



THE IRISH ECONOMY REVIEW & OUTLOOK SEPTEMBER 2003

OVERVIEW

Data published for the first half of the year paint a mixed picture of the Irish economy. On the positive side, growth in manufacturing output averaged 4.3% year-on-year in H1 2003. Retail sales excluding autos increased by 2% year-on-year. The housing sector continued to boom with completions rising by 14.5% in Q1. The agriculture sector also saw a sharp rise in farm output in H1. Meanwhile, employment rose by 1.5% year-on-year in both Q1 and Q2 2003.

Other areas of the economy, though, have been very weak. Investment in machinery and equipment fell very sharply in the opening half of the year. Meanwhile, new car sales were down 6.4% yoy to end August. Growth in government spending has slowed sharply, most notably capital expenditure, which fell by 13% in the first eight months of the year. Tax receipts are also sluggish. There has been a pronounced weakening of external trade. Sharp falls in both export and imports volumes were recorded in H1 2003. However, this is partly due to the ceasing of "carousel" type trading in electrical machinery with the UK which has no impact on activity levels.

Overall, the economy grew at a sluggish pace in the opening half of the year, especially during the opening quarter, when GDP rose by just 0.5% yoy. There are some signs, though, of a strengthening of activity in line with recent trends in most other economies. The PMIs for both the manufacturing and services sector picked up over the summer months. There was a marked improvement in non-agricultural private sector employment during Q2. Exports also picked up in the second quarter of the year.

However, as yet these are only tentative signs of a pick up in activity. Overall, while GDP growth should improve on the 0.5% yoy rate recorded in Q1, it is likely to remain subdued enough for the year as a whole, averaging around 2%. GNP growth should be higher at around 2.8% because of a likely decline in net factor income outflows this year.

Growth, though, can be expected to pick up next year in line with a much stronger performance by the world economy. As a very open economy, Ireland should see a marked improvement in export growth in these circumstances, despite the appreciation of the euro over the past eighteen months. A continuing low interest rate environment should help stimulate domestic demand, while the savings ratio could decline from its current high levels. Spending power should also be boosted by lower inflation. Thus, we look for GDP growth to pick up to around 4% next year.

If our forecasts are correct and the Irish economy does indeed recover next year, it would imply that a soft landing has been achieved in this downturn. The extremely expansionary stance of monetary and fiscal policy in Ireland over the past three years has played a major role in softening the impact of the global downturn. Employment growth has held up reasonably well to date so the rise in unemployment has proved modest enough. Overall, it would be quite a result for the Irish economy, given the long duration of the global downturn, the major shake out in the ICT sector and the unfavourable exchange rate movements since early 2002.

SUMMARY

<i>National Economy (P 3)</i>	Another year of below trend growth for the Irish economy in 2003 reflecting the weak external environment and tightening of domestic fiscal policy.
<i>Construction (P 4)</i>	Another sizeable increase in housing completions is on the cards this year. Non-residential building activity is expected to be weak while public capital spending has been cut back sharply this year.
<i>Agriculture (P 5)</i>	Deteriorating terms of trade mean that farm incomes may not recover that much in 2003 after the 8% fall registered last year, despite higher output volumes.
<i>Industry (P 6)</i>	Industrial output was sluggish in Q2 after a strong Q1. However, a weaker euro and pick-up in global demand suggest that output could improve in H2 2003.
<i>External Trade (P 7)</i>	Exports could decline by some 6% in 2003, and imports by 8%, partly because of the termination of 'carousel' type trading in electrical machinery with the UK.
<i>Balance of Payments (P 8)</i>	The deficit on the current account looks set to climb sharply in 2003, reflecting a big fall in the trade surplus.
<i>Macro Forecast (P 9-12)</i>	Domestic spending has weakened in 2003. Exports and imports are in decline. Thus, GDP growth could slow to 2% from 6.9% in 2002. GNP growth is forecast at 2.8%, boosted by a fall in net factor income outflows.
<i>Consumer Spending (P 13)</i>	A tight budget as well as high inflation and weak confidence suggest that consumer spending may grow by just 2.5% this year.
<i>Labour Market (P 14)</i>	Growth of 1.5% in employment now likely in 2003, a better than expected result. The unemployment rate is expected to average 4.7% in 2003, up modestly from 4.4% in 2002. The average number of hours worked, though, is declining.
<i>Earnings & Wages (P 15)</i>	The pace of wage inflation has moderated but there is considerable variation across sectors. Public sector pay rises sharply, reflecting generous wage increases arising from the benchmarking process.
<i>Prices (P 16)</i>	The rate of inflation has eased to close on 3% as weak demand, a stronger euro and falling oil prices and mortgage rates impact on the CPI.
<i>Monetary Conditions (P 17)</i>	Credit growth remains robust at 14.6% yoy in July 2003. Demand continues to be boosted by strong growth in mortgage lending.
<i>Public Finances (P 18)</i>	The government has tightened budgetary policy. Nevertheless, an EBR of €2bn or almost 2% of GNP is likely in 2003, slightly above the budget target.
<i>Tables (P 19-20)</i>	Historical statistics and economic forecasts.

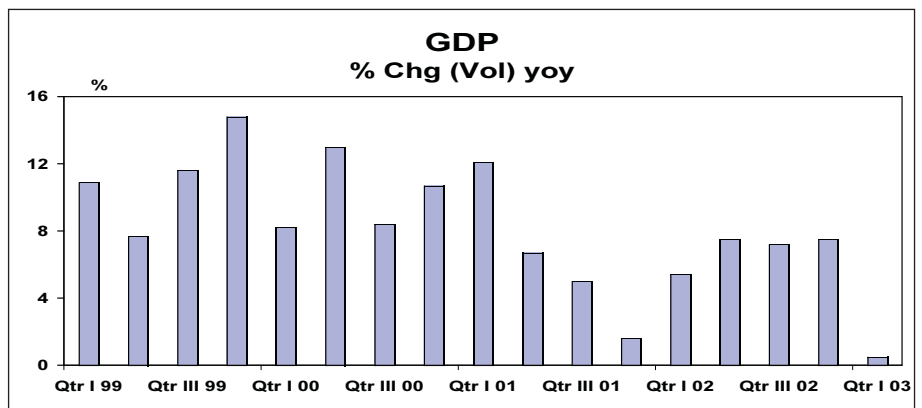
THE NATIONAL ECONOMY

Divergence In 2002 Data

Revised data now show that GDP grew by 6.9% in 2002, while GNP increased by just 0.1%. GNP growth was greatly depressed by a 40% surge in net factor income outflows, largely profit repatriations. Domestic spending rose by 3.5% last year, which is a better indication of the underlying growth performance of the economy.

Very Weak Growth In Q1 2003

Data released for Q1 2003 show very low growth in GDP and GNP which increased by 0.5% and 0.8% yoy respectively. Growth in consumer and government spending slowed, while investment in machinery and equipment contracted sharply. There were marked declines in the volume of both exports and imports.



Economy To Pick Up Momentum In H2

Consumer spending picked up in Q2 while exports strengthened, pointing to a pick up in the growth rate of the economy. Activity should strengthen further over H2 2003 in line with the global upturn and following the further easing of monetary policy in H1 2003. Overall for 2003, we expect GDP growth to average some 2%. GNP growth should be higher at 2.8%, because of lower net factor income outflows.

The Irish economy should improve in 2004 as the global upswing gathers momentum. Exports should recover, helped also by a weaker euro. A continuing low interest rate environment should help support domestic demand. Thus, we look for GDP growth to pick up to 4% next year with GNP growth at around 3.8%.

