

IRELAND



EUROLAND



View from the top

Despite a recovery in growth in the third quarter, the Irish economy remains weak and is estimated to have contracted by just over 1% in 2008. A further contraction is forecast for 2009, as unemployment rises and consumers tighten their belts.

Key metrics

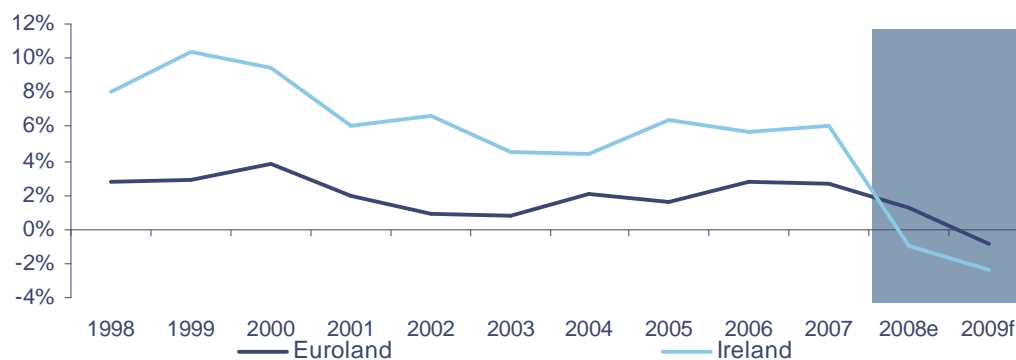
Indicator	2007	2008 <sup>e</sup>	2009 <sup>f</sup>
GDP growth	6.0%	-1.1%	-4.1%
Inflation	2.9%	3.2%	0.7%
Base interest rate	4.0%	2.5%	▼*
General outlook	Negative		

Source: Central Statistics Office; Eurostat; European Central Bank; PricewaterhouseCoopers estimates(e) and forecasts (f)  
\*Interest rate as of January 2009 was 2.50% Inflation measure shown is the Harmonised Index of Consumer Prices (HICP)

Key trends

- Falling consumer confidence is putting downward pressure on consumer spending, resulting in weak retail sales volumes and new car registrations.
- The unemployment rate continues to rise, reaching 7.8% of the labour force in November 2008.
- The rate of consumer price inflation has eased significantly from the summer, and is likely to continue to do so as demand for goods and services weakens further.

Economic growth profile (GDP, annual % change)



Source: Central Statistics Office, Eurostat; PricewaterhouseCoopers estimates (e) and forecasts (f)

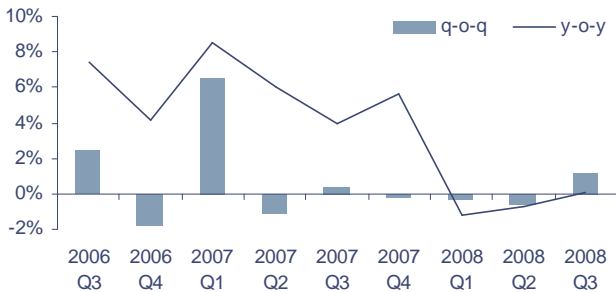
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Ireland

The Irish economy expanded by 1.1% quarter-on-quarter in the third quarter of 2008, while output increased by 0.1% year-on-year, as shown in Chart 1 below.

Chart 1: Irish GDP growth

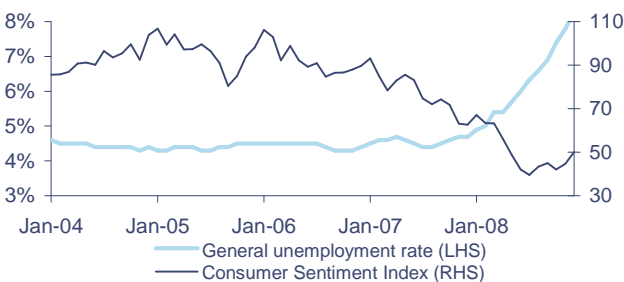


Source: Central Statistics Office

The expansion in the Irish economy in Q3 follows three consecutive quarters of contraction, and is likely to be a technical adjustment, rather than a sign that economic conditions are improving. The fundamentals of the Irish economy remain weak, and the recovery in Q3 is unlikely to prevent the Irish economy from contracting in 2008 as a whole – the first time it will have done so since 1983. We are now estimating a full year contraction in GDP of 1% in 2008, down from 6% growth in 2007 and well below the Irish economy’s long term growth rate.

