Ireland Outlook

Insights into the Irish economy

September 2024

Bank of Ireland

New Irish Economic Forecasts

Once again, erratic and volatile national accounts data for Q2 2024, have led us to revise down our forecasts for the growth of both GDP (-1%) and modified domestic demand (2.3%), but tell us little on the health of the economy. In contrast, the recent rapid pace of job creation means we expect employment to grow 2.4% in 2024 and 1.7% in 2025, helping to drive 2.7% and 3% increases in consumer spending. Investment is expected to grow as housing completions rise to 42,000 in 2025 and non-residential construction activity starts to recover after several years of contraction. Underlying export performance still looks favourable and the net trade contribution to Irish GDP growth should recover as statistical distortions dissipate and global demand improves.

Irish GDP to contract by 1% in 2024

We now expect GDP will contract by 1% in 2024, rebounding to 3.5% growth in 2025 and 4% in 2026. This follows the news Irish GDP contracted by 1% in Q2 2024, the fifth quarterly decline in the last six quarters. This sequence of falls has mainly reflected a surge in 'contract manufacturing' in 2022, unwinding through 2023. Thankfully, these distortions now look to have played out. The latest fall in Irish GDP is even more puzzling, apparently reflecting weaker indigenous firms, despite a sharp pace of job creation and growth in household spending. Hence, we expect modified domestic demand (2.3%) and consumer spending (2.7%) to see robust gains this year.

Employment forecast revised up to 2.4% growth

Official Labour Force Survey data point to little evidence of any material slowdown in the pace of jobs growth. Hence, we have revised up our forecast for employment growth to 2.4% in 2024 and 1.7% in 2025, and the unemployment rate down to 4.3% and 4.2% respectively. This is still an exceptional pace of job gains, and following the news the population grew by 1.9% for a second successive year in 2024. Meanwhile, pay growth has accelerated, with average earnings now forecast to grow by 5% in 2024. These real income gains will drive consumer spending to expand in 2025, seeing 3% growth, even as jobs growth starts to slow.

Budget 2025 will support demand next year

Since our last forecasts the Government's Summer Economic Statement (SES) has committed to a 6.9% rise in public expenditure in 2025 and tax cuts worth €1.4bn. These measures will support domestic demand and household disposable incomes next year. Given the strength of tax revenue growth (12.6%) in the first eight months of 2024, we have left our forecast for the government surplus of €7.4bn this year broadly unchanged, despite spending pressures. The outlook is still uncertain and will depend upon how corporation tax receipts perform in the final four months.

Housing market

We have revised up our forecast for Residential Property Price Inflation (RPPI) to 7.75% in 2024. This follows a 4.7% rise in the first seven months of 2024. Our analysis shows competition for homes intensified during the summer with 40% of transactions now being settled at a minimum 10% premium over the original asking price. In addition, the average mortgage approval for house purchase was €318,300 in July, up 6.2%, pointing to further gains. However, our current forecast is for RPPI to rise 4% in 2025 as affordability is stretched, closer to our forecast for pay growth.

Forecasts	2024f	2025f	2026f
Consumer spending	2.7%	3.0%	2.9%
Government expenditure	3.3%	1.7%	1.7%
Investment	-27.0%	20.9%	1.1%
Building & construction	-0.5%	8.6%	4.3%
Machinery & equipment (core)	3.0%	-4.5%	-5.0%
Modified Investment	0.4%	4.6%	1.9%
Exports	10.5%	3.4%	5.0%
Imports	6.5%	6.0%	4.4%
Modified Domestic Demand	**2.3%**	**3.0%**	**2.5%**
GDP	**-1.0%**	**3.5%**	**4.0%**
Multinational Sector	-8.9%	4.8%	5.0%
Indigenous Sector	2.7%	2.6%	2.7%
Government balance, % GDP	1.5%	1.3%	1.2%
Government debt, % GDP	42.7%	40.6%	38.7%
Employment Growth	2.4%	1.7%	1.5%
Unemployment Rate	4.3%	4.2%	4.2%
CPI Inflation	2.4%	2.0%	2.0%

