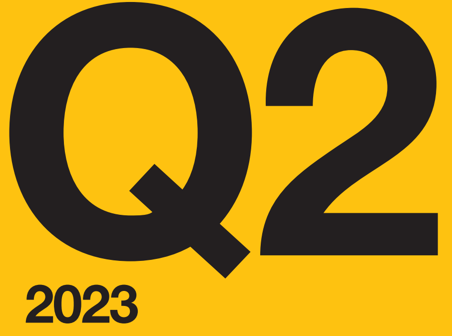

Ibec Quarterly Economic Outlook

Nearing the peak

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The Irish economy has continued to perform remarkably during a period of rising interest rates and inflation globally. Almost all recent indicators of performance have shown an economy outperforming its peers. Whilst the pipeline of investment and demand remains relatively strong, there is also an increasing sense that we may be entering a period of more moderate growth. Over the coming year the economy will experience a mix of natural slowdown following bounce back demand in 2022, the lagged impact of rapid interest rate hikes, the gradual withdrawal of fiscal supports and vulnerabilities in some major trading partners. Whilst the massive volatility of recent years of lockdowns, supply chain crises and inflation will soon be behind us, all the challenges above will contribute to a softening of the macroeconomic environment.

We are now nearing the peak of the economic cycle. In these periods it is crucial to be cognisant of our vulnerabilities. Already costs are a more prominent concern for businesses than in recent years. There are also signs of ongoing caution from households despite strong buffers for some. Government should also be more aware of fiscal concentration, despite significant surpluses. It is important that we do not build top-of-cycle assumptions into either Government or business decision making.

Key indicators

Annual % change	2022	2023	2024
Consumer spending	9.4	4.2	4.0
Domestic Investment	16.7	2.7	5.7
Domestic Demand	11.6	3.4	2.3
Exports	13.9	5.2	4.0
Imports	15.9	6.3	4.0
GDP	9.4	3.2	3.3
Inflation (annual average %)	7.8	4.8	2.3
Unemployment rate (annual average %)	4.5	4.1	3.7

Economic growth

Economic overview

The global economy has proven resilient to high inflation and consequently higher interest rates. This is in line with our expectations in our Q1 Economic Outlook that the ingredients were in place for stronger than expected growth in the US and that a prolonged recession in Europe was unlikely. We are now beyond a period of significant volatility, with global supply chain disruptions, volatile energy prices and inflation now well on the path to more normal levels. However, there are still some concerns in major trading partners. Whilst the US economic performance looks very robust, major trading partners such as the UK, Germany and China are of greater concern. All have material economic vulnerabilities due to rising interest rates and weak domestic demand which may persist through 2023 and 2024. This growth slowdown is not unexpected given the ongoing withdrawal of record fiscal support and the lagged impact from the fastest increase in interest rates since the 1970s. However, it does leave global growth over the coming years quite fragile. For the Irish economy, our recent outperformance is unlikely to continue indefinitely. It is our view that over the coming 18 months we will begin to see some moderation in the rate of growth in the economy. We expect the domestic economy to grow by 3.4% in 2023, in line with previous expectations. However, for 2024 we now expect growth of around 2.3%, resulting from a normalisation of investment levels and some slowdown in the growth of consumer spending.

Signs of moderation

In the past number of months headline data on the Irish economy has suggested both an economy at overcapacity and one in a technical recession (as measured by GDP). However, the variance in headline numbers is quite simply a reflection of an Irish economy where exports, output and thus GDP are both highly globalised and concentrated in a small number of companies. The most reliable data on the overall trend in the Irish economy comes from the labour market. In the year-to-date employment growth has been strong – up 4% annually, or 101,000 workers in Q1. However, some forward looking indicators are now suggesting that we may be seeing some slowdown in the pace of expansion. Administrative data on payroll employees suggests hiring has slowed somewhat from 5% annually at the start of the year, toward 2.5%. At the same time several sources on new job postings have shown a slowdown following a post Covid surge in 2022. Job vacancy data numbers in Q1 (22,800), though elevated (were 15,000 in Q1 2019), are now falling back to more normal levels (from 27,000 in Q1 2022). In the export driven FDI sector, IDA half year results showed a total of 12,000 new job announcements. This is a significant levelling off relative to the post-Covid bounce in H1 2022 where 18,000 jobs were announced and remains marginally below both H1 2021 (12,500) and 2019 (13,500). All this together suggests a mix of normalisation following a post-Covid rush in hiring in 2022 and a gradual levelling off due to frustrated hiring and reassessment of hiring plans in some sectors.

Exports

Irish goods exports have seen some weakness in the first half of 2023. Pharmaceutical exports are down €3.6 billion, or 6% annually. Whilst there has also been a fall of €1.8 billion or 18% in the export of electrical machinery and equipment – driven by falls in exports of integrated circuits and processors. In both cases, investment drivers in the sectors remain strong, with fluctuations in exports representing an unwinding of Covid induced supply chain pressures. Both remain well ahead of their export levels pre-2022. Excluding the volatility in those two sectors, exports have increased by 3%. The performance of food and medical device exports have been particularly strong. Whilst the implementation of UK border controls from October 2023 will have an impact on exporters to the UK, there remains a sense that most companies are well prepared, though the cost implications of additional administration and delays will be challenging. With major investments underway across several FDI driven sectors, particularly the life sciences sector, we expect exports will recover well from this period of unwinding and continue to grow in both 2023 and 2024 by 5.2% and 4.0% respectively.

