IRISH ECONOMIC UPDATE - JULY 2004

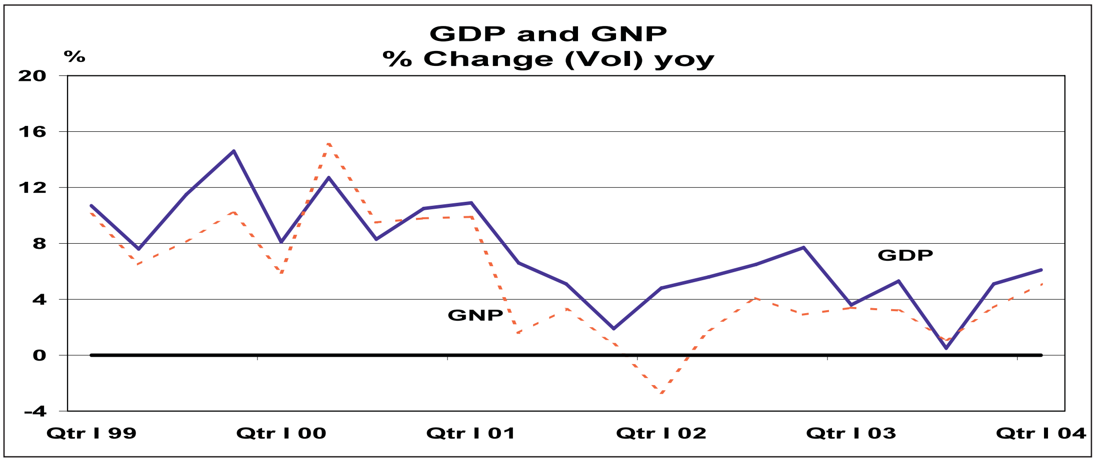
APPROACHING NIRVANA

The latest data show that the Irish economy has moved on to a firm growth path with GDP likely to increase by 5.5% in 2004 and 6% in 2005. Employment is now rising by close to 3% yoy with the unemployment rate low at around 4.5%. Inflation has fallen below eurozone levels. Meanwhile, the general government budget is set to remain broadly in balance this year. This is pretty close to economic nirvana.

- The latest revised data show that the Irish economy weathered the global downturn in the 2001-2003 period extremely well. Furthermore, it looks set to record strong growth in 2004 and beyond. There were clear signs of improvement in the economy during the latter half of 2003 and many indicators have been very favourable in the first half of 2004.

- Tax revenue (excluding the once-off offshore funds receipts) rose by 9.7% in H1 2004, car sales were up by 8.8% while housing starts rose by over 10%. Meanwhile, employment rose by close to 3% year-on-year in Q1 with the Live Register continuing to trend lower in Q2. Exports also picked up considerably in the three month period February - April. Growth in manufacturing output, though, was subdued enough in the first four months of the year, but should accelerate as new capacity comes on stream.

- National accounts data for Q1 2004 show that GDP increased by 6.1% yoy, with GNP rising by 5.1%, boosted by strong growth in investment and a recovery in exports. Import growth at 1.2% yoy looks very low, given the growth rate of 4.8% in both domestic spending and exports in the quarter, as well as a rise in stocks. Overall, though, the data show that the Irish economy started the year on a strong note.



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- The pick up in the Irish economy reflects the improved performance of the global economy. We expect good growth in Ireland's main export markets in H2 2004 and 2005. Though our competitive position has obviously worsened, currency movements have not been too damaging to Ireland. Any further sharp falls by the dollar, though, could prove problematic.

- Overall, the Irish economy has moved on to a strong growth path with real GDP forecast to rise by 5.5% in 2004 and by 6% in 2005. Real GNP is expected to grow by 4.5% this year and by 5% in 2005. These are significantly higher than the forecasts published in our report on the Irish Economy in April. However, the upgrades are largely due to a higher carryover effect from 2003 following significant upward revisions by the CSO to the national accounts data for 2003.

