

# Annual Competitiveness Report 2008

Volume 2: Ireland's Competitiveness Challenge



National  
Competitiveness  
Council



# Annual Competitiveness Report 2008



- ▶ Volume 1:  
*Benchmarking Ireland's Performance*



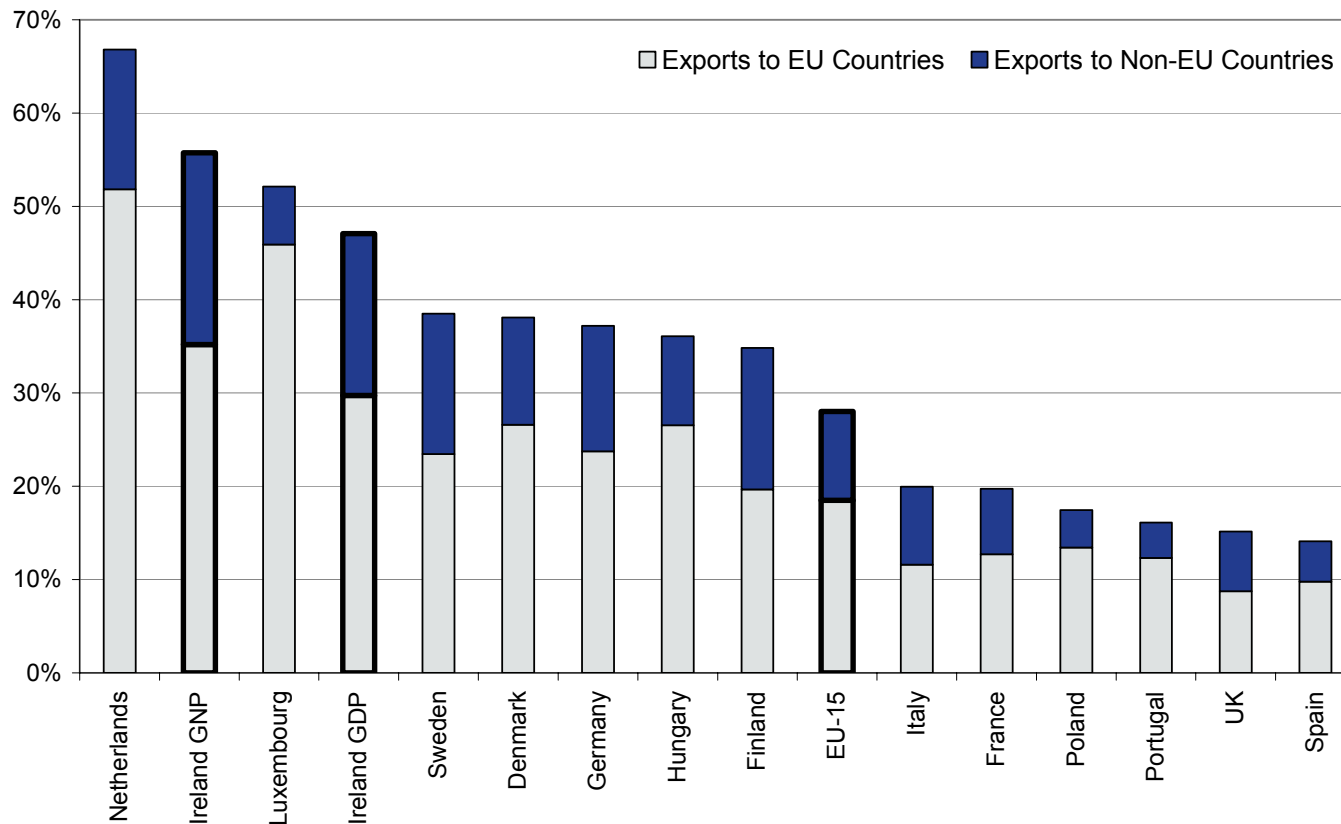
- ▶ Volume 2:  
*Ireland's Competitiveness Challenge*

# Current Performance

- ▶ Economic activity is weakening from historic highs.
- ▶ Construction and related activity is falling, with severe implications for economic growth, unemployment, investment, consumer confidence and demand, and government revenues.
- ▶ *There is no return to growth driven by construction and borrowing.*