Figure 1: GDP growth 2023, %

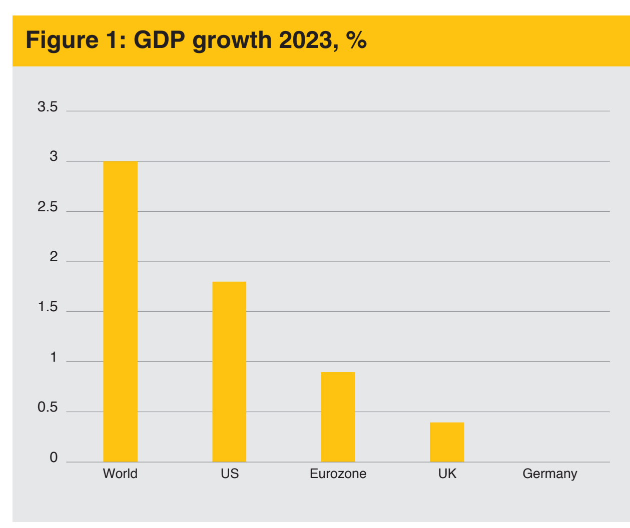


Figure 2: IDA half year job announcements

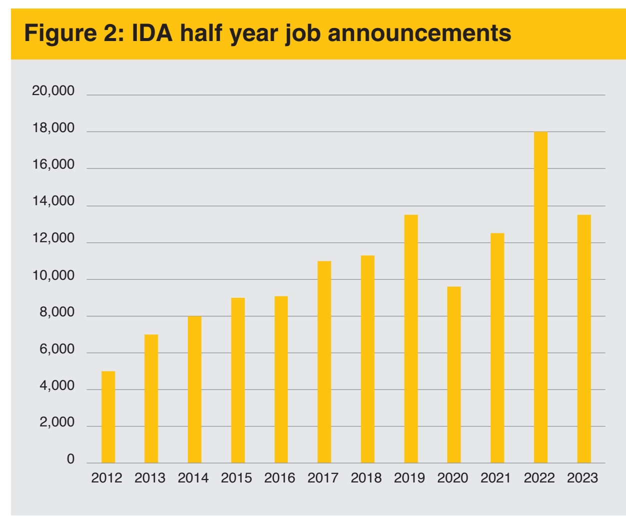
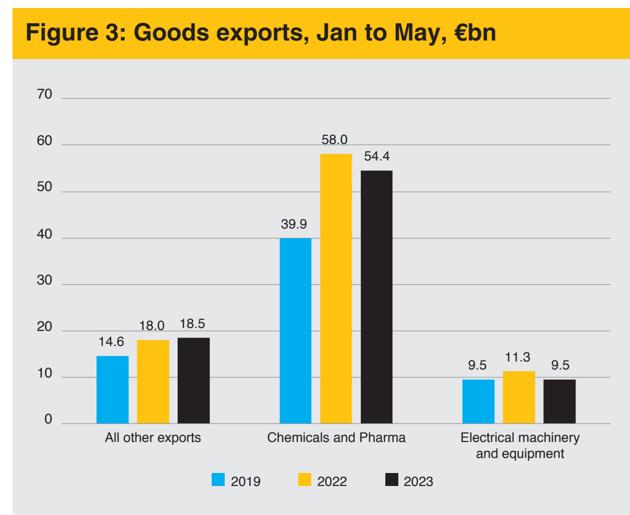


Figure 3: Goods exports, Jan to May, €bn



Domestic demand

Consumer spending

Consumer spending in the first half of the year was somewhat subdued. Sluggish retail sales volumes, up 1.1% annually in the first six months of the year, were offset by a rapid bounce back in spending in the Experience Economy – with accommodation up 12% annually and food services up 30% on the same period in 2022. This activity, to some extent, reflects changing consumption patterns relative to a period where the Covid pandemic remained an influence on consumer behaviour. Overall consumer spending was up almost 5% on a year earlier in Q1 in nominal terms, but down marginally when adjusted for inflation. A similar pattern emerges in data from credit and debit cards – where spending has risen around 11% in the year to March, falling to 4% after inflation is considered. This compares to inflation adjusted growth which ran at around 8% in 2018 and 2019. As 2023 progresses there are several trends which should support growth in consumer spending. Employment will continue to rise, albeit at a more moderate pace. More importantly wage growth will again begin to rise in real terms (after accounting for inflation) in the second half of 2023 and into 2024. This will be offset somewhat by the lagged impact of rising interest rates and rents for some households. We expect that overall consumer spending will grow by 4.2%, a modest upgrade on our Q1 forecast of 3.5%. However, we expect to see some further slowdown in the growth of consumer spending in 2024 toward 4%, with improvements in real incomes offset by a less rapid expansion in employment, the withdrawal of fiscal supports and the lagged impact of rising interest rates.

Inflation

HICP inflation (which excludes mortgage interest payments) in July fell to 4.6%. This is in line with our expectations that overall inflation will fall well below 4% by the end of 2023 and average around 2.5% in 2024. The unwinding of supply chain costs, normalisation of energy wholesale markets and falling commodity prices globally should all result in sustained price normalisation in the second half of the year. This fall in inflation does, however, come at the cost of sustained demand destruction, with the European Central Bank recently increasing the refinancing rate from near zero to a level of 4.25%. It is expected that the ECB will bring in another quarter point hike in September, if data doesn't improve materially before then. However, there is a growing sense we are reaching the peak of the rate hike cycle, with late 2023 and early 2024 likely to see a pause on rising rates. For the Irish economy, the lag in the full impact of these hikes on the domestic economy will only begin to be felt over the coming 24 months as fixed rate mortgages (which are dominant in the market) begin to renew at elevated rates. This will act as a break on demand from certain consumer cohorts for some time. We expect full year inflation for 2023 to run at 4.8% and at 2.3% in 2024. There is now a greater risk that the ECB will overshoot and hikes rates too high than there is of persistent high inflation.

Investment

Ireland has undergone a boom in industrial equipment investment in the past year. The total value of imports of machinery and equipment into Ireland in the 12-month period to April 2024 rose to €50 billion, up from a pandemic low of €33 billion during 2020 and €40 billion annually in 2019. Imports of industrial equipment are now running at 2.5 times the rate they were during the Celtic Tiger. The most recent increase has been driven by an increase in imports of electronic integrated circuits and other items related to semiconductor manufacturing. These imports have increased from an annual run rate of around €1 billion a year in the past decade, to over €9 billion annually in the past 12-months. Whilst some of these investment levels are linked to one-off investments and may normalise in the coming year, we still expect that a strong pipeline of investment will continue to contribute to growth in 2023 and 2024. The normalisation of investment levels this year will slow domestic investment growth to 2.7% in 2023, before rebounding to more normal levels of 5.7% in 2024.

