Republic of Ireland
Rating Report

AA- STABLE OUTLOOK

Credit strengths

- Wealthy, diversified and competitive economy
- Track record of fiscal discipline, favorable debt profile
- Strong institutional environment
- Euro-area membership

Credit challenges

- High public and private debt levels
- Strong dependence on multinational enterprises (MNEs)
- External vulnerabilities and a small, open economy vulnerable to shocks

Rating rationale:

Wealthy, diversified and competitive economy: Ireland benefits from its high wealth levels and competitive economy, supported by high value-added sectors such as pharmaceuticals and information and communication technology, which underpin the country's robust growth potential.

Track record of fiscal consolidation: Strong fiscal discipline before the Covid-19 crisis, declining fiscal deficits going forward and a long maturity of public debt support Ireland's rating.

Strong institutional environment: The country has a well-established institutional framework, a favourable tax regime attracting foreign investment, effective rule of law and low levels of corruption.

Euro-area member status: Euro-area membership supports Ireland's high-growth economic model, helping to attract and retain foreign investment, and provides access to lenders of last resort for banks via the European Central Bank and sovereigns via the European Stability Mechanism.

Rating challenges include: i) still high public debt levels when assessed against underlying economic activity; ii) a strong dependence on MNEs whose corporate tax contributions make up a significant portion of government revenues; and iii) the economy's vulnerability to sudden reversals when considered in the context of a small and very open economy due to shocks of either domestic or international origin.

Ireland's sovereign rating drivers

Risk pillars		Quantitative scorecard		Reserve currency adjustment (notches)	Qualitative scorecard	Final rating
		Weight	Indicative rating		Notches	
Domestic Economic Risk		35%	aaa		0	
Public Finance Risk		25%	aa		0	
External Economic Risk		10%	bb-		-3/3	
Financial Stability Risk		10%	aaa		-1/3	AA-
ESG Risk	Environmental Risk	5%	aaa		0	
	Social Risk	5%	aa-		-1/3	
	Governance Risk	10%	aaa		0	
Overall outcome		aaa		+1	-3	

Note: The sum of the qualitative adjustments, capped at 1 notch per rating pillar, is weighted equally and rounded to the nearest integer. The reserve currency adjustment applies to currencies in the IMF's SDR basket.
For details, please see Scope's 'Sovereign Ratings' methodology. Source: Scope Ratings GmbH

Outlook and rating triggers

The Stable Outlook reflects Scope's view that risks to the ratings are balanced over the next 12 to 18 months.

Positive rating-change drivers

- Meaningful reduction in public debt levels
- Significant decrease in private-sector debt levels

Negative rating-change drivers

- Substantially weaker growth potential
- Reversal of the downward public debt trajectory
- Private-sector and financial system risks increase meaningfully
- Increases in net external debt

Ratings and Outlook

Foreign and local currency

Long-term issuer rating	AA-/Stable
Senior unsecured debt	AA-/Stable
Short-term issuer rating	S-1+/Stable

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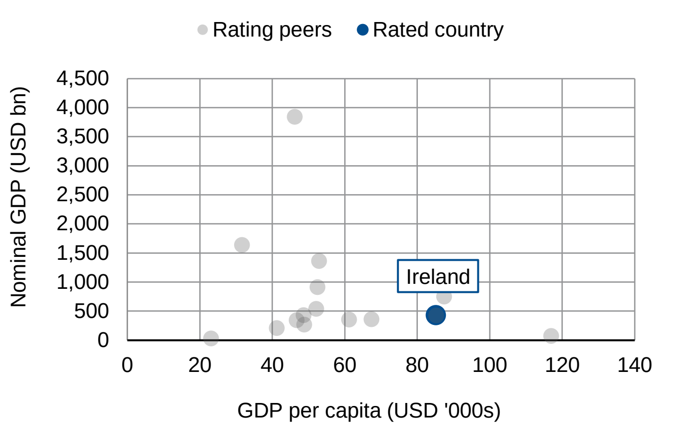
Domestic Economic Risks