Economy

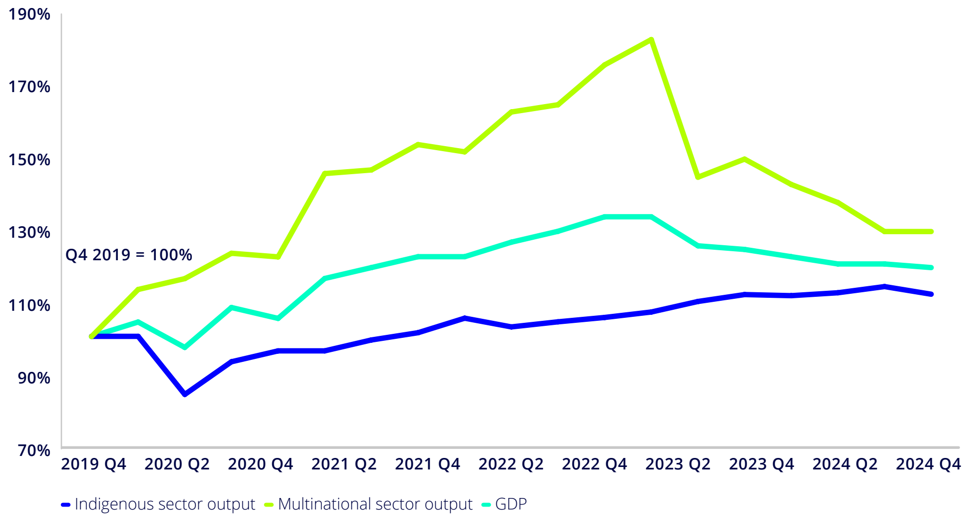
Rapid expansion has continued in H1 2024

Headline GDP contracts again in Q2...

Revised national accounts data indicate GDP contracted 1% in Q2 2024, reversing the 0.6% gain in Q1. GDP has fallen in five of the last six quarters. However, the latest fall reflected a surprise 1.8% contraction in indigenous sectors. Although we assume GDP will bounce back (by 2% in Q3 2024 and 1.3% in Q4) this still leaves calendar year GDP in 2024 down 1% on 2023.

We do not believe the fall in GDP in Q2 is concerning. Consumer spending (1.1%) and employment (0.8%) saw sharp gains in the same quarter. An unusually large €3bn decline in the statistical discrepancy between the expenditure and output (value added) sides of the national accounts – highlights the possibility of revisions to the GDP, or a rebound in the coming quarters. The data imply the financial services and arts/entertainment sectors saw unusual 10% declines in output in Q2.

Irish GDP split into multinational and indigenous sector output



Source: Central Statistics Office.

...but other data shows growth

Other indicators point to continued growth. The CSO's preliminary estimate of the unemployment rate was 4.3% in August. Ireland's composite (52.6), manufacturing (50.4) and services (53.8) PMI readings were all above the 50 no-change level in August, albeit with construction more subdued.

Industrial production data rose 2% in the three months to July, suggesting the distortions from 'contract manufacturing' in the multinational sector have played out. Traditional manufacturing was up 10% in the first seven months, albeit offset by a 16% decline in the multinational dominated modern sector.

Total tax revenues in the first eight months are up 12.6% to nearly €60bn, including sharp gains in income taxes (6.9%), value-added tax (7.5%) and corporation taxes (28%). Meanwhile, gross voted expenditure in the first eight months was close to €64bn, up 13% on the same period in 2023, demonstrating the public sector contribution to demand. The expansion of the domestic economy is also evident in the CSO's index of services sector output, up 1.2% in the three months to July.

