

PRESS RELEASE

24th April 2015

Euro weakness masks domestic cost increases

National Competitiveness Council publishes Costs of Doing Business in Ireland 2015

The National Competitiveness Council (NCC) today launched its *Costs of Doing Business in Ireland 2015* report which was conducted as part of the Governments' *Action Plan for Jobs 2015*. The Costs of Doing Business in Ireland report benchmarks key business costs across over 50 indicators and focuses on areas where Irish enterprise costs are out of line with key competitors. The report concentrates on costs that are largely domestically determined such as labour, property, energy, water, waste, communications and business services, and considers both price levels, and changes in those levels (i.e. price inflation).

The report finds that while costs have fallen significantly since 2009, Ireland remains an expensive location in which to do business, relative to some of our key competitors. Ireland is also the 3rd most expensive location in the euro area for consumer goods and services.

While, in relative terms, Irish cost competitiveness is improving (i.e. although costs are increasing, they are increasing at a slower rate than in many of our competitors), this improvement is largely being driven by external factors beyond the control of domestic policymakers: a weak euro foreign exchange rate, low interest rates, and low international fuel prices have all combined to improve Irish cost competitiveness.

A number of upward domestic cost pressures are now emerging, however, particularly in relation to labour, property and business services. The report concludes, therefore, there is a need to refocus efforts on minimising domestically controllable costs to the extent possible.

Further, the report highlights the difficulty of achieving further cost reductions against a backdrop of low inflation throughout the EU, and the significant risk that recent competitiveness gains will be eroded as economic growth strengthens.

Speaking at the launch of the report, Professor Peter Clinch, Chair of the Council commented "It is vital that we continue to take action to address unnecessarily high costs wherever they arise. In this regard, there is a role for both the public and private sectors alike to manage proactively their cost base and drive efficiency, thus creating a virtuous circle between the costs of living, wage expectations, productivity and cost competitiveness."

He continued "Recent price falls in Ireland are at risk of being reversed as the economy returns to growth and demand increases. Already there are warning signs and domestically determined cost competitiveness is no longer improving. The Irish economy should not rely on benign currency movements to protect our international competitiveness. To allow our companies to compete, and to support growth and jobs, we must minimise those costs over which we have some degree of control. Ultimately, productivity growth must be the basis for economic prosperity – only productivity growth can facilitate improvements in living standards and deliver sustainable employment, whilst simultaneously protecting our competitiveness relative to key competitors".

In the 2014, the Council set out a range of cost-related recommendations, including recommendations designed to enhance labour cost competitiveness (e.g. through reform of income taxes, changes to the PRSI structure for lower paid workers, actions to improve replacement rates for those who face high rates); to

reduce energy costs (by tackling controllable costs and taking measures to enhance energy efficiency and manage peak demand); and to manage property costs (by replacing commercial rates with a site value tax and supporting the long-term development of the property sector). These recommendations will be revisited, and new recommendations for structural reform will be developed in the Council's Competitiveness Challenge 2015 report which will be produced in the second half of this year.

Key Findings

Labour Costs

- Gross and net earnings are the 8th highest in the euro area. Gross earnings are below euro area averages but net earnings are 11.6% above average.
- Following a number of years of marginal decline, Irish labour costs increased in 2012 (+2.2%) and 2013 (+0.7%). In the first two quarters of 2014, labour costs grew by 1%. These rates are less than the euro area average.
- Strong growth in labour costs in Ireland has been recorded in manufacturing and ICT sectors.
- Irish unit labour costs, which measure the average cost of labour per unit of output (and thus capture both cost and productivity changes) increased by 1% in 2013, after several years of improvements.
- Nominal unit labour costs (ULCs) grew at a slower rate than in the euro area, representing a slight improvement in Irish competitiveness. This trend is expected to continue in 2015 and 2016.
- Ireland has the 4th highest national minimum wage in the euro area (measured in euro terms), and the 9th highest when expressed as a percentage of average gross monthly earnings.
- The cumulative impact of increases in income taxes, changes to bands, the introduction of the Universal Social Charge etc. have weakened competitiveness since the onset of recession.
- However, taxes and social insurance rates for married couples with children, particularly for those on the average wage, remain competitive.

Property Costs

- Following several years of significant cost reductions – in terms of both construction and rental costs - the commercial property market is rebounding.
- Capital values increased strongly in all sectors and were up 31.4% over the year, with a particularly strong performance in the retail sector.
- Commercial rents for both office and retail space grew strongly in 2013/2014.
- Concerns persist about the shortage of available prime office space for rent in Dublin, Cork and Galway as the market tightens and vacancy rates decline.
- The importance of commercial rates (which differ by location) as a source of revenue for Local Authorities continues to grow as funding from Central Government is reduced.

Transport Costs

- Diesel prices are 5.5% more expensive in Ireland than in the euro area. The weak euro may result in further fuel price increases (since crude oil is priced in dollars).

- The cost of most transport services in Ireland has remained stable in recent quarters; air transport prices, however, increased significantly (by 12.4%) in the past 4 quarters.
- While it is more expensive (excluding tariffs) to export and import to and from Ireland by sea, Irish administrative processes are efficient and compare favourably with processes in our key competitors.