Figure 4: Total spending on Irish cards, % annual 3-mma

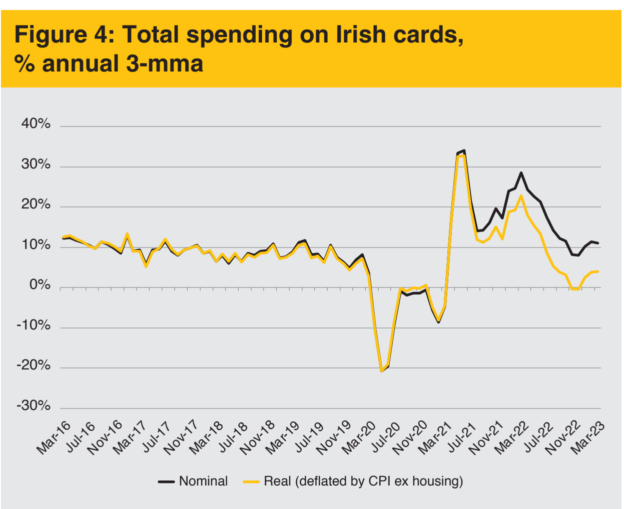


Figure 5: Inflation forecast, annual %

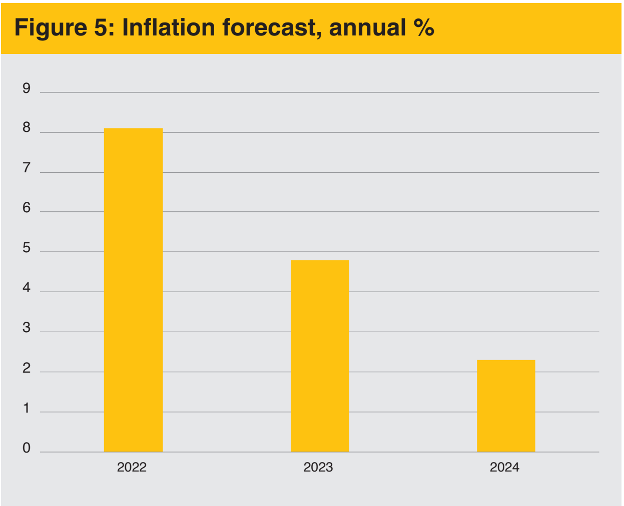
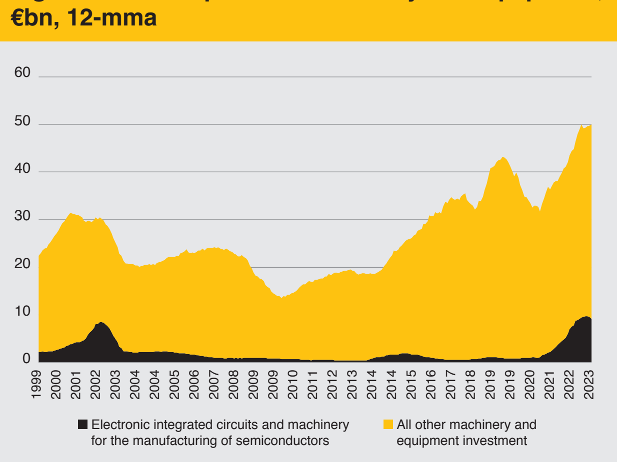


Figure 6: Irish imports of machinery and equipment, €bn, 12-mma



Labour market

Labour market overview

Employment growth has slowed over recent months, as it becomes increasingly difficult to recruit despite high demand. The total labour force continues to grow along with employment, with an additional 86,600 entering the labour force over the past year. While a record low unemployment rate of 3.8% indicates an economy at full employment and now struggling to meet labour demand, a fifth of those working part-time, more than 500,000 people, are underemployed and would prefer to work more hours. In terms of available additional labour, two-thirds of those who would like to work but are unable to do so cite caring obligations or disability or illness as the main barriers. At a time of full employment and growing pressure in the labour market, ensuring the country has the labour it needs to sustain growth will require improved workplace accessibility, child and elder-care supports, and supports for workers with disabilities. Both the underemployment figures and numbers facing barriers to work indicate there is still scope to increase labour supply within the existing population if the correct policy approach is taken.

Unemployment

As of June 2023 there were 159,000 people remaining on the Live Register, excluding some refugees who are eligible for Live Register schemes. Within that number, Live Registrants are roughly evenly split between men and women, with women overrepresented among those who are 'underemployed (i.e working but at sufficiently low hours and income to be eligible for Live Register schemes). About 14% of those on the Live Register are working casually or part-time. One third of those on the Live Register are long-term unemployed, a number that is falling, while the majority are made up of the short-term unemployed. About one fifth are on a labour market activation scheme, including Community Employment, back to education allowances or SOLAS training schemes. Of these, Community Employment and SOLAS training have seen the most uptake, accounting for 69% of all those on activation schemes.