Labour Market

Employment continues to expand at breakneck pace

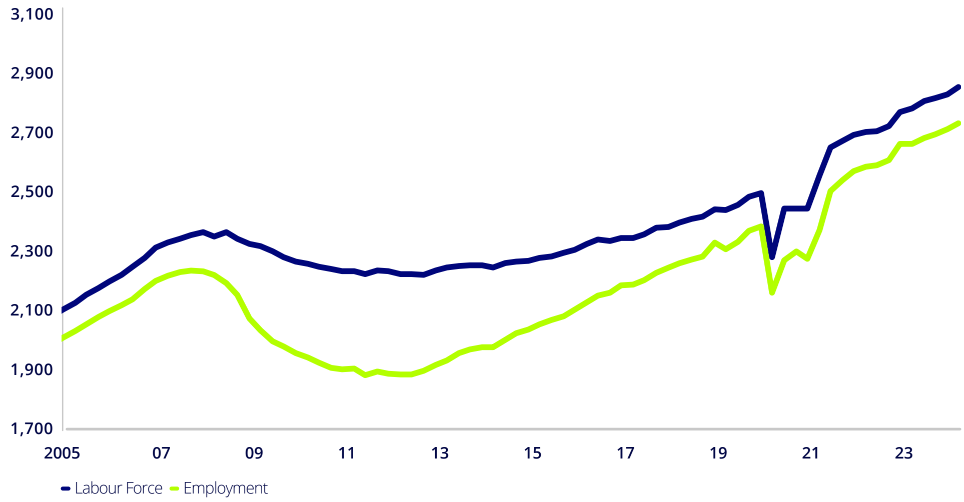
Record numbers at work…

According to the Labour Force Survey (LFS) there has been little material slowdown in job creation. Employment grew by 0.7% in Q1 2024, followed by a further 0.8% rise in Q2 2024, to a fresh record high of 2.74 million.

Notably, 57% of the rise in employment in H1 2024 was accounted for by non- nationals. The CSO's preliminary estimate of the unemployment rate was 4.3% in August, down marginally from 4.4% in Q2.

That said, the CSO's estimate of employees, was up 0.3% in the three months to July, to 2.48 million, a more sedate pace. However, August's PMI surveys indicated firms expanded employment at the fastest pace in six-months and one year respectively, in the manufacturing and services sectors. Hence, we have revised our projections for employment growth up to 2.4% and 1.7% in 2024 and 2025 respectively and for the unemployment rate down slightly, to 4.3% and 4.2%.

Irish Employment and Labour Force



Source: Central Statistics Office

…but pace of employment growth to ease

However, our view remains that skill shortages will still serve to slow jobs growth in 2025 and 2026. In Q2 2024, the participation rate for females reached a fresh record high of 61.4%, so there are probably limited further gains for that source of labour. Also, the population grew at an extraordinary 1.9% (or 99,000) pace for a second successive year in 2024, of which the vast bulk was accounted for by migration (79,000). This is inevitably contributing to a range of bottlenecks in the economy, not least in demand for housing and public services.

Labour Market Forecasts	2024f	2025f	2026f
Employment	2.4%	1.7%	1.5%
Unemployment Rate	4.3%	4.2%	4.2%

Source: Bank of Ireland, Central Statistics Office

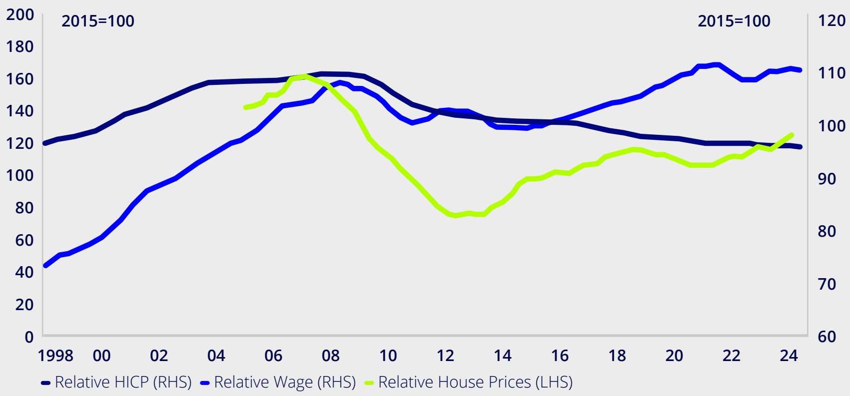
Labour Market

Overheating pressures starting to be felt

So far Ireland's exceptional economic performance has not yet led to a clear deterioration in competitiveness. For example, in August Irish HICP inflation was just 1.1%, half the rate in the euro area.

The lack of overheating pressure has largely been down to the unexpected expansion of the supply side of the economy. Specifically, Ireland's open labour market has facilitated inward migration respond to labour demand. The population has grown by almost 200,000 in the past two years, or by 3.8%, of which the vast bulk, 157,000 was accounted for by net migration. Over half of jobs growth in H1 2024 was accounted for by non-Irish nationals.