# Prosperity Depends on Exports

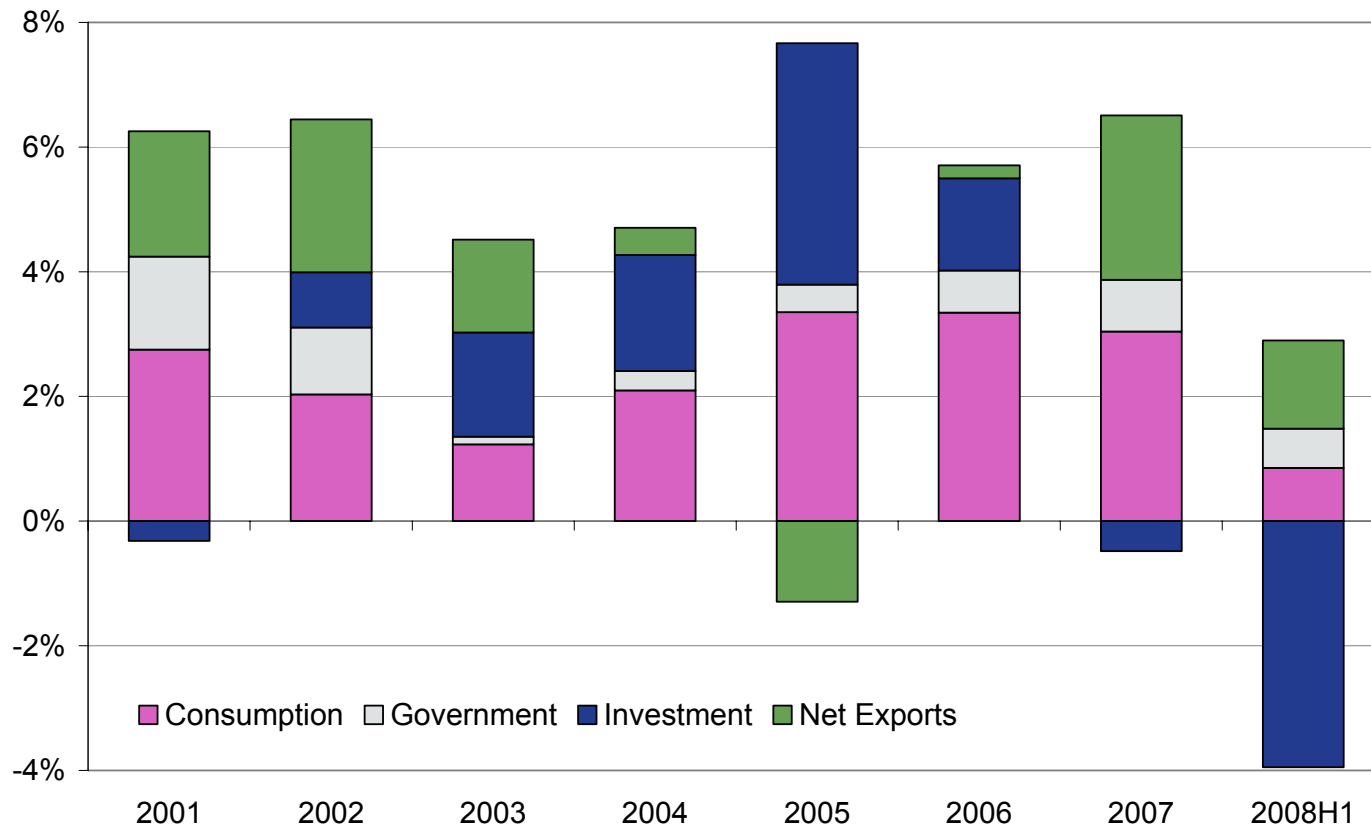
## ► Merchandise exports, % of GDP, 2007



