7. IRELAND

Rapid growth to continue

GDP growth is projected to remain robust over the forecast horizon but the pace is expected to moderate slightly. The activities of multinational enterprises continue to distort headline figures and complicate macroeconomic forecasts. The government deficit is moving closer to balance but risks to the fiscal outlook remain.

Underlying domestic demand to maintain its strong momentum...

In the first half of 2017, Ireland's real GDP grew by 5.7% (y-o-y), well above the euro area average. The headline figures remain volatile and heavily influenced by the activities of multinational enterprises in the country. Modified domestic demand, a measure of domestic activity that strips out the effect of multinationals, grew at robust rates driven by private consumption and construction investment. It is expected to continue to expand at an average rate of 4% over the forecast horizon.

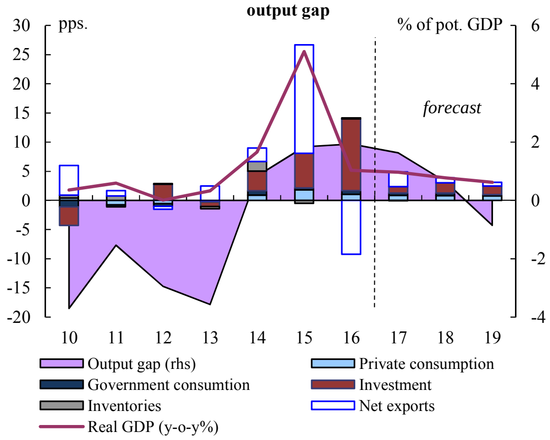
...buoyed by robust employment and investment in construction.

The unemployment rate in Ireland fell to 6.1% in September and is forecast to reach 5.3% by the end of 2019. The strong increase in employment, particularly in full-time employment, is expected to support the further increase in labour income over the forecast horizon. In conjunction with subdued inflation, this is expected to boost consumer spending in the near term.

Investment in construction is projected to contribute substantially to growth in domestic demand, with the strong momentum in residential property investment in 2016 expected to continue in the medium term, supported by government policies. Insufficient housing supply remains a challenge and is expected to show up in house prices and rents. Headline investment figures are likely to remain volatile due to the unpredictable investment in intangibles (e.g. patents and copyrights) by multinationals in Ireland.

Inflation is expected to increase gradually. Consumer prices (HICP) rose only marginally in the first three quarters of 2017 at an average rate of 0.2%. This was due to increasing energy prices and services. However, currency depreciation in the UK, from which Ireland imports much, lowered the price of many goods, offsetting increases in the price of services. Over the forecast horizon, the effect of lower goods prices is expected to moderate, while higher prices for services and residential rents are expected to nudge inflation slightly higher.

Graph II.7.1: **Ireland - Real GDP growth and contributions, output gap**



Trade outlook still clouded by uncertainty

The activities of multinationals in Ireland also have a large influence on the country's export and import statistics. Contract manufacturing [114] weighed on goods exports in 2016 and in the year to June. Total exports of goods dipped by 4.1% (y-o-y), but the contraction was offset by a strong increase in service exports in the first half of 2017. Over the same period, total imports declined by 1.7% (y-o-y) driven by extremely volatile 'imports' of intellectual property services. As a result, net external trade contributed significantly to GDP growth in the first half of 2017. Exports are projected to increase in line with global trade while imports are predicted to gather momentum on the back of strong consumer demand, leading to a moderation of the positive impact of net exports on GDP growth. Given the ongoing negotiations on the terms of the UK withdrawal from the EU, projections for 2019 are based on a purely technical assumption of status quo in terms of trading relations between EU27 and the UK. This is for forecasting purposes only

(114) Contract manufacturing refers to the production of goods abroad on behalf of Irish-domiciled entities for exporting.

and has no bearing on the talks underway in the context of the Article 50 process.

Risks to the outlook are tilted to the downside

The uncertainty surrounding the economic outlook relates primarily to the external environment, including the outcome of the negotiations between the UK and the EU and potential changes to the international taxation environment and US tax and trade policies. A large degree of unpredictability remains and is related to the activities of multinationals with risks being on either side.

Growth outlook positive for public finances

The general government deficit is projected to fall to 0.4% of GDP in 2017, an improvement of 0.4 pps. net of one-offs [115] compared with the previous year's deficit and reflecting the sustained pace of Ireland's economic growth.

Cash returns for the first three quarters of 2017 were broadly in line with government projections despite sizeable shortfalls in personal income tax, excise and stamp duty receipts. Overall, tax revenues increased by 5.4% over the twelve months to September, while expenditure remained below target across all departments except in the health area, where slippages of around EUR 166 million emerged.

