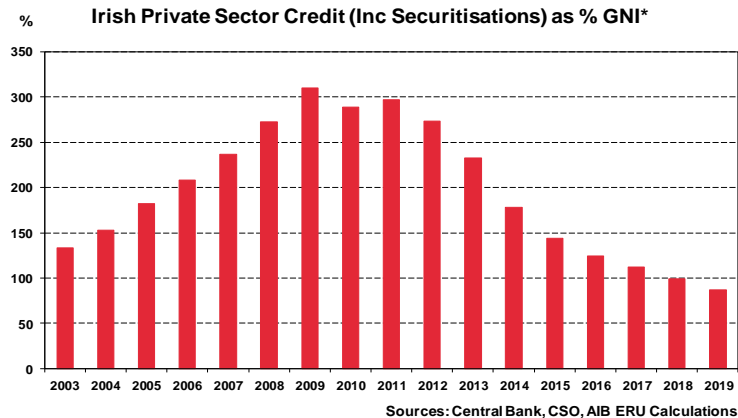
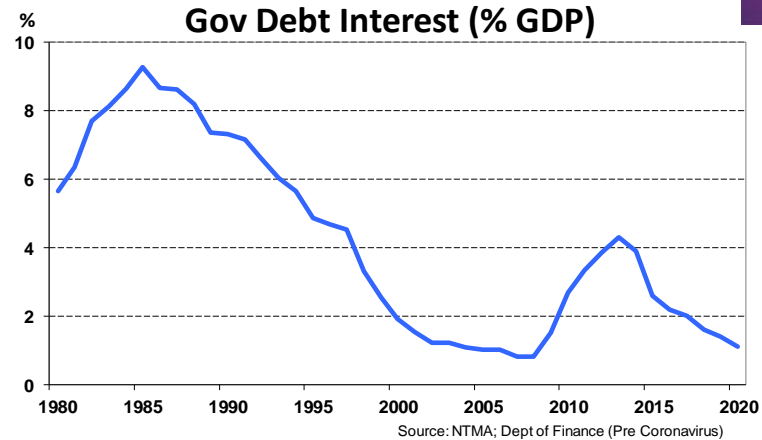
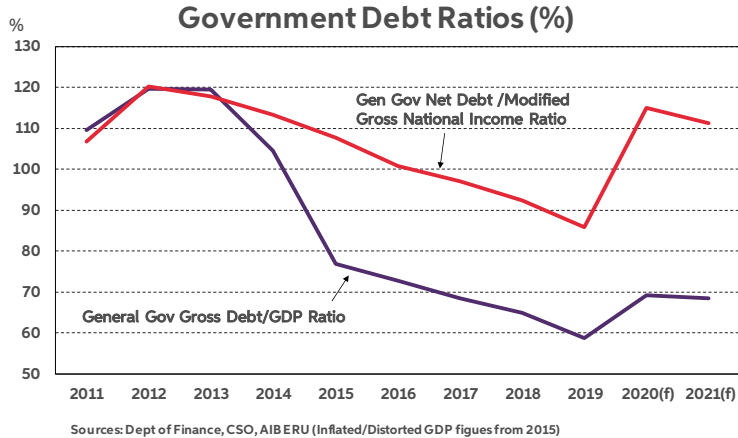
- Rising headship rates added circa 8,000 per year to housing demand in 2002-2011 period
- Shortage of housing, high rents, tighter lending rules saw average household size rise in 2011-16. Thus, headship fell – was a drag of circa 10,000 p.a. on housing demand
- Assume no change in headship in 2016-2021 – 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 2016-21

| Calendar Year | 2017 | 2018 | 2019 | 2020 | 2021 |
|--------------------------------------|----------------|----------------|----------------|----------------|----------------|
| Household Formation | 28,000 | 28,500 | 28,000 | 26,500 | 25,000 |
| <i>of which</i> | | | | | |
| Indigenous Population Growth | 18,500 | 17,500 | 16,500 | 16,500 | 16,000 |
| Migration Flows | 9,500 | 11,000 | 11,500 | 10,000 | 8,500 |
| 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 | 33,500 | 34,000 | 33,500 | 32,000 | 30,000 |
| Completions | 14,400 | 18,100 | 21,250 | 18,000 | 20,000 |
| Shortfall in Supply | -19,100 | -15,900 | -12,250 | -14,000 | -10,000 |

*Headship is % of population that are heads of households.