Figure 7: Numbers in labour force and employment, '000s

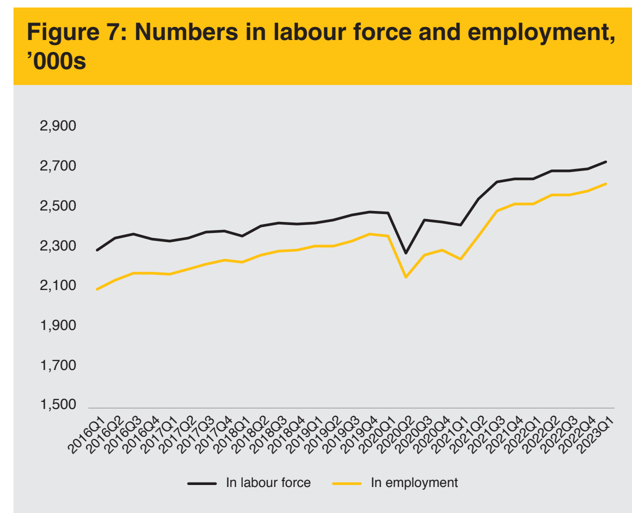


Figure 8: Numbers in labour market activation programmes

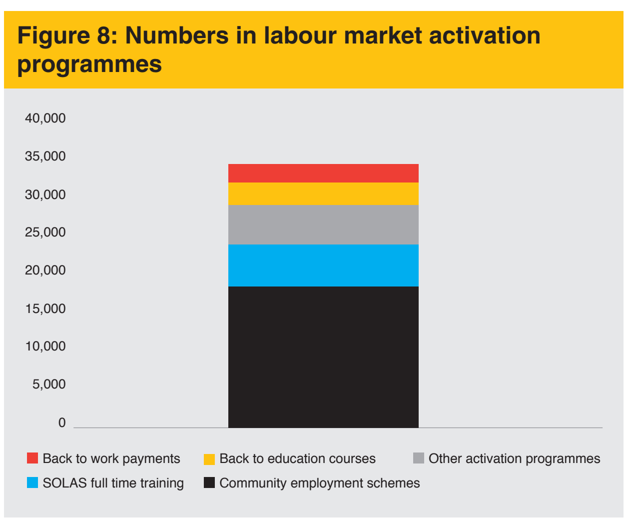


Table 1: Employment, 000s annual average

	2022	2023	2024
Agriculture	**101**	**101**	**100**
Industry & Construction	**487**	**498**	**516**
Services	**1,949**	**1,997**	**2,045**
Total	**2,547**	**2,596**	**2,661**
Unemployment rate (annual average %)	**4.5%**	**4.5%**	**4.3%**

Source: Ibec forecasts

Labour market

Sectoral Employment

While employment growth has continued broadly across sectors over the year so far, it is at a slower pace as available slack in the labour market diminishes. Demand for key skills remains high, with job churn and competition for existing employees ongoing. The total number of PAYE employees has grown by 2.5% annually, and at a more moderate 0.4% between April and May as the hiring boom of the past two years slows. The financial, insurance and real estate, transport and professional and scientific sectors are seeing the fastest growth both annually and month-on-month, with monthly growth in employment in the range of 1.3% for these sectors. There have been marginal reductions in PAYE employees within the ICT, construction and health sectors over the past month, but employment in all three sectors remains above levels seen a year ago. Overall we expect continued growth in employment across all sectors over the coming year, albeit more modestly than in the recent past.

Sectoral remote work

Rather than reversing, rates of remote work have increased marginally over recent months, with the proportion of people working remotely mostly or some of the time up by 2% since last Autumn. Much of that increase is driven by increased numbers in the public sector working remotely, now accounting for about half of workers in the sector. This is along with marginal increases among sectors like ICT, finance and insurance and professional and scientific services, which have all seen rates of remote working in the range of 60-80%. Trends in remote working appear to be stabilising at a relatively high level over time, indicating that the move to remote working post-pandemic is here to stay. A tight labour market and ongoing competition for skills is affecting not just wages but also working conditions, which is contributing to the embedding of remote work in certain sectors. 21% of Irish workers work mostly from home, compared to 13.5% across the EU in 2021, when pandemic pressures on remote work were at their height. This continued strong performance of remote work will have significant implications across sectors in both the location of economic activity and the demands for different types of investment in the years to come.

Regional remote work

Rates of remote working remain high across the country, with a third of people working mostly or sometimes at home in the first quarter of the year. Regionally, remote working rates are highest in the East and Midlands, with 42% of workers in Dublin working remotely some or all of the time, and a third of workers in the Dublin commuter belt. Regional variation in rates of remote working reflects compositional differences in employment across the island, with the regions with a higher concentration of office based services predictably having higher rates of remote workers. Regions with a higher proportion of employment in industry and agri-food report lower rates, with the West and Border regions showing just 29%, and 21% of workers remotely working respectively. Pressures on housing are likely also a factor, with demand for remote working higher in regions with the biggest shortages and highest rent-to-income ratios.

Figure 9: Annual and monthly change in number of employees by sector, %

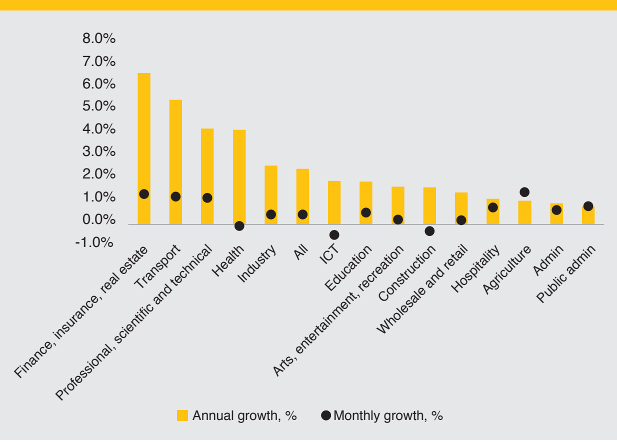


Figure 10: % of employees working remotely by sector

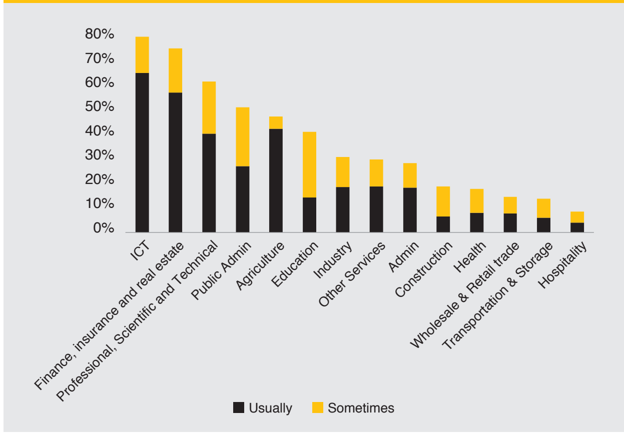
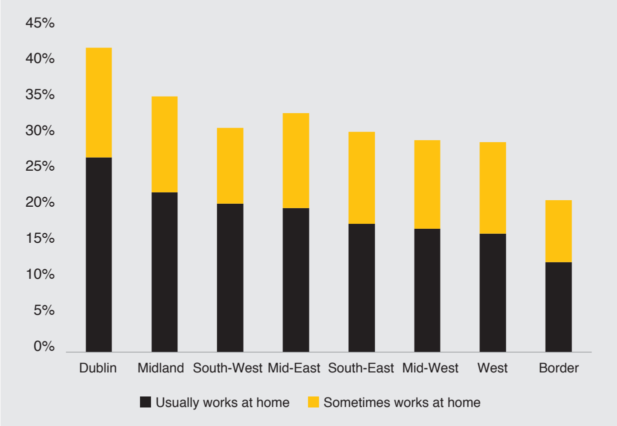


Figure 11: Proportion of employees working remotely by region, %



Regulated labour costs

Context for labour cost increases
Regulated labour costs will continue to grow across the economy in the coming years. The most significant of these changes are the introduction of the Living Wage and pensions autoenrollment – both of which are due to be introduced in 2024.