Chart A: Ireland Competitiveness indicators v the euro area



Source: Eurostat

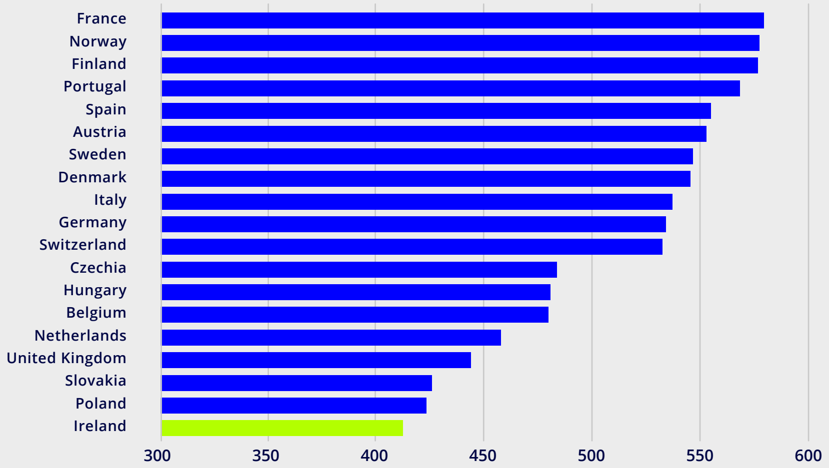
However, bottlenecks, capacity pressures and labour shortages are becoming increasingly evident. In Q2 2024 Irish average weekly earnings were up 5.6%, to €50,000, outpacing the 4.3% growth in euro area compensation per head over the same period. The strength of demand is especially evident in the housing market. In Q1 2024 Irish Residential Property Price Inflation (RPPI) was 6.3%, well ahead of the -0.4% decline in house prices across the euro area. On relative basis (see chart above) Irish house prices are now back to their most expensive level, relative to the euro area, since mid-2009.

Latest Price/cost readings for Ireland and the euro area	Ireland	Euro Area
HICP Inflation	2.2%	1.1%
Residential Property Price Inflation	6.3%	-0.4%
Average Earnings	5.6%	4.3%

Of course, looking at relative prices only tells some of the story. We estimate Ireland's housing stock is now close to 2.18 million which translates, given the latest population estimate of 5.38 million, into 405 homes per 1000 persons. Chart B below indicates this is lowest figure across the entire group of European countries for which Euroconstruct collect data. To close the gap with the United Kingdom, itself close to the bottom of the range, would require an additional 200,000 homes.

Labour Market

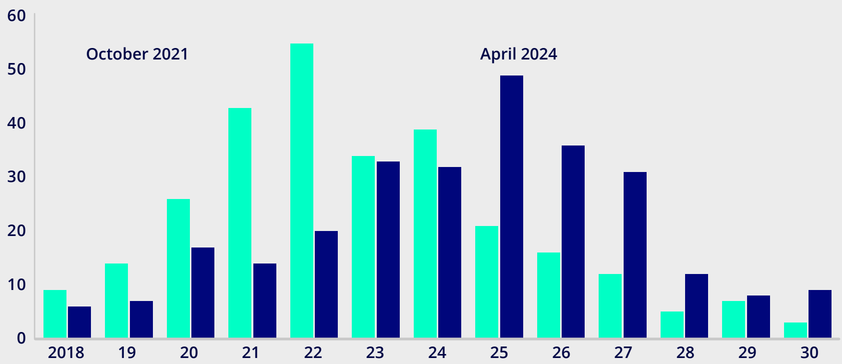
Chart B: Housing Stock per 1000 persons



The Irish Fiscal Advisory Council (IFAC) has also warned that capital stock levels, having converged towards high income EU average levels, are now becoming stretched again as both the population and economy has grown rapidly. Hence, the National Development Plan (NDP) had intended to raise public investment above 5% of gross national income (GNI*) vs the 3-4% seen in most OECD countries.

However, implementation of the NFP has been held back by planning delays and by the build cost inflation which has hurt activity across the non-residential construction sector. IFAC and Department of Expenditure Reform Analysis illustrates the substantial delays to projects set out in the NDP (Chart C).

