



The Irish Economy

**Charting the course to Irish economic
and financial stability**

May 2009

Head of Research: Eamonn Hughes

Tel: +353 1 641 9442

Email: eamonn.g.hughes@goodbody.ie

- Non-partisan call by three of Ireland's largest stockbrokers
- Scale of crisis requires a collective responsibility
- Lessons from previous crises – Sweden, Finland for example – reveal that social and political cohesion are pre-requisites for addressing the problems
- Another lesson is that with some tough medicine, countries can get through these crises
- Scale of issues is multi-faceted

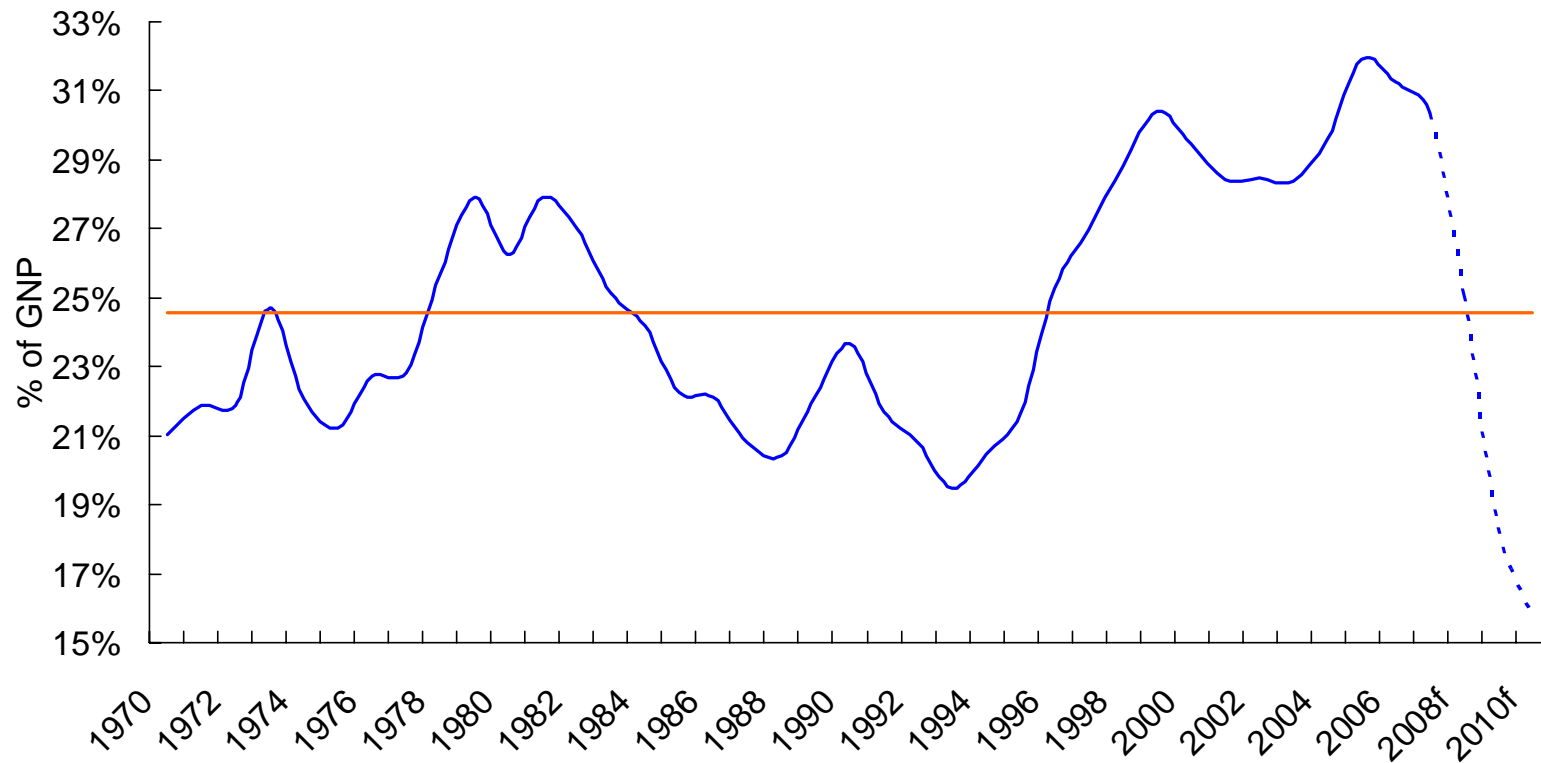
- **Resolving the fiscal crisis** – Consolidation measures of 6% of GDP have already been introduced. Five-year strategy has been laid out
- **Resolving the banking crisis** – NAMA is a welcome step along that path, although full details have yet to emerge, but are imminent
- **Economic recovery** – Still some way off, but improving competitiveness will ensure participation in an international recovery