The Programme for Government gave a commitment to “Progress to a Living Wage over the lifetime of the Government” and “to gradually deliver an automatic enrolment scheme”. These have been progressed over recent years with the Final Design Principles paper for autoenrollment launched in March 2022 and a request for a recommendation on the introduction of the Living Wage from the Low Pay Commission (LPC) in Jan 2021.

At the time of its introduction in 2022 the Department of Enterprise, Trade and Employment (DETE) estimated that a national Living Wage set at 60% of hourly median wages would equate to approximately €13.10/hour, by 2026 this threshold would amount to around €15/hour. Meanwhile pensions autoenrollment will add 1.5% to the employer contributions for enrolled employees in year 1, rising to 3% by year 3.

What will be the impact on labour costs?
Other measures have recently been implemented or are also in the pipeline which will add to business costs. These include Statutory Sick Pay, Pensions PRSI as outlined in Commission on Pensions and various other leaves (parents leave, etc.)

Ibec estimates across sectors show across the whole economy these measures, along with the Living Wage and autoenrollment, would add 4.7% to the wage bill by 2026 and 9% by 2030. For some sectors, with low pensions coverage and high Living Wage levels, these costs may be significantly higher, with costs by 2026 and 2030 respectively adding 13% and 17% to the wage bill in the Experience Economy and between 7% and 12% by 2026 and 2030 in sectors such as retail, wholesale and administrative activities. For many companies in low margin sectors, changes of this magnitude will prove a substantial challenge to ongoing profitability and other investments.

This is before allowing for other new measures which may add directly to the cost burden if implemented or have added indirectly through administrative and ancillary costs, such as:

- The proposed Pay-Related Jobseeker’s Benefit Scheme or any future entitlements.
- The European Union (Transparent and Predictable Working Conditions) Regulations 2022
- Work Life Balance and Miscellaneous Provisions Act 2023
- Gender Pay Gap Information Act 2021
- Protected Disclosures (Amendment) Act 2022
- EU Directive on Pay Transparency
- The Central Bank (Individual Accountability Framework) Act 2023

What is the Ibec ask of Government?
In its 2022 report on the introduction of the Living Wage the LPC recommended that:

“…consideration should be given to the introduction of an economy-wide enterprise support scheme to support eligible businesses in the transition to a Living Wage. Such a scheme, based on the proportion of low wage workers in a firm’s wage bill, could provide a temporary subsidy to qualifying employers.”

Ibec has engaged with Ministers, with the Low Pay Commission, with the Civil Service and across the political spectrum in recent months to raise the issues around the cost implications of these changes, around business concerns about the uncoordinated nature of their introduction and to ensure the recommended cost supports are now put in place in Budget 2024.

In our 2024 Budget submission, we have identified that these supports should include increasing the top-rate employer PRSI threshold above the new Living Wage annually and the introduction of a temporary PRSI credit for employers of lower earning workers, relative to the increases in weekly labour costs which will occur in 2024, 2025 and 2026.

The Government must also produce a clear roadmap on other tax (PRSI, USC, IT) and social welfare (Working Family Payment, Housing Assistance Payment, SUSI grants, childcare subsidies, etc) to ensure that the introduction of the Living Wage does not lead to high marginal effective tax rates for workers and consequently impact on incentives to work.

Fiscal stance

Capital investment

A recent analysis by the Irish Fiscal Advisory Council (IFAC) shows that because of higher inflation and lower nominal spending, real capital spending in the NDP between 2021 and 2025 is now due to be 24% lower than had been planned. In fact, even with recent announcements of additional capital expenditure in the Summer Economic Statement the level of ambition for core Government capital expenditure between 2021 and 2026 has fallen from 4.9% to 4.4% of national income, with ongoing falls beyond that. Capital spending has not been indexed in the same manner as current spending. IFAC estimate almost €20 billion in additional capital spending would be needed between 2024 and 2030 to protect the existing ambition within the NDP. We see an additional need on top of this of at least €10 billion to reflect growing demands for investment in areas such as net-zero commitments which are unfunded, a more rapidly growing population than was allowed for in the National Planning Framework process, and continued deficits in infrastructure which were unaddressed by the previous NDP. In our view, this should be funded through a National Infrastructure Fund using some of the recurring surpluses which are expected over the coming years.

The scale of the surplus

Ireland is in an enviable fiscal position. The current forecasts for a budget balance of an average of nearly 4% of national income in 2024 is significantly higher than even the most well-performing developed economies (except for Norway which expects a surplus in 2024 of almost 25% of GDP). Whilst there are risks that future surpluses might not materialise, there are also significant upside risks. For example, the implementation of an OECD inspired Qualified Domestic Minimum Top-up Tax (QDMTT) from January 2024 brings upside potential for fiscal performance but with further risk of corporate tax concentration in the coming years. Revenue data for 2022 shows that the current effective corporate tax rate on profits in Ireland is 10% for multinational enterprises (10.1% for our top 10 taxpayers), this will increase closer to 15% (depending on substance based carve outs) for most of our major taxpayers from next year. As noted by the OECD impact assessment of the impact of Pillar 2 of the OECD agreement: "Broad QDMTT introduction will shift potential revenue gains from UPE jurisdictions to affiliate jurisdictions where low-tax profits are currently located". On the other hand the negative revenue impacts of Pillar 1 are unlikely to occur for several years. The best response to the impact of this potential further concentration in the tax base is to broaden the tax base elsewhere, whilst using the tax receipts wisely and concentrating increases in corporate tax on non-recurring investments.

Budget 2024

The Government in its Summer Economic Statement outlined an already sizeable increase of nearly €11 billion in tax cuts and spending increases for 2024. These include the headline Budget Day package of core Departmental spending increases of €5.2 billion along with €1.1 billion in net tax cuts. On top of this package the Government has outlined spending pressures of almost €4 billion split between a contingency for the Ukraine humanitarian crisis (€2.5 billion) and other spending (€1.5 billion) such as on schemes running into 2024 dealing with Covid, Brexit, some energy costs, and the implementation of some EU funded schemes (such as the National Recovery and Resilience Plan). The key question over the coming months is how much over and above this might be spent on further 'temporary' supports for households and businesses struggling with the rising cost of living. This in part may be funded through tax increases, such as the proceeds from windfall taxes on the energy sector which are expected to bring in between €280 and €600 million in 2024.