Utility Costs

- Energy comprises a significant component of non-wage costs for enterprises in a range of growth sectors such as food and drink, life sciences, ICT, construction materials and other manufacturing sectors.
- The EU is among the most expensive locations for electricity and gas globally, and within the EU, Ireland is one of the most expensive countries for electricity: Ireland is the 5th and 7th most expensive location in the euro area 17 for SMEs and large electricity users respectively.
- While Ireland is mid-table in the euro area in terms of industrial gas prices, gas prices in the US are substantially lower than in the EU.
- Water and waste water costs for enterprise in Ireland compare favourably to those in competitor markets.
- In terms of waste costs, the cost of landfill has increased from €93 per tonne in 2010 to €113 in 2014 because of increases in the landfill levy. Irish landfill costs are amongst the most expensive of the benchmarked countries/regions.
- Thermal treatment costs (gate fees) in Ireland, although lower than landfill costs, are also among the most expensive in the benchmarked countries/regions.
- Telecom costs are relatively competitive although some concerns persist in relation to the quality (speed) of services available. The data used, however, is based on purchasing power parities which may over estimate Ireland's competitiveness.
- From an enterprise perspective, the widespread availability of advanced broadband services is more of a concern than cost issues. There are some concerns of the lack of competition in the backhaul market which is resulting in higher costs and poorer quality than is desirable.

Credit and Financial Costs

- New business interest rates for non-financial corporations are higher in Ireland than in the euro area – rates are 60% higher for loans up to €1 million and are 81% higher for loans above €1 million.
- In November 2014, interest rates in Ireland for revolving loans and overdrafts were 42% above the euro area average, and this gap has been increasing.

Business Services and Other Input Costs

- Throughout the 2012 to 2014 period, prices for a range of business services (e.g. transport, postal and courier, and computer consultancy services) have been increasing in Ireland. This follows a period of significant price declines over the course of the recession.
- In Q3 2014, business service prices are 6.5% above 2010 levels.
- Overall since 2010, service prices have risen by more than manufacturing prices. Manufacturing products sold within Ireland, however, have increased at faster pace than both services and internationally traded manufacturing products (i.e. exposed to competition).

- Despite reductions in legal costs in recent quarters, Ireland is an expensive location to enforce a business contract.
- Insurance density (premiums per capita) in Ireland is below the euro area average. There appears to be a degree of concentration in the market in terms of the number of providers, but concentration levels are not excessive when compared with other small markets.
- The fall in premium has resulted in significant reductions in underwriting profits for commercial insurance providers in Ireland. The level of profitability in the Irish market makes it somewhat unattractive to prospective new entrants.

Broader Cost Environment

- Ireland's current price level and inflation profile can be described as high cost but rising slowly.
- In 2013, Ireland was the 3rd most expensive location in the euro area for consumer goods and services.
- Irish prices were 16.8% above the euro area average, and prices were above euro area averages for 10 out of 12 categories of goods and services.
- The principal contributors to Irish inflation over the last 12 months are "Miscellaneous goods and services" which is driven by health insurance, "Alcohol and tobacco", "Education", and "Restaurants and hotels".
- After significant price falls over recent years, house prices and rents are on an upward trend again with potentially significant consequences for affordability and knock on impacts on wage demands.

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The full report is available at www.competitiveness.ie

For further information contact Press Office, Department of Jobs, Enterprise and Innovation: Phone: 01-6312200; e-mail: press.office@djei.ie

About the NCC

The NCC reports to Government on key competitiveness issues for the Irish economy and makes recommendations on policy actions required to enhance Ireland's competitive position.

The members of the Council are:

- Prof Peter Clinch, Chair, National Competitiveness Council
- Liam Casey, Chief Executive Officer, PCH International Ltd.
- Kevin Callinan, Deputy General Secretary, IMPACT Trade Union
- Micheál Collins, Senior Research Officer, Nevin Economic Research Institute
- Isolde Goggin, Chair, Competition and Consumer Protection Commission
- John Herlihy, Vice President, International SMB Sales and Head of Google Ireland
- Declan Hughes, Assistant Secretary, Department of Jobs, Enterprise and Innovation
- Danny McCoy, Chief Executive Officer, Ibec
- Jane Magnier, Joint Managing Director, Abbey Tours
- Seán O'Driscoll, Chairman and Chief Executive Officer, Glen Dimplex Group
- Louise Phelan, Vice President of Global Operations, Europe Middle East and Africa, PayPal
- Heather Reynolds, Director, Eishtec
- Dave Shanahan, Head of Strategic Health Initiatives Worldwide, AbbVie
- Martin Shanahan, Chief Executive, IDA Ireland
- Ian Talbot, Chief Executive, Chambers Ireland
- Siobhán Talbot, Group Managing Director, Glanbia

Representatives from the Departments of the Taoiseach, Agriculture, Food and the Marine, Communications, Energy and Natural Resources, Education and Skills, Environment, Community and Local Government, Finance, Justice and Equality, Public Expenditure and Reform, Transport, Tourism and Sport attend Council meetings in an advisory capacity.

The work of the NCC is underpinned by research and analysis undertaken by the Strategic Policy Division, Department of Jobs, Enterprise and Innovation.