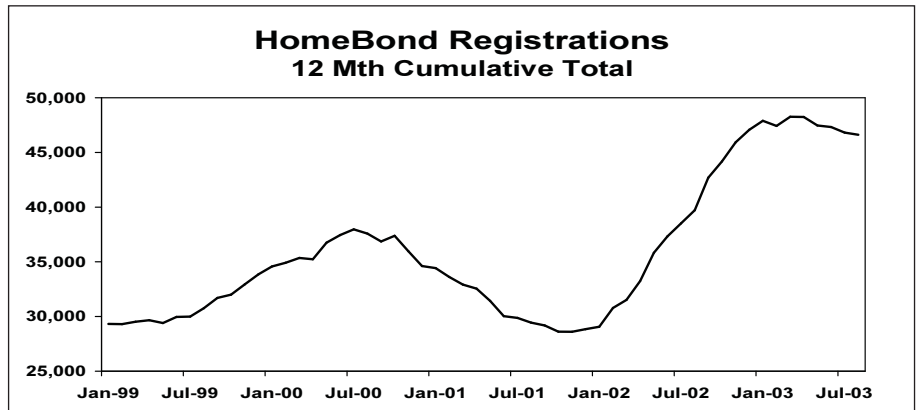
	Volume % Chg yoy	Consumer Spending	Fixed Investment	Exports	Imports	GDP	GNP
2000 Year		8.5	6.8	20.6	21.3	10.1	10.2
2001 Year		5.5	0.1	8.3	6.5	6.2	3.8
2002 Year		2.7	1.7	6.2	2.3	6.9	0.1
2002 Qtr I		3.8	-4.1	7.8	2.0	5.4	-1.7
2002 Qtr II		2.3	0.6	8.5	7.5	7.5	2.2
2002 Qtr III		3.4	7.1	9.1	6.6	7.2	-0.4
2002 Qtr IV		1.3	4.5	-0.4	-6.2	7.5	0.1
2003 Qtr I		1.8	-12.4	-12.8	-13.7	0.5	0.8

CONSTRUCTION

Strong Housing Completions

Not surprisingly, HomeBond registrations have not been able to sustain the pace of growth seen in 2002, when they surged by over 63% to reach record levels. Indeed, registrations in the eight months to August were down some 1.5% yoy. The 12 month cumulative total peaked in March and by August was 3.4% off its highs.

Given the time lag with registrations, a further strong rise in house completions is likely this year. Completions rose by 9.7% in 2002, reaching record levels and climbed by a further 14.5% in Q1 this year. Completions, though, could well fall in 2004 if registrations continue to moderate.



But Weakness In Other Construction Sectors

Total construction output rose by 5% in 2002. Housing should continue to make a strong contribution to growth in construction output in 2003. However, non residential private construction activity is likely to remain depressed while expenditure under the Public Capital Programme is down sharply. Thus, growth in overall construction output may slow to less than 0.5% in 2003.

House Price Inflation Remains Strong

Permanent tsb data show no sign of any decline in house price inflation which, apart from a dip in 12.7% in April, stood between 14% and 15.5% in H1 2003. Indeed, July saw it edge above the top of this range to 15.6% yoy. The main strength is in second hand houses with growth in new house prices more moderate at 10.5% yoy in July. The large increase in house completions could well continue to constrain new house prices and some modest decline in overall house price inflation is possible over the balance of the year.

	HomeBond Registrations	% YoY 3 mth moving avg	Construction Employment ('000)	% YoY	permanent tsb House Prices	
					% MoM	% YoY
2002	Aug	3,282	54.4	190.0	1.9	4.9
	Sep	5,271	75.7			6.7
	Oct	3,989	82.5			9.0
	Nov	3,997	88.1	190.8	3.2	11.0
	Dec	2,488	72.2			13.3
2003	Jan	3,878	55.7			15.2
	Feb	3,565	17.7	188.5	2.9	15.4
	Mar	4,219	11.3			14.5
	Apr	4,042	3.1			12.7
	May	4,954	0.3	190.4	5.1	14.1
	June	3,726	-6.9			14.7
	July	3,401	-10.6			15.6
	Aug	3,082	-7.7			

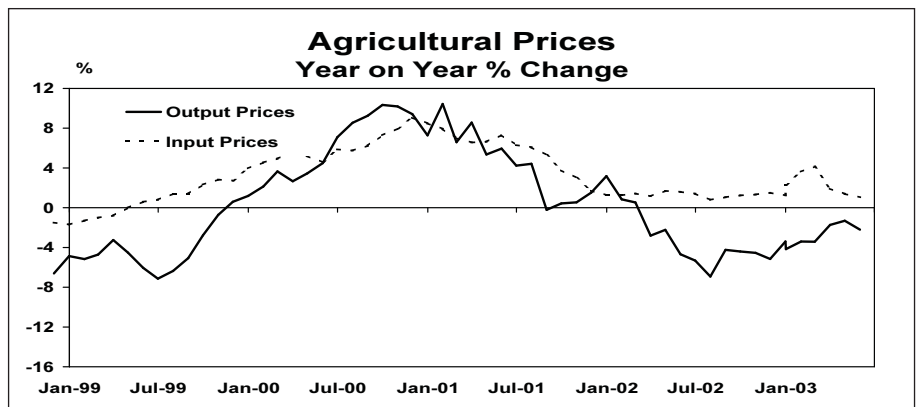
AGRICULTURE

9% Fall In Farm Incomes In 2002

2002 was a poor year for agriculture. Incomes fell 8.1%, compared to an increase of 6.4% in 2001. Downward pressure on both the price and volume of farm output, as well as rising input costs, resulted in a difficult year for the sector, with bad weather also taking its toll.

Output Prices Continue To Decline In 2003

Farm output prices fell by 3.8% in 2002. Although decreases have moderated, output prices continue to fall on a yoy basis. There continue to be declines in some of the livestock areas, with prices for cattle and pigs falling by a respective -1.8% and -12.1% in yoy terms in June. Sheep prices, however, have recovered and were up 3.8%. Milk output prices were down 1.5% yoy in June with cereals down 11.7%.



Input Costs Accelerate

After slowing considerably over the course of 2002, the downward trend in farm input prices was reversed in Q1. Prices were up 4.1% yoy in March, from an average 1.3% in 2002. However, with energy prices stabilising over recent months, the growth in input prices eased back to 1.0% yoy in June.

Small Rise In Incomes Likely in 2003

The volume of farm output has picked up over 2003. Milk production was up an average 3.4% yoy to end July, with cattle slaughterings rising by an average 4.4% yoy in the same period. The good weather conditions over the summer months should be positive for production. However, with farm output prices still at weak levels and input costs only starting to trend downwards again, any recovery in farm incomes in 2003 may prove modest enough, despite the rebound in output.

		Cattle	Milk	Output Prices		Input Prices	
		Slaughterings	Intake	(1990=100)	% YoY	(1990=100)	% YoY
		% YoY	% YoY				
2002	May	-1.3	-0.2	91.7	-4.7	114.7	1.6
	July	9.8	-3.6	90.1	-6.9	114.2	0.8
	Aug	-13.5	-3.6	88.0	-4.2	114.2	1.1
	Sep	4.8	-3.8	89.1	-4.4	114.3	1.2
	Oct	-3.4	-1.6	88.2	-4.5	114.5	1.3
	Nov	-14.4	-10.2	88.4	-5.2	114.3	1.5
	Dec	-1.2	-1.9	91.0	-3.4	114.0	1.2
2003	Jan	-6.6	7.5	92.0	-4.2	115.6	2.3
	Feb	7.5	13.9	91.0	-3.4	117.2	3.6
	Mar	9.5	20.8	90.4	-3.4	118.1	4.1
	Apr	10.4	-0.2	90.7	-1.7	116.5	1.9
	May	-1.1	-0.3	90.5	-1.3	116.3	1.4
	June	13.2	0.7	88.8	-2.2	115.8	1.0
	July	3.1	0.9				