Chart C: Number of Projects by Planned and Estimated or Actual Completion date



Source: Irish Fiscal Advisory Council

Build cost inflation has severely hindered delivery of infrastructure. Ireland's national accounts indicate that build costs in 2023 for non-residential construction were 35% higher than in 2019. Hence, the CSO's index of construction output indicates non-residential activity in 2023 was 15% lower than in 2019, and for civil-engineering activity has been flat over the past five years.

Labour shortages are also an issue. IFAC's analysis also suggested that 180,000 construction workers are likely to be required to realise the NDP's ambitions, well in excess of the 165,000 average over the past 12 months.

Of course, housing, infrastructure and labour costs and availability do not paint the full picture of Ireland's competitiveness. The IMD World Competitiveness yearbook 2024, still placed Ireland 4th across the 67 countries surveyed. This no doubt reflects Ireland's attractive corporate tax regime and comes despite 46th and 38th rankings respectively in the survey questions on prices and basic infrastructure.

Nonetheless, the focus of government policy should now clearly be on delivery of the National Development Plan to alleviate the bottlenecks and capacity pressures that will eventually constrain the growth of the Irish economy.

Consumer

Consumer spending now being driven by real income gains

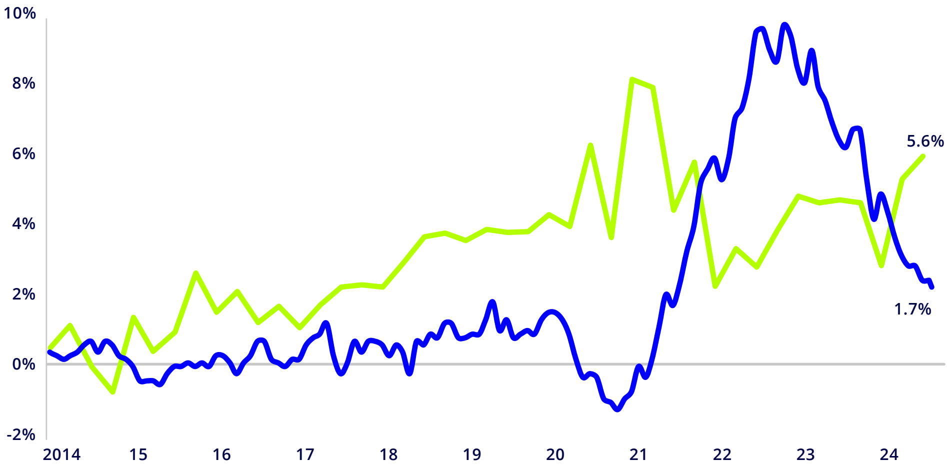
Consumer spending to benefit from lower inflation

Consumer spending has actually being a little softer than we had forecast in July. Consumption rose by 1.1% in Q2 2024, but the initial 0.6% gain in Q1 was revised to zero. Hence, our projection for consumer spending has been revised down slightly to 2.7% growth in 2024, but for 3% in 2025.

Retail sales have been subdued, core sales were down -0.2% in the three months to July. However, the strength of consumption in Q2 2024 was accounted for by services, up 1.9% on the quarter.

Our forecast that employment will rise by 2.4% in 2024 is a key driver of spending. However, the latest estimate is that average weekly earnings grew by 5.6% in the year to Q2 2024, to €50,000 (on an annualised basis) well above current rates of CPI (1.7%) and HICP (1.1%) inflation. Real household incomes are expanding again, after cuts in 2022 and 2023 due to higher energy prices and inflation.

Irish CPI Inflation and Average Earnings growth



Source: Bank of Ireland, Central Statistics Office

The household savings ratio was surprisingly strong in Q1 2024, rising to 14.6%. Our forecasts are conditioned on only a gradual decline in the savings ratio to 14.3% in 2025 and 13.9% in 2026.

