Introduction to the Irish economy: Economic Growth

Economic Growth

Economic Growth is defined as an increase in the (value) amount of goods and services produced in the economy in a given period, usually one year (this measure can be adjusted for inflation). The opposite of economic growth is when the economy is contracting or getting smaller. This is called a recession. A recession is typically defined as two consecutive quarters of economic contraction. Economic growth is usually associated with rising living standards, while periods of recession (where the total value of goods and services is getting smaller) are often associated with falling living standards.

Measuring Economic Growth

GDP

Gross Domestic Product ('GDP') is one way of measuring total economic activity. It adds up the total value of goods and services produced in the domestic economy, irrespective of whether domestic or foreign firms produce them. It can be calculated by adding up total consumption, investment, and Government spending in the economy. Net Exports (Exports minus Imports) are also included. While GDP may not be the best measure of economic activity in the Irish economy it is the standard measurement used by many international bodies, including the European Commission and the International Monetary Fund ('IMF'), to track how economies are performing over time and to compare the size of various economies.

GNP

Gross National Product ('GNP') is a slightly different way to measure economic activity. Gross National Product is calculated the same way as GDP however, it excludes net factor income. Net factor income takes into account money coming into the country from abroad (such as money earned by Irish companies based overseas) and excludes money that leaves Ireland (such as profits of multinationals being repatriated abroad).

In the past, GNP was considered a better measure for the Irish economy than GDP as the large number of multinationals in Ireland meant that significant profits were repatriated abroad. However, in recent years many issues have arisen that meant that both GDP and GNP weren't reflective of the underlying economic activity. This led to the development of new metrics to capture growth in the economy.

GNI*

By adjusting for subsidies received by Ireland from the European Union ('EU') and the taxes paid to the European Union, we arrive at a measure called Gross National Income ('GNI'). The Central Statistics Office ('CSO') also produce a series called Modified Gross National Income (GNI*)[1]. In 2015, there were significant imports of intellectual property assets into Ireland. The way these assets are treated in the national accounts caused GDP to increase by more than 25%. Modified GNI was created in response to this to help capture underlying growth in the economy by excluding distorting effects, such as the depreciation on Intellectual Property ('IP') and on leased aircraft. GNI* also excludes the net factor income of redomiciled Publicly Limited Companies (PLCs).

1 CSO, *Modified GNI*.

Modified Gross National ('GNI*') is:

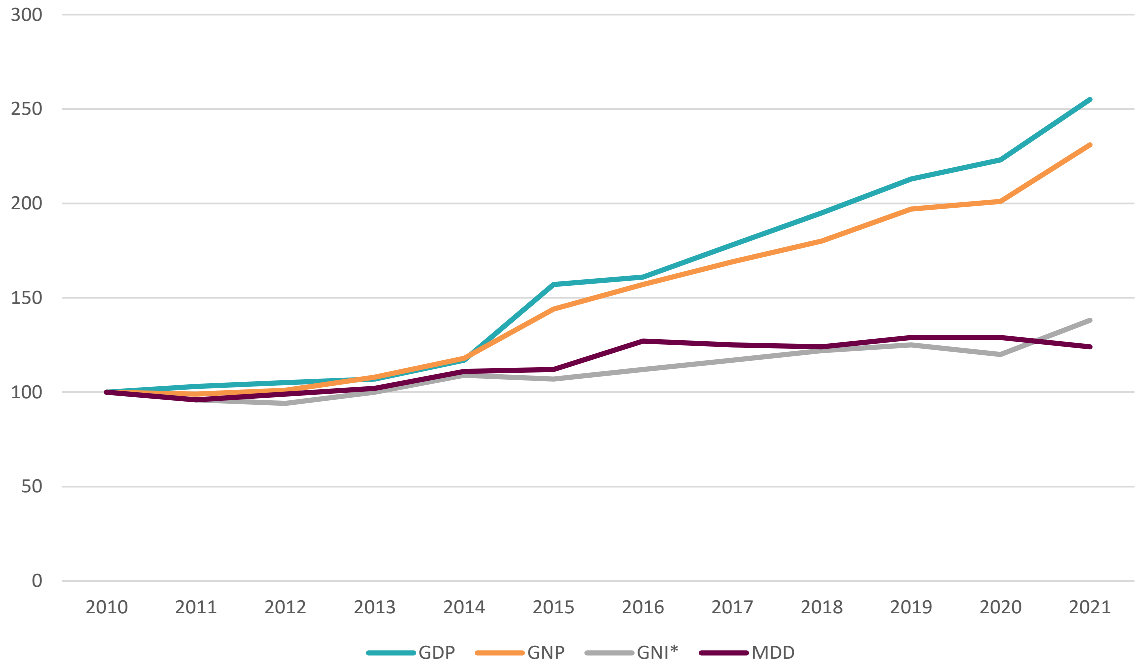
- GNI
- Minus the depreciation on Intellectual Property
- Minus the depreciation on leased aircraft
- Minus the net factor income of redomiciled PLSs.

There are some potential drawbacks to using GNI* as a measure of economic activity in Ireland. GNI* statistics are only produced on an annual basis; quarterly data is not available. In addition, GNI* is calculated in a top-down manner, by subtracting items from headline GDP, rather than by modifying the components of GDP. As noted by the Central Bank of Ireland, this means it is not possible to identify the contribution of specific sectors of the Irish economy to overall GNI*[2].

MDD

Modified Domestic Demand measures all spending by households and Government, and modified investment (total investment excluding some aircraft purchases and Intellectual Property investments). Unlike GNI*, it is produced quarterly and can provide regular updates on the economy's performance. However, it does not capture the contribution of net exports, which positively impact the underlying economy.

Figure One: Irish Economic Growth - GDP, GNP, GNI* & MDD



Indexed to 2010 (2010 = 100).

2 Central Bank of Ireland, *The Disconnection of GDP from Economic Activity Carried out in Ireland*.