INDUSTRY

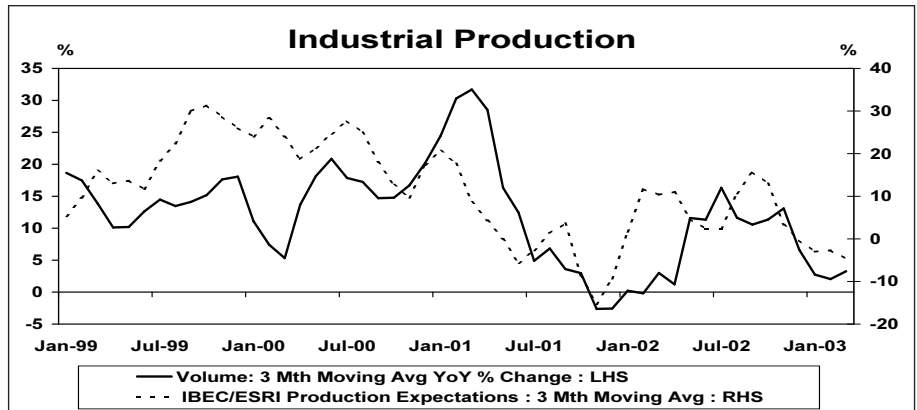
Industrial Production Sluggish In Q2

Industrial production rose by 7.9% last year, but growth was concentrated in H1. Indeed, in H2 2002 output declined, falling by 3.6% qoq in Q3 and a further 1.2% in Q4. The first quarter of 2003 saw output volumes rebound strongly, rising by 7.1% on the quarter. However, this was followed by sluggish growth of just 0.9% in Q2. This left output volumes only 3.4% higher than year earlier levels.

Weak Pharmaceutical Sector

Notably, the pharmaceutical sector has reversed some of its large 2002 gains, with output falling by 17.7% yoy in Q2 this year. However, other high tech sectors such as reproduction of recorded media (+32.8% yoy) and office machinery and computers (+35.1%) expanded strongly in Q2 2003.

Turnover data, however, highlight that currency movements have resulted in sharp price falls in many sectors. Turnover in pharmaceuticals fell a dramatic 48% yoy in Q2 2003 while turnover in the office machinery and computer sector was up just 13% in the same period.



Output Could Pick-Up In H2

Sluggish industrial output in Q2 is consistent with the persistent weakness in some leading indicators of industrial activity such as the PMI and IBEC/ESRI survey. Given the recent weakening of the euro and pick up of global demand, there must be some hope, however, that industrial output will strengthen over the latter part of the year. Indeed, the PMI hit a four month high in August, though still remaining below the critical 50 level that signals growth in the sector.

		Total Industrial Production		Modern	Other	Capacity + Utilisation %	Production+ Expectations 3mth. Mov Avg
		% Change YoY	YoY % 3 Mth Mov Avg	Industries YoY % 3 Mth Mov Avg	Industries YoY % 3 Mth Mov Avg		
2002	June	13.6	11.3	15.9	-1.1	71.4	2.3
	July	11.8	16.3	24.3	-2.9	72.5	2.3
	Aug	9.1	11.6	18.3	-4.5	76.0	10.7
	Sep	10.9	10.6	17.3	-5.6	78.1	15.7
	Oct	13.9	11.4	17.6	-4.8	75.4	13.0
	Nov	14.5	13.1	19.3	-3.0	73.2	3.3
2003	Dec	-7.4	6.6	10.0	-2.6	72.2	-0.3
	Jan	2.0	2.7	5.1	-3.6	74.4	-3.0
	Feb	12.2	2.0	3.6	-2.3	75.4	-2.7
	Mar	-4.9	2.5	3.5	-0.5	73.6	-4.7
	Apr	9.8	5.0	5.7	2.9	73.7	-8.3
	May	0.3	1.4	1.4	1.3	72.1	-9.7
	June	-0.1	3.2	4.0	0.6	74.9	-8.7

+IBEC/ESRI Industrial Survey

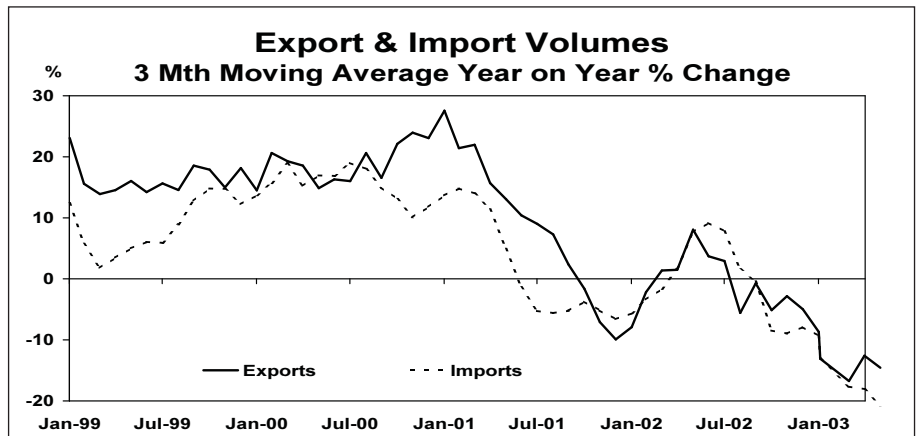
EXTERNAL TRADE

Sharp Decline In External Trade In H1 2003

Merchandise exports fell by 21% in value terms in the first half of the year while merchandise imports declined by 25% compared to H1 2002. Service exports, on the other hand, grew by 11.4% yoy in Q1 2003 while service imports rose by a more modest 1.7%. No data are available yet for external trade in services in Q2.

Downward Pressure On Prices

There are three main factors behind the sharp decline in the value of merchandise trade. First, the strength of the euro against the dollar in H1 2003, which has greatly depressed prices - export and import prices fell by some 6% and 5% respectively in H1 2003. Second, the general weakness of the global economy. Third, the termination of "carousel" type trading in electrical machinery with the UK.



Trade Data To Improve In H2

Merchandise trade should pick up in H2 2003: the euro lost significant ground against the dollar over the summer, the global economy has started to strengthen while the impact of the fall-off in trade in electrical goods with the UK will abate. Nevertheless, there will still be a sharp fall in the value of merchandise trade for the year as a whole.

Overall, we look for marked fall in the total volume of exports and imports of 8% and 6% respectively in 2003. However, trade volumes should show a significant rise in 2004 as the global upswing gathers momentum.

	Exports	Imports	Surplus	Surplus	Import Prices	Export prices	
€m	s.a.	s.a.	s.a.	Unadj	YoY%	YoY%	
					3 Mth Mov Avg	3 Mth Mov Avg	
	June	6950.8	4444.5	2506	3535	-4.1	0.3
	July	8010.1	4737.1	3273	3301	-5.6	-0.1
	Aug	7368.0	4395.0	2973	2663	-6.2	-1.1
	Sep	7587.0	4200.0	3387	3915	-6.0	-0.9
	Oct	7045.0	4003.7	3041	3087	-5.1	-0.5
	Nov	7372.0	4135.0	3237	3244	-4.3	-0.6
	Dec	7239.3	4151.6	3088	2773	-4.1	-0.4
2003	Jan	6644.3	3892.9	2751	2313	-4.8	-1.7
	Feb	6830.8	4000.4	2830	2592	-4.8	-2.8
	Mar	6346.1	3841.4	2505	2923	-4.5	-4.3
	Apr	6970.6	3921.8	3049	2615	-4.1	-4.9
	May	6655.3	3649.6	3006	2864	-4.2	-6.3
	June	6480.0	3760.0	2720	3450		

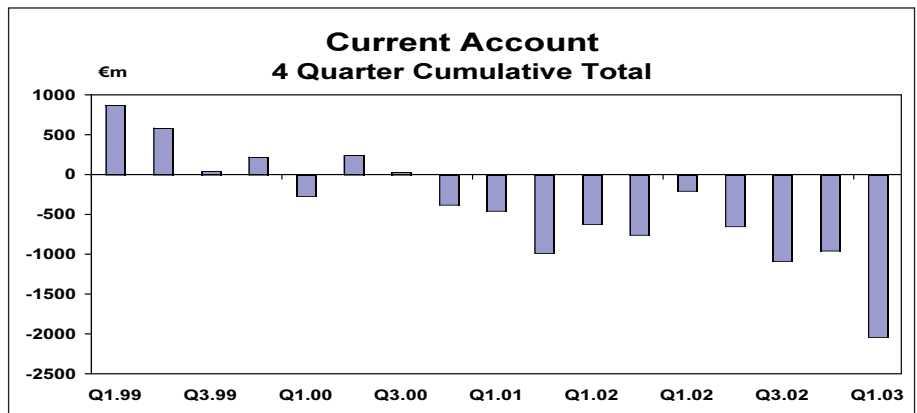
BALANCE OF PAYMENTS

BoP Deficits Revised Upwards

Balance of payments data for Q1 2003 showed a large current account deficit of €1,039m compared to a small surplus in the same period last year. Furthermore, revisions to previous years' data show current account deficits of close to €1 billion in 2001 and 2002, much larger than previously reported.