Consumer confidence has stabilised in recent months, but has fallen significantly since the beginning of 2007, as shown in Chart 2 below, due to the ongoing financial market turbulence, falling house prices and rising unemployment.

Chart 2: Unemployment and consumer sentiment



Source: Central Statistics Office, Economic and Social Research Institute

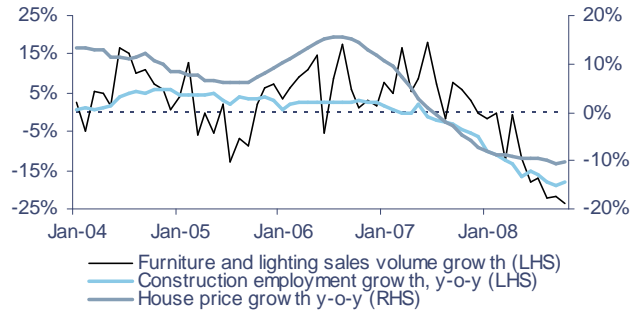
Unemployment has increased rapidly during 2008, with the rate of unemployment reaching 8.3% in December 2008 – the highest rate in 11 years. Falling employment, which tends to undermine consumer confidence, continues to affect retail sales volume growth, which contracted year-on-year for the ninth consecutive month in October 2008.

The most severely affected retail sectors are those linked to the housing market – sales volumes in the furnishing and lighting sector fell by 23.8% in the year to October 2008, as shown in Chart 3 above right.

House prices fell for the twentieth consecutive month in the same month, but the rate of house price deflation appears to have slowed – house prices were 11.1% lower than a year earlier in both September and October. Falling demand for housing continues to impact upon employment in the

construction sector, which fell by 18.1% in the year to October.

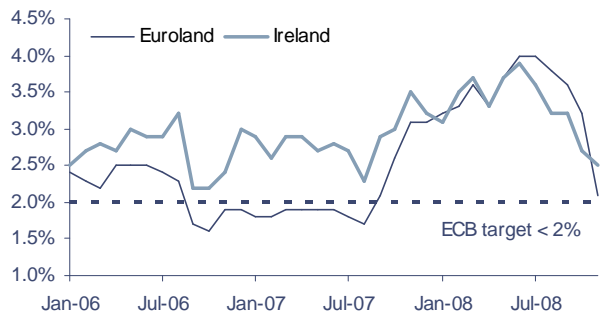
Chart 3: House price inflation, durable goods volume growth and construction employment growth



Source: Central Statistics Office, Permanent TSB

The annual rate of change in the Harmonised Index of Consumer Prices – the EU’s preferred measure of consumer price inflation – eased to 2.5% in November 2008, having fallen from a peak of 3.9% as recently as June, as Chart 4 shows below. Weak demand is likely to see the inflationary pressure ease further into 2009 – in Euroland as a whole as well as in Ireland.

Chart 4: Consumer price inflation



Source: Eurostat

The external sector has helped mitigate weak economic output in recent quarters, but mainly because import volumes are contracting at a faster and more consistent rate than export volumes. Weakening demand amongst Ireland’s main trading partners – the UK, US and Euroland – will result in a tough trading environment for Ireland’s export businesses in 2009.

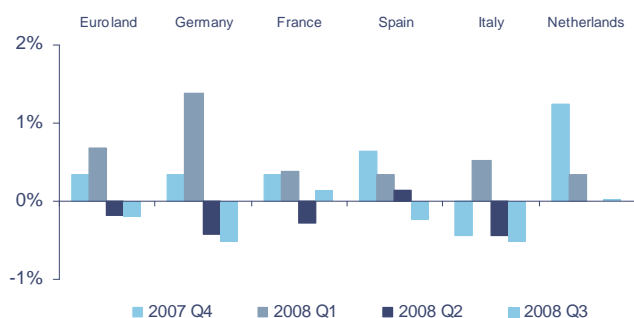
In November 2008, Brian Cowen, Ireland’s Taoiseach, unveiled a five-year plan to stimulate growth in the Irish economy, titled “Building Ireland’s smart economy – A framework for sustainable economic renewal.” The plan outlines a number of measures to promote growth, including proposals designed to make Ireland an international hub of innovation, research and development.

However, the plan is unlikely to prevent another contraction in output in 2009 – we currently forecast a decline in GDP of 4.1%. The risks are firmly on the downside given the uncertainty that remains as a result of the recent global financial turmoil and its impact on consumer demand and business investment in the domestic economy and amongst Ireland’s main trading partners.

