Quarterly Economic Commentary – Summer 2020

DATE

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Scenario Overview

- Given the current uncertainty we conduct a scenario analysis with three scenarios:

1. Baseline: New Normal
    - Government Roadmap.
    - ‘Recovery period’ through Q3 and Q4
2. Benign: “Pandemic Suppression”
    - Effective suppression of disease through testing, tracing, targeted quarantine etc.
    - Normal Economic Activity in Q4
3. Severe: “Second Wave”
    - Second viral wave emerges
    - Strict lockdown measures implemented in Q4

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Summary

	2019	Baseline 2020	Severe 2020	Benign 2020
Output (Real Annual Growth %)				
Private Consumer Expenditure	3	-13	-20	-12
Public Net Current Expenditure	6	11	15	11
Investment	94	-28	-39	-18
Exports	11	-8	-10	-7
Imports	36	-12	-13	-10
Gross Domestic Product (GDP)	6	-12	-17	-9
Gross National Product (GNP)	3	-14	-19	-10
Labour Market				
Employment Levels (ILO basis ('000))	2,322	2,026	1,976	2,081
Unemployment Levels (ILO basis ('000))	121	427	477	371
Unemployment Rate (as % of Labour Force)	5	17	19	15
Public Finances				
General Government Balance (€bn)	1	-28		
General Government Balance (% of GDP)	0	-9		