Large Current Account Deficit In Q1

In terms of the Q1 2003 data, there was a marked fall of almost €2bn from a year earlier in the merchandise trade surplus to €7.5bn. This decline reflects a sharp fall in the value of merchandise exports from €24.6bn to €18.9bn, which greatly exceeded a decline in merchandise imports in the same period.



Decline In Merchandise Trade Surplus

The decline in the merchandise trade surplus in Q1 was partly offset by a contraction in the deficit on trade in services and somewhat lower net factor income outflows. There was a much more modest decline in the merchandise trade surplus in Q2. Nevertheless, the current account deficit in the quarter can be expected to be above the level of €472m recorded in Q2 2002.

Higher current account deficits are likely in H2 2003 also, because of lower trade surpluses. For the year as a whole, we look for a current account deficit of around €2.7bn or 2.5% of GNP, compared to 0.9% of GNP in 2002. The deficit should fall next year, though, possibly to around 1.7% of GNP, as exports recover.

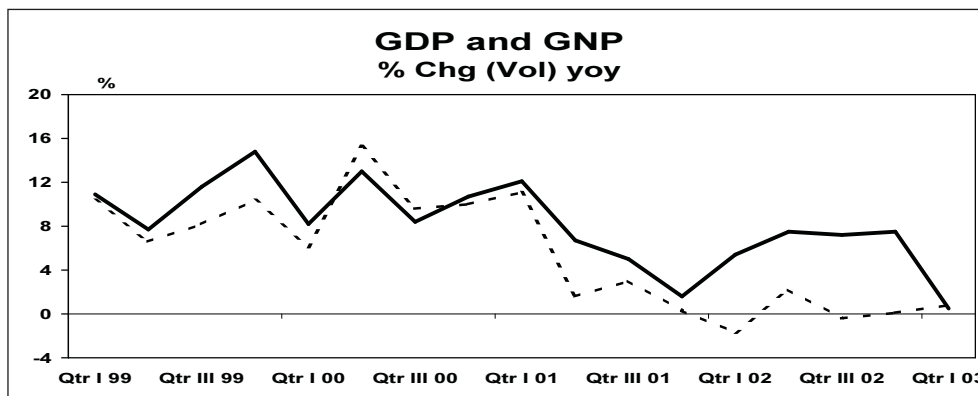
	Balance of Payments (€m)	Goods	Services	Income	Transfers	Current Account
2000 Year		27,266	-13,889	-14,750	994	-379
2001 Year		30,494	-13,259	-18,295	305	-757
2002 Year		37,014	-12,871	-25,914	815	-954
2002 Qtr I		9,511	-3,507	-5,927	-32	45
2002 Qtr II		9,175	-3,200	-6,577	130	-471
2002 Qtr III		9,712	-3,311	-6,705	-7	-310
2002 Qtr IV		8,616	-2,853	-6,705	724	-218
2003 Qtr I		7,534	-2,937	-5,591	-45	-1,039

THE MACRO FORECAST

Weak Q1 Data

National Accounts data for the opening quarter of 2003 show that GDP growth slumped to just 0.5% year-on-year from 7.5% in Q4 2002. Meanwhile, GNP growth picked up to 0.8% yoy from 0.1% in the final quarter of last year. Overall, the data point to a very weak performance by the economy in the early part of the year.

These growth figures are the result of averaging the outcomes of two different measurement procedures (output and expenditure). Interestingly enough, the output measures shows GDP rose by 2.1% yoy in Q1, while on an expenditure basis, it fell by 1.1% yoy. There is no way of knowing precisely which of the measures is the more accurate or, indeed, if the average, which constitutes the official figure, is closer to the truth.



The growth rate of 2% derived on the output basis, though, sits more comfortably with other data on the economy for Q1 2003. The Quarterly National Household Survey showed a rise of 1.5% in employment from year earlier levels. Unless there has been a collapse in productivity growth, this is difficult to reconcile with declining GDP. On top of this, data for manufacturing, construction, agriculture, the government sector and services all showed respectable growth rates in Q1.

External Trade

In our view, the growth figure arrived at using the expenditure basis is probably an underestimate. Our main concern relates to external trade data. Exports are reported to have declined by 12.8% in volume terms in Q1. Imports, meanwhile, are reported to have fallen by 13.7%.

External trade data are being distorted by the termination of 'carousel' type trading in electrical machinery with the UK, which will significantly depress export and import volumes this year. It knocked some 8% off export growth in Q1, suggesting that underlying or real exports declined by close to 5%. A fall in real exports, though, is difficult to reconcile with volume growth of 2.5% in manufacturing output, the vast bulk of which is exported, and a rise of 11.4% in the value of service exports in Q1.

We also find it difficult to fathom how the fall in import volumes, put at 13.7%, is just 1% more than the fall in exports. A number of factors suggest that the gap should be much wider. First, there was a sharp fall of over €0.5bn in imports of transport equipment during Q1, which depressed overall import growth by 2%.

Second, BOP data show that while service exports rose by 11.4% in value, service imports climbed by a paltry 1.7%. Third, the impact in percentage terms of the fall off in 'carousel' type trade with the UK in Q1 is some 2% greater for imports than exports. Thus, in our view, net trade made a far greater contribution to growth in Q1 than suggested by National Accounts expenditure data.

Merchandise trade data for Q2 show a pick up in export volumes in the quarter while imports remained very weak. This should boost the GDP growth rate for the quarter. Nevertheless, merchandise exports remained well down on year earlier levels, reflecting the termination of 'carousel' type trading in electrical machinery with the UK. The impact of this factor on trade will abate during the second half of 2003.

Overall, a marked fall in the total volume of exports and imports is on the cards for 2003 as a whole, which we estimate at 8% and 6%, respectively. Both exports and imports should recover in 2004 as the global economic upswing gains momentum and with carousel type trading with the UK no longer distorting the data. We look for exports and imports to grow by 4.5% and 3.5%, respectively, next year.

Fixed Investment

Investment in machinery and equipment declined in both 2001 and 2002. However, this was more than offset by the continued rise in construction output, reflecting robust growth in housebuilding and public capital spending. Overall, fixed investment grew by 0.1% in 2001 and 1.7% in 2002.

Fixed Investment (% Change, Volume)				
	2001	2002 (e)	2003 (f)	2004 (f)
Housing	6.4	5.1	6.2	1.5
Other Construction	3.3	5.0	-5.0	1.2
Machinery & Equipment	-5.4	-2.7	-15.0	3.3
Total	0.1	1.7	-6.0	2.0

In Q1 2003, investment in machinery and equipment declined by a very sharp 29% yoy, reflecting a big fall off in spending on transport equipment. Although construction spending continued to grow strongly, helped by another big jump in housing output, total investment spending fell by 12.4% yoy in the quarter.

External trade data showed a further marked decline in imports of transport equipment in Q2, pointing to continued weakness in investment in machinery and equipment in the quarter. For the year as a whole, we look for this investment category to decline by 15%. There should be a modest recovery in business investment in 2004 as the global economy returns to a firm growth path.

Housing investment rose by 7.4% yoy in Q1. High levels of HomeBond registrations in recent quarters and strong growth in construction employment point to another sizeable increase in housing output in 2003, possibly of the order of 6%. Investment in housing may start to level off in 2004 given recent indications that the rise in HomeBond registrations is topping out.