1. General environment
2. The Public Finances & Sovereign Debt
3. Competitiveness & the Economy
4. The Banking Sector

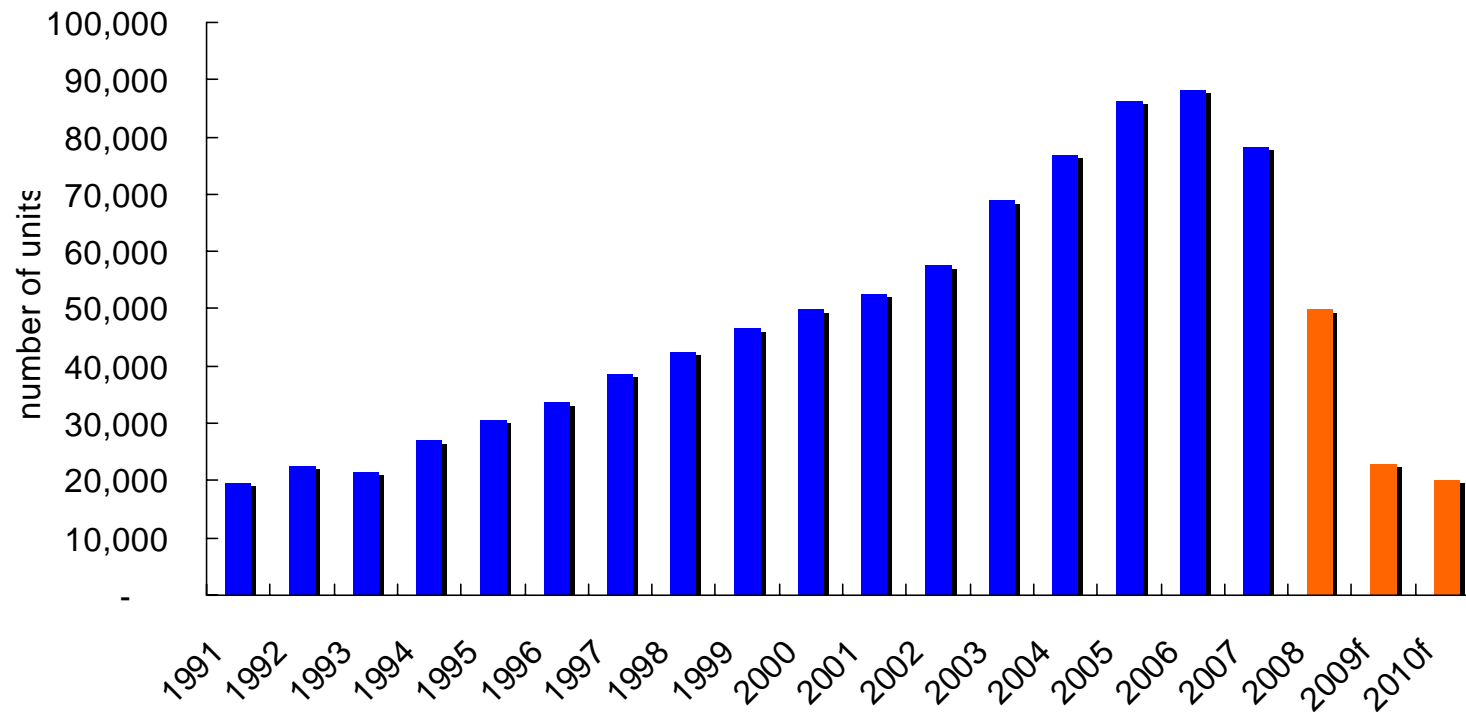
Wrong Place, Wrong Time

Ireland

Construction-led recession in Ireland - Investment as a % of GNP



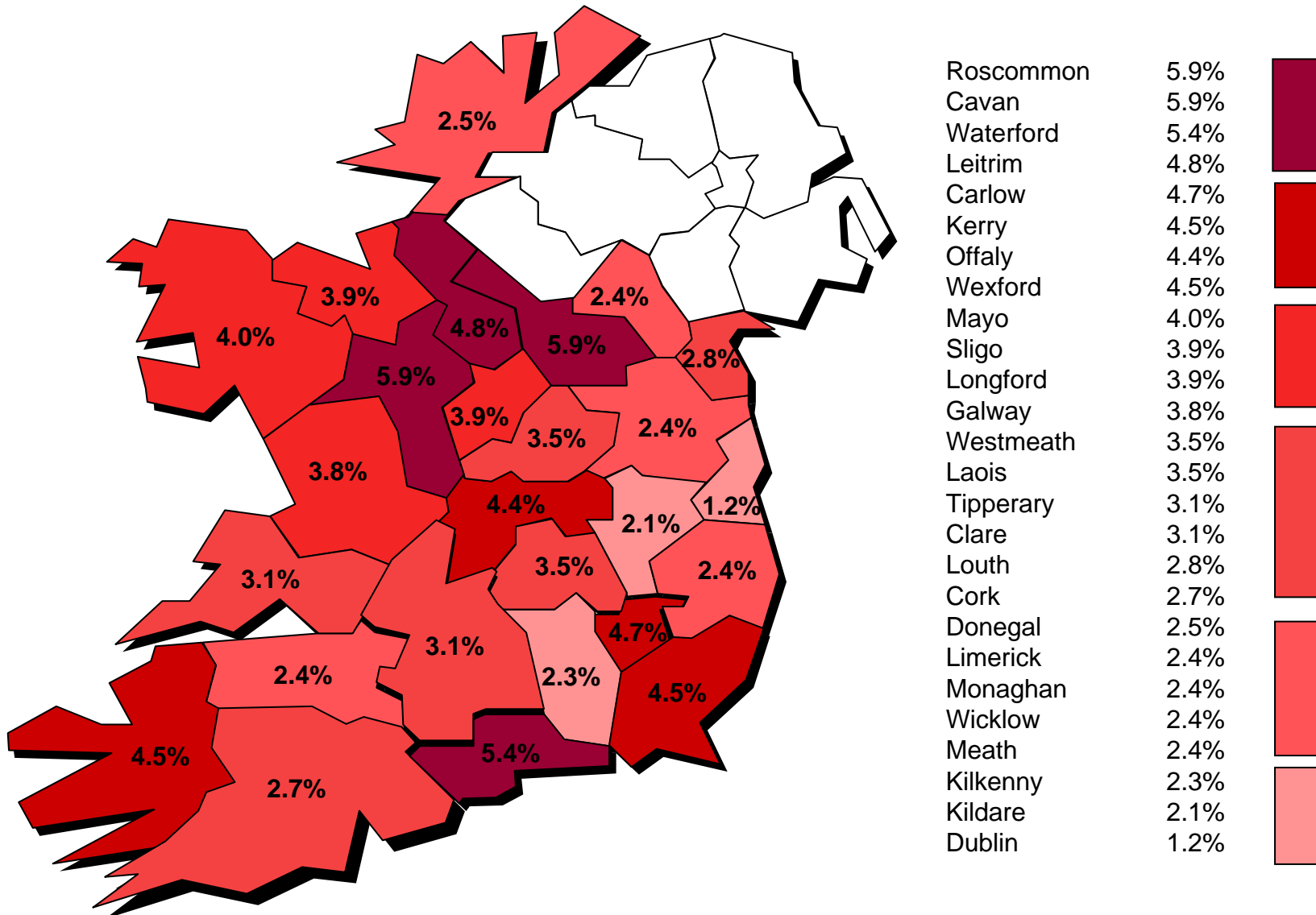
Irish housing output in 2009 set to be the lowest in 16 years



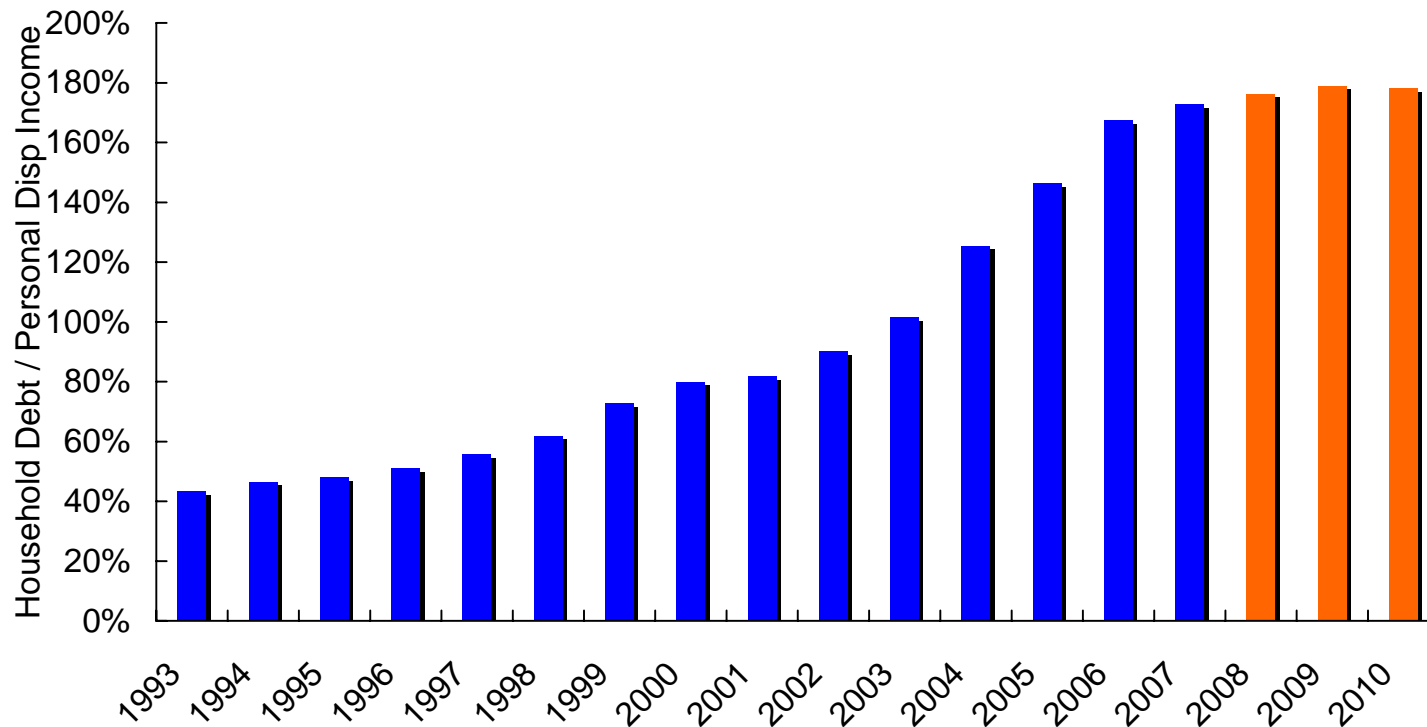
Source: DoELG, Goodbody estimates

Second-hand Houses For Sale (as a % of housing stock)

Ireland



Household debt as a % of disposable income



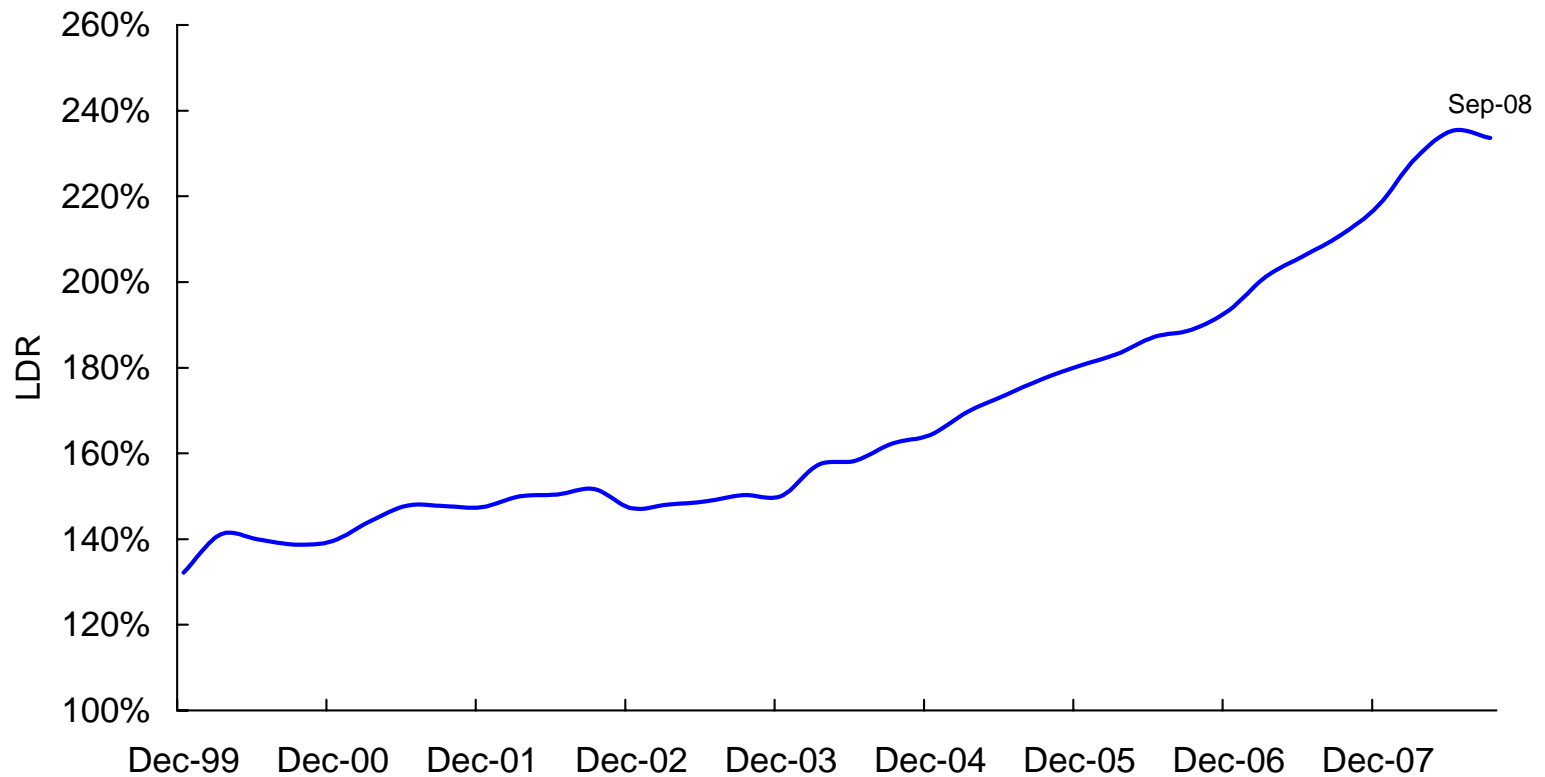
Source: Central Bank of Ireland, Goodbody estimates

