Economic Research

GDP grew 6.7% in 2018, 5% forecast for 2019 18 Mar 2019

The Irish economy grew by 6.7% in 2018 according to CSO data, which was marginally ahead of our 6.5% estimate but below consensus , with many expecting 7.5% or above. Nominal GDP expanded by 8.3%, to €318bn , taking the rise over the last six years to over 80% and hence flattering the debt ratio, which ended 2018 at under 65% from a peak of 120% in 2012.

Last year's outturn in large part reflected a strong carryover effect from 2017, as the economy slowed through the year, with a quarterly rise of 0.9% in q3 followed by just 0.1% in the final quarter. As a consequence annual growth ended the year at 3%, so the carryover into the new year will be much softer in 2019.

Consumer spending growth has been modest in recent years given the strength of employment and household income growth and 2018 saw a 3% advance. Consequently, household consumption now accounts for only one-third of Irish GDP, which is well below the EU norm. In contrast , the Exchequer has taken the opportunity afforded by above target tax receipts, notably from corporation tax, to boost both current and capital spending, with government consumption rising by 6.4% last year.

Construction output has continued to see strong growth, albeit from a weak base, and spending last year in that sector rose by 16%, as in 2017, with house building up by 26% and other building seeing a 12% gain. Investment in machinery and equipment has been more volatile but grew last year by 37% following a decline in 2017, with the rebound strongly affected by a surge in aircraft leasing. The other component of capital formation is Intangibles and that too is extraordinarily volatile, falling by 50% in 2017 and plunging further in the early part of the year before recovering to reduce the average decline in 2018 to 10%. As a consequence investment spending as a whole rose by 9.8% in 2018 after a 31% fall the previous year.

Much of the non-construction investment spending in Ireland is imported as a good or service by the multinational sector and so 2018 also saw a recovery in total imports, which grew by 7%. Export growth was stronger still, at 8.9%, meaning that the external sector made a strong positive contribution to GDP. The current account on the balance of payments also rose, to €29bn, or 9.1% of GDP. GNP , which adjusts GDP for profit and interest flows grew by 5.9%, while modified domestic demand, which strips out the multinational influence on investment, grew by 4.5%.

The slowdown in Irish activity in the final quarter ,as captured in the GDP figures ,is also apparent in some of the high frequency data and has carried into 2019, notably in consumer confidence, car sales, mortgage approvals and house prices. Brexit related uncertainty may well be a strong common factor, and as such could dissipate, but the economy may also be facing constraints on the supply side, particularly in the labour market. The unemployment data for the latter part of 2018 was recently revised and it now transpires that unemployment is higher than thought and has actually ticked up of late. The unemployment rate has also been largely flat for some time now at 5.6-5.7%, and forecasts for a sub 5% reading in 2019 now look unachievable.

Against that, buoyant GDP , driven by exports, alongside employment over the last few years implies that productivity is growing by almost 4% a year, so a deceleration in job creation may not lead to a marked slowdown in output. Indeed, exports and industrial production have started the year on a strong note and so we forecast 5% GDP growth for 2019, despite weaker growth in both personal and government consumption , as well as a further deceleration in the pace of expansion in the construction sector. Of course domestic spending and indigenous exports could be weaker than we envisage depending on how Brexit plays out.

The revised data on the labour market has also prompted us to change our forecasts for labour demand , the labour force and unemployment, with the unemployment rate now set to average 5.4% in 2019. Wage inflation has picked up, to an annual 4.1% in the final quarter of 2018, and this may put some upward pressure on Irish inflation in the service sector. Sterling's recent rally, if sustained, may also mean that the goods prices start to pick up and so the sub-1% CPI inflation trend of recent years may come to an end. The Exchequer has also benefitted from another long standing pattern, this time relating to persistent above target receipts from corporation tax, and this too may turn, which alongside weaker employment growth may mean that the Exchequer records a small deficit rather than the forecast balance.

Real GDP (% change)	**2017**	**2018**	**2019 (f)**
Personal Consumption	1.6	3.0	2.5
Government Consumption	3.9	6.4	4.0
Fixed Capital Formation	-31.0	9.8	10.0
Stocks (% GDP)	1.3	0.5	0.4
Exports	7.8	8.9	7.0
Imports	-9.4	7.0	9.0
GDP	7.2	6.7	5.0
GNP	4.4	5.9	5.5

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