Non-residential construction investment grew by 3.3% yoy in Q1. However, there has been a marked fall off in capital spending by the government since then. It is down by 13% year to date. As a result, we look for non-residential construction spending to fall by 5% in 2003 with little growth likely in 2004. Overall then, we are forecasting that total fixed investment will contract by 6% this year, reflecting the sharp decline in spending on machinery and equipment and cutback in public capital expenditure. At this stage, we estimate that investment spending may show modest growth of around 2% in 2004.

Consumption

The 2003 budget provides for only a small rise in non-pay and non-social welfare government spending. This tightening of budgetary policy has led to a marked deceleration in growth in government spending this year. Overall, we look for volume growth in current government expenditure to decelerate sharply to just 2.2% this year from 9.4% in 2002, with growth of just 2% likely in 2004.

Personal Income, Consumption & Savings (Nominal % Change)				
	2001	2002 (e)	2003 (f)	2004 (f)
Disposable Income	10.1	9.2	6.4	5.9
Consumer Spending	10.1	8.9	6.7	6.5
Personal Savings	10.7	11.5	2.8	0.1
Savings Ratio (%)	9.8	10.0	9.7	9.1

Meanwhile, growth in the volume of personal consumption decelerated to 1.8% yoy in Q1 2003 from an average of 2.7% in 2002. Data on non auto retail sales show an acceleration in the year-on-year growth rate during Q2. We expect the pace of spending to pick up somewhat further in H2 2003. Falling inflation and the continuing steady growth in employment should help underpin spending growth. With the world economy improving, consumer confidence should also pick up in H2 2003. Overall, growth in consumer spending could average around 2.5% for the year as a whole.

The savings ratio has risen steadily over the last number of years, reflecting weak economic conditions and the strong uptake of the SSIA scheme. The savings ratio should decline next year given the expected upswing in the global economy and resulting boost to confidence and employment. This should boost consumer spending which will also benefit from a more subdued inflation environment. A continuing tight budgetary policy, though, may see a further rise in the tax burden. Nevertheless, growth in consumer spending should pick up to around 3.5% in 2004.

GDP & GNP

Our analysis points to a rise of around 2% in GDP in 2003, down from 6.9% in 2002. The deceleration reflects slower growth in domestic spending, especially business investment and government expenditure, and a decline in exports.

The trend in net factor income outflows will have a crucial bearing on GNP. We note that those years in the past decade which recorded very large rises in net factor income outflows were followed by years of only modest increases in such outflows. Indeed, these outflows fell slightly in Q1 2003. Thus, we expect GNP growth of 2.8% in 2003, up from a meagre 0.1% in 2002, helped by lower net factor income outflows.

National Accounts Forecasts (% Change Volume)				
	2001	2002 (e)	2003 (f)	2004 (f)
Private Consumption	5.5	2.7	2.5	3.5
Government Consumption	11.1	9.4	2.2	2.0
Fixed Investment	0.1	1.7	-6.0	2.0
Domestic Expenditure	5.0	3.5	0.4	2.9
Stocks (GNP Contribution)	-0.5	-0.6	0.4	0.0
Exports	8.3	6.2	-6.0	4.5
Imports	6.5	2.3	-8.0	3.5
GDP	6.2	6.9	2.0	4.0
GNP	3.8	0.1	2.8	3.8

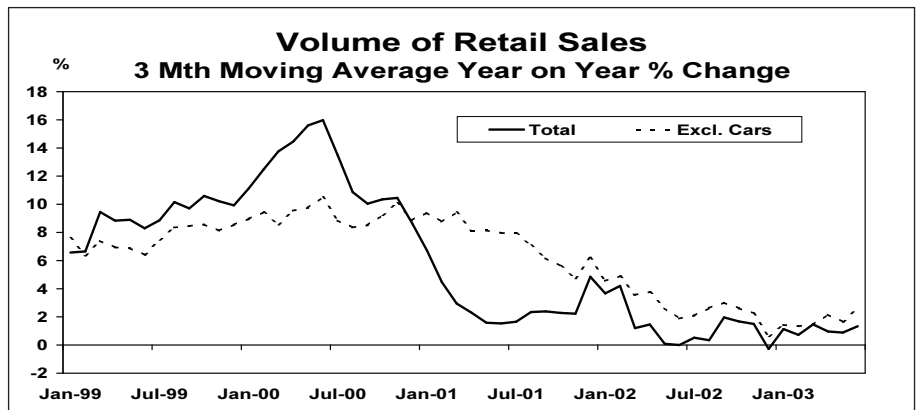
We look for GDP growth to average around 4% in 2004, with GNP rising by some 3.8%. This is based on the view that the world economy will grow quite strongly next year - the IMF is forecasting 4% global growth. This would provide a significant boost to exports. Meanwhile, a continuation of the current low interest rate environment should lift domestic spending, in particular business investment, following the weak performance in 2003.

CONSUMER SPENDING

Weak Retail Sales

Weak car sales and depressed levels of non-auto sales saw retail sales volumes grow by just 0.7% in 2002. Car sales have continued to decline, falling by 6.4% yoy in the eight months to August.

Thus, total retail sales volumes remain subdued growing by just 0.1% in Q2 after having fallen by 0.6% in Q1 2003. As a result, Q2 volumes were up just 1.5% yoy. Non-auto sales maintained their relatively subdued trend, growing by 0.7% qoq in both Q1 and Q2 this year, to give yoy growth in Q2 of 2.6%.



Depressed Consumer Confidence

The depressed level of car sales, in particular, may well reflect the weak state of consumer confidence. Both the EU consumer confidence indicator for Ireland and the ESRI/IIB consumer confidence indicator have fallen to low levels over the past six months. There is a glimmer of hope, though, that confidence could have troughed with the latest ESRI/IIB confidence indicator for August picking up after a particularly sharp fall in July.

Moderate Spending Growth In 2003

The tight budget as well as still relatively high inflation, considerable number of job losses and sluggish consumer confidence are all acting to dampen household spending this year. Overall, consumer spending may grow by around 2.5% this year, with the savings ratio likely to remain relatively high. Growth in consumer spending should pick up to around 3.5% in 2004 as the economy improves.

		Retail Sales Volume S.A		Excl Garages Volume S.A.		SIMI Car Registrations	% Change Year 3 mth moving avg
		% Change Month	% Change Year	% Change Month	% Change Year		
2002	Aug	-0.5	-0.3	0.3	2.7	8,742	-7.2
	Sep	4.1	4.7	2.1	4.2	6,383	3.6
	Oct	-2.3	0.6	-1.8	1.0	5,114	2.5
	Nov	-0.7	-0.8	0.4	1.6	2,127	0.3
	Dec	1.3	-0.7	0.3	-0.6	1,645	-0.6
2003	Jan	0.6	5.0	0.9	3.4	32,772	5.6
	Feb	-2.7	-2.0	-0.8	1.3	19,682	-3.6
	Mar	0.1	1.5	0.0	-0.3	17,898	-5.0
	Apr	2.9	3.4	2.8	5.6	15,729	-8.8
	May	-5.3	-2.3	-5.2	-0.3	14,882	-8.1
	June	4.7	2.9	4.9	2.6	11,249	-8.4
	July					13,246	-7.7
	Aug					6,825	-5.0

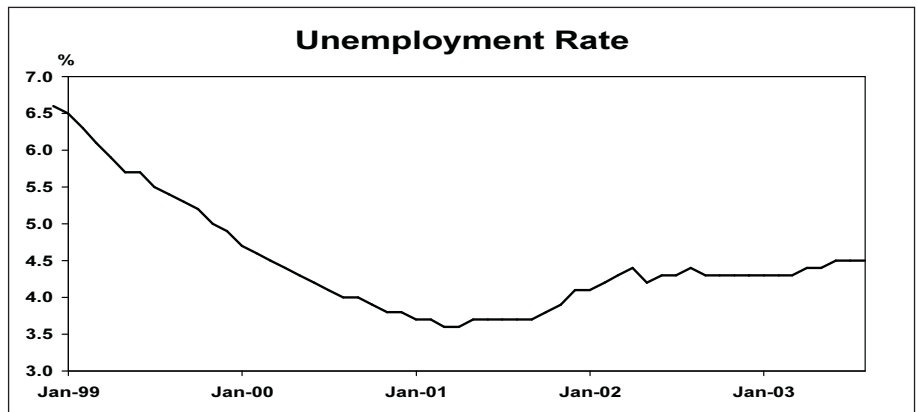
LABOUR MARKET

Employment Growth Surprises In Q2

Employment increased by 28,400 or 1.6% in the year to Q2 2003. This compares with an annual increase of 1.5% in the previous quarter and an average growth rate of 1.4% in 2002. There were 81,400 persons unemployed in Q2 2003, which represents an annual increase of 4,200 but a decrease of 3,500 on the previous quarter. As a result, the unemployment rate fell to 4.4% from 4.6% in Q1.

