

Costs of Doing Business in Ireland 2010

Volume 1

July 2010



Introduction to the NCC

The National Competitiveness Council was established by Government in 1997. It reports to An Taoiseach on key competitiveness issues facing the Irish economy and offers recommendations on policy actions required to enhance Ireland's competitive position.

Each year the NCC publishes the two-volume Annual Competitiveness Report.

- Volume One, **Benchmarking Ireland's Performance**, is a collection of statistical indicators of Ireland's competitiveness performance in relation to 17 other economies and the OECD or EU average.
- Volume Two, **Ireland's Competitiveness Challenge**, uses this information along with the latest research to outline the main challenges to Ireland's competitiveness and the policy responses required to meet them.

As part of its work, the NCC also publishes other papers on specific competitiveness issues.

The work of the NCC is underpinned by research and analysis undertaken by Forfás - Ireland's policy advisory board for enterprise, trade, science, technology and innovation.

Chairman's Preface



After a decade of inflation and high costs, prices in Ireland are moderating. This is good news for our exporters but we need to guard against complacency. Much of the improvement is due to the severity of the recession so it is critical that we act now to put in place the structural changes that are required to ensure that prices do not rise again and erode competitiveness when the economy returns to growth.


Generating sustainable export-led growth is essential to rebuilding our economy. This will require a substantial improvement in cost competitiveness and strong productivity growth in all parts of the economy. Improving our relative cost competitiveness requires the cost of doing business in Ireland to fall relative to that of our trading partners.

During the past decade, Ireland experienced a significant loss in cost competitiveness reflecting a combination of higher price inflation in Ireland and an appreciation of the euro against the currencies of some of our main trading partners. Key business inputs such as pay and incomes, rents, utilities and business services rose sharply for an extended period. However, since January 2008, Ireland has regained some of its lost cost competitiveness as domestic inflation remains below that of our main trading partners and as the euro has weakened.

This report highlights tangible improvements in the cost of doing business in Ireland - there have been significant falls in property and energy costs. However some costs have continued to increase or remain relatively high, particularly in sectors that are not exposed to international competition and are sheltered from the full rigours of domestic competition (e.g. administered prices such as waste water costs, legal fees, education and health costs).

At an economy-wide level we must seek to sustain and further enhance the recent improvements in Ireland's cost competitiveness. Many of the recent price falls in Ireland are largely a cyclical response to the Irish and international recession (e.g. reduced demand, spare capacity, falling interest rates, falling fuel and food prices) rather than a response to structural changes in the Irish economy. Structural or policy induced changes are necessary to ensure that prices in Ireland will not escalate and erode competitiveness when the Irish and international economy return to growth.

In order for the economy to make the necessary transition from a reliance on domestic demand to sustainable export-led growth in the medium term, policies need to facilitate the convergence of Irish costs towards the levels of our trading partners. As prices are now falling in many developed countries, improving our relative cost competitiveness will require us to achieve cost reduction faster than the euro area average.



Comparing prices and costs across countries is a valuable exercise but it is important to remember that cost competitiveness is only one aspect of overall competitiveness. The availability of skilled labour, productivity and innovation performance, quality infrastructure, together with a variety of other factors ultimately determine the ability of a country to compete in world markets and to deliver well paid employment and prosperity for its people. Ireland's national competitiveness performance is assessed in detail in the NCC's forthcoming report, Benchmarking Ireland's Performance.

Dr Don Thornhill
Chairman, National Competitiveness Council

Council Members

Dr Don Thornhill	Chairman
Rory Ardagh	Telecom Property Holdings Limited
Brendan Butler	Director of Strategy, Trade, EU and International Affairs, IBEC
Donal Byrne	Chairman, Cadbury Schweppes Ireland Limited
Shay Cody	General Secretary, IMPACT
Pat Delaney	Director of Sectors and Regions, IBEC
Clare Dunne	Assistant Secretary, Department of Enterprise, Trade and Innovation
Marcus Hewson	
Annette Hughes	Director, DKM Economic Consultants
Seán Murphy	Deputy Chief Executive, Chambers Ireland
Martin Shanahan	Chief Executive, Forfás
William Slattery	Executive Vice President and Head of European Offshore Domiciles, State Street International (Ireland) Limited
Paul Sweeney	Economic Adviser, Irish Congress of Trade Unions
John Travers	Consultant and Founding Chief Executive Officer, Forfás and Science Foundation Ireland
Prof Ferdinand von Prondzynski	President, Dublin City University

