

Quarterly Economic Commentary

David Duffy
Kieran McQuinn
Ciara Morley
Daniel Foley

Autumn 2015

The forecasts in this *Commentary* are based on data available by 23 September 2015. Draft completed 28 September 2015.

Research Notes

A subscription to the *Quarterly Economic Commentary* costs €327 per year, including VAT and postage.

Authors

The *Commentary* is edited by Kieran McQuinn and David Duffy. Kieran McQuinn is an Associate Research Professor, David Duffy is a Senior Research Officer, Ciara Morley and Daniel Foley are Research Assistants at the Economic and Social Research Institute (ESRI).

The *Quarterly Economic Commentary* has been accepted for publication by the Institute, which does not itself take institutional policy positions. It has been peer reviewed by ESRI research colleagues prior to publication. The authors are solely responsible for the content and the views expressed.

Special Articles are published in the *QEC* in order to foster high-quality debate on various aspects of the Irish economy and Irish economic policy. They are subject to refereeing prior to publication.

Research Notes are short papers on focused research issues. They are subject to refereeing prior to publication.

Summary Table

	2012	2013	2014	2015	2016
Output (Real Annual Growth %)					
Private Consumer Expenditure	-0.8	-0.3	2.0	2.8	3.0
Public Net Current Expenditure	-2.2	1.4	4.6	1.0	0.7
Investment	8.6	-6.6	14.3	11.9	9.5
Exports	2.1	2.5	12.1	11.1	7.0
Imports	2.9	0.0	14.7	10.5	7.3
Gross Domestic Product (GDP)	0.2	1.4	5.2	6.0	4.5
Gross National Product (GNP)	1.6	4.6	6.9	5.9	4.0
Prices (Annual Growth %)					
Consumer Price Index (CPI)	1.7	0.5	0.2	0.1	1.0
Growth in Average Hourly Earnings	0.2	-0.4	1.7	2.0	2.3
Labour Market					
Employment Levels (ILO basis (000s))	1,842	1,880	1,914	1,967	2,015
Unemployment Levels (ILO basis (000s))	316	282	243	204	184
Unemployment Rate (as % of Labour Force)	14.7	13.0	11.3	9.5	8.4
Public Finance					
General Government Balance (€ bn)	-14.1	-10.2	-7.6	-3.6	-2.6
General Government Balance (% of GDP)	-8.1	-5.8	-4.1	-1.8	-1.2
General Government Debt (% of GDP)	121.7	123.2	109.7	102.5	96.0
External Trade					
Balance of Payments Current Account (€ bn)	-2.7	5.6	6.8	12.1	14.8
Current Account (% of GNP)	-1.5	3.1	3.6	5.9	6.7
Demand					
Final Demand	1.5	0.9	9.4	8.2	5.9
Domestic Demand	0.7	-1.2	5.7	4.2	4.2
Domestic Demand (excl. Stocks)	1.0	-1.5	5.2	4.7	4.3

The Irish Economy - Forecast Overview and Summary

The pace of the Irish recovery would appear to be increasing; the latest National Accounts indicate that output in the economy grew by over 5 per cent in 2014 and by almost 2 per cent in Q2 2015 alone. Use of the nowcasting model (summarised in the Appendix) suggests the economy is growing through Q3 by approximately 1.5 per cent per quarter in 2015. Accordingly, we now update our forecast for GDP in 2015 to 6 per cent, with GNP expected to grow marginally less at 5.9 per cent. One significant consequence of this is that Irish income per capita, which fell significantly post-2007, is now back to the peak level prior to the financial crisis.

External trade and investment continue to contribute strongly to growth, however, the most noticeable recent trend in the recovery is the increase observed in personal consumption. While household debt levels are still very high, particularly when compared with other European countries, it would appear that the deleveraging which is underway in the economy is not now restricting growth in spending to the same degree as previously. This increase in consumption is also tangible evidence that households are finally experiencing the recovery.

