IRELAND

After expanding very strongly over the past two years, the economy is projected to grow at a more sustainable pace in 2017 and 2018. Notwithstanding this moderation, domestic demand will remain solid. As the labour market tightens, wage pressures will continue to be strong, which is projected to feed into higher inflation. Firms are projected to expand at a slower pace than in past years due to already high labour costs and high external uncertainty, including the final outcome of the Brexit negotiations.

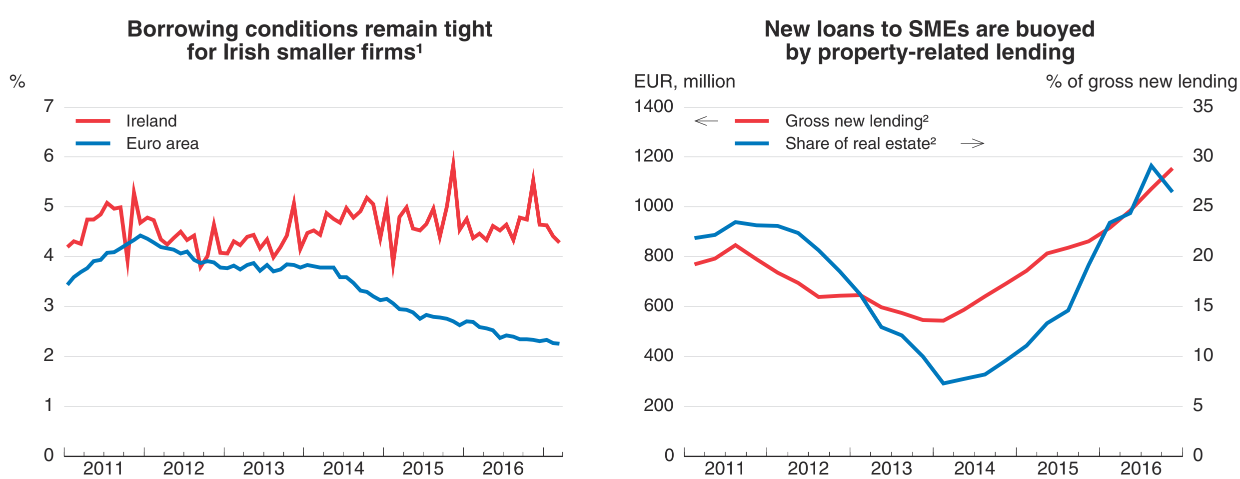
Given elevated uncertainties, policies should firmly focus on underpinning stability and making the economy resilient against shocks. The government should ensure that its medium-term goal of balancing the budget is met, thus leaving room to use fiscal policy to support growth if needed. The authorities should support a further resolution of non-performing loans by improving the process of repossession. They should tighten macro-prudential policies if the rapid rise in property prices fuels new property-related lending more than projected.

Ireland enjoys a high degree of openness to the global economy and has many highly-productive multinational enterprises. It can better take advantage of them by facilitating knowledge spillovers and the expansion of productive firms, which would require strengthening the financial system. Some recently introduced government programmes should improve job mobility. Among them, Springboard, Momentum and ICT conversion courses have been found to be effective in reskilling and upskilling.

The economy is overheating somewhat

GDP grew by 5.2% in 2016. Gross value added excluding volatile components related to multinational enterprises (MNEs) is estimated to have grown at an only slightly slower pace. The headline number for investment was strongly affected by MNEs, but business

Ireland



1. Bank interest rates on loans up to and including EUR 1 million for new businesses.
2. Four-quarter average of gross new lending by banks to Irish resident SMEs. Last observation: 2016Q4.

Source: OECD Economic Outlook 101 database; ECB Statistical Data Warehouse database; and Central Bank of Ireland.

