Economic Research

7.8% Irish growth in 2017, 7% forecast for 2018 16 Mar 2018

The Irish economy grew by a real 7.8% last year according to the preliminary estimate from the CSO, bringing the cumulative increase over the past three years to 45%. Nominal GDP expanded by 7.5% in 2017, to €296bn, and is now over €100bn larger than in 2014. One consequence is that Ireland's headline debt ratio has tumbled, to 68.4% last year from a peak of 120% in 2012, and may now fall below 60% as early as 2020.

Recorded growth of that magnitude implies special factors at work and in Ireland's case the large multinational presence dominates, particularly following the relatively recent changes to GDP methodology. One result is that exports are now dependent on a change of ownership, allowing contract manufacturing (production offshore for an Irish domiciled company) to be classed as a home export. This has had a significant impact and in 2017 total merchandise exports as recorded in the national accounts totaled €194bn, against €122bn recorded as produced in Ireland. The former figure was broadly flat on the previous year, however, but service exports grew by 14%, with the result that total exports expanded by 6.9% in volume terms.

In contrast, imports fell, by 6.2%, mainly as a result of a substantial decline in service imports, in turn dominated by a huge fall in R&D spending by multinationals. The latter is GDP neutral, however, as it is also captured in the Capital Formation component via Intangibles, and spending there plunged by 41%, after more than doubling in 2016. Investment in Machinery and Equipment also fell, by 11%, and although Building and Construction rose strongly, by over 16%, boosted by the recovery in house-building, this was not enough to prevent a 22% fall in overall Capital Formation.

Government consumption grew by 1.8% and Personal Consumption expanded by 1.9%, with the latter surprisingly soft given a 2.9% rise in employment last year and a modest acceleration in pay growth, to 2%. So in sum domestic demand fell sharply, by 8%, largely reflecting the plunge in Intangibles, and thereby making a 6% negative contribution to the change in GDP, offset by a 14% contribution from net exports, with stock building also adding a positive 1%. Profit outflows picked up strongly and as a result GNP lagged that of GDP, expanding by 6.6%. The CSO also produces a modified national income figure , GNI*, which adjusts for other multinational flows, but that will be published later in the year.

On a quarterly basis GDP growth was heavily skewed to the second half of the year, with the economy expanding by 3.2% in the final quarter following 4.8% in q3. Capital formation actually made the strongest contribution to q4 growth, followed by net exports, as personal consumption was particularly weak, expanding by only 0.3%. Indeed, consumption now accounts for less than a third of real GDP, such has been the growth in exports and investment spending in recent years.

The strong end to the year left the annual growth rate in the final quarter at 8.4%, and even if there was no growth through the year the carry-over effect alone would deliver an annual average GDP increase of over 5% in 2018. The quarterly pattern in Ireland is unusually volatile, however, and the national accounts can throw up shocks and surprises but the available high frequency data does suggest that the economy is still performing well and we now expect 7% growth in 2018.

Net exports are again forecast to provide the main positive contribution to growth, albeit much lower than last year as imports are expected to recover on the basis that Intangibles will be broadly flat. Spending on Machinery and Equipment is also likely to recover somewhat , which alongside further growth in Construction should provide a positive contribution from Capital Formation. Personal consumption is also forecast to pick up, albeit modestly to 2.5%, as employment growth may well slow somewhat as we near full employment ,with inflation also expected to be modestly higher.

Ireland's exposure to the global economy is high and the multinational presence also has increased the company specific risk so adverse developments in the international economy would no doubt have a negative impact on the national accounts. Brexit poses a more specific risk given the importance of the UK to indigenous Irish industry, notably the Food sector. Any monetary tightening by the ECB would also prove significant given the share of floating rate debt held by Irish households, although at the time of writing that appears unlikely this year. Overall, risks are certainly plentiful, but our base case is for another very strong GDP reading in 2018.

Real GDP (% change)	**2016**	**2017**	**2018 (f)**
Personal Consumption	3.3	1.9	2.5
Government Consumption	5.3	1.8	2.0
Fixed Capital Formation	61.2	-22.3	7.5
Stocks (% GDP)	1.0	1.0	0.5
Exports	4.6	6.9	7.5
Imports	16.4	-6.2	6.2
GDP	5.1	7.8	7.0
GNP	9.6	6.6	7.0

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