# Economic Insights

GLOBAL STRATEGY GROUP

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## Executive summary

KPMG is pleased to publish the second in a series of insight papers looking specifically at Ireland's economy. For a second year the Covid-19 pandemic has wrought unprecedented changes in the ways we live and work, and devastating consequences around the world for employment, incomes, and businesses.

In the article to follow, we review the underlying structure of Ireland's economy. We have much to be optimistic about as we move out of the crisis and into the recovery years of 2021-23.

The second half of 2021 (H2 2021) is seeing the beginning of a major recovery in domestic consumption. Ireland will continue to punch well above its weight in attracting FDI, and government spending will begin the descent from its pandemic heights whilst underpinning efforts to return young people to work, reduce emissions, and future-proof the economy.  Exports, a lifeline throughout the pandemic, will continue to provide ballast to the Irish economy as ICT and pharma drive record numbers.

## Headline Statistics

**+8.8%** growth in GDP in 2021

**~60%** debt to GDP ratio expected in 2021. Decrease to 58.1% in 2023

**+2.6%** growth in Modified Domestic Demand in 2021

**+~8%** average annual growth in government capital expenditure in 2022-2025

**€62 bn** tax revenue expected to be received in 2021 (~8% increase on 2019)

**-2%** change in exports, Jan-July 2020 v Jan-July 2021

**16.3%** unemployment rate at end-2021

**€12 bn** pent up spending

# Personal Consumption

### CONSUMPTION GROWING AS RECOVERY MATERIALISES

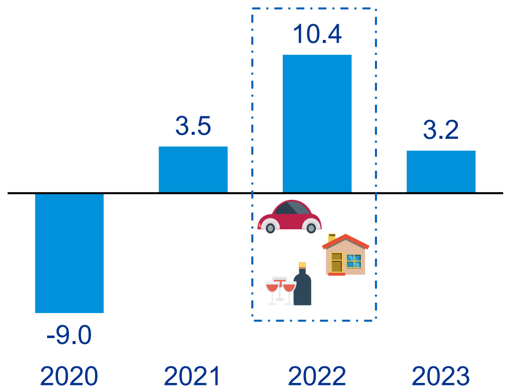
Having tightened spending substantially in 2020, Irish households have additional savings of €12bn, much of which we expect to be spent in H2 2021 and early 2022, as restrictions are removed in October and as consumer confidence returns - barring any major new Covid-19 variants or spikes.

High-cost items like cars, furniture, and home improvements are already benefiting from the spree, and the huge pent-up demand for socialising began to be unleashed, injecting much-needed activity into retail, transport, and hospitality. Challenges into the summer around international travel meant that many Irish holidaymakers chose the staycation over the airport, further boosting consumption in tourism-related industries, with knock-on effects for Ireland's emissions.

The main challenge to the consumption recovery is youth unemployment. Around 17% of 15-24 year olds are not in employment and this will inevitably act as a drag on the recovery since they are generally higher spenders on social consumption. Longer-term growth in consumption will depend on getting this group back to work and we expect the state to prioritise this as signalled in its New Economic Recovery Plan.

Additionally, the removal of Covid restrictions in October will provide young people with greater opportunities to work and to fund further education.

CONSUMPTION OF GOODS AND SERVICES, Y-O-Y %, 2020-2023




**— ~17%** of 15-24 year olds not in employment

**+ €12bn** pent up spending

# Total Investment

### INVESTMENT ON THE VERGE OF SIGNIFICANT GROWTH

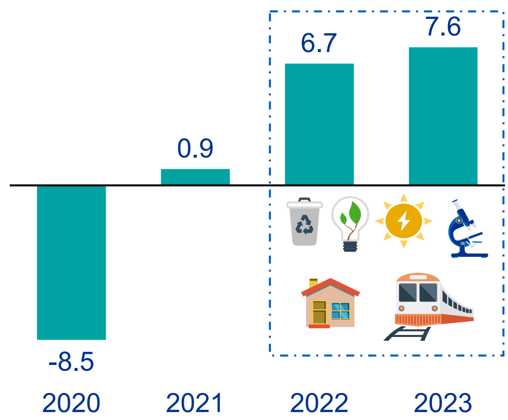
Ireland continues to be a FDI success story and the national focus on that status can be expected as global FDI flows return to pre-pandemic levels. However, investment will take longer to bounce back from the 2020 shock than consumption, with anticipated growth of only around 1% in 2021, rising to a healthier 7% in 2022. Such improvements as are made will come from housing and infrastructure.

Ongoing ambiguities related to Brexit's implementation continue to complicate the picture for multinationals making investment decisions, along with renewed pressure from the OECD to reform corporation tax rates.