Household incomes and spending	2023	2024f	2025f	2026f
Compensation	10.7%	7.3%	6.3%	5.5%
Gross Disposable Income	11.1%	7.3%	5.0%	4.5%
Savings Ratio	13.9%	14.5%	14.3%	13.9%
Nominal Spending	13.2%	6.5%	5.2%	5.0%
Consumer Expenditure Deflator	8.1%	3.6%	2.2%	2.0%
Real Spending	4.8%	2.7%	3.0%	2.9%

Source: Bank of Ireland, Central Statistics Office

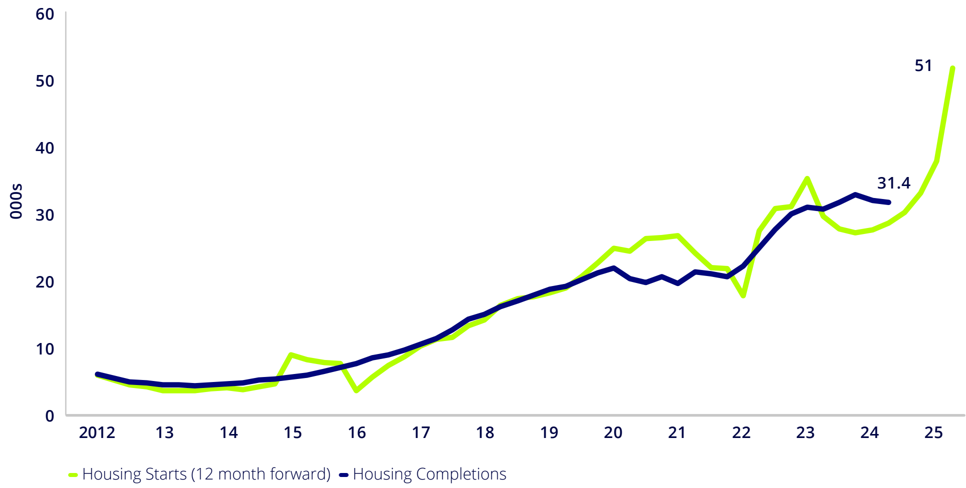
Investment

Construction sector to drive investment spending

House completions to pick up to 45,000 by 2026

Housing completions were 12,730 in H1 2024, down 8.6% on 2023, suggesting disruption from elevated build costs and energy prices was still being felt. We have revised down our forecast for completions to 33,000 in 2024. Housing starts have surged, 51,000 in the twelve months to June, many no doubt brought forward due to the expected expiration of a waiver on development charges and levies. We have stuck with our forecast for 42,000 completions in 2025 and 45,000 in 2026.

Housing Starts and Completions



Source: Bank of Ireland, Central Statistics Office

Non-residential construction to contract again this year

Investment spending on non-residential construction in H1 2024 was down 6.7% on the year. We had hoped it would stabilise, but that now looks too optimistic, and expect a 2% contraction in 2024. This illustrates that build cost inflation is still weighing on public and private investment projects, a disappointing development when capacity pressures and bottlenecks are increasingly evident. In contrast, core machinery and equipment spending in H1 was up 4.3% on the year, still at elevated levels.

Forecasts for Real Investment Spending	2024f	2025f	2026f
Residential	1.4%	27.2%	7.1%
Non-residential construction	-2.0%	1.5%	3.0%
Machinery and equipment (core)	3.0%	-4.5%	-5.0%
Intangible Assets	-55.2%	60.0%	0.0%
Total Investment	-27.0%	20.9%	1.1%
Modified Investment	0.4%	4.6%	1.9%