- **Growth outlook:** Following a 4.9% dip in economic activity as measured by modified domestic demand (MDD) in 2020, the Irish economy recovered well from the Covid-19 crisis in 2021, expanding by 6.5% and exceeding the pre-pandemic level of output. Real GDP increased by 13.5% in 2021, boosted by the strong performance of the multinational sector. The rebound in domestic activity was largely driven by private demand which recovered following the phase-out of pandemic-related restrictions in the summer of 2021, increased government consumption and net exports. Ireland's direct exposure to Russia and Ukraine is low due to the limited trade ties with the two countries. However, as a small and open economy, Ireland will be impacted by the expected slowdown in global economic growth. The rise in energy and commodity prices that followed the invasion should also diminish households' real incomes and negatively impact domestic demand growth. Despite these headwinds, we expect GDP growth to remain resilient in the medium term and to reach 6.1% in 2022 and 4.9% in 2023.
- **Inflation and monetary policy**: Inflation accelerated to 2.5% on average in 2021, up from -0.5% in 2020, largely driven by the release of pent-up demand, supply bottlenecks and rising energy prices. Core inflation was more moderate, averaging at 1.7% over the same period. Similarly to peers, price increases have accelerated further, up to 6.9% in March 2022, and have become more broad-based, with core inflation well above 2% in recent months. The war in Ukraine has caused sharp increases in energy and raw material prices, as well as supply-chain disruptions, which should further fuel inflation over 2022-23.
- **Labour markets**: The economic recovery supported a strong rebound in labour markets, increasing employment by 10.1% in Q4 2021 compared with the same period in 2020. The unemployment rate declined to about 5.5% in March 2022, having increased moderately from the previous month following the phasing out of the Pandemic Unemployment Payment programme. The number of job vacancies increased substantially and stood at about 59% above pre-pandemic level as of end-2021.

Overview of Scope's qualitative assessments for Ireland's *Domestic Economic Risks*

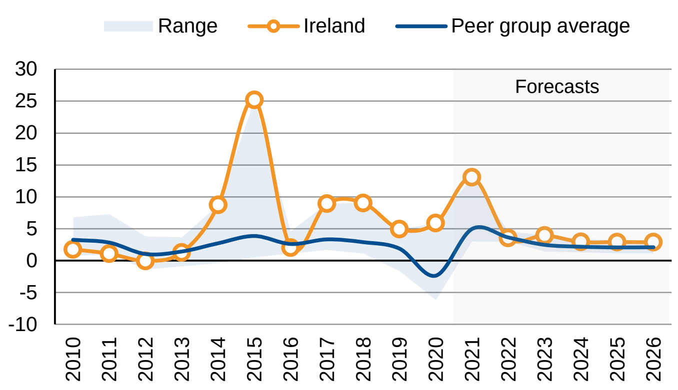
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
aaa	Growth potential of the economy	Strong	+1/3	Strong growth potential, but some uncertainty around longer-term impact of global tax reforms
	Monetary policy framework	Neutral	0	ECB is a highly credible and effective central bank; effective policy framework and transmission over the cycle
	Macro-economic stability and sustainability	Weak	-1/3	Economic structure subject to high volatility; exposure to global crises; reduced Brexit risk although exposure to changes of global corporate tax policy