Source: Eurostat, External Trade

# Sources of Growth

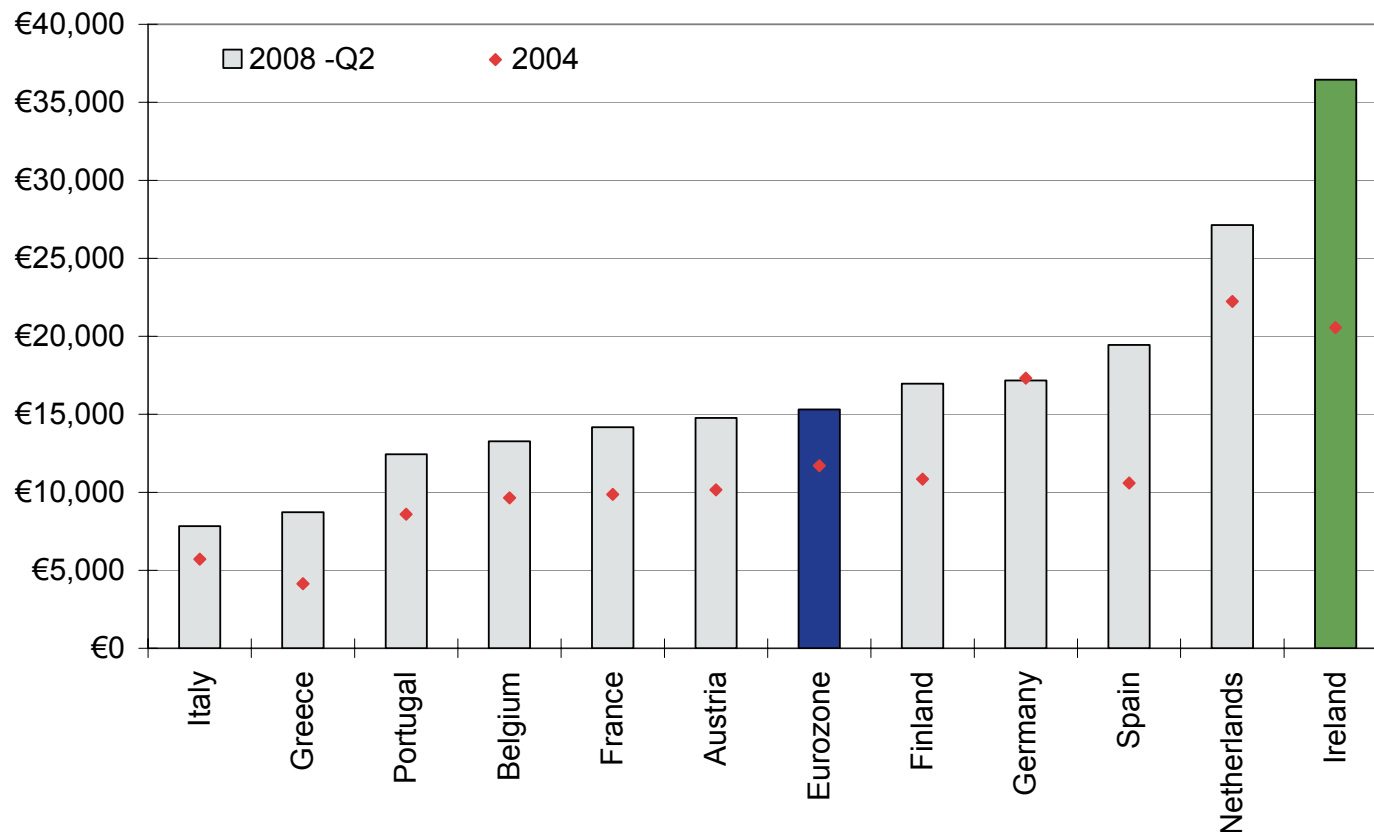
## ► Contribution of Net Exports to Growth