Council Advisers

Paul Bates	Assistant Secretary, Department of Tourism, Culture and Sports Department of the Taoiseach
Mark Griffin	Assistant Secretary, Department of Environment, Heritage, and Local Government
Kevin McCarthy	Assistant Secretary, Department of Education and Skills
Eamonn Molloy	Assistant Secretary, Department of Communications, Energy and Natural Resources
David Moloney	Assistant Secretary, Department of Finance
John Murphy	Assistant Secretary, Department of Transport
Liam Nellis	Chief Executive, InterTrade Ireland

Research and Administration

Adrian Devitt	Forfás
Caoimhe Gavin	Wilton Park House
Mary Twomey	Wilton Place Dublin 2 Tel: 01 607 3000 Fax 01 607 3030 Email: ncc@forfas.ie Web: www.competitiveness.ie

Table of Contents

Executive Summary	6
1. Introduction	12
1.1 Overview of Ireland's Cost Competitiveness	12
1.2 Methodology	14
2. Cost Profiles	16
2.1 Summary Cost Profiles	16
2.2 Sectoral Cost Profiles	17
3. Labour Costs	21
3.1 Labour Cost Indices and Unit Labour Costs	24
3.2 Salary Levels	26
3.3 Social Security Contributions and Labour Taxation	30
4. Property Costs	32
5. Utility Costs	36
5.1 Energy and Fuel	38
5.2 Environmental Utilities	40
5.3 Telecommunications	41
6. Business Services Costs	44
7. The Broader Cost Environment	47
7.1 Consumer Price Levels	49
7.2 Consumer Product Prices	50
7.3 Accommodation	51
7.4. Public and Administered Services	53
Appendix - Summary of Specialist Databases	56

Executive Summary

Ireland experienced a significant loss in cost competitiveness as measured by the real harmonised competitiveness indicator over the past decade reflecting a combination of an appreciation of the euro against the currencies of many of our trading partners and higher price inflation in Ireland. Unsustainable credit fuelled growth created the conditions which led to significant increases in the costs of doing business in Ireland. Key business costs such as pay, rents, utilities and business services rose sharply for an extended period. However, since January 2008, Ireland has regained some of its lost cost competitiveness as domestic inflation remains below that of our main trading partners and as the euro has weakened. By April 2010, Ireland's real harmonised competitiveness indicator (HCI) was 3.4 per cent below its January 2005 position. However, Ireland's real HCI is still 19 per cent above its 2000 level - indicating that despite progress, Irish costs remain high relative to historic levels and those in other countries.

This report highlights tangible improvements in the competitiveness of unit labour costs, and significant falls in property costs and industrial electricity costs. Research from Galstyan highlights that over the period 1980 to 2006 a depreciation in Ireland's real exchange rate of 0.8 per cent was associated with an increase in the trade surplus of one per cent¹, therefore improving cost competitiveness is essential to generating sustainable export-led growth.

A large increase in exports will not provide a panacea for the challenges facing the Irish economy or bring about an automatic reversal in our unemployment trends. However, improving Ireland's attractiveness as a location to do business and export from will be important for restoring the levels of confidence necessary to halt the decline in domestic consumption and investment seen since 2008.

Comparing prices and costs across countries is an important and useful exercise. However, care is required as cost competitiveness is only one aspect of overall competitiveness. The availability of skilled labour, good quality infrastructure, functioning capital and labour markets and a wide variety of other factors ultimately determine the ability of countries to compete in world markets in a fashion that provides its citizens with a good standard of living. All of these factors are assessed in the National Competitiveness Council's report, *Benchmarking Ireland's Performance*. It should also be noted that assessing cost competitiveness is not a precise science due to a range of methodological and data issues.