This is important from a policy perspective, as it indicates there is no macroeconomic rationale to stimulate domestic economic activity. Furthermore, the robust growth rates experienced by the economy, we believe, argue for a policy which does not stimulate economic activity in the forthcoming budget. In framing budgetary policy, it is important to heed the lessons of the past and, consequently, avoid pro-cyclical policy options.

The increased level of activity in the economy has also resulted in a marginal increase in the labour force participation rate in the year-on-year rate to Q2 2015. In light of the increased economic activity, we now believe that unemployment will fall to 9 per cent by the end of 2015 and to 8 per cent by the end of 2016.

The summer months witnessed considerable uncertainty in the Euro Area, particularly in relation to the ongoing difficulties in the Greek economy. In this *Commentary* a Research Note by McQuinn critiques the conduct of European

fiscal policy since 2007 and argues that the absence of a countervailing fiscal policy over this period at European level has exacerbated the difficulties experienced by Member States. McQuinn notes that it is now incumbent on domestic policymakers to address the institutional issues which prevent the formation of an effective fiscal union within the Euro Area.

An ongoing issue of concern within the economy is the slow rate of supply response within the housing sector. This has seen the cost of housing increase significantly with both house prices and rents increasing markedly. This ultimately could pose serious challenges at a macroeconomic level with heightened cost of living pressures threatening the availability of future labour supply via increased inward migration. Notwithstanding this, in the assessment we caution against the use of the taxation system to address supply-side issues, arguing that such measures should only be contemplated under a very particular set of circumstances.

Finally, in light of the higher than expected growth rates in 2015, we now revise upward our forecast for 2016; we believe output will grow at approximately 4.5 per cent next year. This should result in the economy converging to its potential level of output at this point.

National Accounts 2014

A: Expenditure on Gross National Product

	2013	2014	Change in 2014		
	€ bn	€ bn	Value	Price	Volume
Private Consumer Expenditure	85.7	89.0	3.8	1.7	2.0
Public Net Current Expenditure	26.1	27.2	4.3	-0.2	4.6
Gross Fixed Capital Formation	31.7	36.5	15.3	0.8	14.3
Exports of Goods and Services	191.4	215.0	12.3	0.2	12.1
Physical Changes in Stocks	0.8	1.9			
Final Demand	335.7	369.6	10.1	0.7	9.4
less:					
Imports of Goods and Services	156.8	180.3	15.0	0.3	14.7
Statistical Discrepancy	0.5	-0.2			
GDP at Market Prices	179.0	189.3	5.8	1.0	4.7
Net Factor Payments	-27.4	-26.2			
GNP at Market Prices	152.0	162.9	7.1	0.2	6.9

B: Gross National Product by Origin

	2013	2014	Change in 2014	
	€ bn	€ bn	€ bn	%
Agriculture	3.2	3.4	0.2	6.4
Non-Agriculture: Wages, etc.	67.7	70.0	2.4	3.5
Other	64.0	68.4	4.4	6.9
Adjustments: Stock Appreciation	0.6	-0.3		
Statistical Discrepancy	-0.5	0.2		
Net Domestic Product	135.0	141.9	6.8	5.0
Net Factor Payments	-27.4	-26.2	1.2	-4.5
National Income	107.6	115.7	8.0	7.5
Depreciation	28.4	29.3	0.9	3.3
GNP at Factor Cost	136.0	145.0	9.0	6.6
Taxes less Subsidies	16.0	17.9	1.9	11.6
GNP at Market Prices	152.0	162.9	10.8	7.1

C: Balance of Payments on Current Account

	2013	2014	Change in 2014
	€ bn	€ bn	€ bn
X - M	34.6	34.8	0.2
F	-27.4	-26.2	1.2
Net Transfers	-2.9	-2.7	0.2
Balance on Current Account	4.3	5.9	1.6
as % of GNP	2.8	3.6	1.0