Source: Forfás Calculations, CSO National Accounts

# Irrational Exuberance: Inevitable Adjustment?

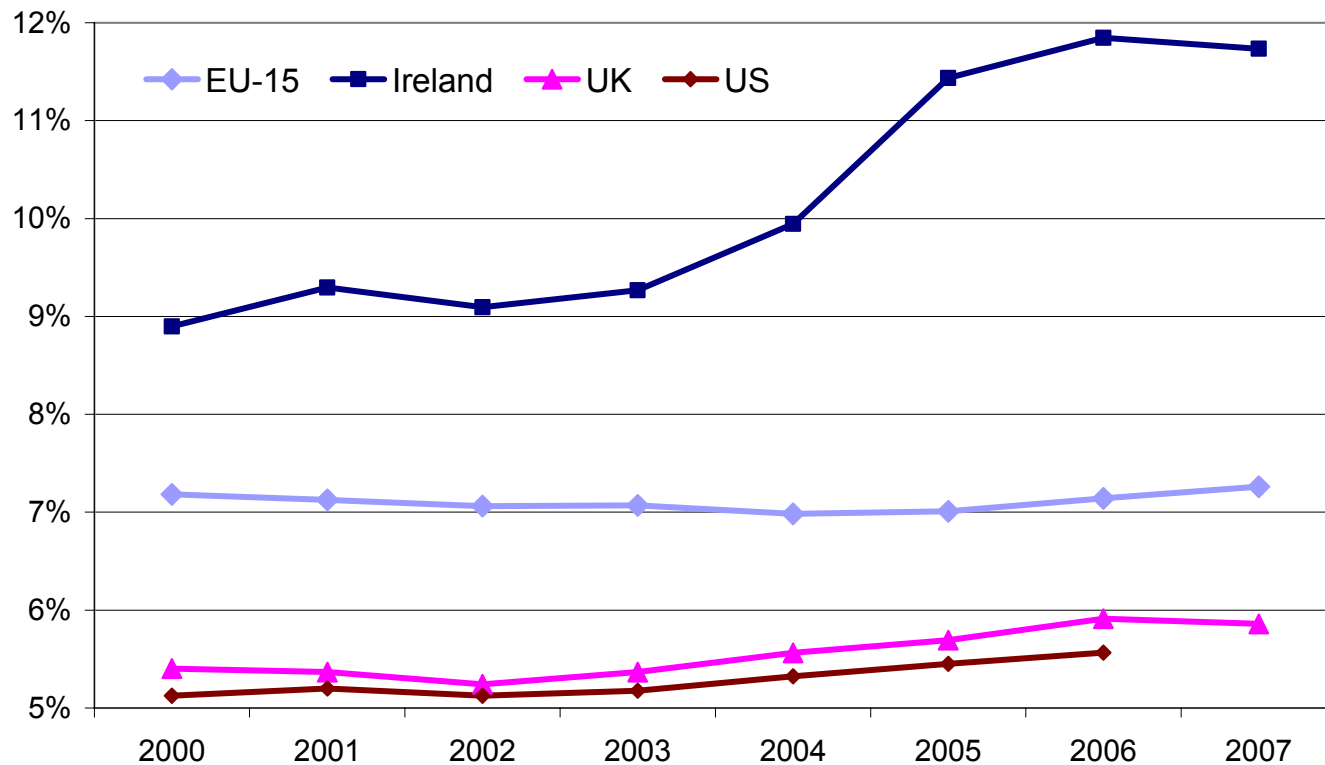
## ► Household Borrowing, per capita



Source: ECB.

# Irrational Exuberance: Inevitable Adjustment?

## ► Share of Construction in Total Employment



Source: Eurostat.

# Benchmarking Summary

## ► Strengths

- Improving export performance in services
- Inward FDI remains strong
- Improving performance: infrastructure, education and R&D
- Government debt, while low, is increasing rapidly

## ► Weaknesses

- Falling world market share, driven by manufacturing
- Dependence on property and household borrowing has been exposed
- Rising unemployment
- Slow productivity growth
- Cost competitiveness remains poor – despite recent disinflation



# Key Competitiveness Challenges

## 1. Restoring Fiscal Sustainability

- ▶ Managing the adjustment

## 2. Regaining Cost Competitiveness

- ▶ Particularly energy competitiveness

## 3. Implementing Public Services Reform

- ▶ Maximising coherence within & across the system

## 4. Positioning for the Upturn

- ▶ Development of Long-term Strategy for Economic Recovery



# 1 Restoring Fiscal Sustainability

# Need for Credibility & Support

- ▶ Rising General Government Balance
  - Budget 2009: 6.5%
  - ESRI QEC Winter: 10.2%
- ▶ Risk of destroying hard won fiscal strength
  - Government debt is increasing rapidly (ESRI est. 47.5% in 2009)
- ▶ Important decisions remain:
  - Balancing taxation, user charges and borrowing;
  - Maintaining necessary capital investment given pressures for current spending;
  - Prioritisation of key projects, and parts of projects, to enhance our competitiveness and resolve infrastructural deficits;
  - Achieving public sector reform to achieve better value.