Household Debt / Disp income ratios - Ireland is moving up the league table

	1995		2005 -08	Year	% increase in ratio 1995-2008
1 Denmark	188	1 Denmark	260	2005	38%
2 Japan	130	2 Netherlands	246	2005	118%
3 Norway	119	3 Norway	195	2006	64%
4 Netherlands	113	4 Ireland	176	2008	267%
5 UK	106	5 UK	173	2008	63%
6 Canada	103	6 Australia	171	2006	106%
7 Germany	97	7 New Zealand	160	2007	67%
8 New Zealand	96	8 Sweden	139	2006	54%
9 US	93	9 US	138	2007	48%
10 Sweden	90	10 Canada	130	2008	26%
11 Australia	83	11 Spain	130	2008	120%
12 France	66	12 Portugal	120	2005	123%
13 Finland	64	13 Japan	109	2007	-16%
14 Spain	59	14 Finland	102	2006	59%
15 Belgium	57	15 Germany	100	2006	3%
16 Portugal	54	16 Austria	88	2006	159%
17 Ireland	48	17 Belgium	75	2006	32%
18 Austria	34	18 France	72	2008	9%
19 Italy	31	19 Italy	66	2006	113%

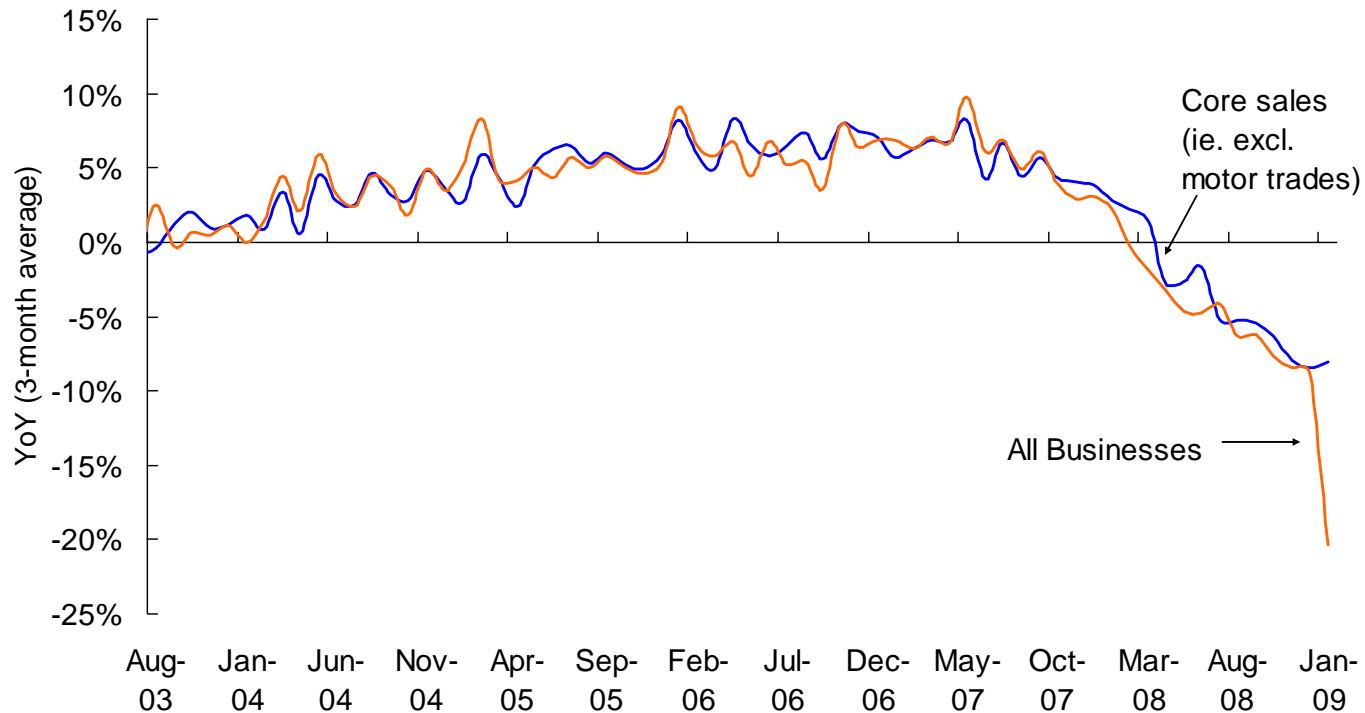
Source: OECD, various central banks, Goodbody estimates