Nominal GDP and GDP per capita, USD '000s



Source: IMF, Scope Ratings GmbH

Real GDP growth, %



Source: IMF, Scope Ratings GmbH

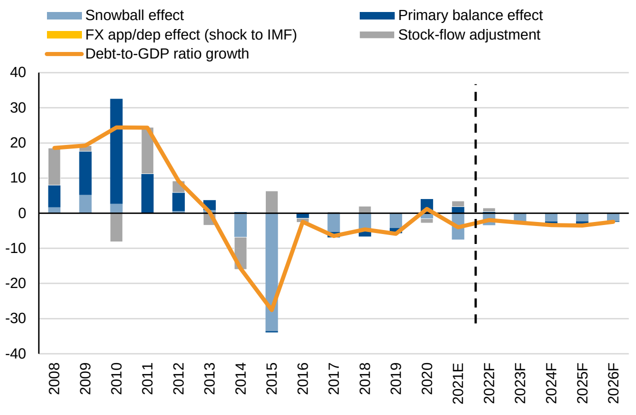
Public Finance Risks

- **Fiscal outlook:** The strong economic recovery in 2021 allowed for a strong rebound in government revenue, while expenditure grew slower than anticipated due to lower pandemic-related health expenditures. Corporate income tax receipts reached a record high EUR 15.3bn, more than 10% above initial projections. These positive developments led to a lower-than-expected general government deficit in 2021, at 1.9% of GDP, or 3.6% of modified gross national income (GNI). We expect a general government deficit of 0.4% of GDP in 2022, and a surplus of 0.2% in 2023. Medium term headwinds to fiscal consolidation relate to the fallout of the Ukraine war and its impact on energy costs. The Irish government rolled out several measures to tackle the rising costs of living, including reduced VAT rates for energy and a significant cut to excise duties on fuel, for a total cost of about EUR 1bn. It also estimates that the costs of hosting Ukrainian refugees could amount to EUR 1.7bn this year, and to EUR 2.5bn in 2023. Additional risks relate to the global corporate income tax reform which could negatively impact corporation tax receipts for Ireland.
- **Debt trajectory:** The debt-to-GNI ratio stood at about 106% at end-2021 (56% of GDP), still above the pre-pandemic level of 95% in 2019. We expect the debt-to-GDP ratio to decrease below pre-crisis level by end-2022, to about 54% of GDP and to gradually decline down to 42% by 2026. Our medium-term view is supported by the large liquidity reserves accumulated by the government throughout the pandemic (EUR 27.5bn at the beginning of 2022) which the government intends to reduce to meet its funding needs, as well as by the recent adoption of a new fiscal framework which caps permanent increases in government expenditures.
- **Debt profile and market access:** Ireland benefits from a favourable debt profile, supported by a high share of public sector debt held by the Eurosystem (28% as of Q3 2021) and by official sector institutions. Its average debt maturity counts among the longest in the euro-area, at 10.9 years as of March 2022, which partially shields it from the gradual increase in interest rates that will follow the global tightening of monetary policy. Similar to peers, Ireland's financing costs have increased moderately in the recent period, with the 10-year government at 0.93% on average in March 2022, up from 0.03% in March 2021.

Overview of Scope's qualitative assessments for Ireland's *Public Finance Risks*

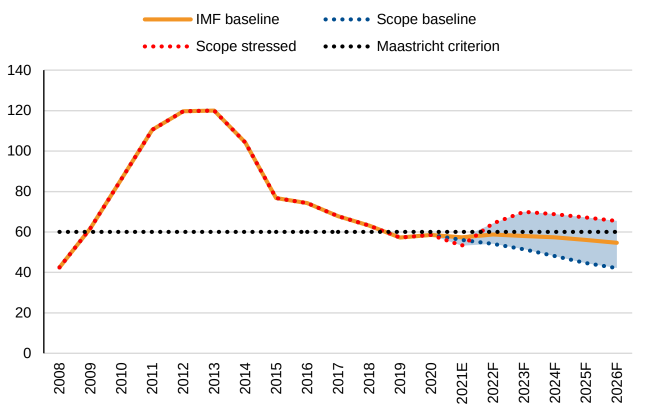
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
aa	Fiscal policy framework	Neutral	0	Prudent fiscal policies with strong fiscal framework; appropriate fiscal response to Covid-19 crisis
	Debt sustainability	Neutral	0	Declining public sector debt levels; debt trajectory vulnerable to adverse shocks
	Debt profile and market access	Neutral	0	Strong market access and debt structure, liquid cash reserves, access to lenders of last resort