Despite progress, the NCC cautions that regaining cost competitiveness is a long and difficult path and that further progress is essential. In this context, it is important to consider that:

- Although prices in Ireland have moderated in the past year, a range of key business inputs in Ireland remain relatively expensive including property, broadband, waste disposal and legal fees.
- Improving our relative cost competitiveness requires the cost of doing business in Ireland to fall relative to that of our trading partners. Therefore, falling prices in Ireland do not automatically

¹ Galstyan V., *Assessing Ireland's Price Competitiveness*, IIS, Trinity College Dublin, 2010.

equate to improvements in cost competitiveness. For example, while the costs of renting a prime industrial unit fell by 18 per cent in Ireland between 2008 and 2009, Ireland's ranking improved by just one place to third most expensive, as rents fell in 12 of the 16 countries benchmarked.

- While the costs of many goods and services have fallen significantly in Ireland in the past two years, there are notable exceptions - particularly in locally trading sectors of the economy. For example, the costs of waste water services increased by 18.8 per cent in Ireland during 2009. The cost of legal services has declined very slowly, and in Q4 2009 they remained 18.4 per cent above the average 2006 price.
- The drivers of falling prices are also important to consider. For example, the cost of industrial electricity in Ireland decreased by 24 per cent - more than any other benchmarked location in 2009. The gap between the price of industrial electricity for large energy users in Ireland and the euro area average has narrowed significantly (from 37 per cent during the second half of 2008 to five per cent during the second half of 2009). However, recent price falls may not be sustainable as they appear to be largely due to falling international fossil fuel prices and a temporary reduction in electricity prices for large energy users. While these improvements in cost competitiveness are very welcome, continuing progress on longer term structural changes are essential if improvements in cost competitiveness are to be sustained.
- The costs of a range of public and administered services continue to negatively affect Irish cost competitiveness. The cost of health and education services continues to rise rapidly, further increasing the gap between these components and the other goods/ services included in the consumer price index. Transport costs, such as urban public transport and taxis, are relatively expensive in Ireland compared with our main trading partners.
- Exchange rates have a significant impact on the relative costs of doing business in Ireland. As they are volatile and outside of our control, it is critical that we concentrate on those cost factors that are, at least to some degree, influenced by Government policy.

Ireland's cost competitiveness has improved in the past two years - as a result of exchange rate movements and adjustments within the Irish economy. It is important to determine if progress to date is sufficient to restore competitiveness and whether further adjustments are necessary. Recent research from the European Commission acknowledges that Ireland has registered significant gains in cost competitiveness in 2008 and 2009². The Commission highlights that Ireland is the only country that provides clear evidence of competitiveness rebalancing. Since the outbreak of the financial crisis in 2007, the intra-euro-area real effective exchange rate (REER) based on GDP deflators has depreciated by almost seven per cent. However, Commission research suggests that the Irish REER remains approximately six per cent overvalued - though it highlights that this figure should be treated with caution³. Similar assessments from the European Central Bank and the IMF estimate that Ireland's real exchange rate is overvalued by four to fifteen percent⁴. Therefore, despite progress to date, Ireland would appear to still have some way to go to achieve relative cost competitiveness with our key trading partners.

² European Commission, *Surveillance of Intra-Euro-Area Competitiveness and Imbalances*, 2010.

³ European Commission, *Surveillance of Intra-Euro-Area Competitiveness and Imbalances*, 2010.

⁴ ECB, IMF 2009 Article IV Ireland Consultation and European Commission Quarterly Report on the Euro Area Volume 8, No.1 (2009).

Similar to the Irish experience over the last ten years, during the 1980s the Finnish economy was characterised by a credit and property price boom, high inflation and a deterioration of competitiveness which was followed by a remarkable economic turnaround over the subsequent two decades. Estimates suggest that the Finnish REER is still undervalued relative to other euro area countries⁵. The Finnish experience illustrates the potential for Ireland to take advantage of the current economic climate to further improve our cost performance and deliver a sustained improvement to our international competitiveness. Volume Two of this report will look in detail at the underlying factors affecting our cost competitiveness and put forward recommendations with regard to how Ireland's cost competitiveness can be improved.

