Economic Research

Irish growth 2.4% in q1, 5.6% now forecast in 2019 15/7/19

Irish GDP expanded by 2.4% in real terms in the first quarter of the year, which followed growth of 8.2% in 2018, the latter a substantial upward revision from the initial 6.7% estimate. Growth in 2017 was also revised higher, by around 1 percentage point to 8.1%. As a consequence nominal GDP last year is now put at €324bn or some €6bn above the initial figure, meaning that the General Government debt ratio ended the year at 63.6%i instead of the preliminary 64.7%.

The revisions also helped to solve, partially a least, the puzzle of the relatively soft consumer spending readings over recent years, as they seemed out of kilter with the very strong growth seen in household incomes. It now transpires that real personal consumption grew by 12% over the last three years instead of the initial 8.6%. The growth in Government consumption was revised down a little, but still marginally outpaced personal consumption over the period, with the Authorities taking the opportunity afforded by falling debt service costs and stronger than forecast corporation tax receipts to boost exchequer outlays.

Turning to 2019 , the higher frequency data had pointed to a strong first quarter and that duly emerged. Personal consumption grew by 0.8% in q1, outpacing government consumption growth of 0.5%, with a strong stock build another positive. Overall domestic demand fell however, following a 25% decline in capital formation, with similar percentage declines in both machinery and equipment and intangibles dwarfing the 5% expansion in construction spending. Multinationals account for most of the intangibles component which is also captured as a service import and as such broadly neutral for GDP (total imports fell by 2.4%). Similarly, aircraft leasing impacts the machinery and equipment component and also imports but underlying spending fell by over 8%, perhaps capturing some of the Brexit uncertainty that is also dampening business investment in the UK.

Export growth was also softer than in recent quarters, at 1%, but still leaving net external trade as the main driver of growth given the fall in imports. Indeed, such is the scale of Irish exports relative to GDP (124%) that developments in personal consumption or government consumption have little impact on the overall growth figure, although having a much bigger effect on households in Ireland.

The data revisions also mean a stronger carry-over effect into 2019 which alongside the buoyant first quarter left annual growth in q1 at 6.3%. Consequently, absent further revisions, average growth this year would be 4% even with no change in GDP through the remaining three quarters. The global environment is certainly less supportive than last year , notably in Europe, and the risks of a hard Brexit are perceived to have risen, which if materialising would certainly have a significant negative impact. However, the available indicators point to continuing Irish growth in q2 and any Brexit fall- out would probably hit in the final quarter and into 2020.

Consequently we feel the current consensus growth forecast for this year, at around 4%, is too low and we have revised up our 2019 estimate to 5.6% from 5%. This reflects stronger personal consumption than initially projected but the key factor is an upward shift in our export estimate, which offsets a decline in capital formation, the latter due to a fall in spending on machinery and equipment.

The Irish unemployment rate has continued to fall and currently stands at 4.5%, raising the issue of whether the economy is now supply constrained. The European Commission believes that Ireland is operating with a strongly positive output gap although the Department of Finance disputes this, albeit believing the previous negative gap will turn modestly positive this year. Wage inflation has certainly picked up (average weekly earnings growth in the private sector accelerated to 4.2% in q1), but to date that has not had a material impact on consumer prices, which continue to be dampened by the stronger euro/sterling rate and a more competitive environment on the Irish High Street; annual CPI inflation was 1.1% in June and we expect the average in 2019 to be 1.0%. On the fiscal side the Government is projecting a small General Government surplus this year and a modestly higher surplus of 0.4% of GDP in 2020, predicated on an orderly Brexit. In the event of a no-deal Brexit the Minister for Finance has indicated that he would allow automatic stabilisers to kick in and support some vulnerable sectors, so allowing a deficit of up to 1.5% of GDP. The Budget is still scheduled for early October and it might be more sensible to delay it for at least a month but that does not seem to be on the cards.

Real GDP (% change)	**2018**	**2019 (e)**	**2020 (f)**
Personal Consumption	3.4	3.0	3.0
Government Consumption	4.4	3.5	3.0
Fixed Capital Formation	-21.1	-1.0	8.3
Stocks (% GDP)	0.4	0.5	0.4
Exports	10.4	12.0	7.0
Imports	-2.9	12.0	8.0
GDP	8.2	5.6	4.5
GNP	6.5	4.1	3.8