REPUBLIC OF IRELAND

Rating Analysis - 9/27/12
Debt: EUR169.3B

EJR Sen Rating(Curr/Prj) BB/ N/A
EJR CP Rating: A3
EJR's 1 yr. Default Probability: 3.0%

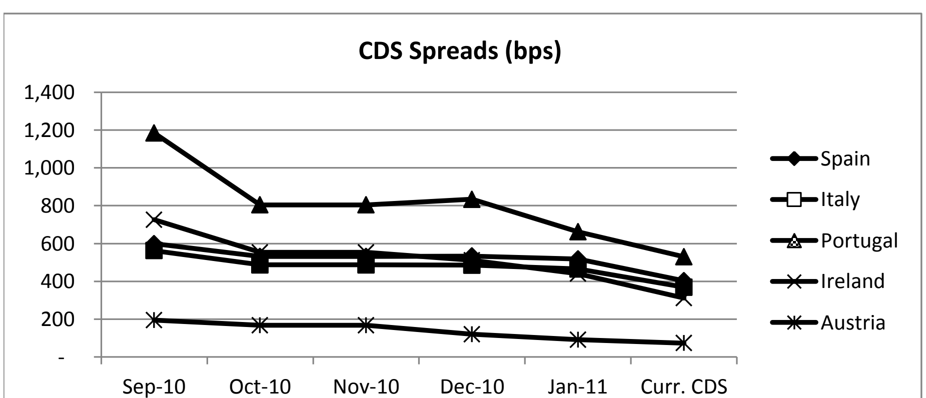
Too little, too late? The key issue is whether the Republic of Ireland can grow its way out of its troubles. IRE has seen its debt to GDP rise from merely 25% in 2007 to 108% as of 2011 because of the cost of bailing out its banks. For the FYE 2011, the deficit was 11.7% of GDP or a total of EUR18B. The markets were elated when IRE reported some GDP growth recently. However with the high likelihood of continued annual deficits, the Republic of Ireland will continue to be dependent on the largesse of the ECB and the EU. The core question is whether Ireland can grow its way out of difficulties. Our view is that it will be extremely difficult; under current conditions, Ireland would have to grow at nearly 10% per annum which is unreasonable. On the budget side, it will be difficult to significantly grow revs in a low growth economy and to shrink expenses. The key item is reducing the overall level of debt; debt in excess of 80% restricts growth and distorts the economy. We expect that IRE will continue to receive assistance but that it will conclude that restructuring debt (or transferring it to the EU) is the most palatable option.

The banks caused Ireland's financial crisis and remained troubled. Allied Irish has a market cap of $33.7B. The Irishgovernment has injected roughly €22 billion in capital into the banks, as reported by the IMF. We are affirming at "BB".

INDICATIVE CREDIT RATIOS	2009	2010	2011	P2012	P2013	P2014
	Annual Ratios (source for past results: IMF)					
Debt/ GDP (%)	65.1	92.5	108.2	132.4	139.8	162.3
Govt. Sur/Def to GDP (%)	-14.0	-31.2	-13.1	-26.8	-10.2	-25.1
Adjusted Debt/GDP (%)	65.1	89.4	105.2	129.3	136.8	159.3
Interest Expense/ Taxes (%)	9.1	14.2	13.7	13.5	16.3	16.8
GDP Growth (%)	-4.5	0.2	2.8	0.8	0.8	0.7
Foreign Reserves/Debt (%)	0.4	0.2	0.2	0.2	0.2	0.1
Implied Sen. Rating	BB	B+	BB-	B	B+	CCC-

INDICATIVE CREDIT RATIOS	AA	A	BBB	BB	B	CCC
Debt/ GDP (%)	45.0	55.0	75.0	85.0	95.0	145.0
Govt. Sur/Def to GDP (%)	4.0	1.0	-2.0	-5.0	-8.0	-10.0
Adjusted Debt/GDP (%)	40.0	50.0	60.0	80.0	120.0	150.0
Interest Expense/ Taxes (%)	7.0	9.0	12.0	15.0	22.0	26.0
GDP Growth (%)	4.0	3.0	2.0	1.0	-1.0	-5.0
Foreign Reserves/Debt (%)	25.0	20.0	15.0	12.0	9.0	7.0