# Restoring Fiscal Sustainability: Revenue

- ▶ Protect existing advantages
  - Competitive labour tax wedge and corporation tax
- ▶ Broaden the tax base
  - Annual property tax; 3-5 year framework; transition provisions
  - Use of user charges to fund high quality infrastructure and services (e.g. road tolls, water, third level, etc.)
- ▶ Support the creation of new advantages
  - Taxation of IP and intangibles, life long learning and business R&D

# Restoring Fiscal Sustainability: Expenditure

## ▶ Important decisions necessary

- Need for a clear transparent assessment process to inform priorities

## ▶ NCC priorities:

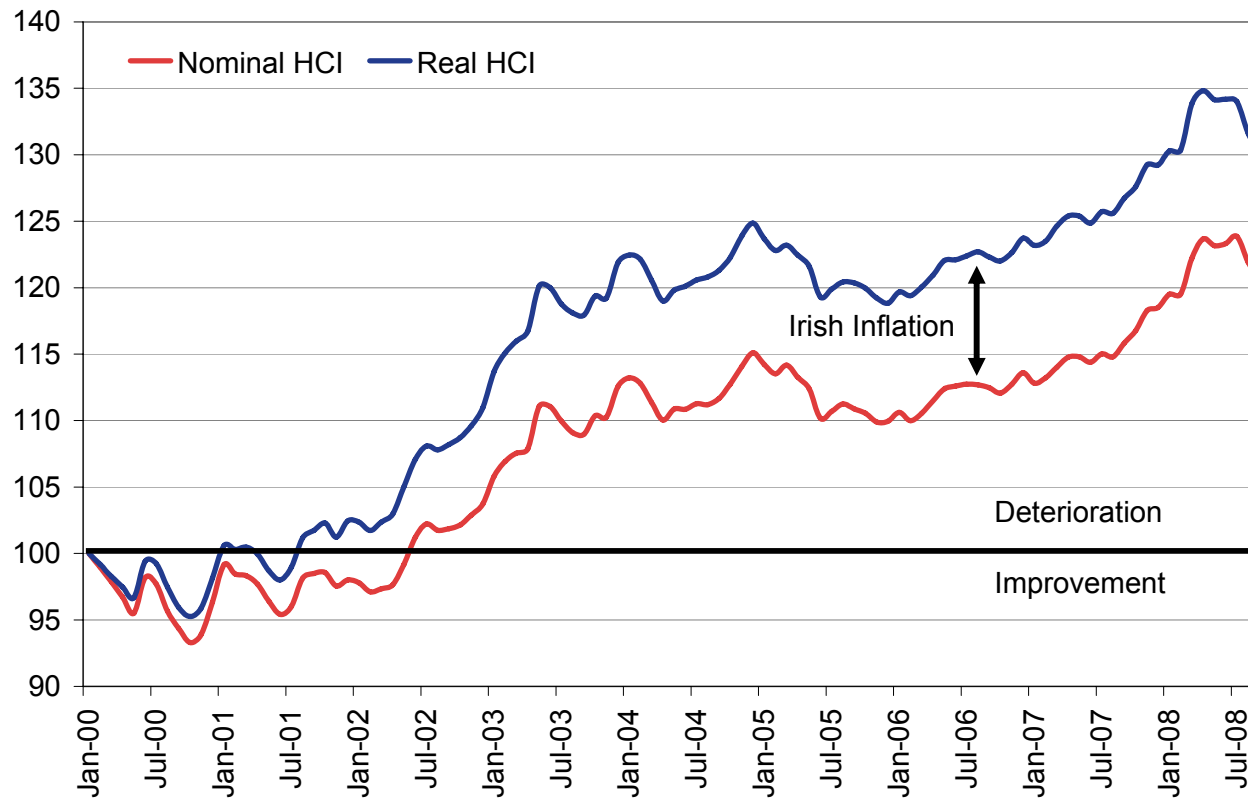
- **Telecoms:** NGN are a new league; can private sector deliver?
- **Successful cities** are essential for regional and national competitiveness – prioritise Dublin and NSS Gateways
- Maintain investment in **research infrastructure** and **commercialisation**.
- Prioritise **key transport projects** (inter-urban road network; the Atlantic corridor; public transport where demand exists).