Private Sector Stabilises After Two Weak Quarters

The results of Q2's Labour Force Survey were better than expected. However, there was a noticeable decline to 37.2 hours in the average number of hours worked per week from 37.7 hours a year ago. Employment growth was once again strongest in the public sector, up 4.8% yoy. However, after declining by a respective 0.6% and 2.2% in each of the two previous quarters, employment growth in the private sector was up 0.2% in the three months to May 2003.



The labour market is holding up better than anticipated, though there is considerable variation in employment growth across sectors. Employment in agriculture has fallen sharply in the past year in particular. Meanwhile, growth in construction and tourism sectors has been strong.

Unemployment Rate Relatively Low

Overall, we expect employment growth of around 1.5% in 2003. After rising by 7,300 to May, the Live Register has risen by 5,100 in the past three months. Thus, the unemployment rate may climb to around 5% in Q3 2003. For 2003 as a whole, the unemployment rate may average around 4.7%, a relatively low level.

	Labour Force		Employment		Unemployment	
	Total (000)	% Chg YoY	Total (000)	% Chg YoY	Total (000)	Rate %
2001						
Qtr II	1,745.6	3.4	1,670.7	5.0	74.9	4.3
Qtr III	1,815.6	2.6	1,737.9	4.1	77.7	4.3
Qtr IV	1,779.1	2.5	1,710.3	3.8	68.8	3.9
2002						
Qtr I	1,775.5	2.5	1,709.9	3.6	65.6	3.7
Qtr II	1,781.9	2.1	1,716.5	2.7	65.4	3.7
Qtr III	1,866.1	2.8	1,786.6	2.8	79.5	4.3
Qtr IV	1,825.5	2.6	1,752.9	2.5	72.6	4.0
2003						
Qtr I	1,825.4	2.8	1,745.5	2.1	80.0	4.4
Qtr II	1,827.0	2.5	1,749.9	1.9	77.2	4.2
Qtr III	1,881.5	0.8	1,794.8	0.5	86.7	4.6
Qtr IV	1,854.7	1.6	1,770.7	1.0	84.1	4.5
2003						
Qtr I	1,857.0	1.7	1,772.0	1.5	84.9	4.6
Qtr II	1,859.7	1.8	1,778.3	1.6	81.4	4.4

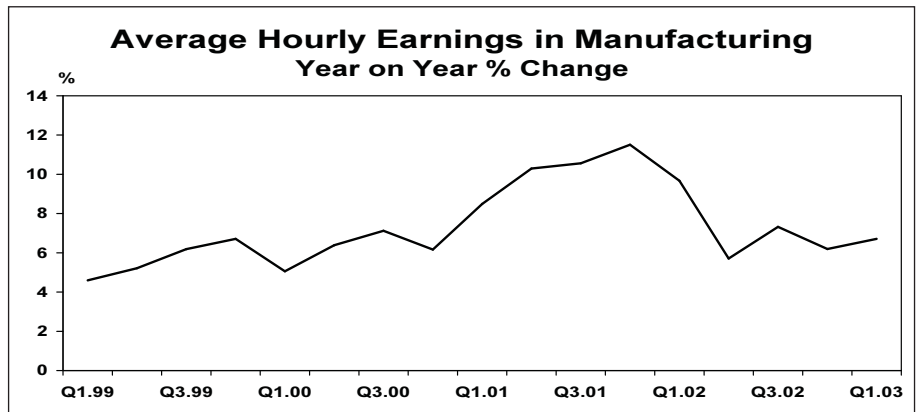
EARNINGS AND WAGE COSTS

Wage Inflation Continues To Moderate

The pace of wage inflation continues to moderate. Nevertheless, data are still showing considerable variation in pay developments across various sectors of the economy. The deceleration in wage growth has been most evident in the distribution and services sectors, where the yoy growth rate in average weekly earnings eased to 4.9% in Q1 2003, from an average 8% in 2002.

But Marked Differences Across Sectors

The yoy growth rate in hourly manufacturing earnings eased to 6.7% in Q1 2003, down from an average 7.7% in 2002. In the financial services sector, average weekly earnings rose by an average 4.4% in 2002, down from 10.9% in 2001. In building and construction, growth in hourly earnings has decelerated from 10.6% in 2002 to 5.5% in Q1 2003.



Wage moderation is expected to remain a feature of the private sector over the remainder of 2003 and into 2004. The current national wage agreement, which provides for wage increases of 7% over an 18 month period, is below wage growth levels of recent years.

High Wage Growth In Public Sector

The public sector wage bill, however, will be boosted by the generous terms of the benchmarking process. This process awarded average wage increases of 9% to public servants. Combined with the terms of the national wage agreement, this implies public sector wage growth of around 16% in 2003/2004.

		Manufacturing € per hour	% Chg QoQ	% Chg YoY	Banking, Insurance & Building Societies (Weekly) % YoY	Building & Construction (Hourly) % YoY
2000	Qtr I	10.02	-0.8	5.1	1.7	13.9
	Qtr II	10.36	3.4	6.4	4.3	9.6
	Qtr III	10.50	1.3	7.1	8.1	8.2
	Qtr IV	10.72	2.1	6.2	10.7	15.6
2001	Qtr I	10.87	1.4	8.5	11.4	13.8
	Qtr II	11.43	5.1	10.3	15.1	11.3
	Qtr III	11.61	1.6	10.6	10.6	12.9
	Qtr IV	11.95	2.9	11.5	6.8	7.0
2002	Qtr I	11.92	-0.3	9.7	9.6	11.5
	Qtr II	12.08	1.3	5.7	5.5	13.6
	Qtr III	12.46	3.1	7.3	0.5	10.8
	Qtr IV	12.69	1.8	6.2	2.1	6.6
2003	Qtr I	12.72	0.2	6.7		5.5

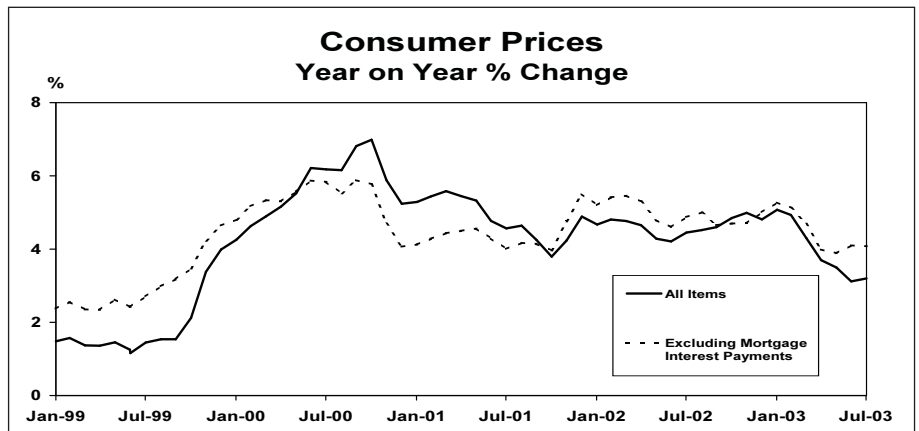
PRICES

Inflation Eases

There has been a marked fall in Irish inflation this year, especially headline CPI inflation. It fell from a rate of 5.1% in February to 3.2% in August. Declining mortgage rates played a major part in the fall, knocking 1.2% off the CPI year to date. Meanwhile, factory gate price inflation has also eased considerably, with the appreciating euro putting severe downward pressure on export prices.