PEER RATIOS	S&P Sen.	Debt as a % GDP	Govt. Surp. Def to GDP (%)	Adjusted Debt/ GDP	Interest Expense/ Taxes %	GDP Growth (%)	Ratio-Implied Rating*
Federal Republic Of Germany	AAA	81.4	-1.0	92.1	11.1	1.9	BBB-
Republic Of Austria	AA+	72.4	-2.6	84.1	9.4	0.4	BBB-
Kingdom Of Spain	BBB+	68.5	-8.5	80.8	12.3	0.4	BB
Republic Of Italy	BBB+	120.0	-3.9	131.2	16.7	-0.5	B
Portugal Republic	BB	106.8	-4.2	117.5	13.0	-3.0	B+



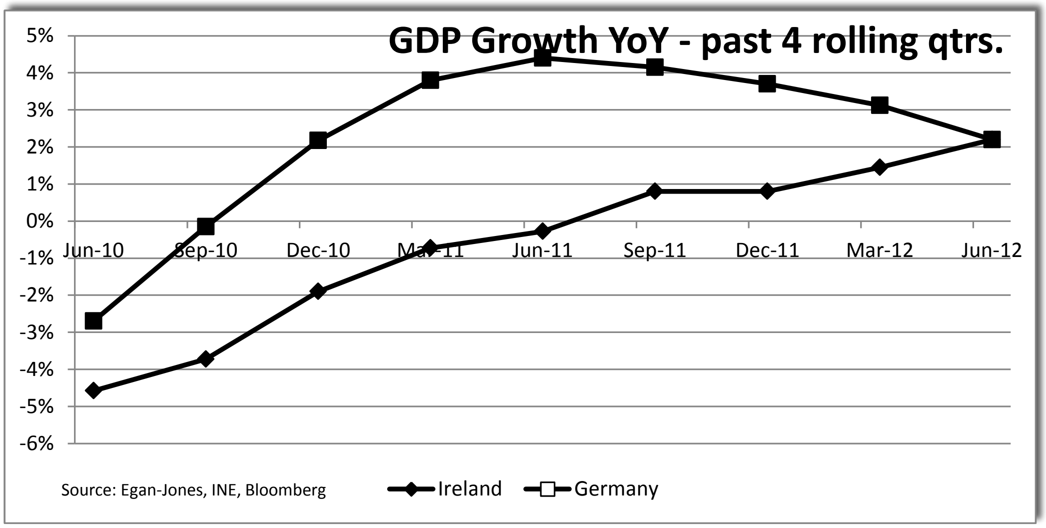
Country (EJR Rtg*)	Current CDS	Targeted CDS
Spain (C)	403	5,000
Italy (C+)	370	4,300
Portugal (CCC+)	531	1,500
Ireland (BB)	312	800
Austria (BBB+)	74	200

* Projected Rating
* EJR's targeted CDS based on rating

Economic Growth

Economic growth has been anemic, averaging less than 2% on an annualized basis. The recent low point was a 10.8% decline in GDP in 2009. On the positive side, four rolling quarter GDP growth has been regularly improving As can be seen in the below chart. be negative on an inflation-adjusted basis while costs on every-day items continue to rise. A major concern continues to be tepid economic growth and an overhang from the pending retirement of the baby boom generation.

Ireland has the advantage of a well-educated population, low taxation, and proximity to the EU market. The major drag on economic growth has been the massive debt the country took on to bail out its banks; the debt has resulted in austerity measures, higher taxes, and reduced growth. A major factor for prospective growth will be the health of the EU.



Fiscal Policy

Irish fiscal policy is a disconcerting with a deficit to GDP at 13.1% and debt to GDP of 108.2%. As can be seen in the chart at right, both measures place the country in the category. Given the slow growth in the economy (i.e., near 2%) and a deficit to GDP of 13.1%, and the high debt level, Ireland will be hard-pressed to grow its way out of its problems. The actions of the ECB are probably more relevant than Ireland's. actions (Ireland will need support over the next couple of years.)

	Deficit-to-GDP (%)	Debt-to-GDP (%)	5 Yr. CDS Spreads
Ireland	13.1	108.2	441
Canada	4.5	31.3	N/A
Germany	1.0	81.4	63
Spain	8.5	68.5	518
Italy	3.9	120.0	466
Greece	9.1	156.4	-

Sources: Bloomberg and IFS

Unemployment

Ireland's unemployment rate of 14.6% exceeds that of Greece and is surpassed only by Spain at 20+%. Given the high unemployment, we question whether Ireland will have the ability to significantly cut its budget deficit in the near future. Another factor which is generally not included in the statistics is the level of emigration; many of the country's brightest see better opportunities. The major driver for reducing unemployment is GDP growth.