## 2 Restoring Cost Competitiveness

# Cost Competitiveness had Weakened

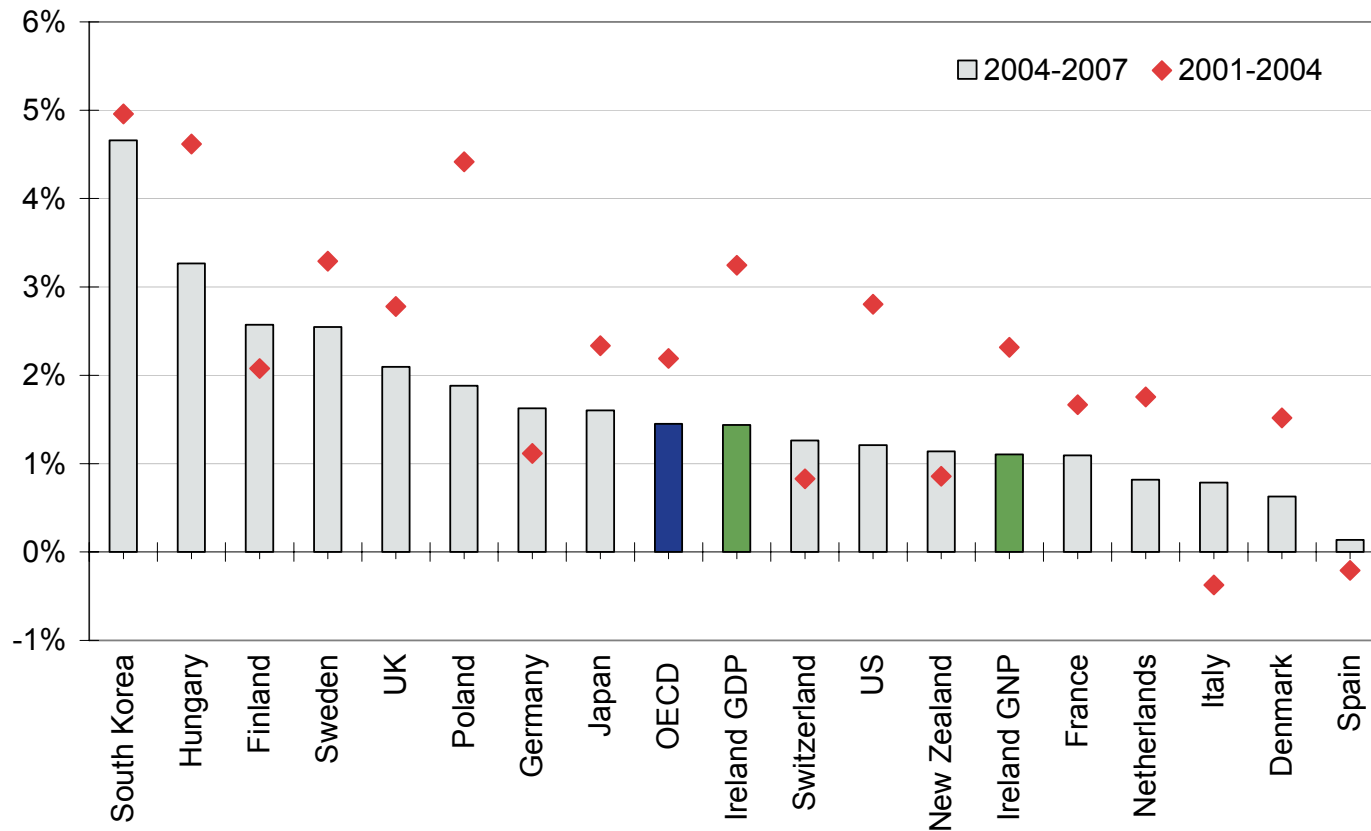
## ► Harmonised Competitiveness Indicator



Source: Central Bank of Ireland; January 2000=100.