Contributions to changes in debt levels, pps of GDP



Source: Scope Ratings GmbH

Debt-to-GDP forecasts, % of GDP



Source: Scope Ratings GmbH

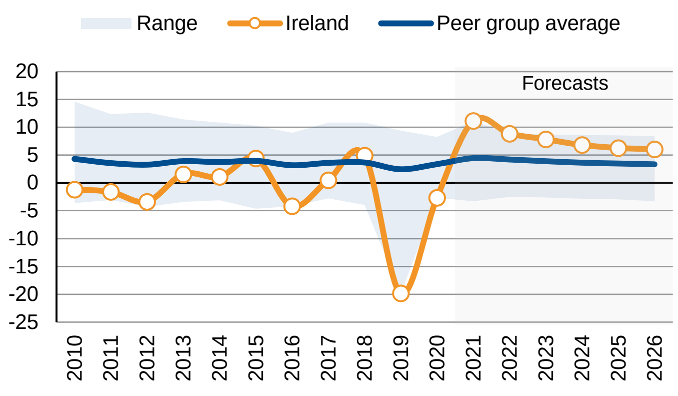
External Economic Risks

- **Current account:** After a moderate deficit of 2.7% of GDP in 2020, Ireland's current account balance swung back to an estimated 13.9% surplus in 2021, following a strong rebound in net exports. The volatility in the current account balance reflects distortions from large scale multinational enterprises (MNE) operations linked to manufacturing and intellectual property imports. Ireland's trade surplus with the United Kingdom reached EUR 17.5bn in 2021, a 55.5% increase from 2020, though the upcoming implementation of checks on goods exports from the EU to the UK should weigh on the Irish trade surplus, especially in the agri-food sector. Direct trade links to Russia are moderate, at about 1% of total exports. The Ukraine war should still weigh on the trade balance, however, mainly through heightened energy and fertilizer prices, as well as through a reduction in demand from Ireland's main trading partners. Looking forward, we expect the current account balance to remain largely positive thanks to strong external demand for the pharmaceutical and information and communication technology sectors.
- **External position:** Ireland's gross external debt is high, albeit declining, at about 685% of GDP as of Q4 2021, down from about 1,000% around 2011. The net international investment position improved to -138% of GDP at end-2021, up from -171% at end-2020. The large, negative net international investment position largely reflects the positions of the financial sector as well as intra-company loans operated by MNEs.
- **Resilience to shocks:** Euro area membership strengthens Ireland's resilience to short-term shocks. Still, the country's small, open economy is highly integrated in global financial markets and is exposed to short-term external shocks, related to the tightening of global financial conditions or to changes in the international tax system such as the OECD-sponsored 'base erosion and profit shifting' reform.

Overview of Scope's qualitative assessments for Ireland's *External Economic Risks*

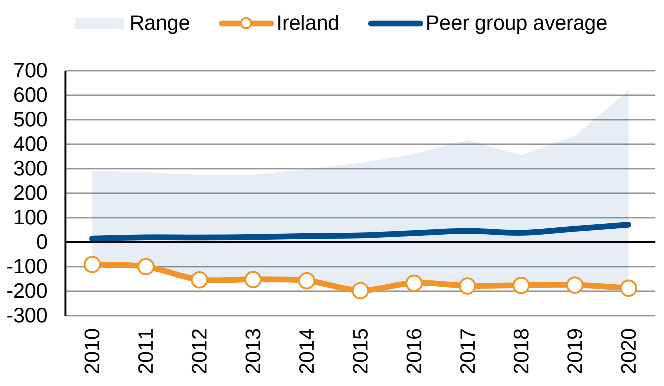
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
bb-	Current account resilience	Weak	-1/3	Volatile current account due to contract manufacturing and intellectual property-related imports; FDI inflows supported by Brexit but longer-term risks from global corporate tax rule changes
	External debt structure	Weak	-1/3	External debt levels much higher than peers'; significant short-term external debt
	Resilience to short-term shocks	Weak	-1/3	Benefits from euro-area membership but exposed to global shocks