Loan to Deposit ratio for Irish residents



Source: Central Bank of Ireland

Consumers in clear retrenchment mode

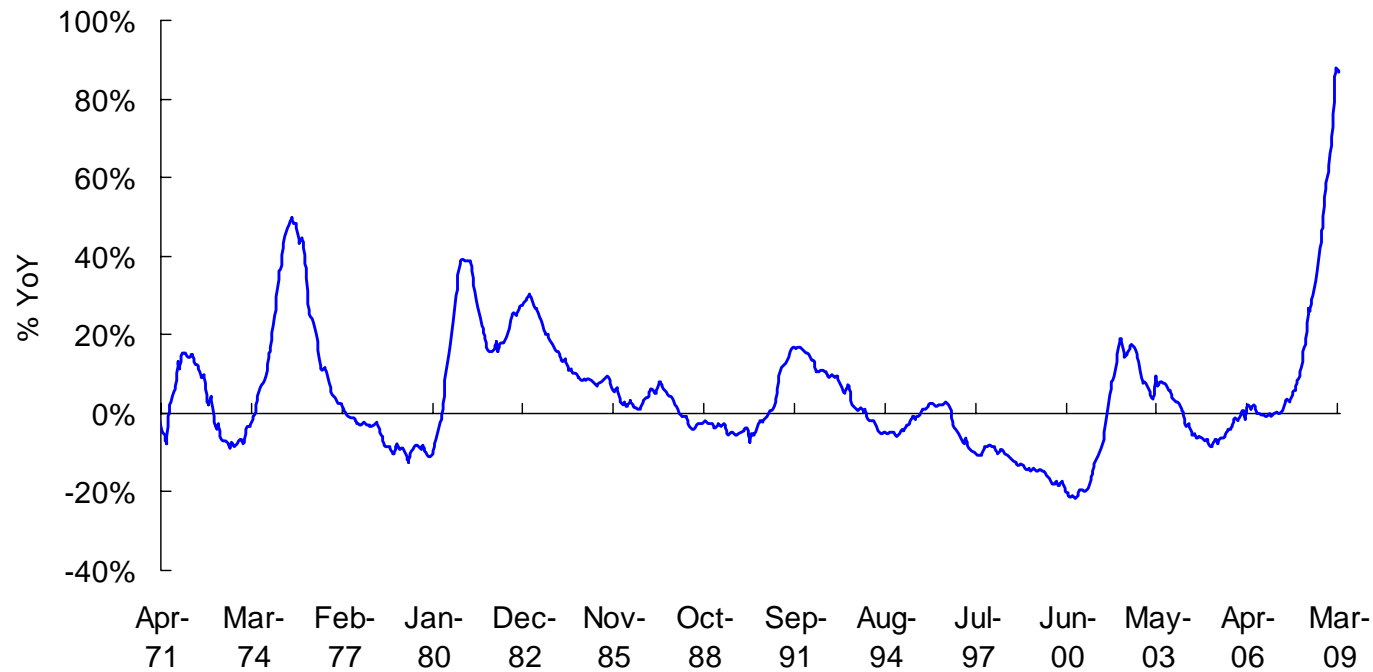


Source: CSO

Deterioration Becoming More Widespread

Ireland

Meteoric rise in Live Register continues



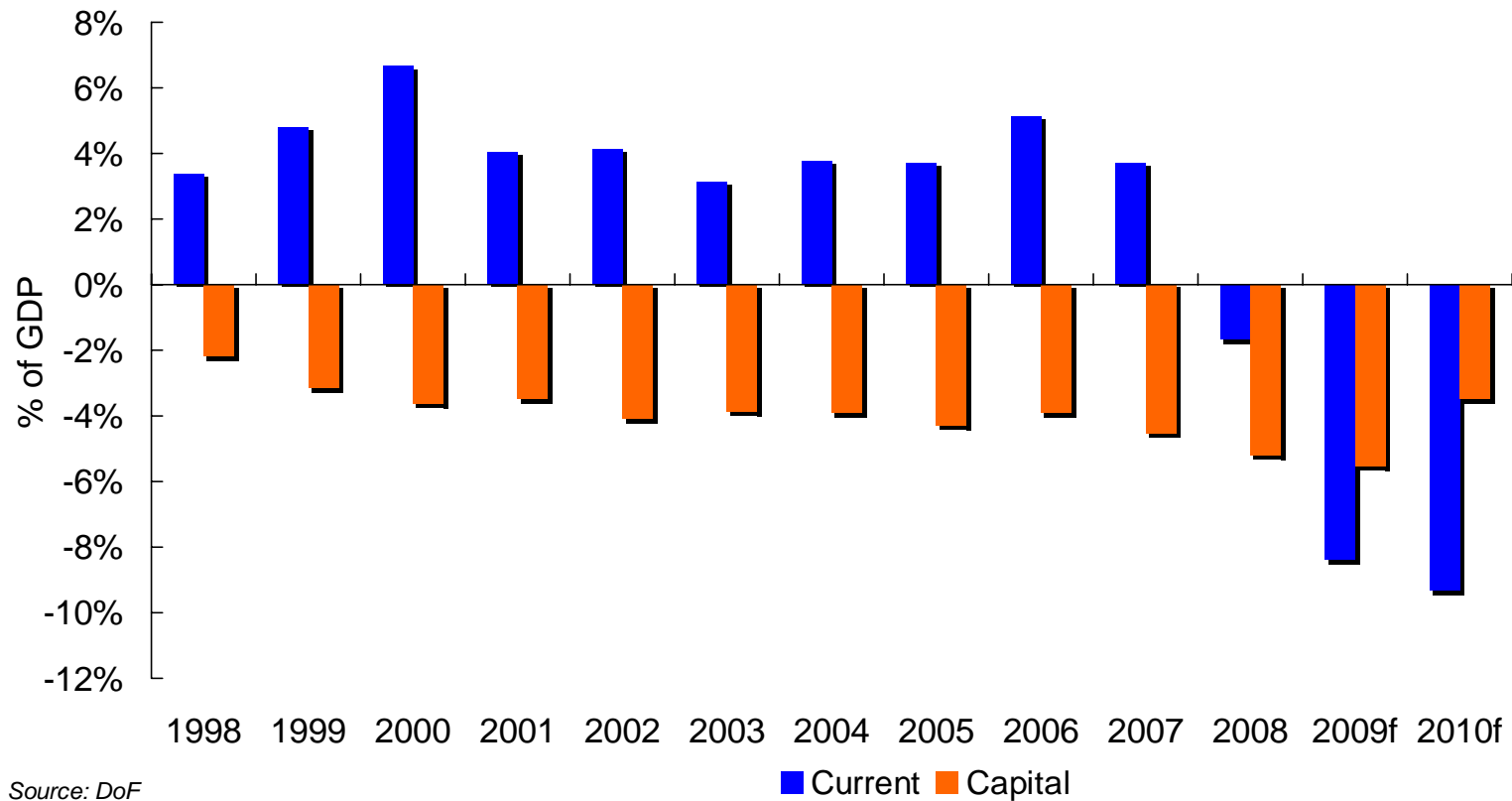
Source: CSO

Growth Components	2006	2007	2008	2009F	2010F
Consumption	7.1%	6.3%	-0.8%	-9.0%	-6.5%
Government	4.8%	6.0%	2.1%	0.0%	0.0%
Investment	4.0%	1.2%	-19.9%	-33.8%	-18.7%
Domestic Demand	5.8%	4.7%	-6.0%	-13.4%	-7.4%
Exports	5.7%	6.8%	-0.4%	-4.5%	-1.2%
Imports	6.3%	4.1%	-4.4%	-9.9%	-4.0%
GDP	5.7%	6.0%	-2.3%	-8.8%	-4.3%
GNP	6.3%	4.1%	-3.1%	-9.5%	-4.9%

Source: Goodbody

The Public Finances

Current a/c balance to blame for ballooning deficit



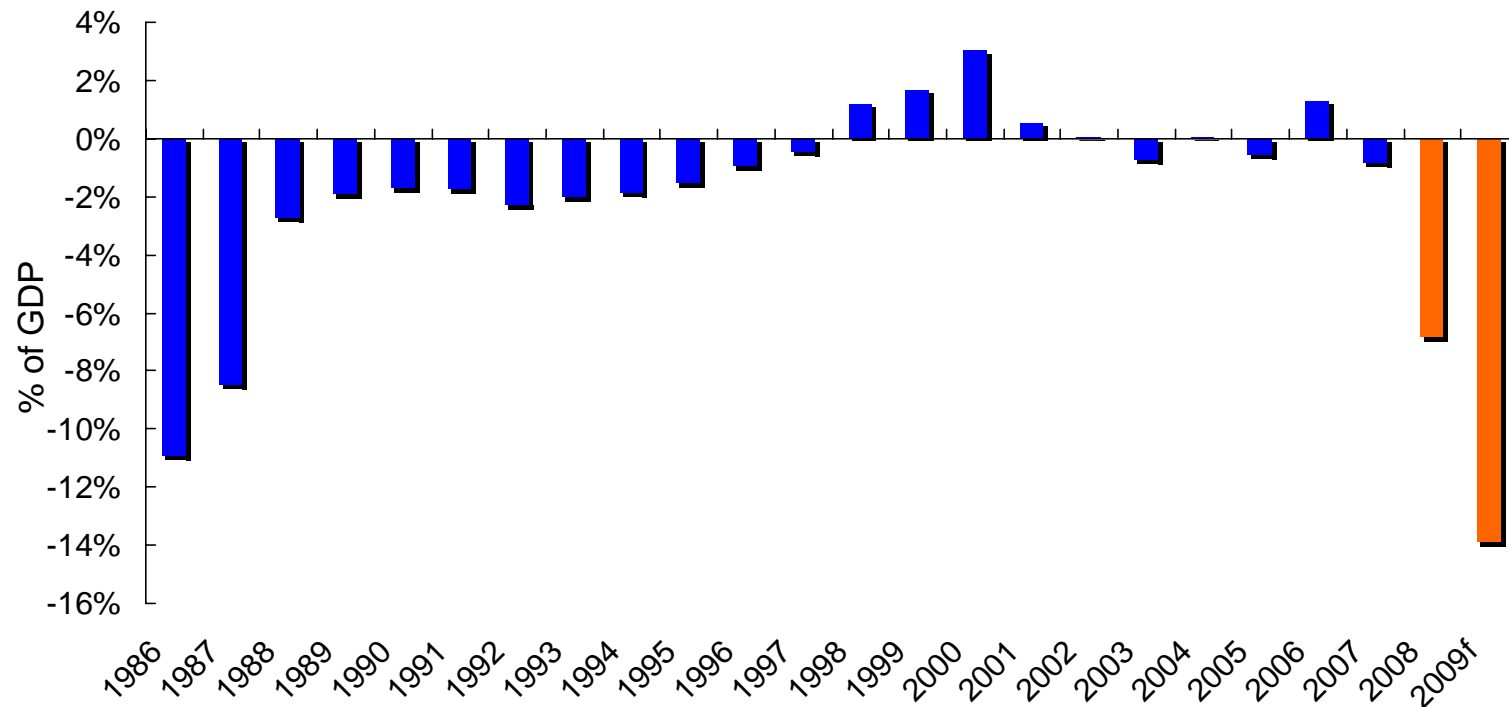
Tax performance

Tax heading	2009e (€m)	% of total			2002-2007		2007-2009	
		2002	2007	2009	€m	%	€m	%
C&E	4,128	15.6%	12.9%	12.6%	1,525	33.3%	-1972	-32.3%
CGT	501	2.1%	6.6%	1.5%	2,517	400.7%	-2644	-84.1%
CAT	265	0.5%	0.8%	0.8%	233	155.0%	-118	-30.7%
Stamp	660	4.0%	6.8%	2.0%	2,028	173.9%	-2535	-79.3%
IT	13,054	31.0%	28.7%	39.9%	4,530	49.9%	-551	-4.0%
CT	3,040	16.4%	13.4%	9.3%	1,546	32.2%	-3309	-52.1%
VAT	11,100	30.3%	30.7%	33.9%	5,660	63.7%	-3445	-23.7%
Total	32,749	100.0%	100.0%	100.0%	18,031	61.6%	-14576	-30.8%