Sources: CSO, DoECLG, AIB ERU.

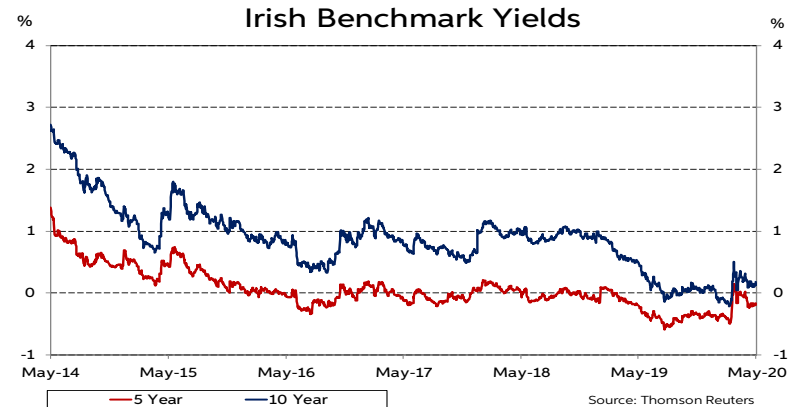
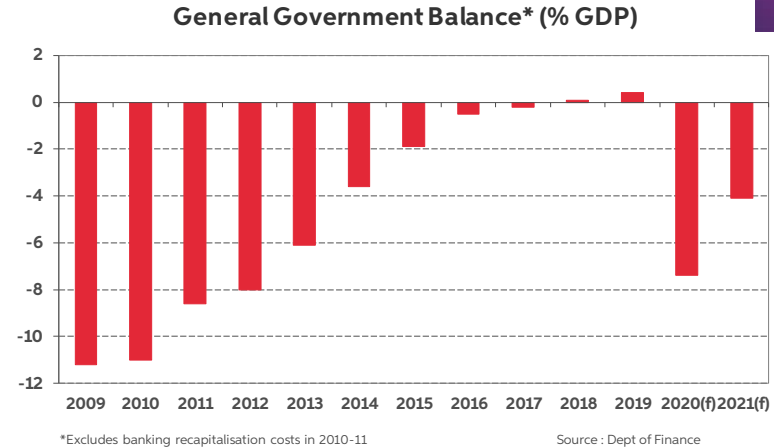
Govt. debt ratios had fallen, private sector deleverages



Large budget deficit in 2020, but bond yields stay very low



- Budget deficit declined sharply over last decade, with small surpluses recorded in 2018 and 2019
- Primary budget surplus (i.e. excluding debt interest) of near 2% of GDP in 2019
- Debt interest costs very low – at 1.4% of GDP
- However, Covid-19 and efforts to mitigate it see the public finances deteriorate in 2020
- Tax receipts 5.7% below profile to end March. Gov spending 13.5% above profile by end April
- Dept. of Finance forecasting budget deficit of 7.4% of GDP this year. Could be even higher
- Gov Debt/GDP ratio has fallen sharply, as have Irish bond yields, in recent years
- Debt ratio will move higher this year
- Bond yields stable despite blow-out in budget deficit and much larger debt issuance in 2020
- Ireland's sovereign debt ratings hold steady; S&P at AA-, Fitch at A+, Moody's A2



Brexit: EU-UK trade talks making little progress



- EU and UK agreed on revised Withdrawal Agreement at last October's Heads of State Summit
- NI to remain within Single Market for goods and have dual EU-UK customs system
- UK left the EU on Jan 31st 2020 in orderly exit. Transition period in place until end 2020
- UK government continues to rule out extending the transition period beyond this date
- Trade talks resume after delay due to virus outbreak, but little sign of progress being made
- Negotiations proving difficult and fractious. Wide gap between both sides
- EU insisting on level playing field for trade, with considerable regulatory alignment, common rules
- UK government puts focus on 'taking back control' and non-alignment with EU
- UK could opt for 'no deal' rather than have close alignment with EU rules – still risk of Hard Brexit
- However, some type of FTA seems likely as it's the best outcome for both the UK and EU
- Could require more time, though, to get a deal done. Extension to transition period a possibility