# Productivity Growth Has Slowed

## ▶ Annual Average Growth in GDP per hour worked

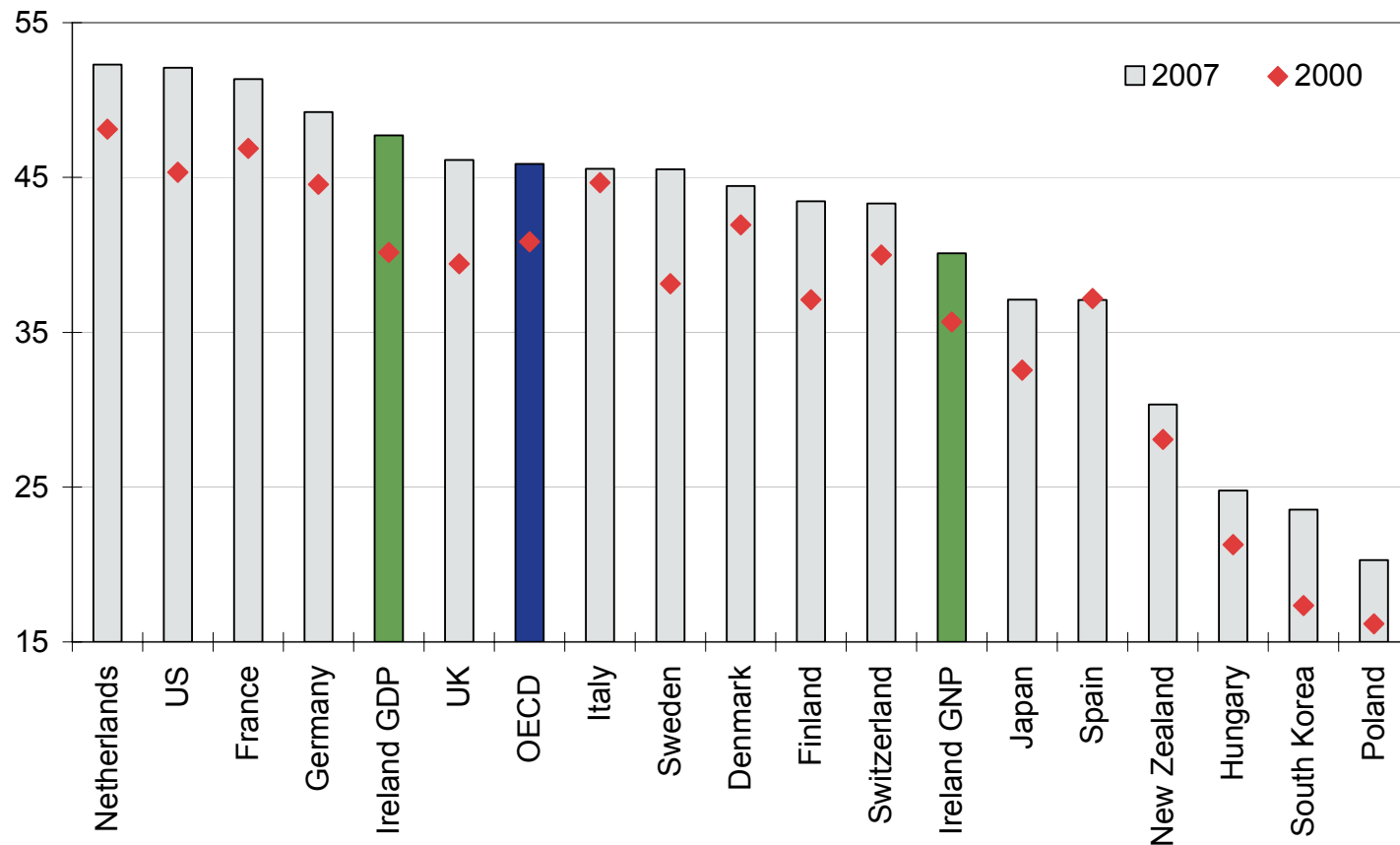


Source: Groningen Growth & Development Database.



# Productivity Levels

## ► GDP per hour worked, 2000 vs. 2007



Source: Groningen Growth & Development Database; Measured in EKS\$.

# Cost Drivers

- ▶ Key costs weakening our competitiveness include:
  - property costs
  - utility costs (electricity; waste disposal)
  - domestic services (including legal; accountancy; IT)
- ▶ Growing concern regarding cost & availability of credit
- ▶ Pay levels remain relatively competitive vis-à-vis high-income locations
  - Significantly more expensive than Accession states and Asia.
- ▶ Current structure of taxes on Labour and Profits supports our competitiveness

# Regaining Cost Competitiveness

- ▶ While the slowdown will ease cost pressures, actions are required to:
  1. Bring long-term inflation expectations back to the Eurozone average - at very least!
  2. Stop the continuing deterioration in Ireland's energy price competitiveness
    - Cost proofing of policies including how best to meet renewables targets
    - Strong regulation to promote competition and efficiency in generation, bringing controllable costs into line with EU
    - Capturing carbon windfalls until 2012
    - Raising energy efficiency

# Regaining Cost Competitiveness, contd.

3. Falling land and house prices support competitiveness
  - A quick adjustment will support employment
4. Limit direct and indirect **government costs**
  - Local Authority charges; Better Regulation Agenda
5. Ensure the availability of **credit** for sound businesses
6. Implement **competition policies** in sheltered sectors
  - Opportune time to tackle embedded interests?
7. Better **use of ICT** to reduce costs
  - eGovernment and ePayments.