## Euroland

The Euroland economy is now in a technical recession after contracting for the second consecutive quarter in the third quarter of 2008. GDP fell by 0.2%, the same rate as that in Q2 2008 (see Chart 5 below). Investment continued to fall during the quarter, down by 0.6%, and was a key driver of the overall contraction.

Chart 5: Quarter-on-quarter GDP growth rates



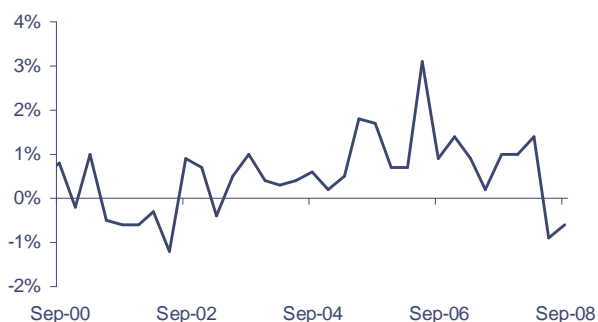
Source: Eurostat

Several Euroland economies are also now officially in technical recession. The German and Italian economies both contracted by 0.5% in Q3, while output in Spain was down 0.2% as the global downturn in activity took its toll.

Retail sales continued to fall in October, down by 0.8%, as consumers became increasingly cautious about spending. Prospects for the crucial Christmas sales season are also looking poor. Euroland's retail Purchasing Manager's Index, an indicator of retail managers' views on economic conditions and prospects, hit its lowest level in November since it was set up in 1998, falling by 8.4%. Overall, conditions in the sector remain gloomy.

In contrast to movements earlier in the year, total investment fell by 0.6% in Q3, as illustrated in Chart 6 below. Over the past year, investment has been increasingly hit by sharply lower business confidence, tighter credit conditions and markedly weaker final demand. Looking forward, it is likely that investment will remain weak in the coming quarters, thereby further dampening economic growth.

Chart 6: Quarter-on-quarter investment

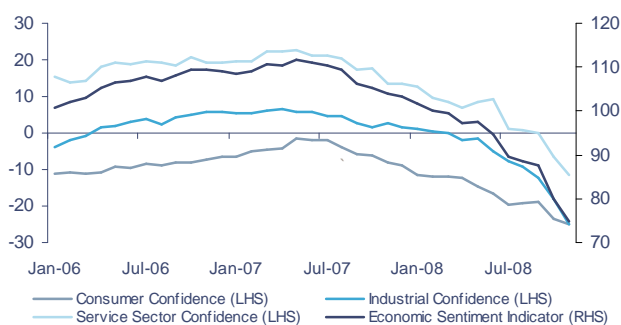


Source: Eurostat

Consumer and business confidence indicators have further deteriorated in recent months. As shown in Chart 7 below, the Euroland economic sentiment indicator, measuring both business and consumer confidence, fell by 6.4% in

November to hit a new record low since it was set up in 1985. Specifically, consumers appear to be becoming more pessimistic about labour market conditions, with the sub-index measuring fears about unemployment jumping in November to its highest level in almost 15 years.

Chart 7: Economic Sentiment Indicator



Source: European Commission

The annual rate of inflation has continued to decline over recent months, retreating from its mid-July peak of 4%. The inflation rate for November was 2.1%, down from 3.2% in October. Preliminary data for December points towards the inflation rate falling to 1.6%. Falling commodity and food prices have contributed to an easing of inflationary pressures across the region.

Easing inflationary pressures have provided greater scope for additional monetary stimulus by the ECB. The bank's key interest rate has been cut by 175 basis points since September and currently lies at 2.5%. As economic conditions worsen in 2009, this trend in interest rate reductions is expected to continue in order to stimulate consumption and investment.

The ongoing effects of financial market instability, tighter credit conditions, weaker external demand and still volatile equity prices will continue to constrain economic activity in Euroland. Consequently, we have revised down our forecasts for economic growth in Euroland to -0.9% in 2009, following an estimated 1.1% growth in 2008.