Current account balance, % of GDP



Source: IMF, Scope Ratings GmbH

Net international investment position, % of GDP



Source: IMF, Scope Ratings GmbH

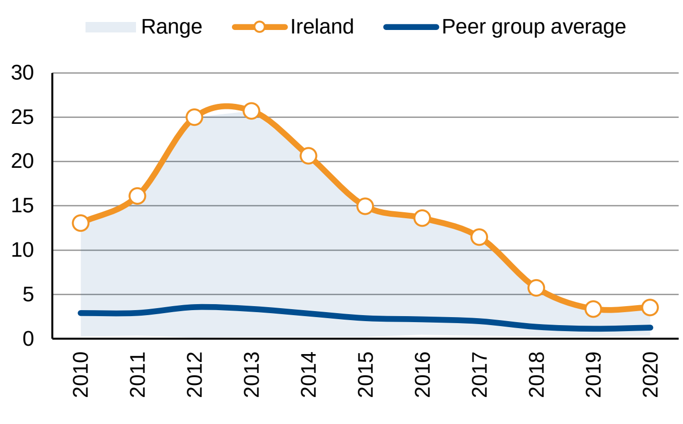
Financial Stability Risks

- **Banking sector:** The Irish banking sector recovered well from the Covid-19 crisis, generating a comfortable aggregate return on equity ratio of 7.6% in Q4 2021, after registering its first year of losses in 2020 since the 2008 financial crisis due to high provisions. Following a moderate decline, the Tier-1 capital ratio edged above its pre-crisis level to 20.8% at end-2021, well above the EU average of 17%. The non-performing loans (NPL) ratio returned to its pre-crisis declining trend, decreasing to 2.8% at end-2021, down from 3.4% in 2020. The upcoming exit of two foreign entrants – Ulster Bank and KBC Ireland – should reduce competition and support margins. Banking system exposures to Russia are low, at EUR 1.7bn, or 0.1% of total on and off-balance sheet financial assets and liabilities of Irish banks.
- **Private debt:** Household balance sheets improved significantly, in large part due to government support measures, as reflected in a declining household debt to disposable income ratio of 99.7% in 2021 Q3, the lowest level on record. Household savings stood at EUR 27bn at end-2021, more than double their pre-pandemic level. Non-financial corporates debt as a share of GDP declined steadily in recent years, down to 165.6% of GDP, though this largely reflects the influence of MNE activity on GDP growth. Despite these improvements, private-sector debt remains elevated, at 196.9% of GDP, well above the 160% EU private sector debt sustainability threshold.
- **Financial imbalances:** After moderating in 2020 due to a fall in transactions, the rise in residential real estate prices accelerated again in recent months in a context of limited supply, up to a year-on-year increase of 15.3% in February 2022. The recent rebound in construction is expected to be hindered by rising building costs, which should in turn hamper the rebalancing of housing supply. To avoid unsustainable mortgage debt levels, the Central Bank of Ireland implements macroprudential measures including limits on loan-to-value and loan-to-income ratios. The size of the Irish financial sector stands at an all-time high compared with the country's domestic economy, amounting to more than EUR 6.7tn in 2020 (32 times the GNI).