Source: DoF

A Liquidity Problem, Not a Solvency One

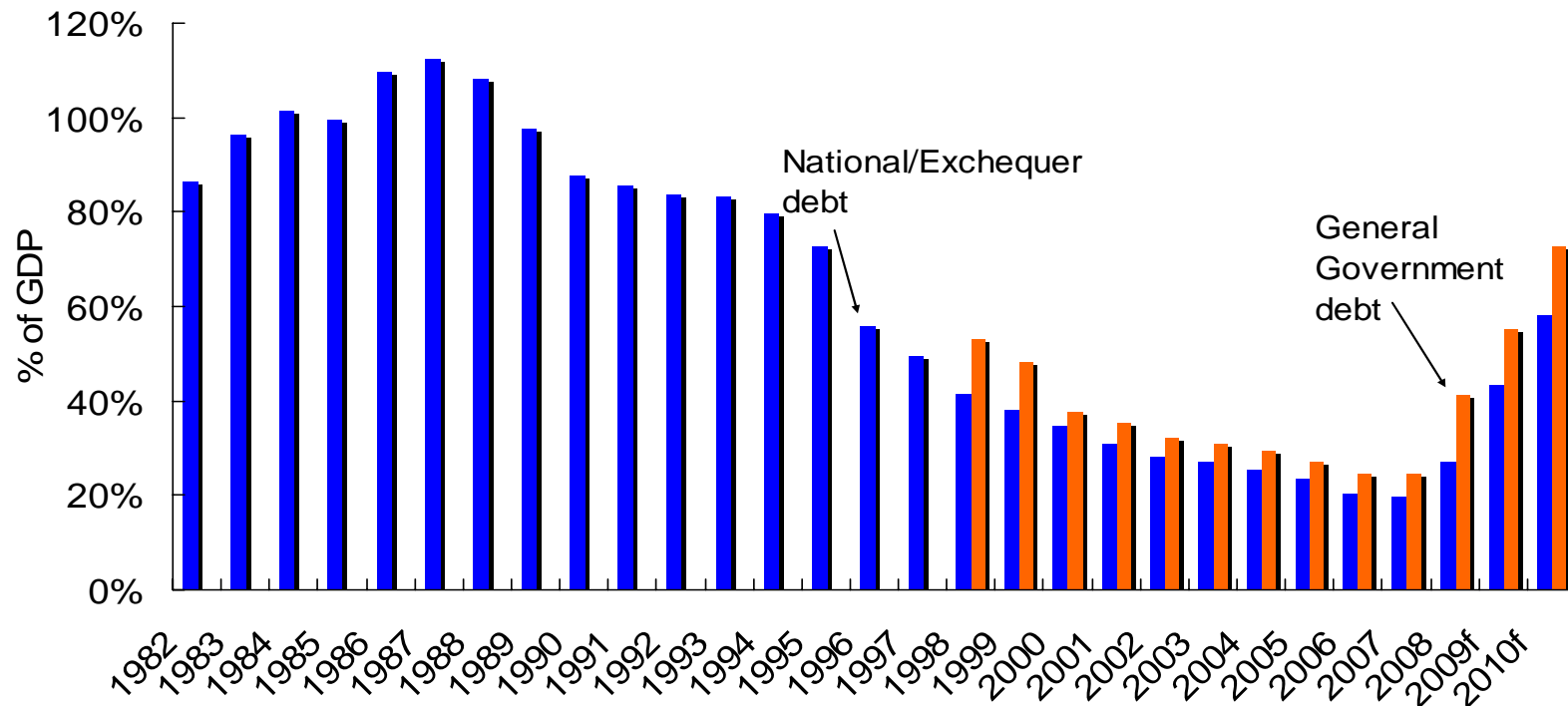
Deficits expected in short term- Exchequer balance as % of GDP