## 3 Public Services Reform

# Performance

## ▶ Irish public service...

- Remains relatively small – despite recent growth.
- Performs relatively well – based on international assessments

## ▶ Concerns remain

- Are the public services are fit for purpose?
- What is their capacity for change?

## ▶ The Challenge is Clear

- In a small open economy, all sectors must contribute to national competitiveness
- Reform must achieve better services with fewer resources

# Avenues for Reform

- ▶ Implementation of the OECD review
- ▶ Reducing unnecessary administrative costs
- ▶ Delivery of more efficient services
  - Across health, County Enterprise Boards, local authorities, etc.
- ▶ Need to maximise coherence
  - Through joined-up policymaking & delivery of public services
- ▶ An example in Education:
  - *Weak relationship between expenditure and student outcomes*
  - *Good teachers, strategies and processes determine outcomes*
  - *Need to reward excellence; share/embed best practice; and support principals in their leadership role.*





# Positioning for the Upturn

## A Long-term Strategy for Recovery

1. Education
2. Energy/Sustainability
3. Targeting Success



# 1 Positioning for the Upturn: Education

## ▶ Education, Innovation & Research Commercialisation

- Low participation in pre-primary and life long learning
- Strong participation in primary and secondary
- Less teaching time devoted to maths, science, technology
- Fewer computers per student than competitors
- Significant progress in research investment; remains significantly behind leading countries

## ▶ Now, we need to address quality at all levels:

- Is our education system really good enough to drive prosperity?
- How can we maximise the quality of education given scarce resources?

# What can we do?

1. Formalise pre-primary education;
2. Formalise continuous professional development among teachers (esp. in maths);
3. Reform strategies & processes, and gear them towards achieving strong outcomes;
4. Raise maths, science and technology skills;
  - Teaching time; subject incentivisation; facilities
5. Deliver on the *Strategy for ICT in Schools*;
6. Improve access to life long learning;
7. Improve higher education linkages

## 2 Positioning for the Upturn: Energy/Sustainability

### ► Energy Security

- Dependence on imported fossil fuels has grown significantly.
- Overall import dependency reached 91% in 2006.

### ► Energy Sustainability

- Per capita CO<sub>2</sub> emissions are 2<sup>nd</sup> highest in EU-15.
- Despite progress, meeting our targets will be very difficult.
- Transport and agriculture sectors are key.

# What can we do?

## ► Security of Supply

1. Interconnection (NI, UK, Europe);
2. Comprehensive review of all energy sources, incl nuclear
3. Ultimately, sustainable energy technologies are needed to establish a clean, reliable, secure and competitive supply.

## ► Environmental Targets

4. Renewables: Need to balance 40% target with competitiveness;
5. Carbon Taxes: Avoid double incidence of tax on ETS sectors; phased intro; use of revenues to enhance competitiveness;
6. Land use planning: sustainability, density & public transport;

### 3 Positioning for the Upturn: Targeting Success

- ▶ As a small regional economy, a risk of under-performance exists.
- ▶ Success is not guaranteed...
- ▶ ...But neither is decline inevitable
- ▶ Our export performance depends on a small number of firms and sectors:
  - Are we proactively supporting new sectors for the future; and
  - Are we enhancing the competitiveness of existing sectors in terms of the required skills, research base, regulation and infrastructure?

# In Summary

- ▶ No magic wand; no single prescription; but detailed policies and consistent implementation are vital
- ▶ Correction is painful but inevitable
  - Shift away from borrowing and construction must continue.
- ▶ Formidable challenges
  - Ensuring the economy is sufficiently competitive;
  - Enabling this transition process to continue;
  - In an environment where fewer resources are available.
- ▶ *Ultimately, we need to provide an operating environment which helps firms to trade successfully on increasingly competitive world markets.*