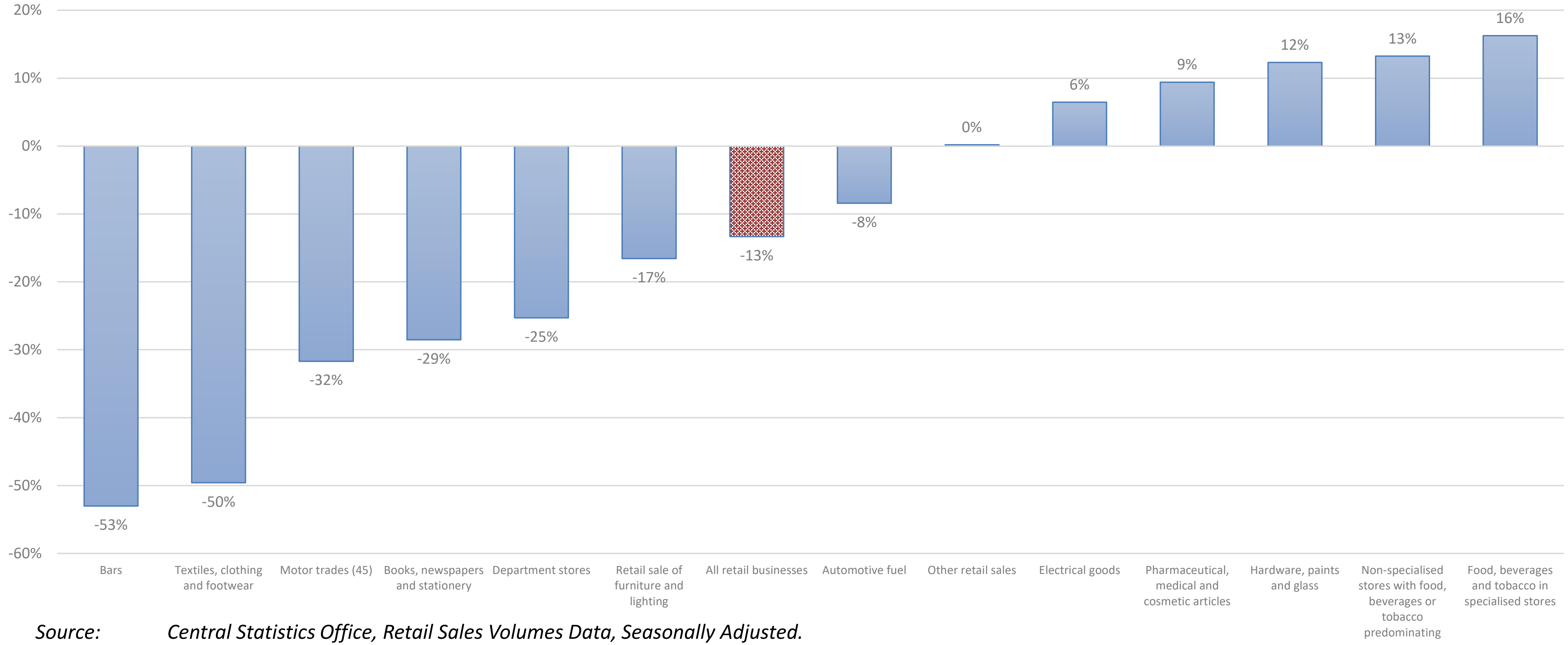
Consumption

Private Consumption

- Baseline: -13.3% Benign: -12.0% Severe: -19.7%

- Overall retail sales expenditure is down 13 per cent in March relative to January/February
- Dramatic fall in certain spending categories and moderate rise in others
  - Expenditure in bars and on clothing is down over 50 per cent
  - Expenditure on motor trade items and in department stores is down over 25 per cent.
  - Expenditure on food and beverages is up by between 13 and 16 per cent for specialised and non-specialised stores
- In order to estimate annual growth for 2020 we use Coffey et al. (2020)
  - Utilise microdata from Household Budget Survey 2015/2016
  - Map changes across the year using a combination of existing data, international literature and judgement
- Decline in consumption will be dampened by extensive income supports introduced this year

CHANGE IN RETAIL SALES – MARCH AS A PERCENT OF JAN/FEB AVERAGE



Source: Central Statistics Office, Retail Sales Volumes Data, Seasonally Adjusted.

COUNTERFACTUAL CONSUMPTION FIGURES BY SCENARIO (% CHANGE FROM 2019)

	New Normal	Second Wave	Pandemic Suppression
Food	-1	-4	-2
Drink and Tobacco	-18	-22	-14
Clothing and Footwear	-25	-41	-25
Housing	-2	-4	-2
Fuel and Light	0	0	0
Non-Durables	5	7	4
Durables	-16	-38	-16
Transport	-34	-48	-30
Miscellaneous	-16	-22	-14
Total	-13	-20	-12
Total (excluding housing and light)	-17	-25	-15

Source: Coffey et al. 2020

Box 1: The Effects of Government Policy on Personal Savings

- Market Income will fall by nearly 17 per cent in 2020
- However, disposable income will fall by less than 4 per cent
- Consumption expected to fall by over 12 per cent
- Net result is a large increase in savings in 2020
    - Personal Savings to increase by over €10 billion
    - Savings rate of nearly 20 per cent

- Future disposition of this household saving could have a significant impact on the nature of the economic recovery
- Increase in consumption in 2021 could act as a significant stimulus to the economic recovery
- Continuing uncertainty in 2021 could postpone such a consumer boom to 2022 or beyond

PERSONAL INCOME, CONSUMPTION AND SAVINGS, € BILLION

	2019	2020	%
Market Income	110.9	92.6	-16.5
Other Income	23.8	23.9	0.4
Taxes	-45.6	-37.2	-18.5
Welfare Payments	27	32.2	19
Disposable income	116.1	111.5	-3.9
Adjustments	1.8	1.7	-5.6
Consumption	105.5	92.4	-12.4
Personal savings	12.2	22	79.7
Savings Rate	10.5	19.7	