Source: Department of Finance

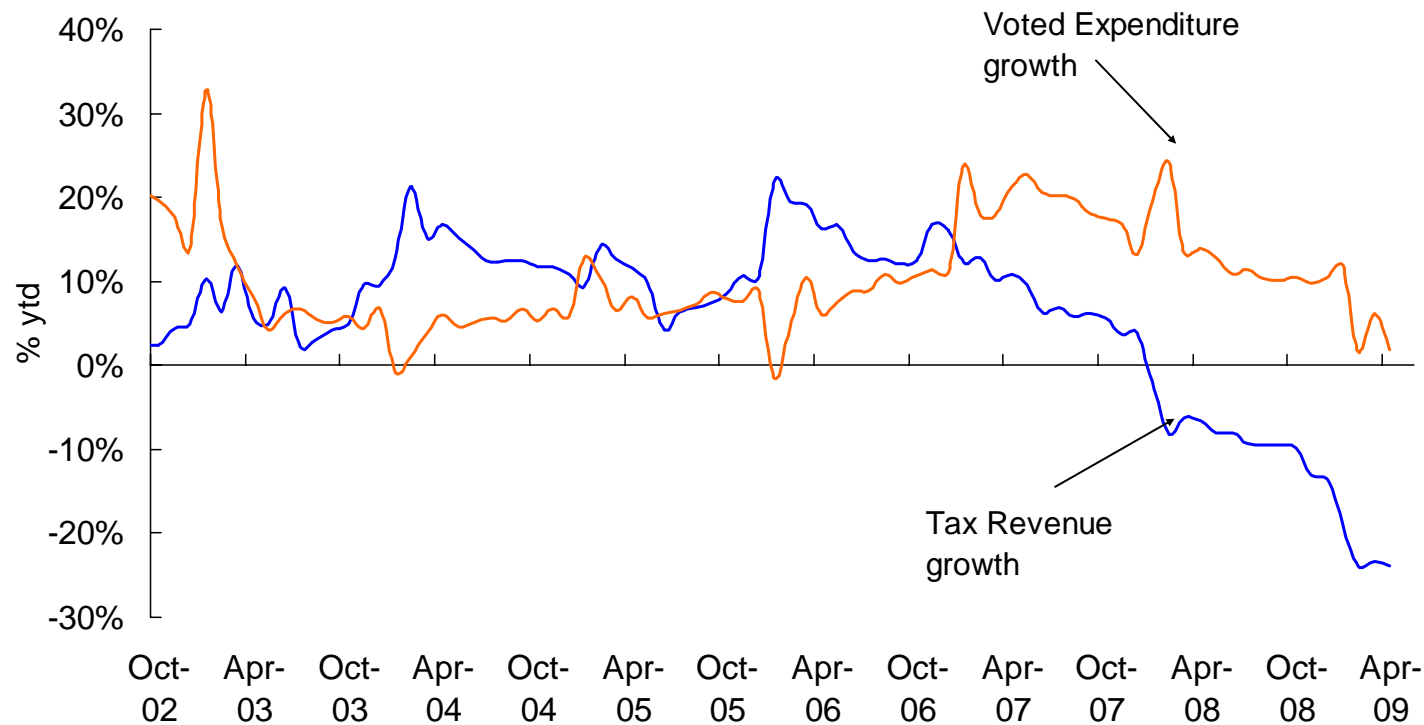
A Liquidity Problem, Not a Solvency One

Government debt levels as % of GDP



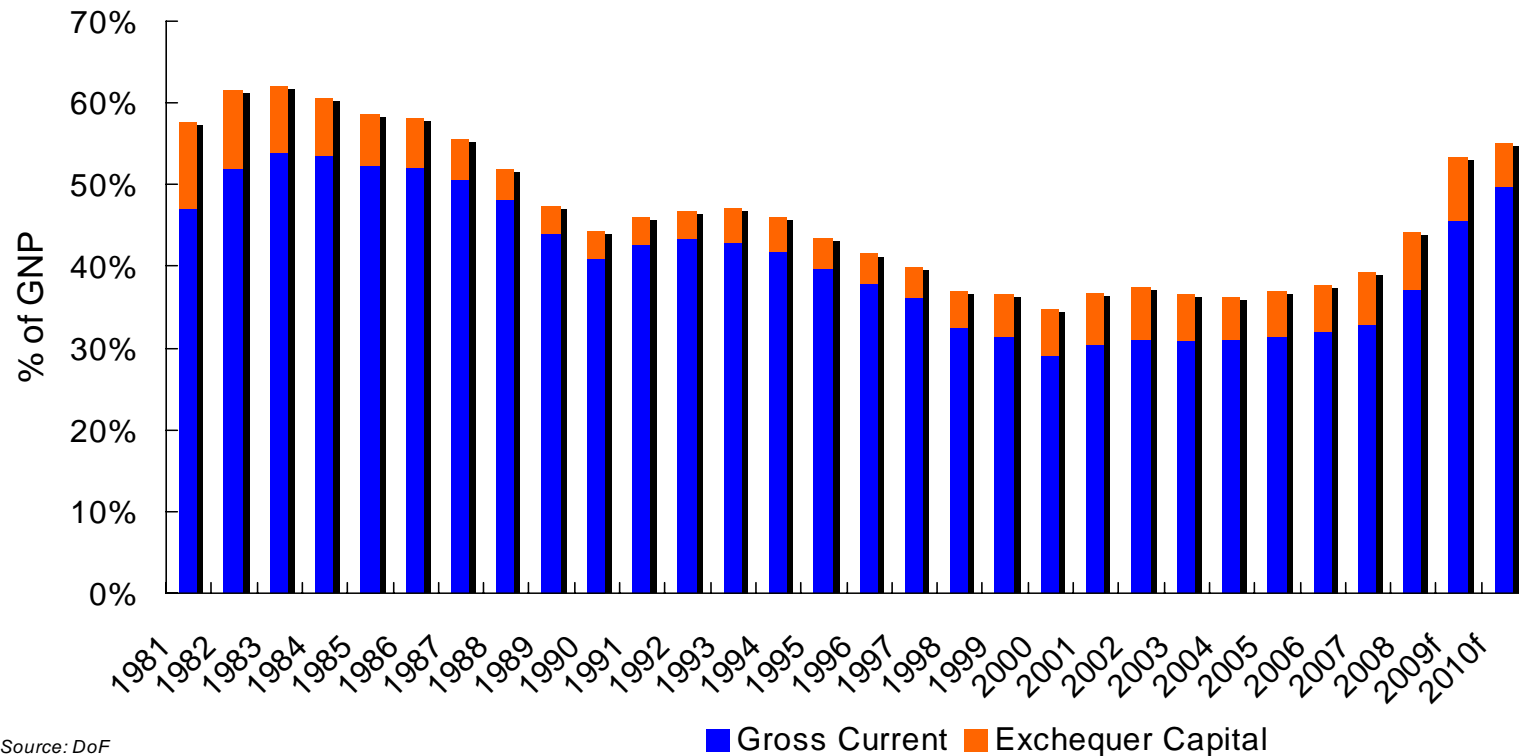
Source: Department of Finance

Spending and tax jaws opening up

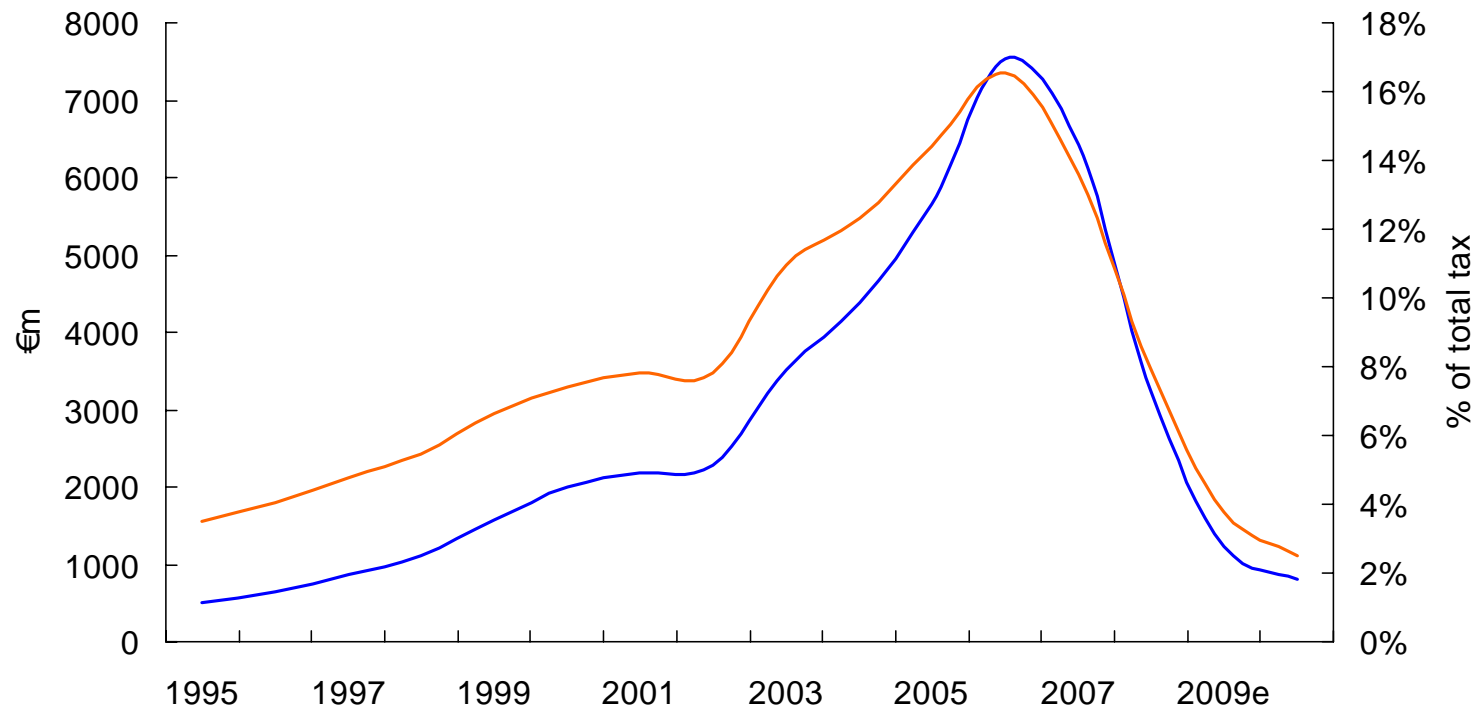


Source: Department of Finance

Government spending (as a % of GNP) back to 1980s' levels



Housing-related taxes* in Ireland



Source: DoF, Goodbody estimates *combines housing estimates for CGT, Stamp & VAT

— Amount (LHS) — Share of total (RHS)

Where Is The Money Spent?

Ireland

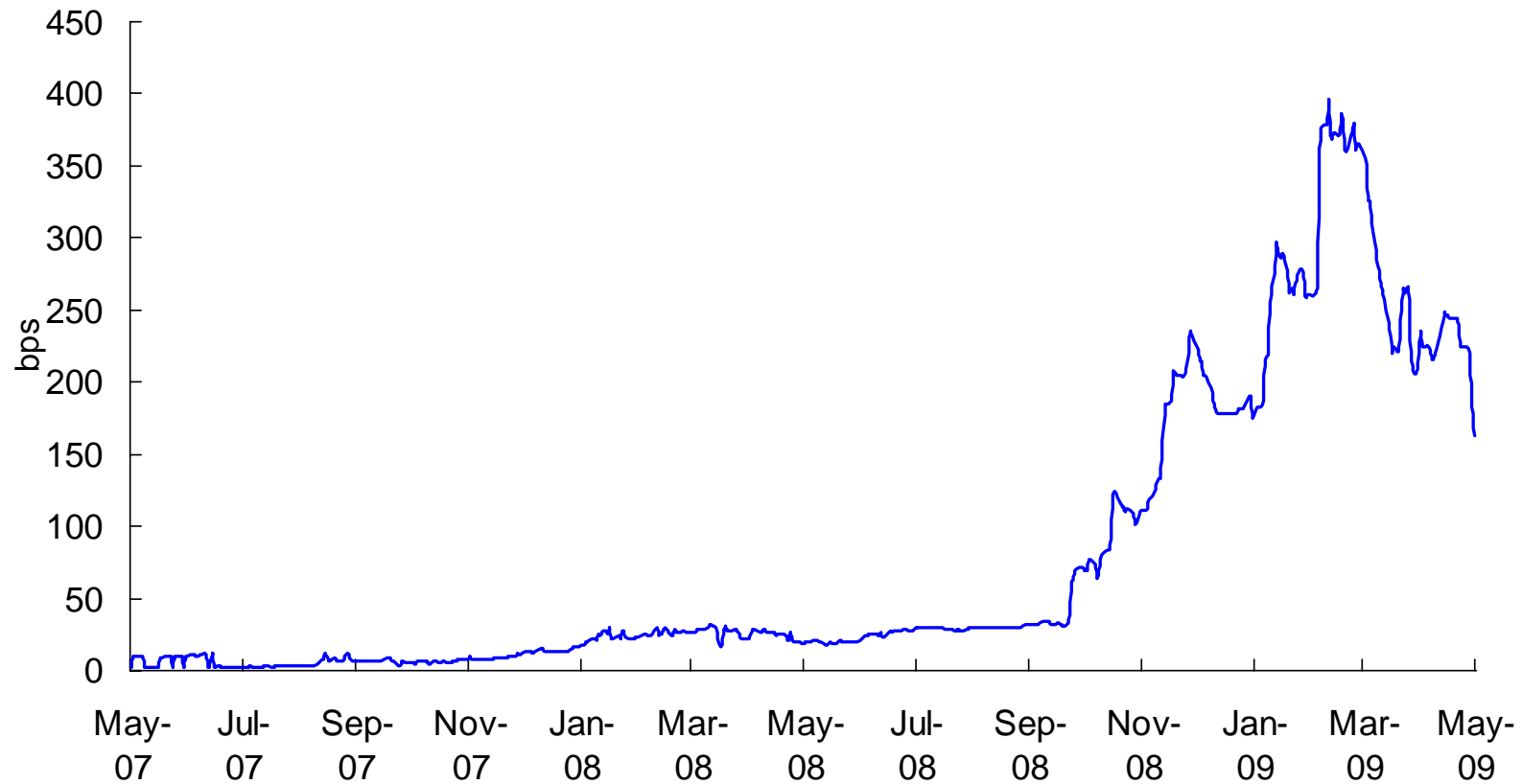
Summary of Voted Supply Services* - Capital & Current - Top 10 spending areas

Budget 2009

Vote. No.		2009		% of Dept. Exp.								
		Estimate - Total Spending	% of Total	Current	% of Total Current	Capital	% of Total Capital	Current	Capital	Pay Bill	% of Total pay bill	Pay as a % of Dept. expenditure
40	Health Services Executive	15,256	24%	14,791	26%	465	6%	97%	3%	8,155	41%	53%
38	Social & Family Affairs	10,545	16%	10,554	19%	12	0%	100%	0%	225	1%	2%
26	Education and Science	9,628	15%	8,739	16%	889	11%	91%	9%	6,679	33%	69%
38	Social Insurance Fund	9,025	14%	9,025	16%	-	0%	100%		-	0%	0%
32	Transport	3,613	6%	725	1%	2,888	35%	20%	80%	68	0%	2%
25	Environment, Heritage and Local Government	3,114	5%	969	2%	2,146	26%	31%	69%	118	1%	4%
31	Agriculture	1,803	3%	1,402	3%	402	5%	78%	22%	364	2%	20%
20	Garda	1,589	2%	1,540	3%	49	1%	97%	3%	1,377	7%	87%
34	Enterprise, Trade & Employment	1,569	2%	1,074	2%	495	6%	68%	32%	351	2%	22%
36	Defence	852	1%	827	1%	25	0%	97%	3%	589	3%	69%
Top ten spending departments		56,996	89%	49,646	89%	7,370	90%	87%	13%	17,927	89%	31%
Total		64,029	100%	55,818	100%	8,231	100%	87%	13%	20,042	100%	31%
Expenditure receipts and balances		13,999		13,553		466						
Net voted total		50,030		42,265		7,765						

Note: Spending would also include a non-voted element which would include EU contributions, interest servicing, on which there is no real control over

5-yr Irish CDS Spread



Source: Datastream

No Longer Top of The Class?