Table 1: Euroland and UK GDP growth outlook

GDP annual % change	2007	2008 <sup>e</sup>	2009 <sup>f</sup>
Euroland	2.7	1.1	-0.9
Austria	3.1	1.8	-0.2
Belgium	2.8	1.4	-0.2
Finland	4.5	2.2	0.4
France	2.2	1.0	-0.8
Germany	2.5	1.4	-1.2
Greece	4.0	2.8	1.2
Ireland	6.0	-1.1	-4.1
Italy	1.5	-0.4	-1.3
Netherlands	3.5	2.1	-0.2
Portugal	1.9	2.8	1.0
Slovenia	6.8	0.4	-0.3
Spain	3.7	1.1	-1.2
UK	3.0	0.9	-1.8

Source: CSO, Eurostat; PricewaterhouseCoopers estimates (e) & forecasts (f)

## Ireland: recent performance and forecasts

	2005	2006	2007	2008 <sup>e</sup>	2009 <sup>f</sup>
<b>Real growth (annual % change)</b>					
GDP	6.4	5.7	6.0	-1.1	-4.1
Consumer spending	7.1	7.1	6.3	-0.9	-3.1
Government	2.9	4.8	5.9	3.0	2.2
Investment	14.2	3.9	1.0	-18.0	-19.0
Export	5.2	5.7	6.8	0.4	-1.3
Imports	8.2	6.4	4.1	-3.4	-3.6
<b>Contribution to GDP growth (%)*</b>					
Consumer spending	3.3	3.3	3.0	-0.4	-1.5
Government	0.4	0.7	0.8	0.4	0.3
Investment	3.6	1.1	0.3	-4.6	-4.0
Export	4.2	4.6	5.4	0.3	-1.0
Imports	-5.5	-4.4	-2.8	2.3	2.4
Domestic demand	7.5	5.4	3.3	-3.7	-5.2
Net exports	-1.3	0.2	2.6	2.6	1.4
<b>Economic structure (% of GDP)*</b>					
Consumer spending	46.6	47.2	47.3	47.5	48.0
Government	13.8	13.7	13.7	14.3	15.2
Investment	27.3	26.9	25.6	21.2	18.0
Export	79.9	79.9	80.5	81.7	84.2
Imports	68.7	69.1	67.9	66.3	66.7
<b>Inflation</b>					
HICP (% change, annual average)	2.2	2.7	2.9	3.2	0.7

Source: Central Statistics Office, Eurostat; PricewaterhouseCoopers estimates (e) and forecasts (f). \*Component shares of GDP may not add up to 100% owing to stockbuilding and statistical discrepancy

## Size of the economy

	2005	2006	2007	Share of 2007 world total
Population (millions)	4	4	4	0.1%
GDP, market rates (US\$ billions)	201	219	253	0.5%
GDP, PPP rates (US\$ billions)	173	189	203	0.3%
GDP per capita, market rates (US\$)	48,705	51,800	58,883	
GDP per capita, PPP rates (US\$)	41,993	44,676	47,169	

Source: International Monetary Fund

Report date: 9 January 2009

## Definitions

Base interest rate – The policy interest rate for Euroland is the main refinancing operations minimum bid rate

Base interest rate forecasts – ▲ increase; ▼ decrease; ◀▶ no change

General outlook – In the Key Metrics table on page 1, the overall economic environment is assessed as being Positive, Stable or Negative

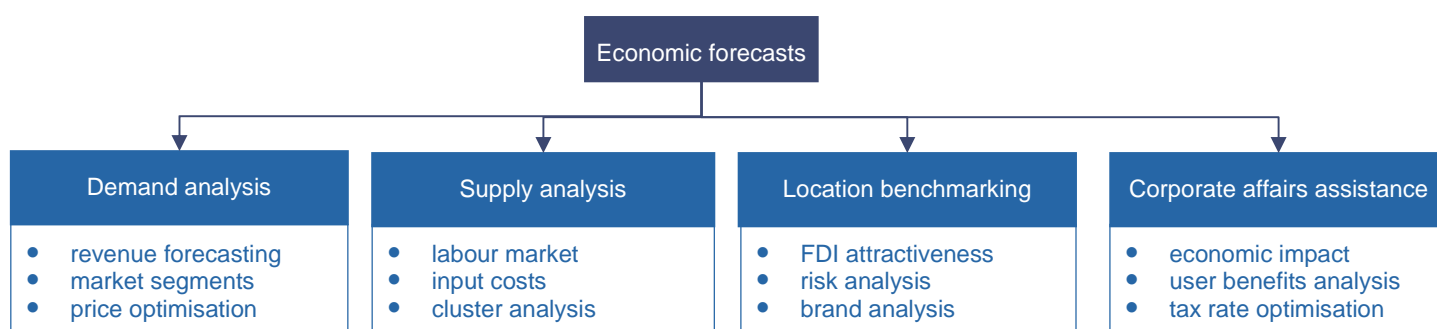
EOP – End of Period;

HICP – Harmonised Index of Consumer Prices

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