StatLink http://dx.doi.org/10.1787/888933503301

Ireland: **Demand, output and prices**

	2013	2014	2015	2016	2017	2018
	Current prices EUR billion	Percentage changes, volume (2014 prices)				
GDP at market prices	180.0	8.4	26.3	5.2	3.7	2.5
Private consumption	79.9	1.8	5.1	2.9	2.6	2.7
Government consumption	30.6	4.5	0.2	4.9	2.0	2.2
Gross fixed capital formation	32.9	18.0	33.7	37.6	8.5	3.7
Final domestic demand	143.4	6.2	11.6	13.5	3.9	3.0
Stockbuilding[1]	3.3	1.6	-0.8	1.2	1.0	0.0
Total domestic demand	146.7	8.3	9.8	14.1	4.0	3.0
Exports of goods and services	190.9	14.4	34.5	2.4	6.3	4.0
Imports of goods and services	157.6	15.3	21.7	10.4	8.8	4.7
Net exports[1]	33.2	1.9	18.3	-6.6	-0.9	0.2
Memorandum items						
GVA[2], excluding sectors dominated by foreign-owned multinational enterprises	_	8.7	4.4	4.4	2.7	2.5
GDP deflator	_	-1.2	4.9	-1.3	0.6	2.8
Harmonised index of consumer prices	_	0.3	0.0	-0.2	0.8	2.0
Private consumption deflator	_	1.5	0.6	1.2	1.6	2.1
Unemployment rate	_	11.3	9.4	7.9	6.9	6.2
General government financial balance[3,4]	_	-3.7	-2.0	-0.6	-0.5	-0.2
General government gross debt[3]	_	124.1	92.7	91.0	90.3	87.6
General government debt, Maastricht definition[3]	_	105.4	78.8	75.6	74.8	72.1
Current account balance[3]	_	1.7	10.2	4.7	4.1	5.3

1. Contributions to changes in real GDP, actual amount in the first column.
2. Gross value added. Data for 2016-2018 are OECD 's estimates.
3. As a percentage of GDP.
4. Includes the one-off impact of recapitalisations in the banking sector.

Source: OECD Economic Outlook 101 database.

StatLink http://dx.doi.org/10.1787/888933505904

investment in the domestic sector continued to recover, albeit from a low base. The unemployment rate has declined rapidly, to below 7% in early 2017. This has led to strong wage growth. In contrast, inflation has been contained, due to earlier declines in energy prices and, more recently, euro-sterling exchange rate developments. Real wages have risen, pushing up household consumption by 3% last year.

Property prices are rising rapidly on the back of strong economic growth and a shortage of housing supply. Property-related loans are increasing fast, contributing significantly to the recent recovery in total new lending. Activity in the construction sector is gaining momentum, but supply is expected to fall short of demand for some time. The sharp rise in prices and lending raises concerns that another bubble may be forming, and the authorities should stand ready to tighten prudential regulations if needed.

Policies should stand ready to react to shocks

Notwithstanding the strong economic recovery, the banking system is still impaired, a legacy of the past property boom. Borrowing conditions remain very tight for SMEs, despite the accommodative euro-area monetary policy, and total new lending is still outpaced by debt repayment. Despite a sizeable reduction over the past years, non-performing loans still account for around 17% of total outstanding loans, and a majority of them are property-related. The current buoyancy of the property market should make it easier for banks to dispose of impaired portfolios.

The fiscal stance is projected to be less contractionary than in past years, as public investment will reverse its past declines. Due to past fiscal efforts and strong GDP growth, the fiscal deficit has diminished sharply and public debt is on a downward path. The government should ensure that its medium-term goal of balancing the budget is met, in order to leave room for fiscal support in the event of shocks from Brexit or other sources.

Growth will fall toward sustainable rates

The Irish economy is projected to expand solidly, but growth will fall toward more sustainable rates. Employment will continue to rise but at a slower pace, while productivity gains in underlying activity remain limited. Wage pressures will remain strong, feeding into higher inflation. Household consumption will slow somewhat as purchasing power is eroded by higher inflation. Investment in the domestic sector will continue to rise, but gradually at a moderate pace.

The economic prospects are surrounded by more uncertainty than usual, including notably the final outcome of Brexit negotiations. The high level of private indebtedness leaves Ireland sensitive to a rise in interest rates. Conversely, property prices might rise more strongly than projected, which would support construction activity in the near term, but might also sow the seeds of another bubble. A rise in protectionism would be particularly detrimental to the Irish economy given its high degree of openness.