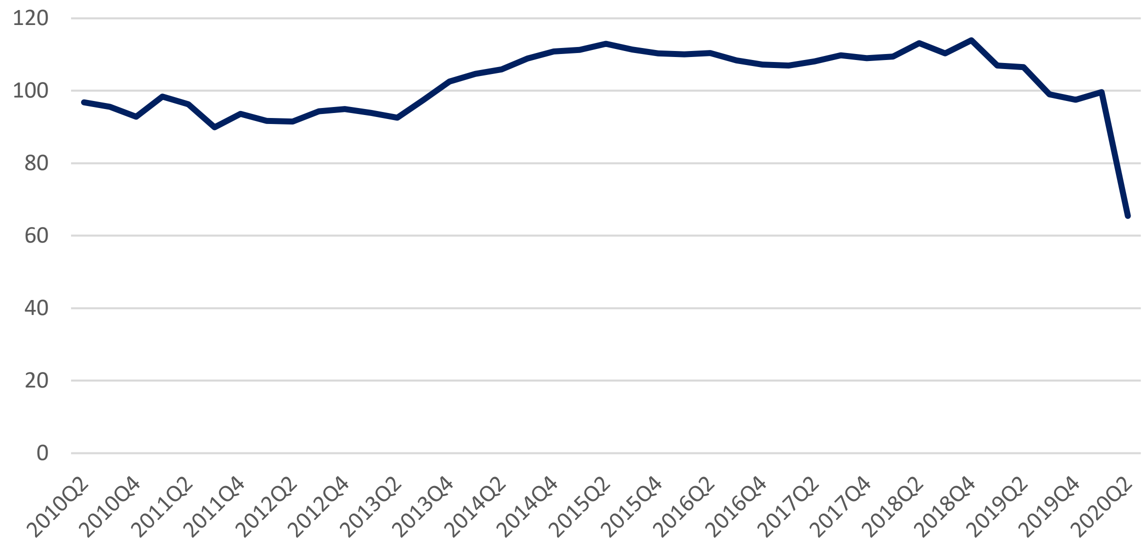
Investment

Investment

- Baseline: -27.6% Benign: -18.4% Severe: -39%

- CSO Business Impact Survey shows 25 per cent of businesses in Ireland have ceased trading
- Large increase in uncertainty coupled with a significant decline in sentiment (Figure on the right)
- Supply chain disruptions likely to limit the ability of companies to make capital expenditures
- Different components of investment likely to be impacted in different ways by the current situation
- Historical data shows a strong contemporaneous relationship between investment in Machinery and Equipment and business sentiment
- This implies investment in Machinery and Equipment will fall significantly in Q2
- Building and Construction may be less impacted by fall in sentiment in the near term due to capital committed
- However, due to physical restrictions, building and construction likely to be significantly curtailed

ECONOMIC SENTIMENT INDEX



Source: Economic Commission

Trade

Exports

- Baseline: -8.2% Benign: -6.7% Severe: -9.7%

- Impact on trade may be spread out over a longer time period than on other components of GDP
    - Recovery of exports dependent on recovery of Ireland’s main trading partners
    - Q1 Q-on-Q GDP growth: EU -3.5%, UK -2.0%, US -4.8%

Imports

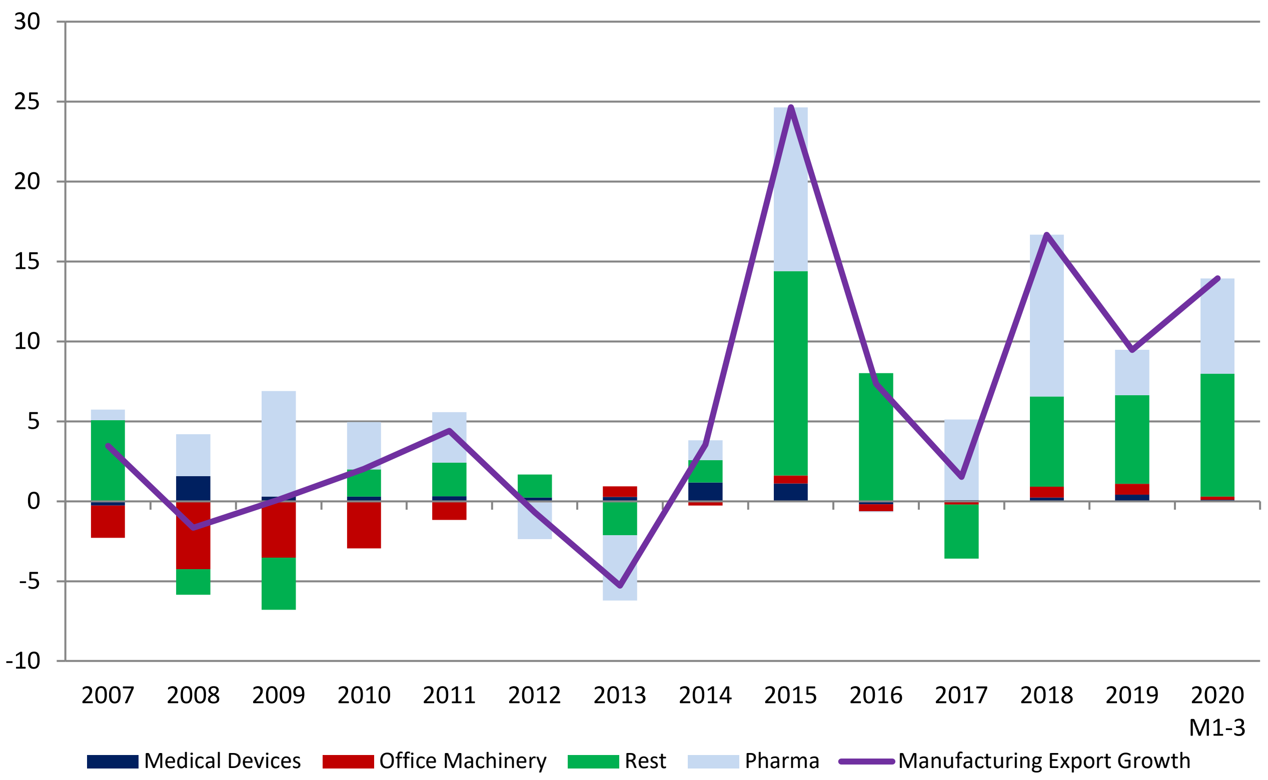
- Baseline: -12.0% Benign: -9.9% Severe: -13.2%