Key points about any EU-UK Free Trade Agreement

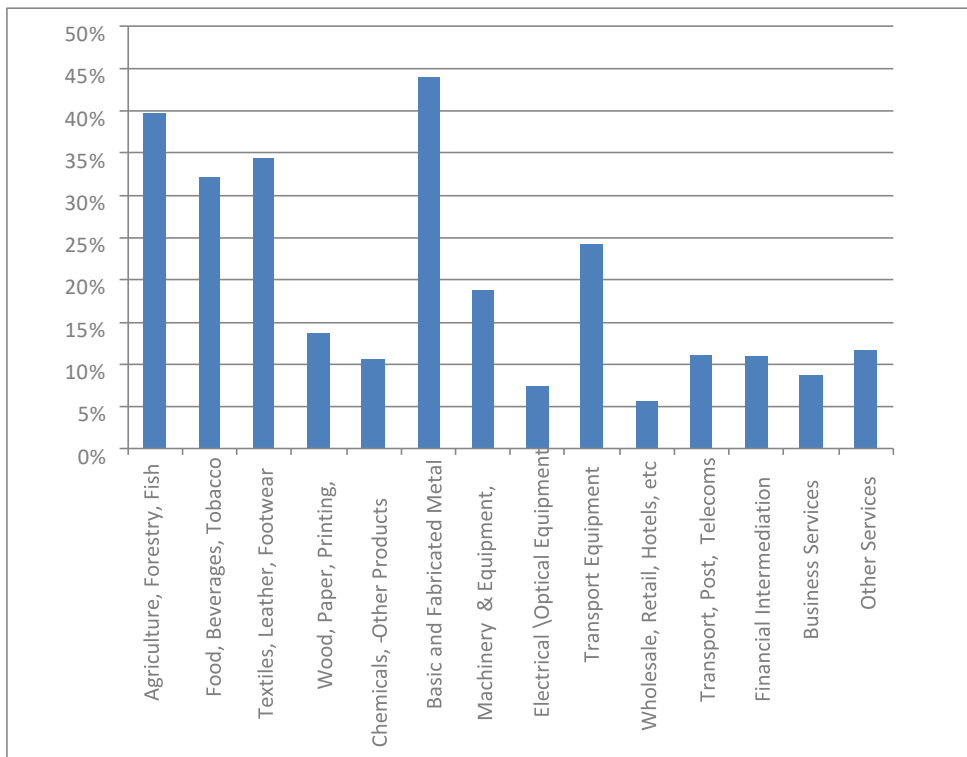


- Any FTA will be much inferior to the EU Single Market, involve extra large admin costs
- Significant restrictions on trade will come into play in a FTA– new customs procedures, compliance with onerous rules of origin requirements, more regulations etc.
- Documentary evidence needed for customs clearance, proof all product made in country, compliance with regulatory standards/rules – non-tariff barriers are big costs
- Trade in agri-food products may require export health certs and could be subject to veterinary border inspections – both exports and imports
- While FTA should allow for continuing tariff-free and quota-free trade in most goods, such agreements generally do not extend to services or, indeed, fishing rights
- EU-Canadian FTA left some tariffs & quotas in place, but included some services
- A big issue is financial services – EU likely to be very wary of giving UK permanent equivalence/passporting rights. Any other equivalence regime can be altered or terminated
- No right of redress for companies via courts under FTA, unlike in the EU Single Market

Food industry is very dependent on UK market

- Food and Beverages account for 25% of Irish exports to UK
- Around 40% of Irish food exports go to the UK – key market for beef and cheese
- UK could impose tariffs on EU food imports to protect its agri-industry if no trade deal
- Other sectors very dependent on UK market include machinery and transport, metal products, textiles
- Even with FTA, there will be new admin trading costs for those exporting & importing with UK –customs clearance docs, rules of origin etc

Share of Exports by Industry Destined for the UK (ESRI)