Overview of Scope's qualitative assessments for Ireland's *Financial Stability Risks*

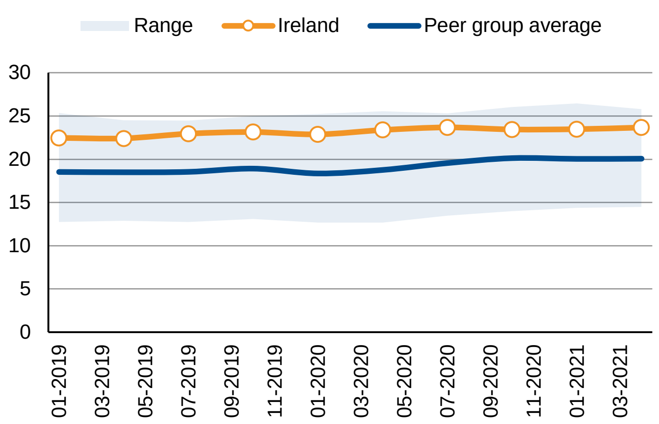
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
aaa	Banking sector performance	Neutral	0	Significantly improved banking-system resilience over last decade, but low profitability and high NPLs when compared with peers
	Banking sector oversight	Neutral	0	Oversight under the Central Bank of Ireland and the ECB as part of Banking Union
	Financial imbalances	Weak	-1/3	Elevated private-sector debt, risks from global financial-market interconnections and increasing size of Irish financial system

NPLs, % of total loans



Source: IMF, Scope Ratings GmbH

Tier 1 ratio, % of risk-weighted assets



Source: IMF, Scope Ratings GmbH

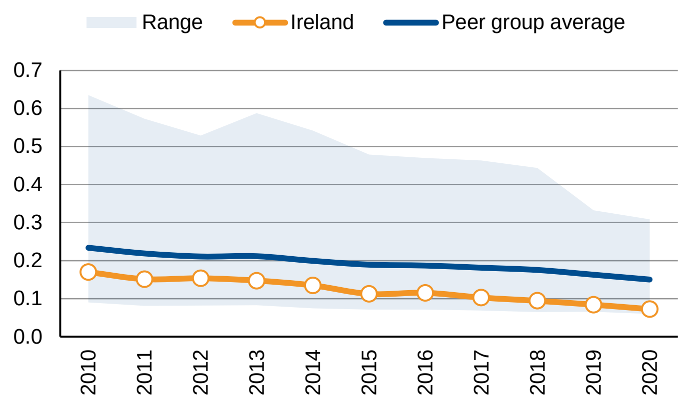
ESG Risks

- **Environment:** Ireland's environmental sustainability record is mixed, with one of the highest per capita greenhouse gas emissions in the EU. Its energy mix remains largely fossil fuel based and is dominated by oil (51.7%) and gas (17.5%). The government has adopted ambitious climate goals, aiming to reduce carbon emissions by 51% by 2030 and to attain climate neutrality by 2050. It has rolled out several policies to this end, including large scale investments in renewable energy generation capacities, and a carbon tax, currently valued at EUR 41 per tonne, with the commitment to raise it to EUR 100 per tonne by 2030. It also recently launched a National Retrofitting Scheme aimed at boosting homes' energy efficiency.
- **Social:** Ireland benefits from more favourable demographic trends than its rating peers and is expected to maintain one of the lowest old-age dependency ratios in the EU in the coming decades. The European Commission expects age-related expenditures to increase to 19.4% of GDP by 2070, well below the EU average (25.9%). The country faces significant socially-related credit challenges compared to peers, however, as reflected in a high share of the population at risk of poverty or social exclusion and a high share of young people neither in employment nor in education and training. The gender employment gap is high, at 12pps, 1.1pps above the EU average and well above that of peers including the Netherlands (8.9pps), Austria (8.4pps) or Finland (2.9pps)
- **Governance:** Ireland benefits from a stable political environment and is currently led by its first grand coalition between rival conservative parties Fianna Fáil and Fine Gael and the Green party. Current Taoiseach Micheál Martin rose to the premiership in June 2020 and will hand over the leadership to Leo Varadkar at the end of 2022, as part of a rotating premiership arrangement. The ruling coalition has come under strain in recent months, however, after a string of political scandals and voter dissatisfaction with the government's handling of long-standing challenges related to housing shortages and healthcare.