Key Findings

The objectives of this paper are to understand what costs drive competitiveness and to analyse Ireland's relative cost competitiveness performance across four key business inputs - labour, property, utilities and business services. It also looks at the broader cost environment that indirectly impacts on the cost of doing business here.

The report uses the most up to date internationally comparative cost data. It is important to note, however, that as much of the data is collected on an annual basis there may be a time lag in capturing more recent changes in cost levels.

Sectoral Cost Profiles

- Based on KPMG⁶ case study firms, it is clear that the cost profile of firms varies significantly across sectors. A large proportion of costs for services sectors (89 per cent) and research and development (87 per cent) are location sensitive. In manufacturing sectors, 46 per cent of costs are determined locally - the majority of costs (e.g. raw materials, capital goods) are set on world markets.
- For manufacturing sectors, the contribution of labour costs to total location sensitive costs varies from 45 per cent in the plastic sector to 56 per cent in the medical devices sector. Transport costs are a major component of locally determined costs for manufacturing operations. This is significant for Irish agri-food firms given the regional dispersion of the sector. Utilities are also a significant cost input for a number of manufacturing sectors (six per cent for the case study agri-food firm and seven per cent for the case study chemicals firm).
- For service sectors, labour costs account for 74 per cent of total costs. Taxes and property leasing costs are significant for service operations.
- For R&D sectors, 70 per cent of total costs are accounted for by labour. The leasing of property is a major cost element across all benchmarked R&D sectors. Due to substantial grants for R&D operations, taxes amount to less than 0.9 per cent of locally determined costs for the case study biotechnology R&D operation and 0.6 per cent for the case study product testing operation. In the clinical trials sector, on average grants exceed taxes and provide a 3.2 per cent cost write off.

⁵ European Commission, Surveillance of Intra-Euro-Area Competitiveness and Imbalances, 2010.

⁶ KPMG, Competitive Alternatives, 2010.

Labour Costs

- Labour costs are the largest single location sensitive cost component for services (83 per cent) and R&D (80 per cent) operations. Labour costs account for 52 per cent of location sensitive manufacturing costs.
- Labour cost growth rates show the change in the cost of employing workers over time. Ireland's growth rates exceeded the euro area and EU-27 average between 2004 and 2007. However, growth rates in Irish labour costs slowed significantly in 2008 and the first half of 2009 and were lower than the EU-27 and euro area-16 average.
- Total labour costs include wages, taxes on income and employer and employee social security contributions. Ireland has the tenth highest total labour costs level in the OECD and is in line with a number of western European countries. Ireland has the fifth highest net wage level in the OECD-28, 35.5% above the OECD-28 average. This is due, in part, to Ireland's low tax wedge on labour.
- Irish salary levels across a range of job categories of relevance to internationally trading firms are broadly similar to the euro area average. Irish salaries are generally higher than those in the US for comparable positions and for most comparable positions in the UK. While Irish salary levels remain significantly below those in the most expensive countries (such as Denmark, Germany and Japan), they are generally a multiple of those available in Eastern Europe (Poland and Hungary) and India - countries that we are increasingly competing with for trade and investment.
- Ireland has one of the highest statutory minimum wage rates in Europe at €8.65 per hour (€1,462 per month). However, when measured as a percentage of the average industrial wage, the minimum wage in Ireland is seventh highest within the EU. 1.3 per cent of employees were receiving the minimum wage in Q2 2009⁷. It is notable, however, that a large proportion of employees in receipt of the minimum wage are concentrated in a small number of sectors such as tourism and retail.
- Ireland has one of the lowest levels of employers' social welfare contributions. The Irish rate is significantly lower than the OECD average and the euro area average which reduces the total costs of labour here on a relative basis.