Ireland

Sovereign Debt Rankings

Country	S&P rating	GGD as % of GDP				GGB as % of GDP				Bond spread*
		2007	2008	2009f	2010f	2007	2008	2009f	2010f	
Austria	AAA	59.5	59.4	62.3	64.7	-0.4	-0.6	-3.0	-3.6	64.0
Finland	AAA	35.1	32.8	34.5	36.1	5.3	4.5	2.0	0.5	51.5
France	AAA	63.9	67.1	72.4	76.0	-2.7	-3.2	-5.4	-5.0	36.3
Germany	AAA	65.1	65.6	69.6	72.3	-0.2	-0.1	-2.9	-4.2	0.0
Luxembourg	AAA	7.0	14.4	15.0	15.1	3.2	3.0	0.4	-1.4	n/a
Netherlands	AAA	45.7	57.3	53.2	55.2	0.3	1.1	-1.4	-2.7	42.1
Ireland	AA+	24.8	40.8	54.8	68.2	0.2	-6.3	-11.0	-13.0	165.3
Belgium	AA+	83.9	88.3	91.2	94.0	-0.3	-0.9	-3.0	-4.3	55.8
Spain	AA+	36.2	39.8	46.9	53.0	2.2	-3.4	-6.2	-5.7	60.9
Slovenia	AA	23.4	22.1	24.8	25.8	0.5	-0.9	-3.2	-2.8	n/a
Portugal	A+	63.6	64.6	68.2	71.7	-2.6	-2.2	-4.6	-4.4	80.1
Cyprus	A+	59.5	48.1	46.7	45.7	3.4	1.0	-0.6	-1.0	n/a
Italy	A+	104.1	105.7	109.3	110.3	-1.6	-2.8	-3.8	-3.7	80.0
Slovakia	A+	29.4	28.6	30.0	31.9	-1.9	-2.2	-2.8	-3.6	n/a
Malta	A	62.2	63.3	64.0	64.2	-1.8	-3.5	-2.6	-2.5	n/a
Greece	A-	94.8	94.0	96.2	98.4	-3.5	-3.4	-3.7	-4.2	162.4
Eurozone avg.		66.1	68.7	72.7	75.8	-0.6	-1.7	-4.0	-4.4	

Source: Bloomberg, European Commission

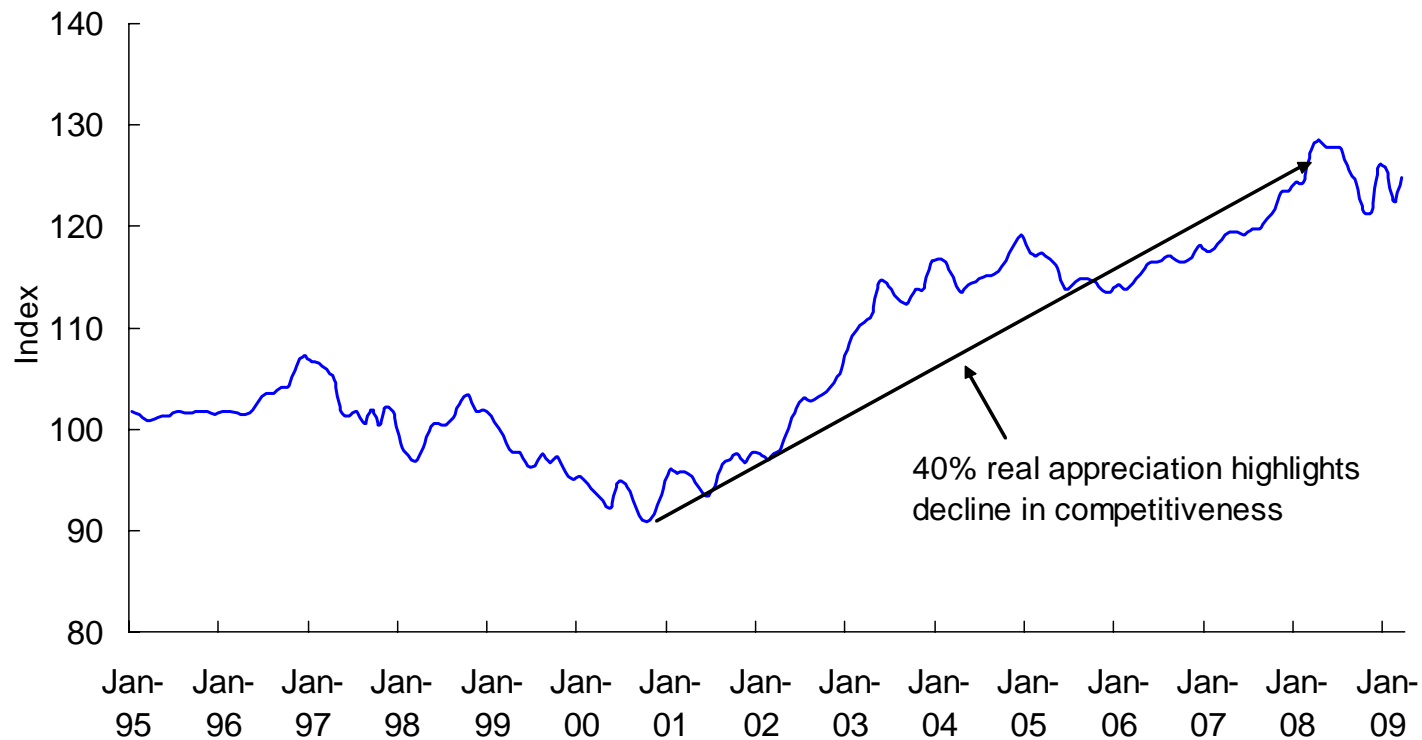
*Current 10-year bond yield spread with German bunds

- Setting out a plan to reduce deficit and stick to it
- This plan must be credible and transparent – recent road shows are a step in the right direction
- Recent budget concentrated too much on taxes – successful fiscal consolidations are focused on reductions to current spending
- Tax base must also be broadened – Commission for Taxation report is imminent
- Solvency risks are exaggerated, liquidity risks less so
- Domestic savings are on the increase

The Economy

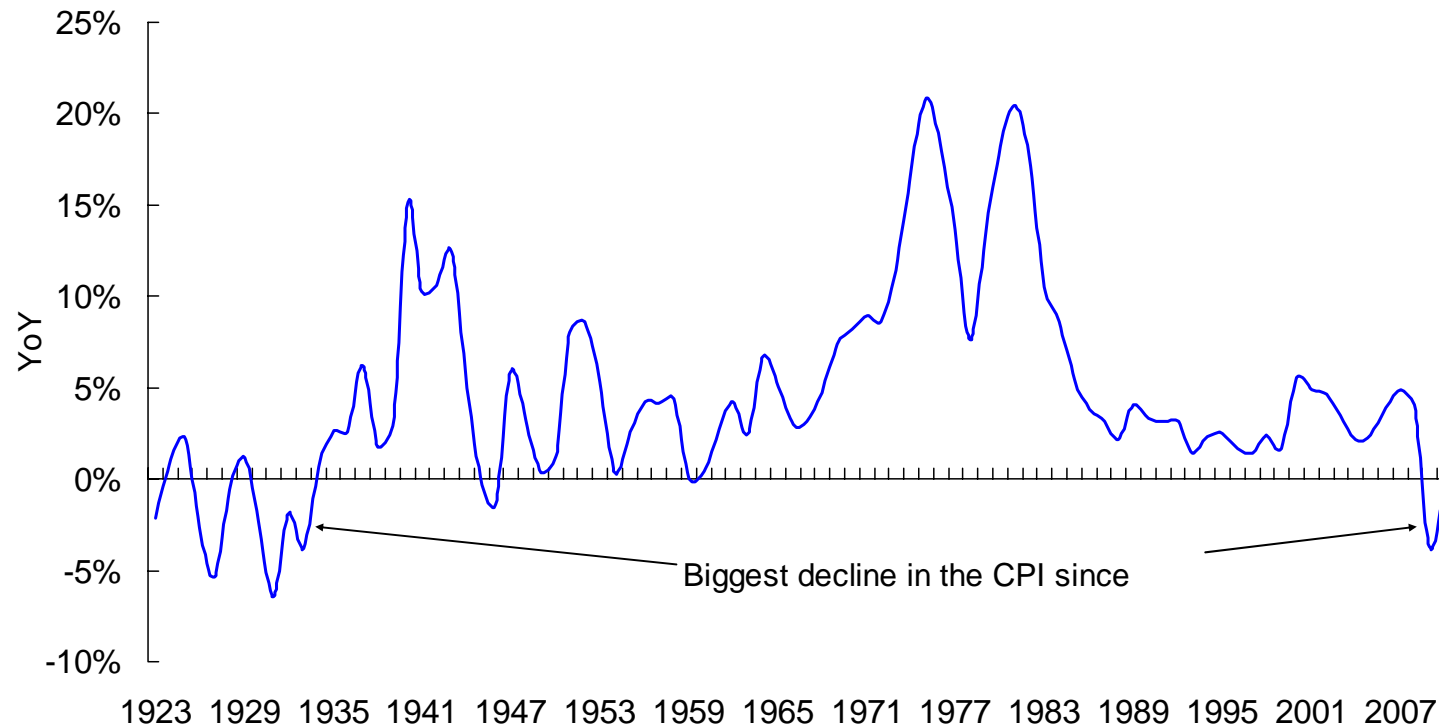
- Fiscal stimulus is out of our hands – must piggy-back on European and US measures
- Past experience suggests that an improvement in competitiveness acts as a trigger to economic recovery
- Wage costs are dropping fast in the private sector and will see largest fall in consumer prices in 2009 since 1933
- Commitment to 12.5% corporation tax must remain a key plank of industrial policy here
- Choosing winning sectors – Green energy?