Unemployment (%)	2010	2011
Ireland	14.6	14.6
Canada	7.6	7.5
Germany	7.4	6.8
Spain	20.3	22.9
Italy	8.3	9.2
Greece	14.2	20.7

Source: Intl. Finance Statistics

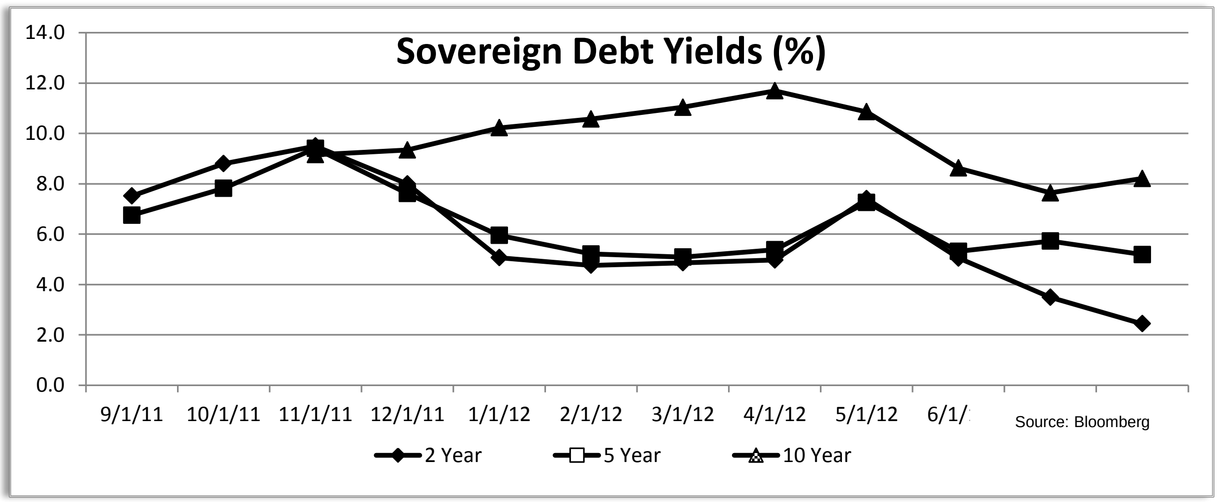
Banking Sector

The Irish Banking sector continues to be stagnant. Loan growth rates recorded by some banks have been the result of portfolio acquisitions rather than organic growth. The yield curve in the banking system continues to be on a downward trend with no abatement in sight. The ECB's actions will further depress already depressed yield curve in the banking industry. The Irish banking industry is heavily concentrated with the top two banks in equal to 187% of GDP.

Bank Assets (billions of local currency)	Assets	Cap/ Assets %
BANK IRELAND	155	6.6
ALLIED IRISH BK	137	10.6
	-	
	-	
	-	
Total	292	
EJR's est. of cap shortfall at 10% of assets less market cap		(3)
Ireland's GDP		156

Funding Costs

Despite weak credit metrics, Ireland has seen a significant decline in its funding costs over the past couple of years because of the positive GDP growth and the support of the ECB. However, as can be seen below, Ireland's 10 year funding costs is near 8%, which exacerbates the country's deficit. With the ECB's extraordinary efforts, we expect that Ireland will be able to further reduce its funding costs.



Ease of Doing Business

Major factors for growing the economy are the ease of doing business and the economic freedom; although not the sole factor for determining economic growth, a country which makes it easy for businesses to operate and provides a reasonably free environment to conduct business has a good chance for growth. The chart on the right indicates that with an overall rank of 10 (1 is best) is strong.

The World Bank's Doing Business Survey*	2012 Rank	2011 Rank	Change in Rank
Overall Country Rank:	**10**	**8**	**-2**
Scores:			
Starting a Business	13	9	-4
Construction Permits	27	28	1
Getting Electricity	90	90	0
Registering Property	81	76	-5
Getting Credit	8	8	0
Protecting Investors	5	5	0
Paying Taxes	5	5	0
Trading Across Borders	21	21	0
Enforcing Contracts	62	37	-25
Resolving Insolvency	10	9	-1

* Based on a scale of 1 to 183 with 1 being the highest ranking.

