

**National
Competitiveness
Council**



Opening Statement

Professor Peter Clinch, Chair

National Competitiveness Council

for the

Select Committee on Budgetary Oversight

8 May 2019

Select Committee on Budgetary Oversight

Opening Statement by Professor Peter Clinch

Chairman, National Competitiveness Council

8 May 2019

Chair, Members of the Committee, thank you very much for inviting me here today in my role as Chair of the National Competitiveness Council (NCC). With me today is Marie Bourke, Head of the Council secretariat and Manus O' Donnell, Economist with the Council secretariat. As you are aware, the NCC has recently published 'The Cost of Doing Business in Ireland 2019' that sets out how Ireland is performing relative to competitor jurisdictions, a copy of which has also been circulated to you. I look forward, this afternoon, to our discussion on the findings of this report. I would also intend referring to the research and recommendations to Government in the Council's annual report, Ireland's Competitiveness Challenge.

National Competitiveness Council

The National Competitiveness Council was established by Government in 1997 as part of the Partnership 2000 Agreement. The Council reports to the Taoiseach and the Government, through the Minister for Business, Enterprise and Innovation, on key competitiveness issues facing the Irish economy and offers recommendations on policy actions required to enhance Ireland's competitive position.

In accordance with the European Council recommendation of September 2016 on the establishment of National Productivity Boards by euro area countries, in March 2018, the Government designated the NCC as the body responsible for analysing developments and policies in the field of productivity and competitiveness in Ireland.

The Council serves as an independent voice and, in an advisory capacity to Government, offers recommendations on areas to improve competitiveness and productivity. The Council members, who serve in a voluntary capacity, are appointed by the Minister for Business, Enterprise and Innovation and are drawn from civil society (e.g. union representatives, business representatives, business persons, and academia). These members have an interest in, and an understanding of, the factors that affect the competitiveness of the Irish economy and of the policy domains that can influence productivity levels in the economy.

The work of the Council is underpinned by research and analysis providing an evidence-base for its policy recommendations. Each year, in accordance with its Terms of Reference, the NCC publishes a number of reports:

- The Costs of Doing Business in Ireland report is a statistical report which benchmarks key business costs and highlights areas where Irish enterprise costs are out of line with key competitors;

- Ireland's Competitiveness Scorecard, which provides a comprehensive statistical assessment of Ireland's competitiveness performance including wider competitiveness indicators other than costs;
- Ireland's Competitiveness Challenge, which uses the information generated in the reports just mentioned, along with the latest research and data, to outline the main challenges to Ireland's competitiveness, and the policy areas to address these challenges;
- A Productivity Statement which tracks the productivity performance of the Irish economy.

These are the main deliverables of the Council. However, the Council also produces a series of short competitiveness bulletins, submissions and other papers on specific competitiveness issues. (e.g. electricity charges, insurance, legal costs and international competitiveness rankings). In the past the Council has made submissions to the Action Plan for Jobs and, more recently to Future Jobs 2019.

Productivity, Competitiveness and Costs

Ireland's ability to compete in international trade and sell our goods and services abroad is a key determinant of our wages, living standards and our ability to finance social services like health, education and social protection. It also allows our economy to be a successful member of the eurozone and withstand the shocks that are beyond our control. Competitiveness is part of the DNA of sustainable jobs: If we want to provide and sustain good, well-paid jobs for our citizens and ensure that these are sustainable, maintaining our competitive edge is crucial.

Competitiveness is a complex concept and results from many factors. Along with labour-force participation, two of the principal factors determining competitiveness performance are productivity and cost-competitiveness. In the medium term, productivity improvement must be the primary driver of Irish competitiveness and is the key determinant of sustainable employment, wages, living standards and the ability to finance social services.

Costs are an important key element of national competitiveness. Maintaining cost-competitiveness is critical to the overall competitiveness of firms based in Ireland and to maintain the virtuous circle between the cost of living, productivity growth and wage rates. If costs in Ireland are too high relative to productivity, it damages Ireland's competitiveness and threatens jobs. Irish businesses would find it more difficult to export, and internationally mobile firms would be disincentivised from locating here. Ultimately, prohibitive costs would make international trade and investment more expensive, reducing the Irish economy's beneficial exposure to the international economy. To be competitive, however, an economy does not need to be low-cost if it can find ways to boost productivity.

Ireland's overall economic performance indicates that we are continuing to maintain a strong competitiveness position. The recovery has continued apace. Economic growth is strong, and unemployment is relatively low. This is very good news.