- Related to decline in consumption and investment
    - COSMO: 1 % decline in consumption in a year reduces imports by 0.6%
- Some sectors to be more impacted than others
    - Machinery & Equipment and consumer durables likely to be significantly impacted

Box 2: Export Scenarios Following The Coronavirus Outbreak

- Modelled based on NiGEM
  - 20 per cent reduction in world demand for Irish exports in the first two quarters of the year
  - Global demand rebounds over second half of 2020
- Incorporate these impacts into COSMO
- Baseline Scenario: Reduced spending internationally, increase in business uncertainty, reduction in hours of work, temporary lockdown of economies
- Benign scenario: Figure on the right shows export growth has held up reasonably well. May indicate that due to the composition of Irish exports, exports may suffer less negative effects than other countries
- Severe: longer-term strict lockdown with only limited success in containing the spread of the virus, thus dampening activity around the world for a longer period and leading to permanent losses

SECTORAL CONTRIBUTIONS TO IRISH MANUFACTURING EXPORT GROWTH (PERCENTAGE POINTS)



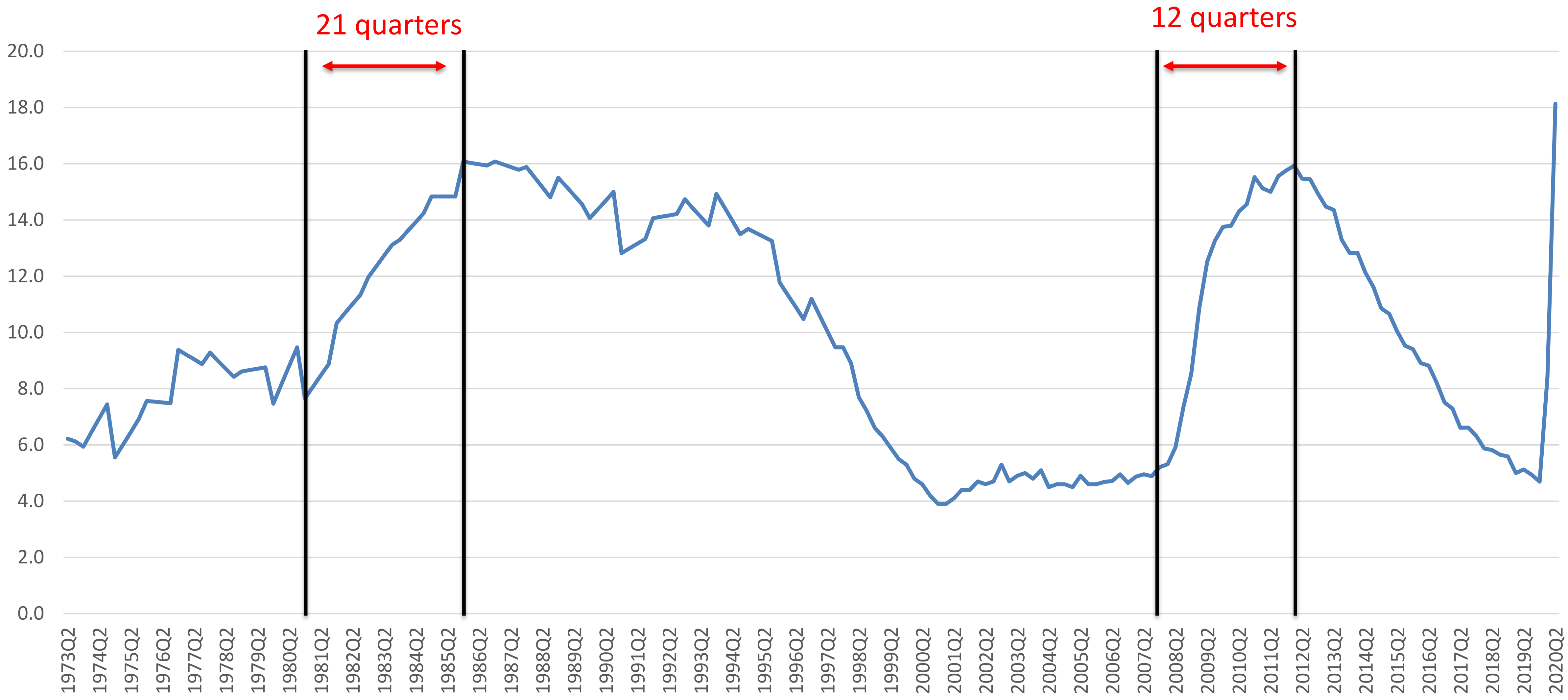
Labour Market

Unemployment

- Baseline: -17.4% Benign: -15.2% Severe: -19.4%

- Covid-19 adjusted unemployment rate increased to over 28% in April
- This equates to nearly 700k people receiving unemployment benefits
- Sectors most impacted as per Beirne et al. (2020):
  - Wholesale and retail trade
  - Accommodation and food service activities
  - Construction
- Live Register – April 2020
  - 816k on Live Register or availing of Covid unemployment payment