Headline CPI Rate Falls To Close On 3%

Core CPI inflation (ex mortgages) declined from 5.3% in February to 4.1% in August. The strength of the euro, lower oil and food prices as well as weak economic activity, which has helped put downward pressure on service sector inflation, have all played a part in the decline in the core CPI rate.



The deceleration in inflation would be even more impressive but for the hikes in indirect taxes and public sector charges over the past year. These have added around 2% to inflation. But for these increases, the Irish HICP rate would now be in line with the average for the eurozone.

Inflation Rate Of 2.5% Likely In 2004

Inflation should ease further over the balance of the year. The headline CPI rate is likely to average around 3.7% in 2003 with the core rate averaging around 4.3%. Inflation could fall further in 2004, depending on the extent to which the Minister eschews hikes in indirect taxes and the rise in public service charges moderates. At this stage, we think that headline CPI inflation may average around 2.5% in 2004, assuming no change in mortgage rates.

	Consumer Prices				Mfg. Output Prices		
	All Items		Ex Mort. Interest		Total	Domestic	
	% MoM	% YoY	% MoM	% YoY	% YoY	% YoY	
	Aug	0.6	4.5	0.6	4.9	-2.2	1.7
	Sep	0.5	4.5	0.5	5.0	-1.7	1.7
	Oct	0.5	4.6	0.4	4.7	-2.4	2.2
	Nov	0.1	4.8	0.1	4.7	-3.0	2.5
	Dec	0.7	5.0	0.6	4.7	-2.5	3.2
2003	Jan	-0.4	4.8	0.1	5.0	-5.3	2.7
	Feb	1.0	5.1	1.0	5.3	-7.1	2.6
	Mar	0.8	4.9	0.8	5.1	-7.1	2.1
	Apr	0.3	4.3	0.5	4.7	-7.5	1.4
	May	-0.1	3.7	-0.2	4.0	-10.0	0.1
	June	0.0	3.5	0.0	3.9	-10.6	-0.4
	July	-0.8	3.1	-0.3	4.1	-8.2	0.1
	Aug	0.7	3.2	0.6	4.1		

MONETARY CONDITIONS

Growth in Credit Picks Up Pace

In 2002, the annual rate of growth in private sector credit accelerated from 10.5% in April to 15% in December. The demand for credit has remained strong in 2003, averaging 15.4% in yoy terms in the first seven months of the year. Underpinning this demand for credit is buoyant mortgage lending. Excluding, the mortgage component, the annual rate of growth in private sector credit averaged 9% to end 2002 and 10.0% in the seven months to July 2003.

Buoyant Housing Market Fuels Mortgage Demand

The renewed vigour of the housing market in 2002 saw the annual rate of growth in mortgage lending accelerate from 17.9% in January to 23.1% by year end. This strong demand for mortgage financing has been maintained in 2003 with the annual growth rate averaging 23.7% in the period to July 2003.

Some Moderation In Lending Likely

With house price inflation likely to ease over the balance of the year and the overall pace of economic activity remaining subdued, growth in private sector credit should moderate from the levels seen in H1 2003. However, we do not anticipate a marked fall in the headline growth rate.



Interest Rates At Historic Lows

The ECB cut interest rates by 50bps to 2% on 5th June. Rates are now at their lowest level since World War 2 and are expected to remain at very accommodative levels for some time. Against this, the rise in the value of the euro since mid 2002 represents a tightening of monetary conditions. This is reflected in the marked rise in yoy terms in the central bank's trade weighted exchange rate index of Irish competitiveness over the past year.

		Private Sector	Residential	Interest Rates ^		EuroVersus ^	TWI #
		Credit *	Mortgages +	3Mth	Mortgages	US\$	
		% Chg yoy	% Chg yoy	%	%		(% Chg yoy - Mthly Avg)
2002	Aug	13.8	20.4	3.34	4.50	0.9833	4.1
	Sept	13.5	21.1	3.28	4.50	0.9756	2.7
	Oct	13.5	21.2	3.24	4.50	0.9763	2.8
	Nov	13.9	21.8	3.03	4.50	0.9948	4.3
	Dec	15.0	23.1	2.85	4.28	1.0376	5.1
2003	Jan	16.1	23.2	2.79	4.05	1.0816	6.3
	Feb	15.9	23.8	2.52	4.05	1.0730	8.1
	Mar	16.3	23.6	2.51	3.89	1.0973	8.5
	Apr	16.1	23.6	2.52	3.89	1.0973	8.8
	May	15.5	23.6	2.26	3.89	1.1822	10.2
	June	13.5	23.9	2.13	3.53	1.1413	8.2
	July	14.6	24.2	2.11	3.45	1.1477	6.9
	Aug			2.15	3.45	1.0979	6.7

* Excludes transactions between credit institutions and IFSC companies plus valuation effects
+ Includes securitisations ^ End Month
Trade Weighted Competitiveness Indicator for Ireland (CB)

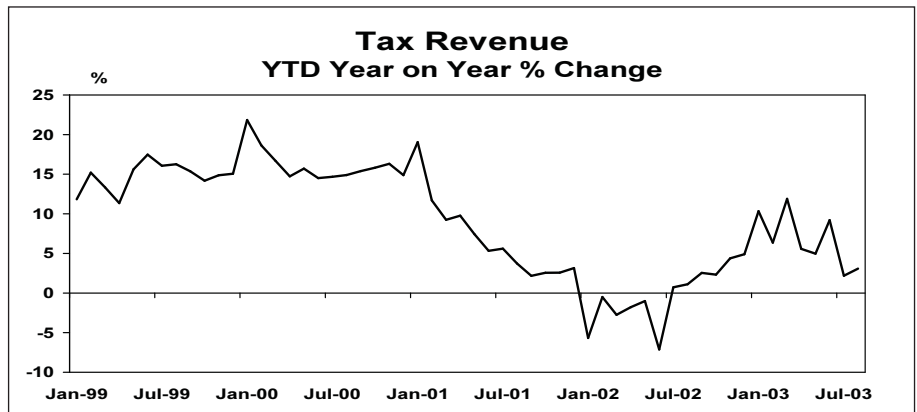
PUBLIC FINANCES

Taxes Receipts Slightly Behind Schedule

Exchequer returns for the first eight months of 2003 show tax receipts are a bit behind schedule, rising by 3.1% compared to the increase of 4.6% projected for the period. Excise duties and corporation taxes are well behind schedule, while stamp duties are ahead of target. Meanwhile, government spending was up by 5.6% at end August, below the 12.8% forecast for the period. It is expected to finish the year close to the target increase of 6.8% set for 2003 as a whole.

Exchequer Finances Move Into Deficit

An Exchequer Borrowing Requirement of €1.87bn was projected in the 2003 budget, compared to a small surplus in 2002. At end August, the EBR amounted to €892m compared to a surplus of €952m at the same stage in 2002. We would point out that this does not represent a significant deterioration in the underlying situation of the public finances from last year. The Minister drew down some €1.75bn in once off funds last year to keep the Exchequer finances in surplus. But for this, there would have been an EBR of around €1.65bn in 2002.



EBR Of Around €2bn In 2003

A likely modest shortfall in tax receipts in 2003 should be partly offset by lower debt interest payments and EU budget contributions. Thus, the EBR outturn is likely to be around €2bn. This should equate to a General Government deficit of around €1bn or 0.7% of GDP. A somewhat higher deficit seems likely in 2004. Overall, the public finances look set to remain well within the 3% deficit limit set down in the Stability and Growth Pact.