Overview of Scope's qualitative assessments for Ireland's *ESG Risks*

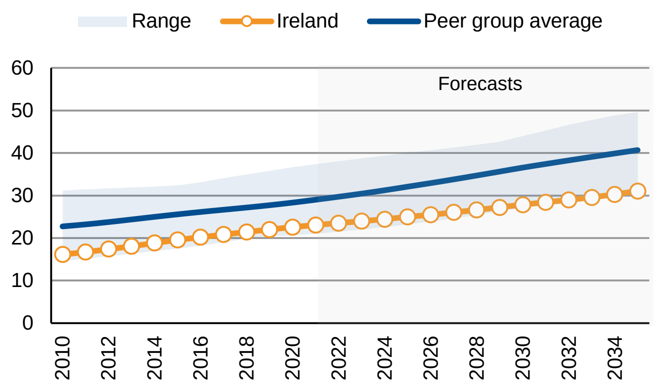
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
aaa	Environmental risks	Neutral	0	Mixed record on environmental sustainability; however, ambitious climate action objectives
	Social risks	Weak	-1/3	Favourable demographics, but moderate income inequality and risks from social exclusion
	Institutional and political risks	Neutral	0	Stable political environment under the nation's first grand coalition

CO2 emissions per GDP, mtCO2e



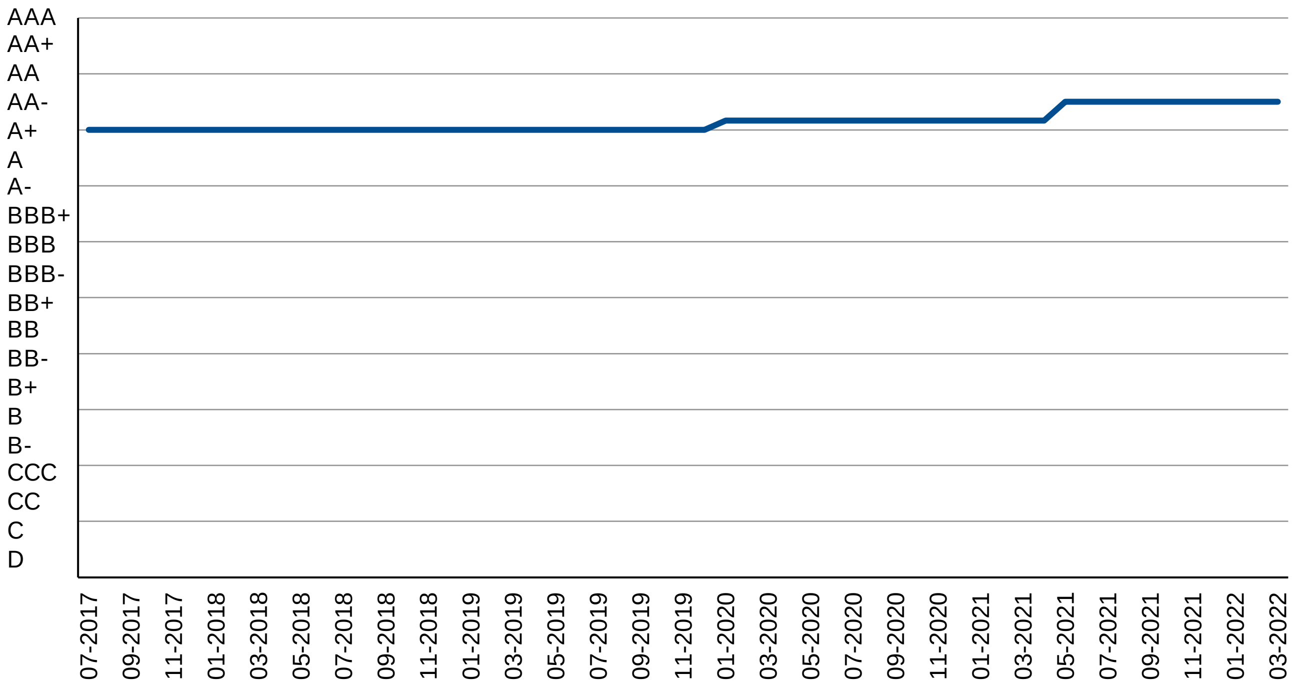
Source: European Commission, Scope Ratings GmbH