Figure 12: Planned capital spending versus NDP targets, % of national income

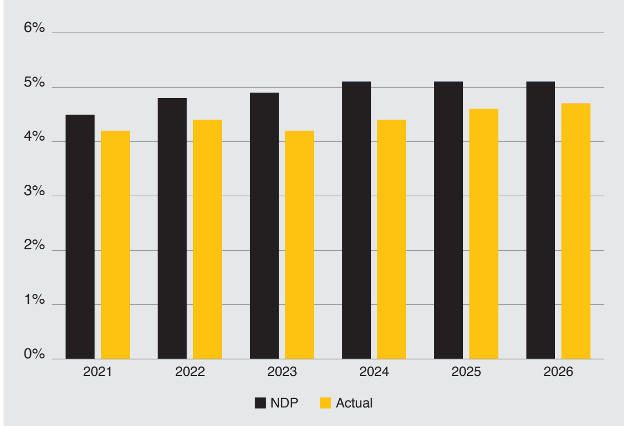


Figure 13: General Government Surplus in 2024, % of national income

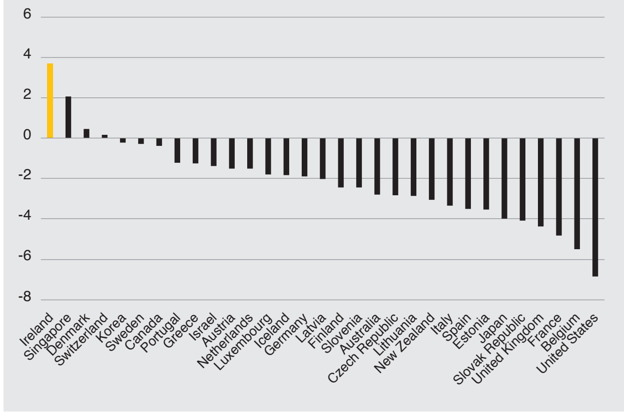
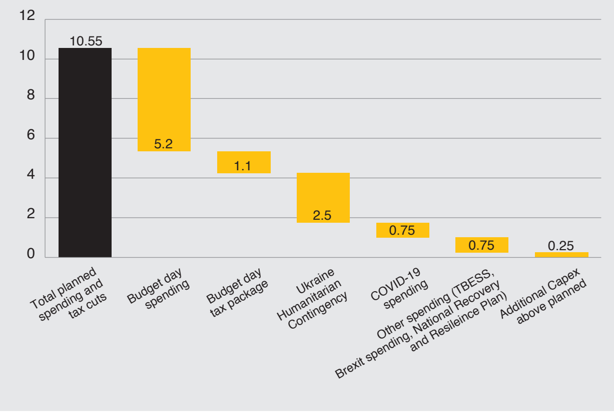


Figure 14: Distribution of planned Budget spending and tax cuts, € billion



International economies

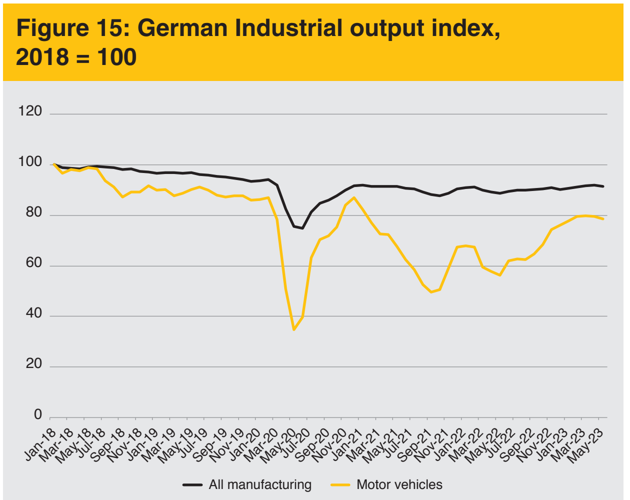
Monetary policy

In the US, the rate of inflation fell to 3% in June. US interest rates rose to 5.25%-5.5% in July and are now expected to hit their peak in the coming months before falling gradually from 2024. Despite this, demand has remained steady, with job creation still growing strongly. The prime age employment to population ratio, a good measure of labour market capacity, rose to 80.9% in June, now back above its pre-pandemic level. In the Eurozone inflation is falling, down to 5.5% in June, albeit more slowly than in other developed economies. However, most analysts expect inflation below 3% in the Eurozone by next year. Some concerns still remain about a recession in Europe, driven by a slowdown in German manufacturing and further hikes in interest rates. Significant sectors of German manufacturing have bounced back pre-pandemic (BioPharma and electronics), however others such as the large chemical and car manufacturing industries are still well below their pre pandemic norms. Forward looking indicators are also concerning. For example, the S&P Purchasing Managers Index for July showed the sharpest fall in new orders in European manufacturing since 2009. It remains our view that the challenges faced by European manufacturing mean we are more likely to see very slow growth than an outright recession this year. The July economic outlook from the IMF predicted a slowdown in Eurozone growth from 3.5% in 2022 to 0.9% in 2023.

UK

The rate of inflation in the UK stood at 7.3% in June, down from 7.9% in May. This is the result of a sharp increase in interest rates, with the Bank of England base rate now at 5%. There are opposing income and wealth effects which will drive UK consumer behaviour in 2023 and 2024. On one hand, inflation in the UK is expected to fall to 5% by the end of 2023 and 2% by the end of 2024 – giving a boost to real incomes which have stagnated for some time. On the other hand, increasing interest rates have increased the share of household income going to mortgage repayments, rising from 6% over the past decade to closer to 8% over the coming years. At the same time, house prices have begun to fall. The Nationwide House Price Index fell by 3.4% in June, with falls of up to 4.5% in more expensive parts of the South-East. With rising borrowing costs and falling mortgage drawdowns, there is a risk of a psychological 'wealth effect' where households spend less when they feel their wealth is eroding, even on unrealised capital gains like dwelling house prices.