However, as the economy continues to grow, ensuring our model is sustainable and balanced takes on even more significance. The risks to Ireland's prosperity are increasing. International economic uncertainty and the return to protectionist trade policy in certain key global economies, along with developments in US tax policy and an evolving international tax landscape, pose a threat to our future economic growth and stability.

Domestically, a small fraction of firms provides the major part of Ireland's productivity performance, value added, exports, and corporate tax receipts, disguising the majority of under-performing firms where productivity growth is stagnant or falling. The narrow range of exporters, products and services exported, and the reliance on a small number of export markets, pose serious concerns.

The vulnerabilities in the fabric of the Irish economy, coupled with the challenging global environment, endanger the hard-won medium-term sustainability of our economy. It has never been more important in the economic life of our country, that these vulnerabilities are recognised and diagnosed, and that government policy strengthens our productivity performance and competitiveness to secure Ireland's future prosperity.

The Council tracks the three main international competitiveness indicators for Ireland:

- the World Economic Forum Global Competitiveness Report;
- the World Bank Ease of Doing Business; and,
- the Institute for Management Development World Competitiveness Rankings.

While Ireland still ranks highly in these indices, we have been falling down the rankings in recent years. In the 2018 IMD World Competitiveness Yearbook Report, Ireland is ranked 12th (out of 63 countries), a fall of six places on 2017 rankings. In addition, Ireland fell six places from 17th to 23rd in the latest World Bank's annual "Ease of Doing Business report 2019". Ireland is ranked 23rd out of 140 countries in the World Economic Forum Global Competitiveness Report.

Ireland's Competitiveness Challenge 2018

The Council's Competitiveness Challenge report, published in December 2018, identifies a range of recommendations that addresses both immediate competitiveness issues, and more medium-term challenges aimed at enhancing Ireland's competitiveness and productivity performance. As in previous years, the Council has sought to strike a balance between addressing issues that are well-known, (e.g. housing, climate action and the availability of talent), with challenges that are emerging, (e.g. traffic congestion) and the combined hidden costs of proposed regulation (e.g. the new water tariff regime, water abstraction, work-life balance and pension reform). Three overarching themes are considered:

1. Ensuring the sustainability of the economic model
2. Maintaining Cost Competitiveness

3. Narrowing the productivity gap between the “best and the rest”

The Cost of Doing Business Report 2019

The Council published the Cost of Doing Business in Ireland report on the 12th of April last. As mentioned, the report has two main aims, to:

- flag any areas where business costs in Ireland out-of-line with our international competitors; and,
- build the evidence base for the NCC’s Competitiveness Challenge document, which makes recommendations regarding the areas of policy emphasis to deal with competitiveness issues.

The report achieves this by benchmarking the Costs of Doing Business in Ireland relative to international competitors using the latest available data on various cost indicators.

Headline Results

The report describes the overall cost profile in Ireland as ‘high-cost, slowly increasing’.

In 2018, prices in Ireland increased by 0.7%. This was the slowest rate of inflation of all euro area economies, and it was the joint slowest rate of price increases in the EU (alongside Denmark). Inflation was faster than in previous years (in 2017, prices in Ireland rose by just 0.3%), but still well below the price growth rate for the euro area as a whole, (1.8%) and the UK, (2.5%). The fact that our low growth is below comparator countries is very welcome from a cost competitiveness perspective.

However, we note that Ireland remains an expensive location. So, while average prices are increasing slowly, they are doing so from a comparatively high base.

The report identifies a number of emerging pressure points in our economy which have the potential to significantly erode our competitiveness further. The major cost factors for Irish businesses are labour costs, the rental price of commercial property, interest rates, and the continued increase in insurance costs.

Labour Cost

Labour costs (€30.90/hour) in Ireland are broadly in line with the euro area average but above the UK (€25.70). Labour costs grew by 2.9% in 2018 – four times faster than the rate of inflation (0.7%).

Labour costs vary considerably between different sectors in Ireland. The latest Eurostat data (2018) shows labour cost in certain sectors in our economy are also out of line with UK and euro area, for example, in the Utility sector (electricity and gas), labour costs are €53/hr in Ireland compared to €37/hr in the UK and €48/hr

in the euro area and, in the ICT sector, labour costs are €47/hr in Ireland, €35/hr in the UK and €41/hr in the euro area.

In 2018, in most sectors of the economy, labour costs were greater than, or equal to, the UK. Hourly labour costs in Ireland grew by 6.1%, 4.5% and 4.3% in the ICT, Construction and Financial sectors respectively compared to 4.1%, 5.4% and 2.4% in the UK.

Property Costs.