National Accounts 2015

A: Expenditure on Gross National Product

	2014	2015	Change in 2015		
	€ bn	€ bn	Value	Price	Volume
Private Consumer Expenditure	89.0	92.4	3.8	1.0	2.8
Public Net Current Expenditure	27.2	27.9	2.6	1.6	1.0
Gross Fixed Capital Formation	36.5	41.2	12.7	0.7	11.9
Exports of Goods and Services	215.0	244.2	13.6	2.3	11.1
Physical Changes in Stocks	1.9	1.0			
Final Demand	369.6	406.6	10.0	1.7	8.2
less:					
Imports of Goods and Services	180.3	201.6	11.8	1.2	10.5
Statistical Discrepancy	-0.2	-0.2			
GDP at Market Prices	189.3	205.0	8.3	2.2	6.0
Net Factor Payments	-26.2	-28.5			
GNP at Market Prices	162.9	176.3	8.2	2.2	5.9

B: Gross National Product by Origin

	2014	2015	Change in 2015	
	€ bn	€ bn	€ bn	%
Agriculture	3.4	3.4	0.0	1.0
Non-Agriculture: Wages, etc.	70.0	73.5	3.4	4.9
Other	68.4	83.5	15.1	22.1
Adjustments: Stock Appreciation	-0.3	-0.3		
Statistical Discrepancy	0.2	0.2		
Net Domestic Product	141.9	160.4	18.6	13.1
Net Factor Payments	-26.2	-28.5	-2.3	8.9
National Income	115.7	131.9	16.2	14.0
Depreciation	29.3	25.0	-4.3	-14.7
GNP at Factor Cost	145.0	156.9	11.9	8.2
Taxes less Subsidies	17.9	19.3	1.5	8.2
GNP at Market Prices	162.9	176.3	13.4	8.2

C: Balance of Payments on Current Account

	2014	2015	Change in 2015
	€ bn	€ bn	€ bn
X - M	34.8	42.5	7.7
F	-26.2	-28.5	-2.3
Net Transfers	-2.7	-2.7	0.0
Balance on Current Account	5.9	11.3	5.3
as % of GNP	3.6	6.4	3.0

National Accounts 2016

A: Expenditure on Gross National Product

	2015	2016	Change in 2016		
	€ bn	€ bn	Value	Price	Volume
Private Consumer Expenditure	92.4	96.6	4.5	1.5	3.0
Public Net Current Expenditure	27.9	28.9	3.6	2.9	0.7
Gross Fixed Capital Formation	41.2	46.1	12.0	2.2	9.5
Exports of Goods and Services	244.2	266.3	9.1	1.9	7.0
Physical Changes in Stocks	1.0	1.0			
Final Demand	406.6	438.9	7.9	1.9	5.9
less:					
Imports of Goods and Services	201.6	218.2	8.2	0.9	7.3
Statistical Discrepancy	-0.2	-0.2			
GDP at Market Prices	205.0	220.7	7.7	3.0	4.6
Net Factor Payments	-28.5	-31.4			
GNP at Market Prices	176.3	189.1	7.3	3.2	4.0

B: Gross National Product by Origin

	2015	2016	Change in 2016	
	€ bn	€ bn	€ bn	%
Agriculture	3.4	3.5	0.1	2.5
Non-Agriculture: Wages, etc.	73.5	77.0	3.6	4.9
Other	83.5	93.2	9.6	11.5
Adjustments: Stock Appreciation	-0.3	-0.3		
Statistical Discrepancy	0.2	0.2	0.0	0.0
Net Domestic Product	160.4	173.7	13.3	8.3
Net Factor Payments	-28.5	-31.4	-2.9	10.2
National Income	131.9	142.3	10.4	7.9
Depreciation	25.0	26.5	1.5	6.0
GNP at Factor Cost	156.9	168.8	11.9	7.6
Taxes less Subsidies	19.3	20.3	0.9	4.8
GNP at Market Prices	176.3	189.1	12.8	7.3

C: Balance of Payments on Current Account

	2015	2016	Change in 2016
	€ bn	€ bn	€ bn
X - M	42.5	48.1	5.6
F	-28.5	-31.4	-2.9
Net Transfers	-2.7	-2.7	0.0
Balance on Current Account	11.3	14.0	2.7
as % of GNP	6.4	7.4	1.4