Trade weighted index highlights decline in competitiveness



Source: Central Bank

Deflation to be a reality in Ireland in 2009



Source: CSO

The Banking Sector

Systemic Banking Crises in Developed Economies since 1970

Country	Systemic Banking Crisis (starting date)	Share of NPLs at peak (in %)	Fiscal Cost (gross, as % of GDP)	Output loss (IMF) (as % of GDP)	Minimum real GDP growth rate (in %)
Czech Republic	1996	18.0	6.8		-0.8
Finland	1991	13.0	12.8	59.1	-6.2
Hungary	1991	23.0	10.0		-11.9
Japan	1997	35.0	24.0	17.6	-2.0
Korea	1997	35.0	31.2	50.1	-6.9
Norway	1991	16.4	2.7		2.8
Slovak Republic	1998	35.0			
Spain	1977		5.6		0.2
Sweden	1991	13.0	3.6	30.6	-1.2
United States	1988	4.1	3.7	4.1	-0.2
Average		21.4	11.2	32.3	-2.9

Source: Laeven and Valencia, 2008. "Systemic Banking Crises: A New Database", IMF Working Paper.

Debt of banks guaranteed by Irish Government (€m)*

As of	AIB Jun-08	BOI Sep-08	Anglo Sep-08	IL&P Jun-08	EBS Jun-08	Irish NW Dec-07	Total
Customer loans	132,814	144,289	72,151	41,005	16,595	12,332	419,186
Shareholder's equity	9,555	6,382	4,125	2,639	612	1,510	24,823
Shareholder's equity + undated subord	11,340	9,591	7,263	2,639	862	1,510	33,205
Total debt	74,636	82,927	39,543	28,501	9,073	7,242	241,921
Total debt ex liquid assets	34,531	45,051	15,328	22,013	5,999	3,878	126,800
Total debt + deposits	161,619	173,592	91,042	43,098	18,976	14,492	502,819
Total debt + deposits ex liquid assets	121,514	135,716	66,827	36,610	15,903	11,128	387,698

Source: Company reports

*Postbank Ireland also insured, but no figures available

Bad bank writedown assumptions

	AIB	BOI	Anglo	Others	Total
Loans transferred at book value (€m)					
Commercial investment	6,239	6,961	10,822		24,022
Residential investment	1,221	1,289	980		3,490
Commerical development	7,164	4,512	7,246		18,922
Residential development	14,012	8,710	8,361		31,083
Contractors	1,049	0	0		1,049
Total	29,685	21,471	27,410	6,423	84,989
Write down (%)					
Commercial investment	8.1	10.3	13.3		11.1
Residential investment	8.0	9.5	6.9		8.2
Commerical development	21.7	19.3	22.8		21.5
Residential development	20.5	16.7	19.0		19.1
Total	17.0	14.7	17.4	16.5	16.5

Source: Goodbody estimates

Post NAMA - Capital, Dilution & NAV - Base Forecasts

	AIB			BOI			
	2009f	2010f	2011f	2010f	2011f	2012f	
Equity tier 1 (with no equity recap & €3.5	3,432	2,609	1,993	2,659	1,170	-167	
RWA	97,678	97,794	95,791	72,547	68,208	69,418	
Equity to RWA (ex equity injection)	3.5	2.7	2.1	3.7	1.7	-0.2	
Tangible NAV(with no equity recap & €3.	4,154	2,959	2,343	2,320	333	-1,004	
Dilution							
	4%	36.8	60.0	66.3	19.1	58.5	71.3
	5%	64.2	72.3	75.0	48.4	66.9	75.4
	6%	75.0	78.9	80.1	62.2	72.5	78.5
Tangible NAV per share							
	4%	3.31	1.93	1.60	2.07	0.78	0.55
	5%	2.27	1.64	1.46	1.69	0.85	0.64
	6%	1.87	1.49	1.38	1.51	0.89	0.71

Source: Goodbody estimates

- A hard reality with no quick fix
- No economic recovery without stable public finances and a functioning banking sector
- A test of politics as well as economics
- A collective effort is required
- Pain in the short-term will lead to gain in the medium-term once imbalances in the economy are worked through

Regulation AC

"I hereby certify as follows: All of the views expressed in this research report accurately reflect my personal views about any and all of the subject securities and issuers. No part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed by me in this report".

Goodbody Stockbrokers is the stockbroking arm of Allied Irish Banks plc (AIB Group). Goodbody Stockbrokers is regulated by the Financial Regulator and is a member firm of the Irish Stock Exchange and the London Stock Exchange. This publication has been approved by Goodbody Stockbrokers. The information has been taken from sources we believe to be reliable, we do not guarantee their accuracy or completeness and any such information may be incomplete or condensed. All opinions and estimates constitute best judgement at the time of publication and are subject to change without notice. The information, tools and material presented in this document are provided to you for information purposes only and are not to be used or considered as an offer or the solicitation of an offer to sell or to buy or subscribe for securities.

We would like to advise you that the Research Analyst for Kingspan holds shares in Kingspan.

We would like to advise you that the Research Analyst for AIB Group holds shares in AIB Group.

This document is intended for the use of professional investors only. This report is not to be relied upon in substitution for the exercise of independent judgement. Nothing in this report constitutes investment, legal, accounting or tax advice, or a representation that any investment or strategy is suitable or appropriate to your individual circumstances, or otherwise constitutes a personal recommendation to you. Goodbody Stockbrokers does not advise on the tax consequences of investments and you are advised to contact an independent tax advisor. Please note in particular that the bases and levels of taxation may change. Private customers having access, should not act upon it in anyway but should consult with their independent professional advisors. The price, value and income of certain investments may rise or may be subject to sudden and large falls in value. You may not recover the total amount originally invested. Past performance should not be taken as an indication or guarantee of future performance; neither should simulated performance. The value of securities may be subject to exchange rate fluctuation that may have a positive or adverse effect on the price or income of such securities. Market data included in this report is at close of business of the previous working day. Goodbody Stockbrokers and its associated companies and/or its officers may from time to time perform banking or Corporate Finance services including underwriting, managing or advising on a public offering for, or solicit business from any company recommended in this report. They may own or have positions in any securities mentioned herein and may from time to time deal in such securities. Goodbody Stockbrokers is a registered market maker to the majority of companies listed on the Irish Stock Exchange and their equivalent on the London Stock Exchange. Taxation rates and the basis of taxation are subject to change without notice. Protection of investors under the UK Financial Services and Markets Act 2000 may not apply. Irish Investor Compensation arrangements will apply. For US Persons Only: This publication is only intended for use in the United States by Major Institutional Investors. A major Institutional investor is defined under Rule 15a-6 of the Securities Exchange Act 1934 as amended and interpreted by the SEC from time-to-time as having total assets in its own account or under management in excess of \$100 million. Investors should be aware, that where appropriate, research may be disclosed to the issuer (s) in advance of publication in order to correct factual inaccuracies. Goodbody Stockbrokers are satisfied that such disclosures will not compromise the report's objectivity. Please see <https://research.goodbody.ie> for other important disclosures. Goodbody Stockbrokers has procedures and policies in place to identify and manage any potential conflicts of interest that arise in connection with its research business. Goodbody Stockbrokers analysts and other staff who are involved in the preparation and dissemination of research operate and have a management reporting line independent to its Corporate Finance business. Chinese walls are in place between the Corporate Finance arm and the Research arm to ensure that any confidential and or price sensitive information is handled in an appropriate manner.

All material presented in this report, unless specifically indicated otherwise is copyright to Goodbody Stockbrokers. None of the material, nor its content, nor any copy of it, may be altered in any way, transmitted to, copied or distributed to any other party, without the prior express written permission of Goodbody Stockbrokers. All trademarks, services marks and logos used in this report are trademarks or service marks or registered trademarks or service marks of Goodbody Stockbrokers.

GSB uses the terms "buy", "add", "reduce" and "sell". The term "buy" means that the analyst expects the security to appreciate in excess of 15% over a twelve month period. The term "add" means that the analyst expects the security to appreciate by up to 15% over a twelve month period. The term "reduce" means that the analyst expects the security to decline by up to 15% over the next twelve months. The term "sell" means that the security is expected to decline by in excess of 15% over the next twelve months. In the event that a stock is delisted the firm will automatically cease coverage. If however the firm ceases to cover a stock for any other reason the firm will disclose this fact.

Goodbody Stockbrokers, Ballsbridge Park, Ballsbridge, Dublin 4, Ireland

T (+ 353 1) 667 0400 F (+ 353 1) 667 0280 W www.goodbody.ie E goodbody@goodbody.ie