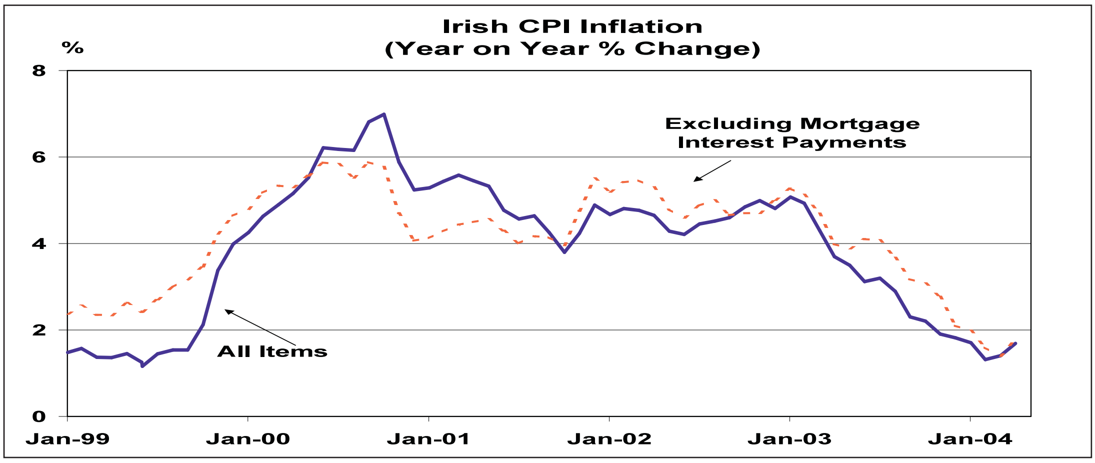
- The Irish economy has three very favourable domestic factors at work which support a positive outlook for H2 2004 and 2005. The first is the strength of the labour market. Irish labour supply is growing at a rate of around 2.7%. However, net job creation has been maintained at a sufficiently high rate to limit the rise in the unemployment rate to some 4.5%.

- The labour market data for Q4 2003 and Q1 2004 were very encouraging, showing a rise of over 50,000 year-on-year in total employment, heavily weighted towards full-time private sector jobs. Employment is forecast to grow by 2.8% in 2004 and 3% in 2005.

- A second major support for the economy has been the fall in the annual rate of inflation. The core CPI rate is likely to average around 2% this year, down from 4% in 2003 and 5% in 2002, despite the sharp rise in oil prices. There are clear disinflationary forces at work in the economy, which have brought Irish inflation down below eurozone levels.

- Looking to 2005, core inflation may pick up to around 2.5% while the headline rate will rise even further, depending on the degree of ECB induced mortgage interest rate increases. The growth in wage income slowed in 2003 and should remain moderate for 2004 and 2005 given the conclusion of recent pay talks which provide for wage rises of 5.5% over eighteen months.

- A third supportive factor is that the economy has limited imbalances. The public finances finished 2003 on a favourable note with the general government budget in small surplus. The projected general government deficit target for 2004 of just over 1% of GDP is likely to be well undershot. Indeed, thanks to unexpected buoyancy in tax receipts, the general government budget should be broadly in balance this year. This would augur well for the 2005 budgetary arithmetic.



- Meantime, official interest rates in the euro area remain at extremely low levels and may not begin to be increased until 2005. Given the importance of variable rates to the Irish corporate and personal sectors, the continuing low interest rate environment will support the economic recovery and provide invaluable support to the Irish housing market.

- For many, the main domestic risk is perceived to be the outlook for the Irish property market. We are positive on the outlook for this sector in view of the impressive performance of the labour market, the strong underlying demand for residential property and the limited downside to affordability in 2004 and 2005, given the likely continuation of a low interest rate environment. We expect that the annual growth in house prices will slow down to about 7% by end year helped by rising supply. House completions look set to rise by a further 10% this year to around 75,000.

REVISIONS TO 2003 NATIONAL ACCOUNTS DATA

Irish national accounts are subject to sizeable revisions, partly due to the large weighting of external trade in GDP/GNP. That said, the revisions to the 2003 national accounts figures published last week were quite remarkable, given that the previous estimates were published just three months ago. The revisions are set out in the following table.

REVISIONS TO 2003 NATIONAL ACCOUNTS (%)

	Old	New	Revision
Consumer Spending	1.9	2.6	+0.7
Government Spending	2.1	2.5	+0.4
Fixed Investment	-2.9	3.4	+6.3
Total Domestic Spending	0.8	2.8	+2.0
Stock Changes (€bn)	0.95	0.5	-0.45
Exports	-5.8	-0.8	+5.0
Imports	-5.6	-2.3	+3.3
GDP	1.4	3.7	+2.3
Net Factor Income (€bn)	20.0	20.7	+0.7
GNP	3.3	2.8	-0.5

In particular, there were upward revisions to the volume of exports and imports of 5% and 3.3%, respectively. Even more dramatically, fixed investment is now believed to have risen by 3.4% last year compared to the initial estimate made three months ago of a 2.9% fall.