The IDA has announced a strategic target of increasing the number of FDI firms in Ireland by 20% by 2024, via supportive measures such as targeted funding for pharma and med tech investment, strategic property and site solutions for MNCs, and a focus on training and upskilling.

For longer-term recovery as competition for FDI heats up through 2021 and into 2022, it will be critical for Ireland to keep a laser focus on its competitiveness in areas such as digitisation, disruptive technology, and the future of work, as well as fend off challenges over its corporation tax rate.

INVESTMENT IN THE IRISH ECONOMY, Y-O-Y %, 2020-2023




**+ ~7% growth** in investment in 2022

**+ 50,000 jobs** to be supported through 800 investments in 2021-24

*Sources: Department of Finance (April 2021, June 2021, July 2021), CSO (July 2021)*

# Government

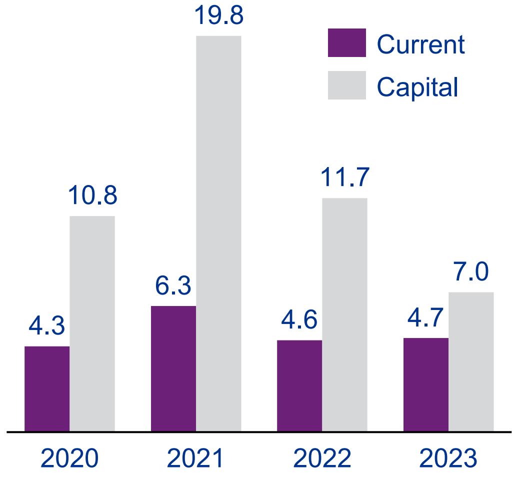
## GOVERNMENT STEPPED IN TO CUSHION PANDEMIC IMPACT

Government spending ballooned in 2020 as governments around the world scrambled to deploy life support systems for industries and individuals. In the Irish context, this effect was especially large relative to euro area neighbours, amounting to ~€38bn in support over 2020 and 2021, resulting in a substantial deficit in both years. Excepting new Covid-19 spikes, those revenue life support systems have been largely phased out as of Autumn 2021, but strategic capital spending will continue to underpin the recovery. A total of ~€11bn has been announced in capital projects for 2021, with major cash injections from the EU's Covid-19 recovery fund as well as the Brexit fund adding to government options.

According to the Summer Economic Statement, 2022-25 will see core capex grow by over 8% on average, and Budget 2022 projects a €1.1 billion rise in capital investment. Policymakers have choices about how to spend these funds to best effect and the Recovery Plan, targets infrastructure, job creation and green initiatives. Specific projects in the Recovery Plan include retrofitting, rail investment in Cork, and rural and science investment.

Beyond 2021, the government faces pressure to reduce the deficit and public debt to sustainable levels and stave off concerns about creditworthiness in an inflationary environment, making additional revenue-raising measures more likely.

GOVERNMENT SPENDING, Y-O-Y %, 2020-2023




+ **€38bn** spent on Covid-19 supports in 2020-21

+ **~8%** annual average growth in capital expenditure is expected in 2022-25

# Exports

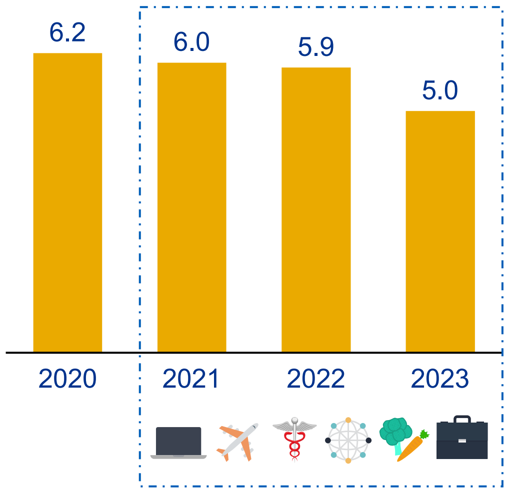
## IRELAND'S EXPORTS CONTINUE TO GROW

Ireland's exports have remained buoyant during the pandemic, doing much to offset difficulties elsewhere in the economy. This has been driven primarily by MNC pharma and medical goods as well as ICT, which will continue to be the main drivers of growth this decade. Exports reached €124 billion in the fourth quarter of 2020, the highest level on record, though this has masked serious difficulties for particular sectors such as tourism and transport which saw simultaneous falls of ~70%.

As ever, the relationship with the UK economy looms large. Trade flows with the UK fell in H1 2021 but are rising as the UK picture improves. Trade with NI is at an all-time high due to Brexit, though the impact of border controls has yet to be realised.