Property Costs

- The value of commercial properties in Ireland peaked in Q4 2007. While the rate of decline has slowed in the second half of 2009, the value of retail properties fell by 29 per cent, offices by 28 per cent, and industrial premises by 27 per cent between Q4 2008 and Q4 2009.
- The cost of constructing and renting both industrial and office units declined sharply in Ireland during 2009. However, the impact of these decreases on Irish cost competitiveness was relatively muted as there have also been significant cost decreases in many other countries.
- The cost of constructing a prime industrial site fell by 14 per cent in Ireland between 2008 and 2009 - the second sharpest fall across the benchmarked countries. However, given significant price falls elsewhere, Ireland remains the third most expensive benchmarked location.
- Office rental costs fell by almost 25 per cent in Ireland in 2008 and fell a further 18 per cent in 2009. Following these declines, Ireland is now a cheaper office rental location than the US and

⁷ CSO, Earning and Labour Costs, Quarter 2, 2009, Preliminary Estimates, 2009.

Italy. However, Singapore and Spain both experienced significant price falls in 2009 (49 per cent and 23 per cent respectively) and are now cheaper locations to rent office space than Ireland.

- With regard to local authority taxation on property, the average annual rate of valuation peaked in 2009 but this decreased by an average of 1.8 per cent in 2010.

Utility Costs

- For large energy users, the price of electricity decreased by more in Ireland (-24 per cent) than in any other benchmarked location in 2009. Ireland is now the sixth most expensive of the 14 benchmarked countries. Although electricity costs for SMEs also fell between 2008 and 2009 (-15 per cent), Ireland is the third most expensive location benchmarked.
- While the average cost of treated water services in Ireland increased by 2.8 per cent in 2009, Ireland remains competitive with our main trading partners on this measure. However, there was a significant increase in the cost of waste water services (18.8 per cent) in Ireland during 2009.
- Ireland was the most expensive benchmarked location for the landfilling of non-hazardous waste in 2008. Proposals to increase the landfill levy further and introduce an incineration levy will weaken cost competitiveness further.
- With regard to telephone costs, Ireland is the fourth cheapest benchmarked location for international calls, averaging 19 per cent less than the euro area average. The cost of high usage mobile packages is significantly cheaper in Ireland than the euro area average.
- Ireland is an expensive location for broadband services on a per megabit basis; at \$16.31 per megabit, the cost in Ireland is significantly higher than the OECD - 28 average of \$7.24.

Business Services Costs

- According to the Services Producer Price Index which is experimental CSO data, the overall cost of services fell by four per cent in the year to Q1 2010.
- There were significant disparities in the rate of reduction at a sectoral level with computer service costs falling by 16.1 per cent between their peak in Q3 2007 and 2009. For the same period the legal, accounting, PR and business management consultancy category decreased by 1.8 per cent.
- Accountancy costs fell from Q1 2008 onwards and by Q4 2009, they were 6.8 per cent below 2006 prices. Conversely, the cost of legal services have not responded significantly to the recession, and in Q4 2009 they were 18.5 per cent above the average 2006 price.
- Limited data is available on insurance costs across countries. High insurance density (insurance spend per capita) can reflect both high insurance costs and a requirement for high coverage levels. Among the benchmarked locations, Ireland has the fifth highest density of non-life insurance (i.e. motor, property, employer's liability, public liability, travel and other business insurance) per capita but is below the euro area average.

Broader Cost Environment

- Following a period of significant growth, the consumer price index peaked in 2008 when prices were 26.3 per cent higher than 2001 prices. Since then the index has fallen and prices at the end of Q1 2010 were 7.8 per cent below the peak level. Between February 2009 and February 2010, Ireland experienced a 2.4 per cent decrease in the harmonised index of consumer prices, the highest in the euro area and the second highest decrease among EU member states.
- A comparison of consumer costs between major cities indicates that Dublin's cost competitiveness across a basket of goods improved between 2008 and 2009 as the city moved three places up the affordability rankings.
- Irish employees have high purchasing power levels relative to employees in many of our key trading partners. The average Irish employee must work a shorter amount of time than those in most other benchmarked locations to earn enough to buy branded consumer goods such as an iPod Nano or a Big Mac.
- Ireland is an expensive location for purchasing groceries. For a comparable basket of food and non-alcoholic beverages, Ireland ranks as the second most expensive European country, 19.4 per cent above the euro area-16 average (Fig. 7.2.2).
- By the end of Q2 2009, housing affordability for those in employment had returned to levels last experienced in the year 2000. Dublin remains an expensive location to rent residential accommodation relative to other European cities.
- The costs of a range of public and administered services continue to negatively affect Irish cost competitiveness. The cost of health and education services continues to rise rapidly, further increasing the gap between these components and the other goods included in the consumer price index. Transport costs, such as urban public transport and taxis, are relatively expensive in Ireland compared with our main trading partners.
- Although public sector wages do not have a direct impact on the cost of doing business in Ireland, as a significant component of the cost of public and administered services they do have an indirect effect. The starting salary for primary teachers in Ireland in 2010 is 15 per cent above the OECD-25 average, while the top salary scale for primary school teachers in Ireland is 33 per cent above the OECD average. In the health sector, Ireland had the highest average salary for medical specialists and fourth highest salary for nurses.