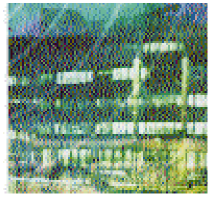
This largely reflects the fact that investment in machinery and equipment is now said to have increased by 1% last year compared to the initial estimate of a 13% decline. The net result of all these revisions is that GDP growth in 2003 is now put at 3.7%, compared to the previous estimate of 1.4%.

Furthermore, GNP growth in 2002 was revised upwards from 0.1% to 1.5%. The main implication of all these revisions is that the downturn in the Irish economy in the 2001-2003 period was much milder than originally estimated. GDP growth over the period averaged 5.3% with GNP growth averaging 2.7% according to the latest data. Domestic spending held up well, averaging growth of 3.7%, helped by strong rises in government spending and housebuilding activity.

Meanwhile, GDP growth in Q4 2003 is now put at 5.1% yoy, up from the previous estimate of 2.7%. As a result, there is a much larger carryover effect into 2004 of almost 3.5%. Not surprisingly then, we have had to make significant upward adjustments to our 2004 growth forecasts. GDP growth is now forecast at 5.5% compared to 4.0% previously, with the GNP growth forecast upped to 4.5% from 3.5%.

By any standards, the revisions by the CSO to the 2003 national account data are remarkable. They paint quite a different picture of economic activity last year and have major implications for forecasts for 2004. We recognise that the CSO has to meet tight deadlines in terms of supplying national accounts data to Eurostat. Economists also like to have data published in a timely fashion. However, if it comes to a choice between speed and accuracy, it is preferable to have correct data, even if one has to wait that bit longer for them. Nonetheless, it is disappointing that the CSO is not able to make a better stab at producing accurate annual national accounts data three months after the end of the year.

Oliver Mangan
6th July 2004



IRISH MACRO ECONOMIC FORECASTS

Annual average % change unless stated	**2002**	**2003**	**2004 (f)**	**2005 (f)**
Real GNP	**1.5**	**2.8**	**4.5**	**5.0**
Real GDP	**6.1**	**3.7**	**5.5**	**6.0**
Domestic Expenditure	3.7	2.8	3.6	4.1
Personal Spending	2.8	2.6	3.0	4.0
Government Spending	8.6	2.5	3.0	3.0
Fixed Investment	3.0	3.4	5.3	5.0
Contribution of Stocks to GDP growth	-0.3	0.5	-0.1	0.2
Total Exports	5.7	-0.8	5.0	7.0
Total Imports	3.3	-2.3	3.0	6.0
Level of GDP (€bn, current prices)	128.0	134.8	145.5	158.0
Level of GNP (€bn, current prices)	104.5	111.7	120.5	130.0
Industrial Production (Vol)				
Total	7.9	6.3	8.0	10.0
Modern	11.8	7.9	9.0	12.0
Other	-2.3	1.3	5.0	4.0
Housing				
Average House Price (end year)	13.3	13.7	7.0	4.0
House Completions ('000)	57.9	68.8	75.0	70.0
Labour Market				
Employment Growth	1.4	1.8	2.8	3.0
Labour Force Growth	1.9	2.0	2.7	2.9
Unemployment Rate (%)	4.4	4.7	4.5	4.3
Net Immigration ('000)	41.3	29.8	30.0	30.0
Inflation				
CPI	4.6	3.5	2.1	3.0
Core CPI	5.0	4.0	2.1	2.5
Irish HICP	4.7	4.0	2.3	2.6
Mfg Output Prices (Home Sales)	2.5	0.8	-0.4	1.5
External Account				
Trade Balance (% of GNP)	20.3	18.6	18.5	18.5
Current Account Balance (% of GNP)	-1.5	-1.7	-1.5	-1.5
Public Finances				
General Government Balance (€ million)	-258	280	0	-500
General Government Balance (% of GDP)	-0.2	+0.2	0.0	-0.3
General Government Debt /GDP ratio (%)	32.3	32.0	30.5	29.5
Private Sector Finances				
Real Personal Disposable Income	4.4	2.4	4.7	4.5
Personal Savings Ratio (%)	10.5	11.2	11.1	10.8
Private Sector Credit % (end year)	15.0	17.9	20.0	15.0

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