Ireland's 2018 Draft Budgetary Plan includes new spending measures of around 0.4% of GDP and a moderate reduction of personal income tax. These expansionary measures are partly financed by revenue raising measures of near 0.3% of GDP. Due to the resilient outlook for GDP and domestic demand, the deficit is still expected to fall to 0.2% of GDP in 2018 and, based on a no-policy change assumption, to remain unchanged in 2019. Risks to the fiscal forecast are on the downside, mainly reflecting uncertainty as regards the economic outlook and the volatility of some sources of government revenues.

The structural deficit is estimated to fall to ½% of GDP in 2018 from 1⅓% of GDP in 2017 and to improve further in 2019. Gross general government debt is projected to fall to 69.9% of GDP in 2017, from 72.8% of GDP in 2016, and to further decline to 69.1% and 67.2% of GDP in 2018 and 2019 respectively. This is contingent on continued robust GDP growth and the realisation of primary budget surpluses.

[115] These mainly relate to the deficit-reducing EFSF pre-paid margin repayment in 2016 (0.2 % of GDP).

Table II.7.1:

Main features of country forecast - IRELAND

	2016			Annual percentage change					
	bn EUR Curr. prices	% GDP	98-13	2014	2015	2016	2017	2018	2019
GDP	275.6	100.0	4.0	8.3	25.6	5.1	**4.8**	**3.9**	**3.1**
Private Consumption	90.8	33.0	3.8	2.1	4.2	3.2	**2.6**	**2.6**	**2.4**
Public Consumption	34.1	12.4	1.8	4.1	2.2	5.2	**3.3**	**3.5**	**1.9**
Gross fixed capital formation	87.7	31.8	2.9	18.2	28.2	60.8	**3.5**	**5.6**	**4.6**
of which: equipment	20.5	7.5	6.4	21.6	-0.7	27.9	**-2.7**	**5.7**	**4.5**
Exports (goods and services)	335.0	121.6	7.3	14.4	38.4	4.6	**3.9**	**4.5**	**4.3**
Imports (goods and services)	274.4	99.6	6.8	14.9	26.0	16.4	**2.2**	**4.7**	**4.6**
GNI (GDP deflator)	227.7	82.6	3.6	8.7	16.5	9.9	**3.0**	**3.4**	**2.9**
Contribution to GDP growth: Domestic demand			2.8	5.0	7.9	14.2	**2.4**	**3.0**	**2.5**
Inventories			0.0	1.7	-0.4	0.1	**0.0**	**0.0**	**0.0**
Net exports			1.4	2.3	18.6	-9.2	**2.5**	**0.9**	**0.6**
Employment			1.9	1.7	2.5	2.8	**2.9**	**2.2**	**1.9**
Unemployment rate (a)			7.7	11.3	9.4	7.9	**6.1**	**5.5**	**5.3**
Compensation of employees / head			3.6	1.8	2.1	2.0	**2.6**	**2.5**	**2.4**
Unit labour costs whole economy			1.5	-4.4	-16.6	-0.2	**0.7**	**0.8**	**1.2**
Real unit labour cost			-0.5	-4.1	-22.3	-0.2	**0.2**	**-0.3**	**0.0**
Saving rate of households (b)			-	6.6	6.6	6.3	**6.7**	**6.6**	**6.4**
GDP deflator			2.1	-0.4	7.3	0.0	**0.5**	**1.1**	**1.3**
Harmonised index of consumer prices			2.2	0.3	0.0	-0.2	**0.3**	**0.8**	**1.2**
Terms of trade goods			0.5	-5.2	8.0	2.3	**0.0**	**0.7**	**0.1**
Trade balance (goods) (c)			21.7	20.9	43.3	38.4	**34.3**	**33.2**	**32.7**
Current-account balance (c)			-1.7	1.6	10.9	3.3	**2.9**	**2.5**	**2.3**
Net lending (+) or borrowing (-) vis-a-vis ROW (c)			-1.4	-1.8	10.4	1.5	**1.2**	**0.9**	**0.7**
General government balance (c)			-4.0	-3.6	-1.9	-0.7	**-0.4**	**-0.2**	**-0.2**
Cyclically-adjusted budget balance (d)			-4.1	-4.1	-2.9	-1.7	**-1.3**	**-0.5**	**0.3**
Structural budget balance (d)			-	-4.0	-2.1	-1.9	**-1.3**	**-0.5**	**0.3**
General government gross debt (c)			54.3	104.5	76.9	72.8	**69.9**	**69.1**	**67.2**

(a) as % of total labour force. (b) gross saving divided by adjusted gross disposable income. (c) as a % of GDP. (d) as a % of potential GDP.