Source: Bank of Ireland, Central Statistics Office

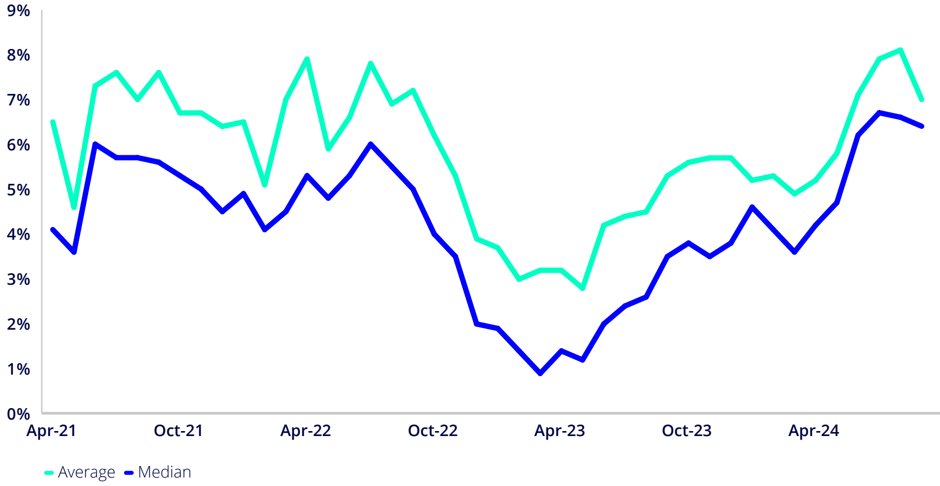
Housing Market

Residential property prices to rise 7.75% through 2024, 4% through 2025

Stiff competition in housing market

The CSO's official Residential Property Price Index (RPPI) rose by 9.6% in the twelve months to July 2024. So far, year-to-date (December to July) it is up 4.7%. Our analysis indicates that competition for homes intensified through the summer. The premium homebuyers paid over the original asking price rose from 5% at the median in Q2 2024, to 6.6% through July and August.

Premium paid over original asking price



Source: Bank of Ireland, Central Statistics Office

Demand factors driving prices

The pick-up in house price inflation is clearly being driven by the buoyant labour market, with earnings growth up 5.6% in the year to Q2 2024. This is evident in the mortgage market. The average mortgage approval for house purchase in July was €318,300, up 6.2% on the year. In addition, Central Bank data shows leverage amongst first-time-buyers with mortgage debt rose through 2023, and likely continued to do so in 2024, as the regulatory threshold on loan-to-income ratios was relaxed.

Hence, we have revised up our forecast for RPPI inflation to 7.75% in 2024 and 4% in 2025.

In contrast to residential property prices, the growth of activity in the housing market has been constrained by the lack of stock for sale. We estimate residential transaction volumes in Q1 and Q2 2024 were down 8% and 2% respectively on the same periods of 2023. There are currently just 12,900 homes listed for sale on MyHome, still close to a record low.

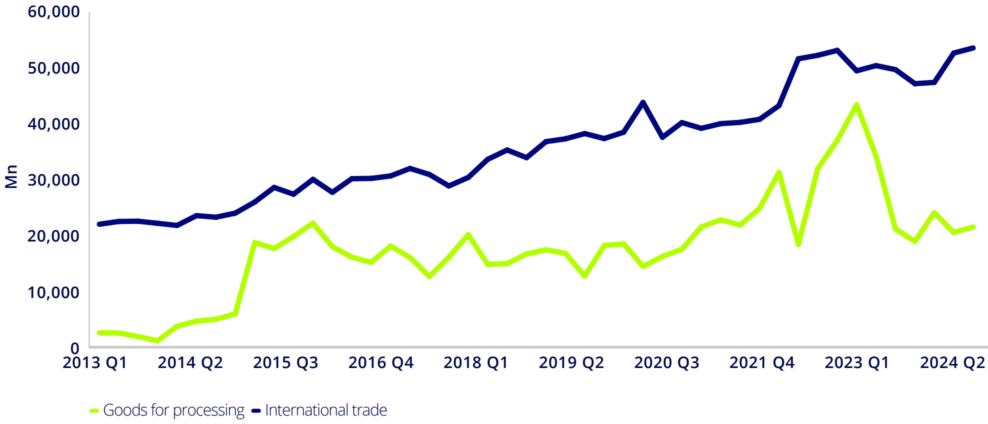
Exports

Export sector performing well, peering through the statistical fog

MNC activity clouds export picture...

We have revised our forecast for export growth in 2024 to 10.5%. However, again, this reflects a statistical distortion, related to the transfer of intellectual property assets (recorded as service export) that is neutral for GDP, also showing up as negative investment spending. Thankfully, the distortions from the decline in 'contract manufacturing' appear to have played out, although they are still the key reason we expect Irish GDP to contract by 1% in 2024.

Irish goods export trade



Source: Central Statistics Office

...but underlying position appears healthy

Peering through the statistical fog, the underlying performance of the Irish export sector looks positive. Although industrial production was down 12% in the first seven months, this entirely reflected the modern sector as traditional manufacturing was up 10% on the year. Similarly, the monthly measure of goods export volumes (excluding contract manufacturing) was up 6.5%, with nominal pharmaceutical exports up 18%, in the first seven months of 2024. Business, financial and ICT services exports also saw rapid growth in H1.