  - 1.2m on Live Register, availing of Covid unemployment payment or wage subsidy scheme
  - Up 728k (142%) in comparison to March
  - 400k increase in the number of people on the wage subsidy scheme compared to March

Unemployment rate: Irish economy 1973q1 – 2020q2



Box 3: Job Loss Distribution

- Look at pandemic unemployment claims relative to employment in Q4 2019
- Claims amongst younger workers represent a far greater share than for other age categories
- Claims by men for the payment represent a higher share of employment (27.6%) than for women (24.0%)
- Claims are highest in the Border region (29.5%) and lowest in Dublin (24.3%)

- Live register figures from the CSO show that claims for non pandemic related welfare payments of Jobseekers Benefit and Jobseekers Allowance have risen by 13,333 and 19,293 respectively between February and April
- An estimated 65,000 people above the age of 66 employed in the final quarter of 2019. These workers are not entitled to make a claim for the PUP, jobseekers allowance or – in most cases – jobseekers benefit

	(1)	(2)	(3)
	PUP claims at 10/5/2020	**Aged 18-66 in work, 2019q4**	**Col. 1/Col 2 (%)**
Total	589,638	2,275,420	25.9%
Age:			
18/19	26959	45908	58.7%
20-24	93,309	197,259	47.3%
25-34	135223	498211	27.1%
35-44	141,610	634,202	22.3%
45-54	111759	528128	21.2%
55-59	43,591	204,893	21.3%
60-66	37187	166820	22.3%
Sex:			
Men	335,989	1,216,696	27.6%
Women	253649	1058723	24.0%
Region of residence (NUTS3):			
Border	51,586	174,834	29.5%
West	55192	210292	26.2%
Mid-West	54,823	207,092	26.5%
South-East	52211	186379	28.0%
South-West	82,964	325,412	25.5%
Dublin	171874	706926	24.3%
Mid-East	85,828	335,452	25.6%
Midlands	33292	129034	25.8%

