Economic Research Unit

Economics Weekly

Bank of Ireland

Irish economy beginning to feel competitiveness pressures

This week we published new Irish economic forecasts; downgrading projections for both GDP (-1%) and modified domestic demand (2.3%) growth in 2024, but mainly on the back of statistical distortions and volatile data. The bigger picture is that Ireland's exceptional pace of employment (2.7%) and population (1.9%) growth has continued in H1 2024, ahead of our expectations. Whilst welcome news in many respects, Ireland's extraordinary economic performance is increasingly evident in bottlenecks, capacity pressures and labour shortages. Hence, in a special box in our new Irish economic outlook document, we highlight pay pressures and house price inflation in Ireland are starting to stand out from other euro area economies. In this context, we also illustrate that build cost inflation, the Covid-19 pandemic and other factors such as planning issues have hindered delivery of the National Development Plan.

Projections for Irish GDP growth revised down, but job creation beating expectations: Our new forecast is for Irish GDP to contract by 1% in 2024, with modified domestic demand growth revised down slightly to 2.3%. This reflects the statistical distortions, and volatile data, that led to Irish GDP contracting in Q2 2024 by 1%, down for a fifth time in the past six quarters, despite a range of other indicators pointing to a buoyant economy. In contrast, Irish employment rose by 0.7% in Q1 2024 and by a further 0.8% in Q2, to a fresh record high of 2.74 million. Remarkably, over half (57%) of job creation over the past twelve months has been accounted for by non-Irish nationals. It also follows the news that the Irish population grew in 2024 by 1.9% (99,000) to 5.38 million. <u>Click here to download the full Ireland Outlook publication.</u>

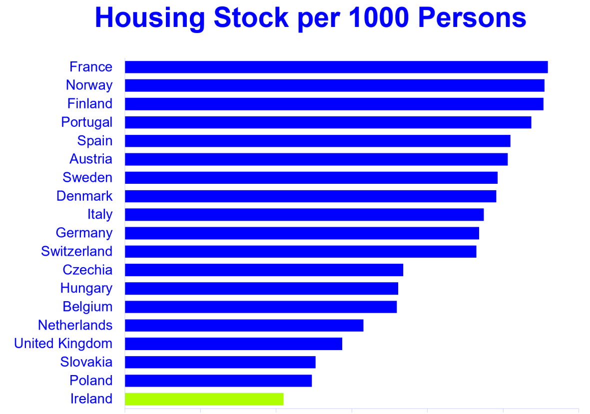
Some evidence of competitiveness pressures: Ireland has not seen this level of inward migration since the 2007/08 period. This time around there is less evidence of any bubble in lending, the construction sector, house prices or investment spending. However, there are signs that overheating pressure may be starting to emerge. For example, the CSO indicate average earnings grew by 5.6% in Q2 2024, vs 4.3% growth in the euro area. Whereas the ECB and others expect European pay growth to recede in 2025, most forecasters are projecting Irish pay growth to stay in the 4-5% range. Similarly, Irish house price inflation is currently running at 9.6% in July, whereas in the euro area residential property prices fell by -0.4% in the year to Q1 2024, again indicative of Ireland's tight housing market.

Deficits in housing, infrastructure and capital stock emerging: Looking at relative prices doesn't tell all the story. We estimate Ireland's housing stock is now 2.18 million, which translates into 405 homes per 1000 persons. The chart below shows this is close to the bottom of a range of European countries. To close the gap with the United Kingdom would require an additional 200,000 homes. The Irish Fiscal Advisory Council (IFAC) has also warned that whilst the stock of capital investment and infrastructure converged to European averages over the past two decades, it is now falling behind. Nonetheless, the latest IMD World Competitiveness Yearbook still placed Ireland 4th across 67 countries surveyed, no doubt reflecting the attractive corporate tax regime, but despite Ireland slipping to 38th on the survey question on basic infrastructure.

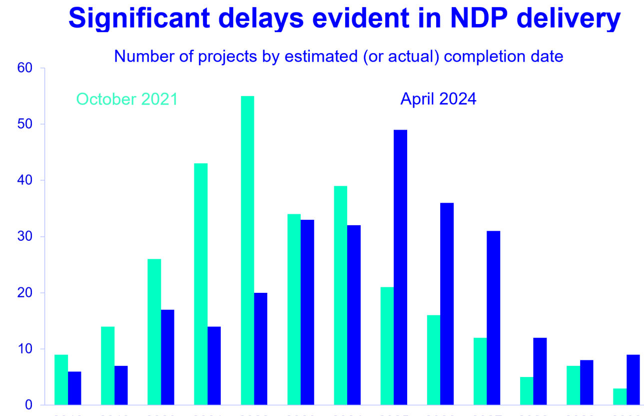
Delays in the delivery of the NDP and infrastructure: Ireland's National Development Plan (NDP) had planned to invest 5% of gross national income on infrastructure, vs the 3-4% typically seen in most European countries. Irish national accounts data imply build costs on non-residential construction in 2023 were 35% higher than in 2019. This has contributed to a fall in non-residential output, down 15% over the same period. Similarly, civil engineering activity (infrastructure) has been flat over the past four years, despite the sharp rise in public capital expenditure from €8.1bn in 2019 to €11.8bn in 2023. Hence, delivery of the National Development Plan has been delayed. The chart below shows that many projects that had been scheduled to be completed in 2024 are now not estimated to be delivered until 2025-2027 and beyond. Clearly, ensuring better delivery of public capital investment will be a challenge for the next government.

Chief Economist: Conall Mac Coille

Housing Stock per 1000 Persons



Significant delays evident in NDP delivery



Source: Euroconstruct

Source: NDP, Department of Public Expenditure, and Fiscal Council workings.

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