Economic Freedom

As can be seen below, Ireland is above average in its overall rank of 76.9 for Economic Freedom with 100 being best.

Heritage Foundation 2012 Index of Economic Freedom

World Rank 77*

	Rank**	2011 Rank	Change in Rank	World Avg.
Business Freedom	**92.8**	92.0	0.8	64.3
Trade Freedom	**87.1**	87.6	-0.5	74.8
Fiscal Freedom	**73.9**	72.1	1.8	76.3
Government Spending	**30.4**	47.1	-16.7	63.9
Monetary Freedom	**76.7**	80.7	-4.0	73.4
Investment Freedom	**90.0**	90.0	0.0	50.2
Financial Freedom	**70.0**	70.0	0.0	48.5
Property Rights	**90.0**	90.0	0.0	43.5
Freedom from Corruption	**80.0**	80.0	0.0	40.5
Labor Freedom	**78.4**	77.5	0.9	61.5

*Based on a scale of 1-100 with 100 being the highest ranking.

**The ten economic freedoms are based on a scale of 0 (least free) to 100 (most free).

Source: The Heritage Foundation & Wall Street Journal

Assumptions for Projections

	Peer	Issuer	Base Case	
Income Statement	**Median**	**Average**	**Yr 1&2**	**Yr 3,4,5**
Taxes Growth%	4.9	8.1	**2.0**	**2.0**
Social Contributions Growth %	1.4	(10.7)	**0.5**	**0.5**
Grant Revenue Growth %	0.0	0.0		
Other Revenue Growth %	5.0	(13.2)	**5.0**	**5.0**
Other Operating Income Growth%	0.0	0.0		
Total Revenue Growth%	4.7	0.8	**1**	**0.7**
Compensation of Employees Growth%	(1.2)	(1.0)	**(1.0)**	**(1.0)**
Use of Goods & Services Growth%	1.2	(7.7)	**(7.7)**	**(7.7)**
Social Benefits Growth%	1.7	2.0	**2.0**	**2.0**
Subsidies Growth%	(6.1)	(27.3)		
Other Expenses Growth%	(72.2)	(72.2)	**(2.0)**	**(2.0)**
Interest Expense	0.0	3.0	**3**	
Balance Sheet				
Currency and Deposits (asset) Growth%	(100.0)	0.0		
Securities other than Shares LT (asset) Growth%	(2.2)	(28.7)	**1.0**	**1.0**
Loans (asset) Growth%	14.4	27.7	**2.0**	**2.0**
Shares and Other Equity (asset) Growth%	(1.7)	(0.3)	**2.0**	**2.0**
Insurance Technical Reserves (asset) Growth%	0.0	0.0		
Financial Derivatives (asset) Growth%	0.0	16.0	**2.0**	**2.0**
Other Accounts Receivable LT Growth%	3.9	6.3	**2.0**	**2.0**
Monetary Gold and SDR's Growth %	0.0	0.0	**5.0**	**5.0**
Other Assets Growth%	0.0	0.0		
Other Accounts Payable Growth%	2.5			
Currency & Deposits (liability) Growth%	0.0	11.0	**2.0**	**2.0**
Securities Other than Shares (liability) Growth%	6.1	(5.2)	**(3.7)**	**(3.7)**
Loans (liability) Growth%	14.2	87.7	**87.7**	**78.9**
Insurance Technical Reserves (liability) Growth%	0.0	0.0		
Financial Derivatives (liability) Growth%	0.0	2,034.2	**2.6**	**2.6**
Addl debt. (1st Year) million EUR	0.0	0.0		

Base Case
ANNUAL REVENUE AND EXPENSE STATEMENT (MILLIONS EUR)