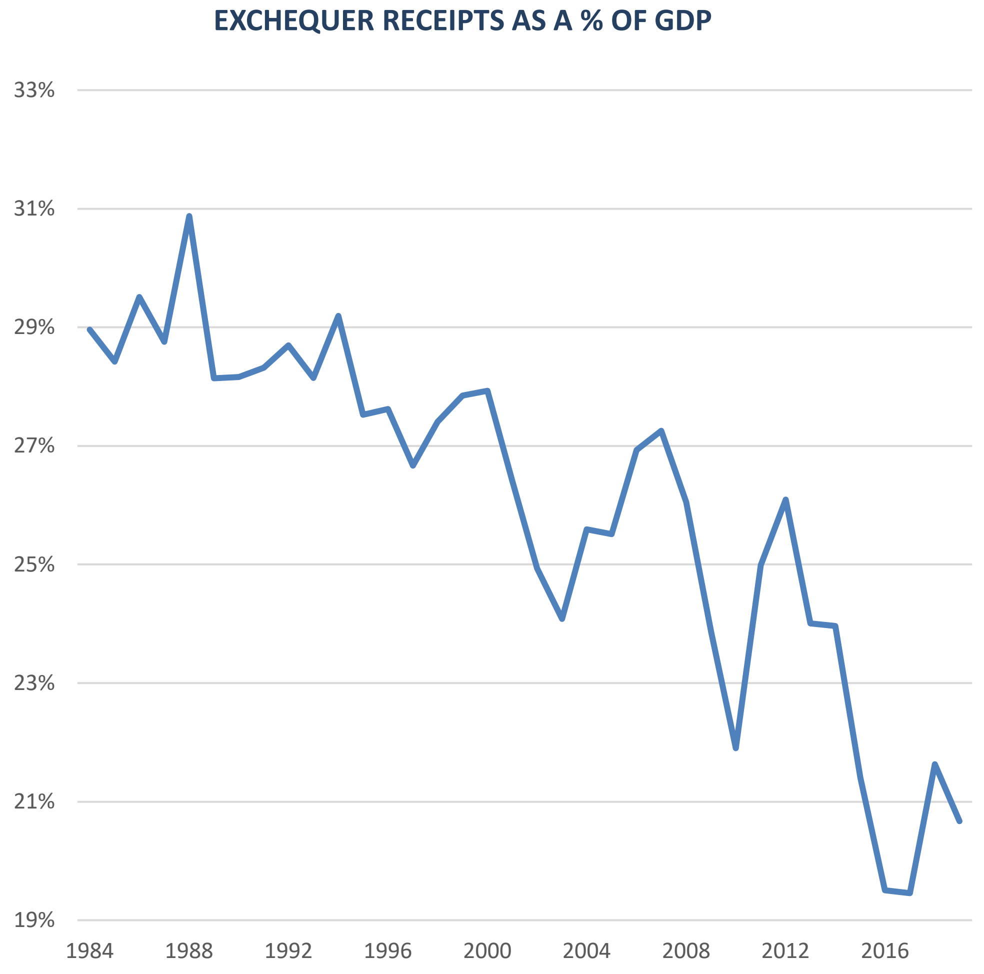
Public Finances - Baseline

- GGB (% of GDP) 2019: 0.4%   GGB (% of GDP) 2020: -9.0%
  Debt to GDP 2019: 58.6%   Debt to GDP 2020: 65.6%
- Significant decline in revenue forecast in SPU (€14.9bn decrease relative to 2019)
  - Taxes on production and imports (VAT, excise duty) -19.5%
  - Current taxes on income, wealth (PAYE, corporation tax) -14.4%
  - Social contributions (PRSI) -12.1%
- Significant increase in public expenditure forecast (€9.6bn increase relative to 2019)
  - Social payments (Unemployment benefit) +13.5%
  - Subsidies (Wage subsidy scheme) +120%
  - Intermediate consumption (Health related expenses) + 18.8%
- SPU suggests 7.4 per cent deficit of €23bn

- We assume pandemic payments stop at end of June and unemployed move to standard unemployment payments
- Revenue to decline by €18.1 billion, Expenditure to increase by €10.7bn
- Forecast a deficit of €27.5bn

Box 4: How much are Government taxation receipts likely to fall due to the Covid-19 slow-down?