1. Introduction

Generating sustainable export-led growth is essential to rebuilding our economy. This will require a substantial improvement in cost competitiveness and strong productivity growth in all parts of the economy. A large increase in exports will not provide a panacea for the challenges facing the Irish economy or bring about an automatic reversal in our unemployment trends. However, improving Ireland's attractiveness as a location to do business will be important to restore the levels of confidence necessary to boost investment and halt the decline in domestic consumption seen since 2008. It will also help to stabilise government revenues through corporation and income tax receipts.

A high cost base is a damaging legacy of the housing and domestic consumption boom. Improving our relative cost competitiveness requires the cost of doing business in Ireland to fall relative to that of our trading partners.

The NCC has benchmarked Ireland's cost competitiveness for a number of years and has extended the scope of the Cost of Doing Business, 2010 to address three issues:

1. How does Ireland compare on key business input costs?
2. What makes markets function/not function?
3. What actions are required to improve performance?

This paper addresses the first issue - i.e. it analyses Ireland's relative cost competitiveness performance across four key business inputs - labour, property, utilities and business services (e.g. accounting and legal services). It also looks at the broader cost environment that has an indirect impact on the cost of doing business here.

The other two issues will be examined in phase two of the project which will be completed later in the year.

1.1 Overview of Ireland's Cost Competitiveness

Strong domestic growth in recent years created the conditions which led to significant increases in the costs of doing business in Ireland. Key business inputs such as pay and incomes, rents, utilities and business services rose sharply for an extended period.

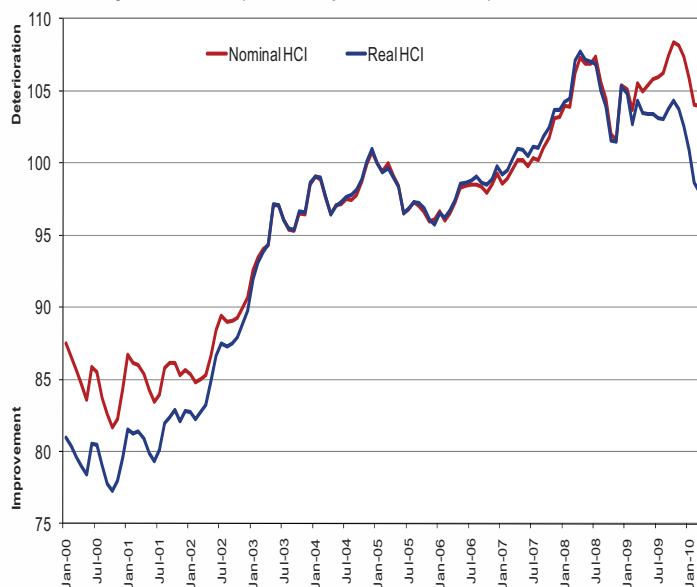
The recession induced fall in demand and the strength of the euro (as imports become cheaper) is resulting in a fall in the price level in Ireland. Irish inflation, as measured by the CPI, declined by 1.1 per cent in the year to May 2010⁸. Inflation fell significantly across most goods and services groups in 2009 and Q1 2010, but exceptions remain. Clothing and footwear (-12.6 per cent) and food and non-alcoholic beverages (-6.3 per cent) experienced the most significant price decreases over the year. Education (9.1 per cent) and transport (4.9 per cent) both increased during the 12

⁸ CSO, Consumer Price Index, March 2010.

months. Inflation, as measured by the HICP (which excludes mortgage interest payments⁹), declined by 2.4 per cent in the year to April 2010, compared to an increase of 1.5 per cent in the euro area and 3.7 per cent in the UK.

