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Irish Economic Forecast:4% growth in 2020 ,7% in 2021

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We were an outlier in terms of our Irish GDP forecast for most of the year, in anticipating a much smaller contraction than the consensus, given the early evidence that the export sector was proving much more resilient than the domestic economy, reflecting its high weighting of Pharma, organic chemicals, medical devices and ICT. The consensus eventually duly shifted to a modest fall in GDP, but the release of the third quarter national accounts has precipitated a further upward move and we now expect a positive figure for the year, with growth of around 4%, which would not only make Ireland an outlier in the EU, in avoiding a contraction, but would also probably outstrip China in terms of the rise in GDP.

GDP grew by 11.1% in q3 according to the CSO following a revised 3.2% fall in q2 and a 3.6% contraction in the first quarter. This left annual growth in q3 at 8.1% and the average annual growth over the first three quarters at 3.6%. Absent a huge fall in q4 (and data revisions) it seems highly likely the change in 2020 Irish GDP was positive, and strongly so. Of course, this masks a huge divergence between the external and domestic sectors, with Consumer spending falling an estimated 7.5%, Investment down 15%, and only marginally offset by a 9% increase in Government consumption. GDP growth is therefore all due to exports which we estimate rose by 5% and their huge weight in the national accounts (129%). The corollary to that export performance was higher multinational profits and as the third quarter saw an unusually large profit outflow, the growth in GNP, which adjusts for profit and interest flows, will be lower, at a forecast 2.0%.

The path of the pandemic presents one degree of uncertainty as we move into 2021, and even with the positive news on a vaccine further domestic Lockdowns are certainly possible on top of the current one. In addition, Brexit may dampen some external trade, despite the emergence of a free-trade agreement on goods. That said, the Irish economy is likely to enter the coming year with strong annual carry over and in the first half of next year the large contraction in H1 2020 will drop out of the annual growth measure. The first quarter figure may be soft due to the January Lockdown, however, but we still expect growth of 7% over the year, fuelled by further export growth and a recovery in domestic demand.

Consumer spending is likely to rebound (we forecast 10% growth) and construction is also expected to pick up strongly, with a recovery also in spending on machinery and equipment. The rise in domestic demand will also be reflected in imports which we forecast to grow by 13%, so offsetting the impact of a projected 8.0% rise in exports.

The fall in domestic demand in 2020 had a big impact on jobs in certain sectors, notably personal services, hospitality and tourism, although employment as officially measured did not fully reflect this as many workers were furloughed and received transfer payments from the State. Consequently the official unemployment rate averaged some 6% in 2020, from 4.9% the previous year, but may well continue to rise over the first half of 2021 before falling back as some firms close for good and others cut back on staff; we forecast a 6.7% average figure for the year. The CSO estimate that if one assumes all those receiving pandemic unemployment payments were deemed unemployed this covid adjusted unemployment rate exceeded 20% at times, but will fall as the economy re-opens. Weekly earnings held up well for those in work , rising by an estimated 4%, which alongside the increase in transfer payments ensured a similar rise in household income despite the pandemic impact on domestic economic activity.

The combination of income growth and restricted consumption resulted in a huge rise in forced savings, pushing the savings ratio to 34% in the second quarter, before falling back to some 20% in q3, against 12.3% for 2019.. This forced saving was also reflected in bank deposits, which also rose substantially, and by the second quarter of the year household deposits and cash exceeded household debt by a record €28bn. The savings ratio is also likely to fall, but the pace and degree of that fall is highly uncertain; we expect an average of 15% from around 20% in 2020..Weak consumption allied to slumping energy prices also translated into falling consumer prices, with inflation declining to -1.1% in November. Base effects alone should ensure a return to positive inflation in 2021, and we forecast an average 0.5%.

The combination of much higher transfer payments and lower tax receipts pushed up the fiscal deficit but revenue proved more resilient than expected, with the result that the Exchequer deficit came in lower than the Government had expected only a few months earlier, at €12.3bn, with the General Government deficit at an estimated €19bn, or some 5.2% of GDP. The debt ratio probably ended the year around 60% of GDP, up from 57.3%, with the primary deficit offsetting the positive impact of growth exceeding the interest rate on the debt, now under 2%. The 2021 Budget forecast a deficit of over €20bn or 5.7% of GDP, but this was predicated on a no-deal Brexit and growth of just 1.7% and therefore looks far too high.

Table 1 Irish GDP Forecast

Real GDP (% change)	2019	2020(e)	2021(f)
Personal Consumption	3.2	-7.5	10.0
Government Consumption	6.3	9.0	5.0
Investment	74.8	-14.3	23.0
Construction	8.0	-10.5	12.0
M+E+I	98.7	-15.0	25.0
Stocks (% of GDP)	0.5	1.3	0.8
Exports	10.5	5.0	8.0
Imports	32.4	-3.2	13.0
GDP	5.6	4.0	7.0
GNP	3.4	1.8	9.0

The weight of exports in Irish GDP, and the composition of those exports, makes Ireland more akin to a secular growth stock rather than the cyclical economy traditionally assumed by Irish forecasters, which also helps to explain why the consensus has consistently underestimated growth in recent years. This also makes Ireland highly unusual if not unique, in being a very high income developed economy yet with the growth characteristics of a developing one.