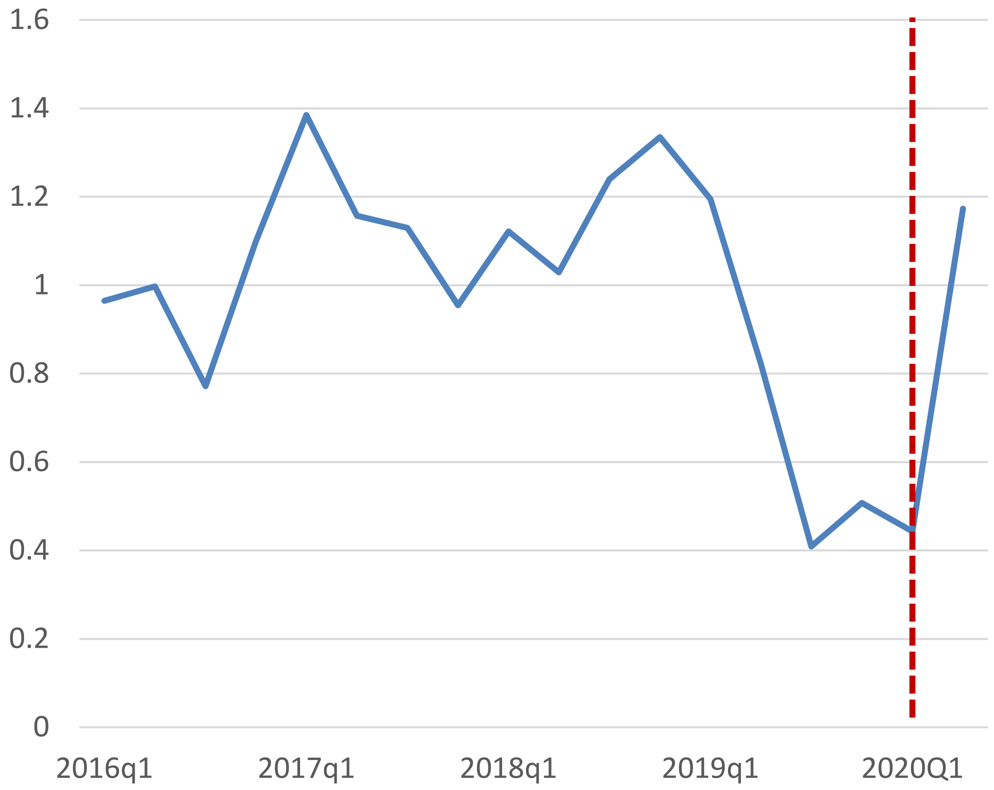
- Previous work by Deli et al. (2017) examined the sensitivity of taxation revenue to underlying economic activity
- A 10 per cent reduction in output levels results in total taxation receipts declining by 11 per cent
- Use these parameters to nowcast the level of taxation receipts for the present year, by using our nowcast/forecast of economic activity for 2020
- Given our forecast that output is set to contract by over 12 per cent in 2020, that would indicate that taxation receipts will decline from €59.3 bn in 2019 to just over €51 bn in 2020.
- In total, we expect that under our baseline scenario, total taxation receipts will fall by 16 per cent in 2020.



BOX 5: What are the short-run implications for the spreads on Irish bond yields of the Covid-19 downturn?

- Sovereign yields: financial market's view of the sovereign's ability to meet repayment obligations on its debt
- Cronin, Dunne and McQuinn (2019) model yield spread on government debt, households disposable income and banking exposure
- Using this model forecast spreads in Q2 2020
- Impact of the shock is to cause the spread to increase back up to 2018 levels
- Monetary policy actions by the ECB will be crucial in offsetting these deteriorating conditions and keeping Irish yields low

ACTUAL AND SIMULATED SPREADS (%) IRISH BOND YIELDS: 2016Q1 – 2020Q2



Assessment

- Fiscal stimulus needed to kickstart the economy in the second half of the year/2021
  - Environmental and sustainability projects
  - Social and affordable housing
    - No overheating in the domestic economy!
    - Allen-Coghlan and McQuinn (2020) suggest housing supply could be significantly impacted due to Covid-19
  - Supports for large enterprises/SMEs should aim at expanding grants / cash injections
- Clear and specific guidance from European institutions
  - Concerning the fiscal strategies available to member state countries essential
  - Proposed €500bn recovery fund a move in the right direction but more is needed
- Possibility of increase in mortgage arrears
  - If income supports are tapered off and payment breaks expire
  - Financial stability concerns could arise?