Figure 15: German Industrial output index, 2018 = 100



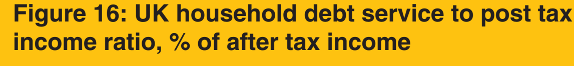


Figure 16: UK household debt service to post tax income ratio, % of after tax income

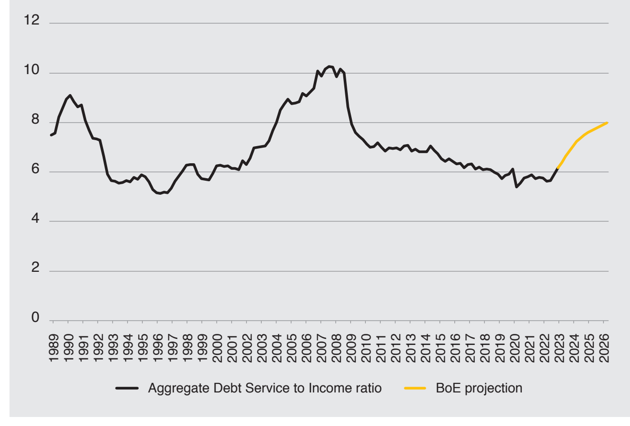


Table 2: Forecasts for global growth and inflation, 2023

	US	UK	China	Eurozone	World
GDP growth, %	1.8	0.4	5.2	0.9	3.0
Inflation, %	4.5	6.8	2.0	5.3	7.0

Source: IMF

Capacity pressures

Public sector capacity

A public sector that has not expanded to match the rapid growth in private sector activity has led to increasing pressure on state bodies, regulators, and essential personnel for the delivery of infrastructure and services. An Bord Pleanála casework statistics demonstrate the ongoing pressure building within the State's systems. While both planning appeals and total planning cases had fallen in the early part of the year, the proportion dealt with within the 18-week target has dropped to just 31% for appeals and 34% for planning applications, compared to 69% pre-pandemic. Wait-times and congestion in the courts also has a material impact on key areas like housing and conducting of commercial business, with the number of commercial, bankruptcy and probate cases increasing year-on-year. Similiar backlogs are widespread across many areas of the public sector. The country's ability to sustain economic growth is dependent on the State having the capacity to absorb the resources and investment being generated to deliver on the required infrastructure and services.

Commuting and transport

Use of public transport has increased substantially in the year so far compared to both the previous year and pre-Covid levels. Total public transport trips across all public transport types, excluding the Dublin Luas, were up 34% on their pre-Covid level, indicating both an increase general population mobility and a growing preference for public transport above other forms. As population increases, return to offices and employment growth all place growing demands on our transport infrastructure, driving growth in public transport usage. Additionally, the impact of increased fuel costs, combined with significant state subsidies of public transport have precipitated an increase in public transport trips. In contrast car journeys in Dublin fell marginally, by 2%, in the year so far compared to the same period pre-Covid, while they remain largely unchanged outside of the capital. As the low carbon transition continues and fuel costs increase, demands on our public transport system will predictably increase and will need to be provided for accordingly.

Population growth and distribution

Data released from the recent Census has highlighted not only Ireland's faster than projected population growth, but also the changing distribution of people around the country in response to economic and social factors. There is significant movement within the state, with about 26% of Irish-born residents currently living in a county other than the one they were born in. Counties within commuting distance of Dublin tend to have a higher proportion of residents who were not born in the county, with 68% of those living in Meath not born in the county and similar figures for Kildare and Wicklow. Dublin's commuter belt also tends to have the youngest population on average as the draw of employment in Dublin, along with push effects from housing shortages in the capital encourage the redistribution of the working age population into the greater Leinster region. In contrast, rural counties like Donegal, Kerry and Roscommon skew older, with the average age of Donegal residents at 40.8 years.

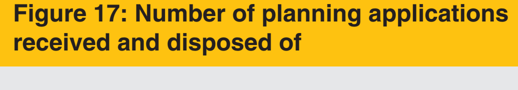


Figure 17: Number of planning applications received and disposed of

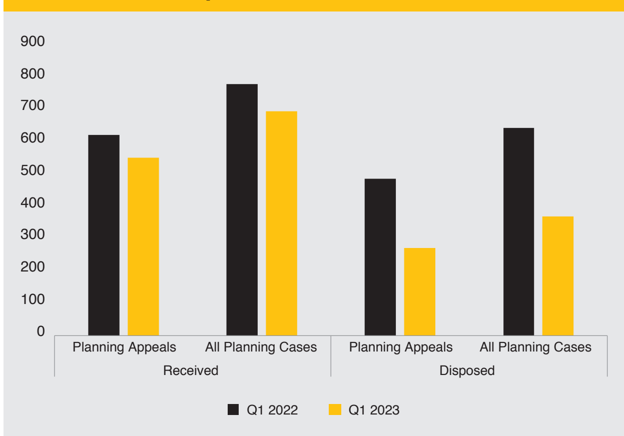


Figure 18: Public transport journeys excluding Luas in the year to date

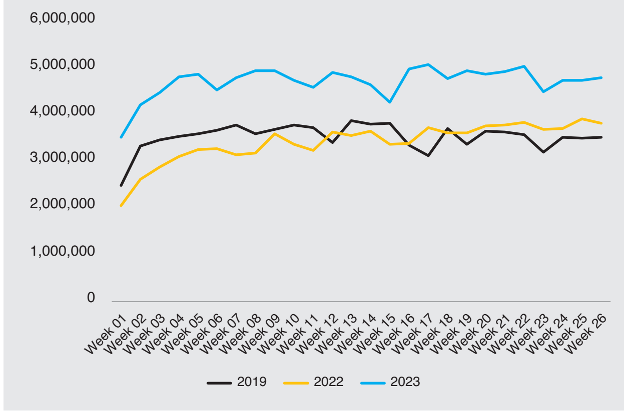
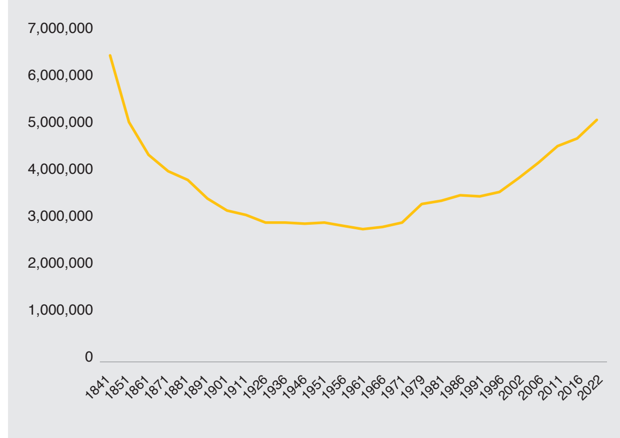