€m		Exchequer Balance	Current Budget	Capital Budget	Tax Receipts	
					Supply Services	YTD YoY % Change
		4 Quarter Rolling Total				
2001	Qtr III	2,070	6,045	-8,634	15.4	11.0
	Qtr IV	3,178	6,972	-3,794	14.9	8.7
	Qtr I	3,353	7,080	-3,724	9.2	21.5
	Qtr II	2,764	7,111	-4,348	5.3	19.7
2002	Qtr III	2,368	6,306	-3,937	2.2	18.9
	Qtr IV	650	4,726	-4,076	3.2	22.1
	Qtr I	-198	4,430	-4,630	-2.8	16.5
	Qtr II	-2,154	2,862	-5,015	-7.1	21.1
2003	Qtr III	-1,690	3,626	-5,317	2.6	20.3
	Qtr IV	95	5,402	-5,307	4.9	14.3
	Qtr I	-718	4,592	-5,309	11.9	14.5
	Qtr II	-756	4,066	-4,822	9.2	9.6

HISTORICAL STATISTICS

National Accounts and Balance of Payments Data

	GNP €m Curr Prices	GDP €m Curr Prices	GNP per capita € Curr Prices	Real GNP %	Real GDP %	Real PCE %	Real Fixed Investment %	Curr A/C €M	Curr A/C % of GNP
1992	35,543	40,034	9,999	2.3	3.3	2.9	-1.8	406	1.1
1993	38,578	43,240	10,794	3.4	2.7	3.0	-3.5	1,585	4.1
1994	41,785	46,503	11,653	6.3	5.8	4.4	12.0	1,267	3.0
1995	46,693	52,641	12,966	8.2	9.7	4.3	12.7	1,359	2.9
1996	51,554	58,080	14,315	7.8	8.4	6.5	16.1	1,605	3.1
1997	59,083	67,123	16,142	9.7	9.0	7.2	21.4	1,629	2.8
1998	68,161	77,543	18,398	7.9	7.6	7.3	16.9	627	0.9
1999	76,670	89,614	20,474	8.9	8.7	9.6	7.5	226	0.3
2000	88,095	102,845	23,263	10.2	10.1	8.5	9.3	-379	-0.4
2001	96,448	114,743	25,124	3.8	3.8	5.5	-1.8	-757	-0.8
2002	103,429	129,344	26,541	0.1	0.6	2.7	-0.6	-954	-0.9

Activity Indicators

	Labour Force '000	Employment '000s	Unemployed '000s	Unemp Rate %	Manuf Employment % YoY	Building Employment % YoY	Retail Sales Vol % YoY	Manuf Prod % YoY	House Completions
1992	1,372	1,165	207	15.1	1.5	-2.0	2.3	10.2	22,464
1993	1,403	1,183	220	15.7	0.6	-6.0	1.4	5.4	21,391
1994	1,432	1,221	211	14.7	2.8	2.4	3.3	12.8	26,863
1995	1,459	1,282	177	12.2	6.6	4.5	2.7	20.	30,575
1996	1,508	1,329	179	11.9	3.3	8.2	6.2	8.4	33,725
1997	1,539	1,380	159	10.3	5.8	9.3	7.5	19.4	38,842
1998	1,621	1,494	127	7.8	2.9	8.7	7.8	21.3	42,349
1999	1,688	1,591	97	5.7	-0.8	6.5	9.5	15.0	46,512
2000	1,746	1,671	75	4.3	3.9	6.1	11.9	15.7	49,812
2001	1,782	1,717	65	3.7	0.9	1.7	3.1	10.2	52,602
2002	1,827	1,750	77	4.2	-4.5	0.5	0.7	8.5	57,695

Inflation Indices

	Consumer Prices %	Underlying Inflation (Ex Mort %)	HICP % YoY	Manufacturing Output Prices %	Home Sales Component %	Agricultural Output Prices	% Chg In New House Prices	Hourly Earnings Manuf. %	Hourly Earnings Cons. %
1992	3.0	2.8		1.7	2.6	3.0	3.5	4.6	10.9
1993	1.5	2.0		4.6	2.6	7.0	0.9	5.8	7.0
1994	2.4	3.0		1.1	2.2	1.5	4.1	1.8	4.5
1995	2.5	2.4		2.5	3.6	2.2	7.2	2.4	5.6
1996	1.6	1.9		-0.5	1.6	-4.9	11.8	2.6	3.8
1997	1.5	1.2	1.2	0.3	0.8	-6.6	17.2	2.9	8.8
1998	2.4	2.4	2.2	2.7	0.4	-0.6	22.6	5.1	9.0
1999	1.6	2.8	2.5	1.9	1.6	-4.5	18.5	5.6	7.7
2000	5.6	5.4	5.2	7.5	7.5	6.7	13.9	6.2	12.6
2001	4.9	4.3	4.0	1.7	2.4	4.5	8.1	10.3	11.3
2002	4.6	5.0	4.7	-1.2	2.1	-4.4	8.3	7.2	10.8

Public Finances

	Exchequer Balance €m	Exchequer Balance % of GNP	Current Bud. Balance €m	Current Bud. Balance % of GNP	Capital Borrowing €m	Capital Borrowing % of GNP	General Government Balance/GDP	Debt/GDP Ratio Maastricht	National Debt €m
1991	-636	-2.0	-381	-1.2	255	0.8	-2.3	96	32,223
1992	-905	-2.6	-566	-1.7	339	1.0	-2.4	93	33,450
1993	-876	-2.4	-481	-1.3	395	1.1	-2.3	97	36,006
1994	-853	-2.0	19	0.1	872	2.1	-1.7	91	37,111
1995	-796	-1.7	-460	-1.0	336	0.7	-2.2	83	38,358
1996	-555	-1.1	371	0.7	926	1.8	-0.3	74	37,980
1997	-298	-0.5	767	1.3	1,065	1.8	1.2	65	38,966
1998	948	1.4	2,655	4.0	1,707	2.6	2.4	55	37,510
1999	1,512	2.0	4,365	5.8	2,853	3.8	2.1	49	39,851
2000	3,049	3.5	6,970	8.0	3,921	4.5	4.4	39	36,511
2001	650	0.7	4,726	4.9	4,076	4.2	1.6	37	36,186
2002	95	0.1	5,402	5.2	5,307	5.1	-0.1	34	36,359



ECONOMIC FORECASTS

MAIN ECONOMIC INDICATORS AND FORECASTS

	Real GNP %	Inflation Rate %	Balance of Payments % GNP	Unemployment Level (‘000)	Rate %	Exchequer Balance % GNP	Debt/GDP (M’tricht) %
1996	7.8	1.6	3.1	179	11.9	-1.1	74
1997	9.7	1.4	2.8	159	10.3	-0.5	65
1998	7.9	2.4	0.9	125	7.6	1.4	55
1999	8.9	1.6	0.3	96	5.6	2.0	49
2000	10.2	5.6	-0.4	76	4.3	3.5	39
2001	3.8	4.9	-0.8	71	3.9	0.7	37
2002	0.1	4.6	-0.9	82	4.4	0.1	34
2003 (f)	2.8	3.7	-2.5	88	4.7	-1.9	34
2004 (f)	3.8	2.5	-1.7	93	4.8	-2.5	34

NATIONAL ACCOUNTS FORECASTS (% Change Volume)

Expenditure Basis	2000	2001	2002	2003 (f)	2004 (f)
Private Consumption	8.5	5.5	2.7	2.5	3.5
Government Consumption	7.4	11.1	9.4	2.2	2.0
Fixed Investment	6.8	0.1	1.7	-6.0	2.0
Domestic Expenditure	7.9	5.0	3.5	0.4	2.9
Stocks (GNP Contribution)	0.7	-0.5	-0.6	0.4	0.0
Exports	20.6	8.3	6.2	-6.0	4.5
Final Demand	14.9	6.6	4.8	-3.1	3.8
Imports	21.3	6.5	2.3	-8.0	3.5
GDP	10.1	6.2	6.9	2.0	4.0
Net Factor Income	9.2	19.6	40.9	-1.1	4.8
GNP	10.2	3.8	0.1	2.8	3.8

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