Demand for Irish exports should improve slightly. May's OECD Economic Outlook forecast that Irish export markets would grow by just 1.2% this year, but by 2.9% in 2025. Similarly, in July the IMF revised up marginally its forecast for global GDP growth to 3.3% next year. Although, concerns have grown that both euro area and US growth may be faltering, Ireland's concentration in defensive sectors (med-tech, pharmaceuticals) and in ICT, should see underlying export growth improve in 2025.

Export and Trade forecasts	2020	2021	2022	2023	2024f	2025f
Irish Exports	13.8%	14.1%	13.5%	-5.8%	10.5%	3.4%
Irish Exports Markets	-9.8%	8.7%	6.0%	-0.4%	1.2%	2.9%

Source: Bank of Ireland, CSO, OECD

Inflation

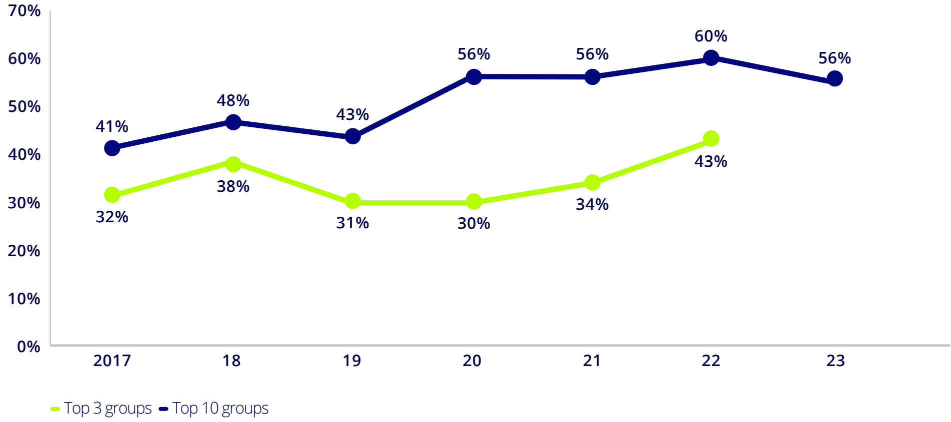
Budget 2025 set to support demand

Public finances in a healthy state

The public finances have continued to perform well in 2024. Tax revenues of almost €60bn were collected in the first eight months of 2024, up 12.6% on the year, broad based across income taxes (6.9%), value added taxes (7.5%) and corporation taxes (28.4%). Gross voted spending has also grown rapidly, up 12.9% to €63.6bn. This has led to a slight improvement in the central government surplus, from €1.7bn in the first eight months of 2023, to €2.8bn in 2024. On this basis the government is well ahead of its projection to run a surplus of €8.6bn.

However, the Department of Finance has itself warned spending pressures are building. In the first eight months current spending was 4% ahead of Departmental allocations, including the Department of Health which is 10% or €1.45bn ahead of target. Once off spending measures in Budget 2025, but implemented this year, will also depress the surplus. Also, some of the 28% growth in corporate taxes may reflect timing factors, with calendar year growth by end-2024 likely to be more subdued. Hence, we have left our forecast for the government surplus broadly unchanged at €7.4bn in 2024, falling to €7bn in 2025 and 2026.

Concentration of Irish Corporate Tax receipts



Source: Irish Fiscal Advisory Council

Election pressure risks bigger budget package

The Summer Economic Statement (SES) has set out that a total budget package of €8.3bn will be set out in Budget 2025. This is intended to deliver spending growth of 6.9%. The €8.3bn is split between €1.4bn of tax cuts, €1.8bn of spending still to be allocated, €3.7bn to maintain existing levels of public service provision and €1.4bn to implement the National Development Plan. However, ahead of a general election there is clearly a risk further spending measures could add to the size of the planned budget package.

One rational for a cautious approach in Budget 2025 is research by the Irish Fiscal Advisory Council showing the top 3 groups accounted for 43%, or close to €10bn of the corporate taxes collected in 2022.

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