Brexit to lower growth rate of Irish economy



- **Multiple hits to the Irish economy if there is a no EU-UK Trade deal** at end of transition period: further sharp fall in sterling, weak UK economy, disruption to trade/supply lines, tariffs, new administrative and regulatory costs etc.
 - Sharp fall-off in trade with UK likely if there is no trade deal, with the **shock front loaded** - around half of the impact on trade would take place in the first two years, per ESRI
 - Central Bank estimate GDP would be 5% lower if the UK moves to WTO rules at end of transition period. ESRI also put impact of no-deal hard Brexit at circa 5%
 - **Economy would also be impacted by UK move to FTA** as this would result in new significant non-tariff barriers, imposing costs and making trade more difficult with UK
 - **Central Bank estimate Irish GDP would be 3.5% lower in long term under a FTA**
- **Copenhagen Economics** have examined various Brexit scenarios
 - Estimate impact by 2030 is to **reduce Irish GDP** by 2.8% under a EEA scenario, **by 4.3% in a standard FTA, but 3.5% in enhanced FTA** with closer regulatory alignment
 - CE estimate GDP would be 7% lower in a WTO (no trade deal) scenario

Key medium-term Irish growth drivers remain in place



- Favourable medium-term drivers of strong Irish growth remain in place
- House building picking up from still low output levels – big focus of next government
- Government spending supportive of growth
- Activity to be aided by continuing very low interest rate environment
- Still an attractive destination for FDI
- Labour market dynamics supportive of growth
- Economy has deleveraged, big jump in savings
- World economy expected to rebound from 2021
- Strong Irish growth of circa 6% possible next year after sizeable fall in GDP in 2020
- A UK-EU FTA will lower Irish growth somewhat, possibly by around 0.5% per annum for some years

| Irish GDP Forecasts | | |
|-------------------------|-------|------|
| % Vol | 2020 | 2021 |
| IMF | -6.8 | 6.3 |
| ESRI | -7.1 | N/A |
| Department of Finance | -10.5 | 5.8 |
| Central Bank of Ireland | -8.3 | N/A |
| European Commission | -7.9 | 6.1 |
| AIB | -7.5 | 6.3 |

| IMF: WEO Irish Forecasts | | |
|--------------------------|------|------|
| % | 2020 | 2021 |
| GDP | -6.8 | 6.3 |
| Unemployment Rate | 12.1 | 7.9 |
| CPI | 0.4 | 1.7 |
| Current Account* | 6.3 | 5.3 |
| Budget Balance* | -7.4 | -4.1 |

*% of GDP (Department of Finance for Budget f/c)

AIB Irish Economic Forecasts



| <i>% change in real terms unless stated</i> | 2018 | 2019 | 2020 (f) | 2021 (f) | 2022 (f) |
|---|------------|------------|-------------|------------|------------|
| GDP | 8.2 | 5.5 | -7.5 | 6.3 | 3.5 |
| GNP | 6.5 | 3.3 | -6.5 | 5.5 | 3.0 |
| Personal Consumption | 3.4 | 2.8 | -8.0 | 5.0 | 3.0 |
| Government Spending | 4.4 | 5.6 | 12.0 | -5.0 | 2.0 |
| Fixed Investment* | -21.1 | 94.1 | -8.0 | 4.8 | 4.0 |
| Exports | 10.4 | 11.1 | -6.0 | 6.3 | 5.0 |
| Imports* | -2.9 | 35.6 | -5.4 | 5.3 | 4.7 |
| HICP Inflation (%) | 0.7 | 0.9 | 0.0 | 0.7 | 1.0 |
| Unemployment Rate (%) | 5.8 | 5.0 | 13.5 | 9.0 | 7.1 |
| Budget Balance (% GDP) | 0.1 | 0.4 | -7.5 | -4.0 | -2.5 |
| Gross General Gov Debt (% GDP) | 63.5 | 59.3 | 67.5 | 66.0 | 64.0 |

*Data for 2018 & 2019 very distorted by aircraft and intangibles

Source: CSO, D/Finance; AIB ERU Forecasts

Risks to the Irish economy



- Main risk is obviously the coronavirus – will weigh heavily on growth this year
- Persistence of virus or fresh outbreak could delay global/Irish recoveries
- Highly open nature of Irish economy means it is quite exposed to global recession
- Brexit remains a challenge given uncertainty about future EU-UK trading relationship
- Questions around Ireland's corporation tax regime (Apple ruling, moves on tax harmonisation in EU, OECD tax reform/minimum tax rate proposals, Trump views on Pharma) could impact FDI
- Supply constraints in new house building activity, with output still at very low levels
- Competitiveness issues - high Dublin house prices, high rents, high personal taxes, high wages
- Credit constraints – tightening of lending rules, on-going deleveraging, weak credit demand

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.