	Dec-09	Dec-10	Dec-11	PDec-12	PDec-13	PDec-14
Taxes	35,723	34,647	37,443	38,192	38,956	39,735
Social Contributions	11,986	11,475	10,251	10,303	10,354	10,406
Grant Revenue	0	0	0	0	0	0
Other Revenue	7,939	8,714	7,567	7,945	8,342	8,759
Other Operating Income	0	0	0	0	0	0
Total Revenue	55,648	54,836	55,261	56,439	57,652	58,900
Compensation of Employees	20,532	19,108	18,912	18,718	18,526	18,336
Use of Goods & Services	10,205	9,302	8,583	7,919	7,306	6,741
Social Benefits	27,169	27,106	27,636	28,176	28,727	29,289
Subsidies	893	879	639	639	639	639
Other Expenses	9,997	36,426	10,121	35,698	9,919	34,984
Grant Expense	0	0	0	0	0	0
Depreciation	2,535	2,501	2,468	2,468	2,468	2,468
Total Expenses excluding interest	71,331	95,323	68,359	93,618	67,586	92,457
Operating Surplus/Shortfall	-15,683	-40,487	-13,098	-37,179	-9,934	-33,557
Interest Expense	3,246	4,937	5,143	5,143	6,341	6,658
Net Operating Balance	-18,929	-45,424	-18,241	-42,322	-16,275	-40,215

Sources: Historical - IMF, Projections - EJR

Base Case
ANNUAL BALANCE SHEETS (MILLIONS EUR)

ASSETS	Dec-09	Dec-10	Dec-11	PDec-12	PDec-13	PDec-14
Currency and Deposits (asset)						
Securities other than Shares LT (asset)	8,700	10,110	7,206	7,278	7,351	7,424
Loans (asset)	3,358	3,489	4,456	4,545	4,636	4,729
Shares and Other Equity (asset)	21,638	23,795	23,725	24,200	24,683	25,177
Insurance Technical Reserves (asset)				0	0	0
Other Accounts Receivable LT	8,395	7,776	8,263	8,428	8,597	8,769
Monetary Gold and SDR's						
Additional Assets	29,414	18,212	18,010			
Total Financial Assets	71,915	63,988	62,363	63,178	64,009	64,855
LIABILITIES						
Other Accounts Payable						
Currency & Deposits (liability)	10,308	13,711	15,218	15,218	15,218	15,218
Securities Other than Shares (liability)	94,756	84,050	79,663	76,752	73,948	71,246
Loans (liability)	2,851	34,982	65,660	107,982	124,256	164,471
Insurance Technical Reserves (liability)	(1)	(1)	(1)	(1)	(1)	(1)
Financial Derivatives (liability)	16	38	811	832	854	876
Other Liabilities	6,179	5,566	5,282	8,986	8,986	8,986
Liabilities	114,109	138,346	166,633	209,770	226,875	267,936
Net Financial Worth	(42,194)	(74,358)	(104,270)	(146,592)	(162,866)	(203,081)
Total Liabilities & Equity	71,915	63,988	62,363	63,178	64,009	64,855

Sovereign Rating Methodology

Egan-Jones takes the perspective of the investor as its primary point of view when developing the ratings it issues for sovereigns. Therefore, in the case of sovereign ratings, we attempt to take a more holistic view of credit quality to include not only analytic comparisons of various sovereign issuers but also the impact on our quantitative and qualitative analyses by current global, sovereign, governmental and market events, including the effects of government investments in speculative, volatile or other high risk investment products. For example, many sovereign issuers have taken on significant exposures of major financial institutions over the past several years. Hence, we calculate the under-funding of financial institutions and include this amount in the total indebtedness of sovereigns. (We use a base assumption that no country can afford to allow its major banks to fail and therefore we believe that there will almost always be an intervention by either a host or allied nation should financial institutions or markets require support at some measurable level.)

Generally we devise modeling calculators and do an analysis that examines the debt load of a country with respect to its GDP and other economic indicators. The analysis is then adjusted to reflect the outlook on a myriad of factors that reflect the firm’s overall view of the sovereign debt and the quality of the country’s ability to meet and thrive under such load. Some of the qualitative factors that impact our ultimate assessment of credit quality such as the flexibility, stability and overall strength of the economy, ease of tax collection, acceptance of contract law, ease of doing business, and prospects for future growth and health. The non quant issues are generally subjective and a moving target, so each rating of a sovereign may differ because of the non-quantitative nuances being addressed. Note, debt levels for many sovereign issuers have increased over the past decade and has accelerated recently, effecting the implied ratings.

Nota Bene

History has proven that defaults on domestic public debt do occur. In fact, seventy out of three hundred twenty defaults since 1800 have been on domestic public debt (1). Egan-Jones does not view a country's ability to print its own currency as a guarantee against default. Additionally, Egan-Jones generally views cases of excessive currency devaluation as a de facto default.

1. "This Time Is Different: Eight Centuries of Financial Folly", Reinhart & Rogoff, p.111, 126