Residential property prices are now roughly where they were at the start of 2005. The average rent in Dublin was €1,527 in Q1 2018. Similarly, rents have also been growing since 2013 and have been increasing by over 5% per annum for the last four years.

Over the last year, there has also been a steady increase in commercial property prices and the cost of constructing office space. In 2018, the construction cost per square metre of a prime office building in Dublin was \$3,065, lower than London (\$3,919) but above cities like Amsterdam (\$2840) and Munich (\$2798). In the office rental market, in the last five years, prices are up 15.9% in Dublin Suburbs and up 16.5% in Galway.

Transport Costs

In recent years, aggregate transport-sector prices in Ireland have increased moderately. In 2018, the average prices per litre of petrol and diesel were €1.43 and €1.34 respectively. Over the course of 2018, petrol prices increased by 2.8% and the price of diesel increased by 4.6%.

Traffic has increased across the road network (3%) and traffic congestion in the cities has worsened as highlighted by the fact that 11% of all commuters spend an hour or more commuting to work in 2017. The TomTom Traffic Index, which measures congestion on the road networks across 390 cities across the world, found that, in 2017, the congestion level in Dublin (43%) was higher than major European cities like London (40%), Paris (38%) and Brussels (38%). This is a form of 'hidden inflation' which is not picked up in price indexes.

Utility Costs

Utility prices have fallen due to the fall in global oil prices. Electricity prices in Ireland have fallen (0.8%) since the first half of 2014 but in the first six months of 2018 remain higher than the UK and euro area average.

Similarly, gas prices in Ireland have also fallen (13%) since the first six months of 2014, however, the fall was lower than in the euro area (25%) and the UK (36%). So, this would point to a relative competitiveness loss.

Credit and Financial Costs

Businesses in Ireland face higher interest rates than the average business in the euro area. The cost of credit remains very high compared to the euro average. In 2014 Irish companies faced a similar interest rate (3%) to counterparts in Germany and France, whereas now the rate is higher for Irish companies at 3.3% and lower in these economies (2%). This means that an Irish business faces costs that are 65% higher than their EU counterparts.

Business Services and Input Costs

The service sector continues to be the main source of upward price pressure, as it has continued to rise since early 2015. The CSO Services Producer Price Index, which measures changes in the average level of prices charged by producers, shows that prices for a range of business services (e.g. freight transport by road, postal and courier activities, computer programming and consultancy, legal, accounting and consultancy, advertising and market research services) have been increasing in Ireland. In the year to 2018, service producer prices increased by 3.1 % in Ireland and were 7 % higher relative to 2015. In comparison, the corresponding figures for Euro area was 1 % and 1.8 %.

Tax Rates

The Irish average tax rate for those earning the average income is low compared with other OECD countries. However, the marginal tax rate for a person earning the average wage is the second highest marginal tax rate at 49% among the high-income OECD countries.

The Council acknowledges the measure introduced in Budget 2019 which raised the entry point for the higher rate of income tax from €34,550 to €35,300 (single worker). We must continue to reform our tax system and make it internationally competitive so that Ireland continues to attract highly qualified international talents on these shores.

Conclusion

To conclude - the 'Cost of Doing Business in Ireland 2019' report gathers information and provides a snapshot of the cost profile in Ireland. It is a significant input into the subsequent analysis of policy implications and associated structural reforms required to address Ireland's cost base, which are included in our report Ireland's Competitiveness Challenge published annually.

In the Challenge report we published last December, these were addressed under the theme of "Maintaining Cost Competitiveness", along with other recommendations to address the challenges under the other two themes of:

- "Ensuring the sustainability of the economic model" and
- "Narrowing the productivity gap between the 'best and the rest'".

Some of the key recommendation relating to cost competitiveness, included in the report, relate to measures to address housing affordability through the intensified delivery of housing supply measures in the Rebuilding Ireland Action Plan, expediting the implementation of the recommendations from the Cost of Insurance Working group, the need to develop sectoral-level data on water and waste and the development of a more comprehensive and representative data set on the cost of legal services.

I would like to acknowledge the absolute commitment shown by Government in relation to improving Ireland's productivity and competitiveness through various policies and initiatives including the actions to be progressed in 2019 in the Government's Future Jobs initiative. The Council greatly welcomes the publication by the Government of the Future Jobs Plan and believes it is an important policy document for framing enterprise and economic policy in the years ahead. The Council will continue to advocate for competitiveness and productivity to be central pillars of our economic policy.

I would like to thank the Chair and the Committee for affording the Council the opportunity to meet today. I am looking forward to our discussions.

ENDS