There is scope for diversification of Ireland's export markets, with Enterprise Ireland (EI) encouraging exporters to look at markets such as Japan, South Korea, and Mexico. EI is also targeting an increase in the share of exporters led by women, as well as decarbonisation and increasing the number of SMEs that are digital exporters.

EXPORTS FROM THE IRISH ECONOMY, Y-O-Y %, 2020-2023

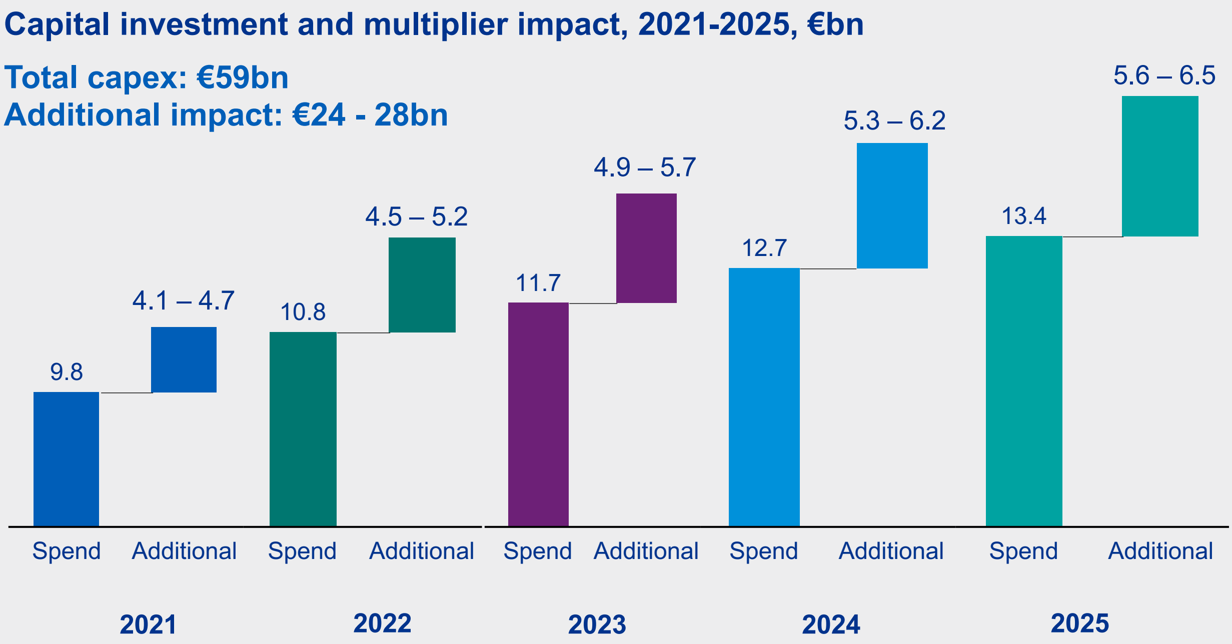



− **~70%** fall recorded in tourism and transport in 2020

+ **€124bn** reached in exports in Q4 2020

*Sources: Department of Finance (April 2021, June 2021, July 2021), CSO (July 2021)*

# Food for thought: investing to recover




**Additional impacts may arise in sectors across infrastructure, construction, transport and warehousing, utilities, professional services, communications, amongst others.*

Assuming no major resurgence of the pandemic, Ireland can be confident of a strong recovery. But wisely targeted investment can still ensure a steeper climb back to pre-pandemic levels and a more resilient post-pandemic outlook. Policymakers have a range of options at hand for investing in the recovery. Project Ireland 2040 set out the 10-year capital envelope for the period 2018-2027, starting from a baseline of €4.6 billion capital investment in 2017. The starting point for the capital envelope for the 10-year period 2021-2030 is significantly different, with planned core capital investment of €9.8 billion for 2021.

We reviewed the potential multiplier impact of this spend, estimating the additional contribution it can bring about in the period 2021-25. The total indirect output to be created is in a range of ~€24-28 billion. This additional impact from the State's capital programme will be vital to the domestic economy's growth over the coming years. With the recently launched National Development Plan setting out an ambitious investment plan, the sod on many projects will be turned in 2022.

# Get in touch

**LEADING STRATEGY AND ECONOMIC ADVISORS.**
Our Strategy team works with public and private sector clients across industries to adapt to change and to create value. Developing coherent and robust strategies at a time like this is vital. We specialise in business planning support, in particular in deal and growth strategy, enterprise wide transformation and operational excellence, impact modelling, and econometrics.

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