Old age dependency ratio, %



Source: United Nations, Scope Ratings GmbH

Appendix I. Rating history



Appendix II. Rating peers

Rating peers are related to sovereigns with an indicative rating in the same rating category or in adjacent categories per Scope's Core Variable Scorecard.

Peer group*
Austria
Denmark
Estonia
Finland
Germany
Ireland
Luxembourg
Netherlands
Norway
Sweden
Switzerland

Publicly rated sovereigns only; the full sample may be larger.

Appendix III. Statistical table for selected CVS indicators

This table presents a selection of the indicators (24 out of 29) used in Scope's quantitative model, the Core Variable Scorecard.

	2016	2017	2018	2019	2020	2021E	2022F	2023F
Domestic Economic Risk								
GDP per capita, USD 000s'	62.6	69.5	78.8	80.6	85.2	102.4	108.2	114.8
Nominal GDP, USD bn	298.8	335.3	385.2	399.2	425.5	516.3	550.5	590.1
Real growth, %[1]	2.0	8.9	9.0	4.9	5.9	13.5	5.2	5.0
CPI inflation, %	-0.2	0.3	0.7	0.9	-0.5	1.9	5.7	2.7
Unemployment rate, %[1]	8.4	6.7	5.8	5.0	5.8	6.3	5.2	5.3
Public Finance Risk								
Public debt, % of GDP[1]	74.3	67.8	63.2	57.3	58.5	56.1	54.1	51.5
Interest payment, % of government revenue	8.2	7.5	6.2	5.1	4.4	4.2	4.3	3.9
Primary balance, % of GDP[1]	1.5	1.5	1.6	1.6	-4.0	-1.2	0.2	0.6
External Economic Risk								
Current account balance, % of GDP	-4.2	0.5	4.9	-19.9	-2.7	13.9	10.2	8.4
Total reserves, months of imports	0.10	0.11	0.11	0.10	0.13	-	-	-
NIIP, % of GDP	-166.3	-177.8	-175.9	-174.4	-187.3	-	-	-
Financial Stability Risk								
NPL ratio, % of total loans	13.6	11.5	5.7	3.4	3.5	-	-	-
Tier 1 ratio, % of risk weighted assets	25.4	23.5	23.4	23.1	23.4	23.7	-	-
Credit to private sector, % of GDP	48.4	44.3	40.8	36.0	32.4	-	-	-
ESG Risk								
CO^2 per EUR 1,000 of GDP, $mtCO^2e$	115.7	103.1	94.6	84.5	72.9	-	-	-
Income quintile share ratio (S80/S20), x	5.2	4.8	-	-	-	-	-	-
Labour force participation rate, %	72.9	72.9	73.2	73.5	-	-	-	-
Old age dependency ratio, %	20.2	20.8	21.4	22.0	22.6	23.1	23.5	24.0
Composite governance indicator[2]	1.4	1.4	1.4	1.3	1.4	-	-	-

[1] Forecasted values are produced by Scope and may differ from those presented in the charts of the previous sections
[2] Average of the six World Bank Governance Indicators
Source: European Commission, IMF, World Bank, Central Bank of Ireland, Scope Ratings GmbH

Appendix IV. Economic development and default indicators

IMF Development Classification	Advanced economy
5y USD CDS spread (bps) as of 22 April 2022	16.4

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