Figure 19: Population by census year



Housing and construction

Housing planning

Despite difficulties within the construction sector and rising interest rates placing pressure on financing of developments, total housing units granted planning permission were up 37.8% annually in the first quarter of the year, roughly evenly split between houses and apartments. Over the same period, the total number of planning applications granted actually fell by 29%, indicating a higher number of housing units per application and a continued shift towards multi-home developments and away from one-off homebuilding as building costs and interest rates reduce their viability. An increasingly disproportionate number of units are granted for Dublin County, accounting for two thirds of all new units which received permission and 83% of all new apartments. While additional housing is urgently needed in every region, the continued dominance of Dublin in planned units indicates the extreme shortage of rental units outside the capital is likely to continue for the foreseeable.

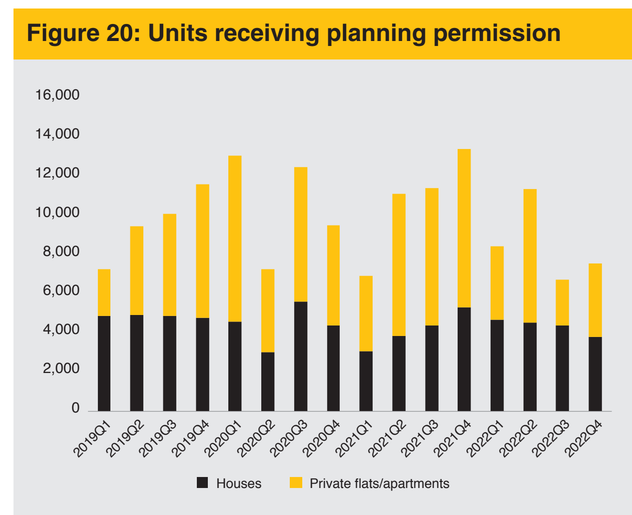


Figure 20: Units receiving planning permission

Construction output

There are growing pressures within the construction industry due to a backdrop of rising inflation and interest rates. Despite this, building and construction output saw an uptick in the early part of the year compared to a more muted 2022. The volume of total construction is up 7.5% in Q1 compared to Q4 2022 with non-residential building in particular seeing a significant bounce back. Despite this, output in both residential and commercial building remains below their pre-pandemic levels. The impact of inflation on the sector is apparent in the divergence between value and volume of production, with the value of output up 11.6% on an annual basis compared to just a 2.8% increase in volume terms. Looking to the future, the BNP Paribas June Construction PMI showed an expansion in activity for the first time in 7 months, with new orders increasing. Significant demand from households, businesses and the state are contributing to the buoyancy of the sector despite external factors.

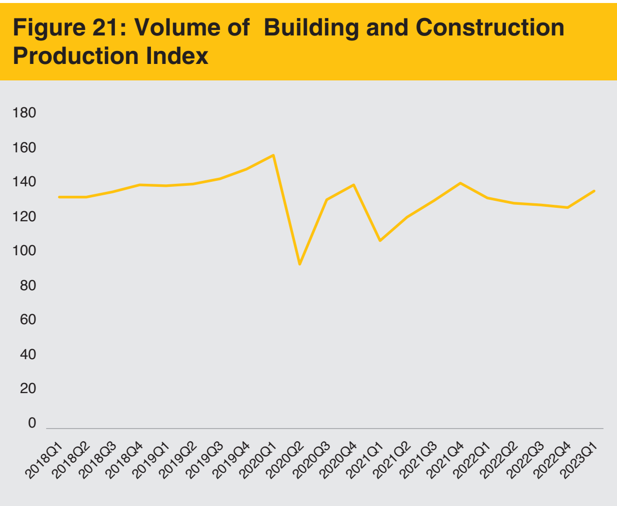


Figure 21: Volume of Building and Construction Production Index

Mortgage lending

The past year has seen the fastest and most sustained increases in interest rates in the history of the Eurozone. While rising rates naturally place pressure both on existing mortgage holders and affordability for new homebuyers, despite an average 2.7% rate for new mortgages in late 2022, both the number and total value of new mortgages in the year were up significantly versus the previous year. The number of new mortgages and value of new mortgage lending were both up by 25% annually. The volume of house buying and mortgage refinancing were also up last year as households scrambled to get ahead of expected ECB rate hikes as Irish retail banks were slower to pass on increases than their European counterparts. This window has effectively closed, with average new mortgage lending rates currently at 3.5%. Mortgage affordability is likely to weigh on new borrowing this year, although years of built-up demand continues to underpin house prices despite the worsening interest-rate environment.

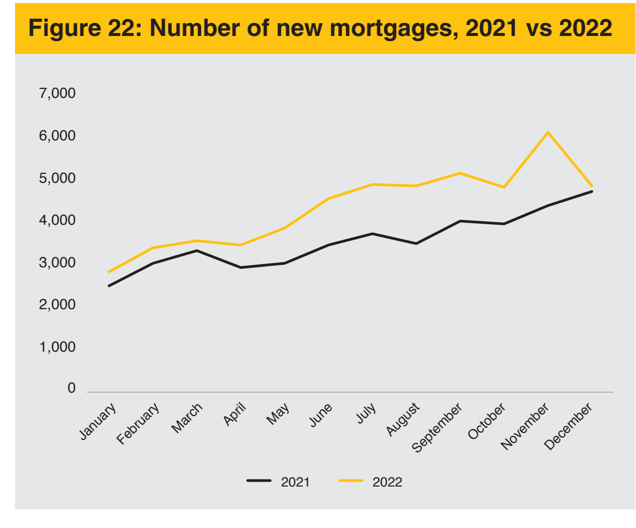


Figure 22: Number of new mortgages, 2021 vs 2022

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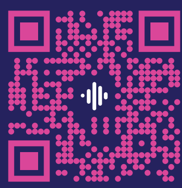

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