Ireland experienced a 7.7 per cent loss in cost competitiveness (real HCI) between January 2005 and April 2008 reflecting a combination of an appreciation of the euro against the currencies of many of our trading partners (nominal HCI) and higher price inflation in Ireland. Ireland has regained some of its competitiveness since then because of falls in relative prices and favourable exchange rate movements vis-à-vis key trading partners. In April 2010, Ireland's real HCI was 3.4 per cent below the January 2005 value (Fig. 1.1). However, the real HCI remains 19 per cent above the January 2000 level.

Figure 1.1: Harmonised Competitiveness Indicators, 2000 - April 2010 (January 2005 =100)¹⁰



Source: Central Bank of Ireland

It is important to seek to determine if progress to date is sufficient to restore competitiveness and whether further adjustments are necessary. Recent research from the European Commission¹¹ acknowledges that Ireland has registered significant gains in cost competitiveness in 2008 and 2009. The Commission highlights that Ireland is the only country that provides clear evidence of competitiveness rebalancing. Since the outbreak of the financial crisis in 2007, the intra-euro-area REER based on GDP deflators has depreciated by almost 7 per cent. However, Commission research suggests that the Irish REER remains approximately 6 per cent overvalued - though it highlights that this figure should be treated with caution¹². Similar assessments from the European Central Bank and the IMF estimate that Ireland's real exchange rate is overvalued by 6 - 10 per cent¹³.

Recent price falls in Ireland are largely a cyclical response to the Irish and international recession (e.g. reduced demand, spare capacity, falling interest rates, falling fuel and food prices) rather than a response to structural changes in the Irish economy. Structural or policy induced changes are necessary to ensure that prices in Ireland will not escalate and erode competitiveness when the Irish and international economy return to growth.

⁹ Other items such as home and motor insurance and motor tax are excluded from the HICP.

¹⁰ The nominal HCI is a nominal effective exchange rate for the Irish economy that reflects, on a trade-weighted basis, movements in the exchange rates vis-à-vis 56 trading partners. The real HCI (deflated by consumer prices) takes into account relative price changes along with exchange rate movements.

¹¹ Surveillance of Intra-Euro-Area Competitiveness and Imbalances, European Economy 1|2010

¹² Based on 'current account norms' and 'net foreign asset stabilisation' assessments.

¹³ ECB, IMF 2009 Article IV Ireland Consultation and European Commission Quarterly Report on the Euro Area Volume 8, No. 1 (2009).

In order for the economy to make the necessary transition from a reliance on domestic demand to sustainable export-led growth in the medium term, policies need to facilitate the convergence of Irish costs towards the levels of our trading partners. As prices and costs are now falling in many developed countries, this means that in order to improve our relative cost competitiveness we need to achieve reductions in costs faster than the euro area average.

1.2 Methodology

Chapter 2 uses sectoral cost profiles to assess the importance of various costs to 17 sectors of the economy. The cost profiles have been developed using KPMG's Competitive Alternatives 2010 report¹⁴.

The following cost components are captured;

- Labour Costs
- Property (leased facility)
- Utilities
- Transport
- Interest and Depreciation
- Total Taxes (net of grants)
- Location Insensitive Costs


Using the Competitive Alternatives study, the NCC has created indicative cost profiles for a number of sectors which are of importance to the Irish economy. The values for the various costs components of the case study firms in each of the ten benchmarked locations were used to create average sectoral cost profiles. The profiles enable an indication of the varying importance of the different cost components to individual sectors.

For chapters 3 to 7, internationally comparable unit cost data was collected for Ireland and a number of key trading partners¹⁵. Given that the prices of internationally traded business inputs are set on world markets (e.g. industrial equipment or commodity raw materials), this report concentrates on the costs that are largely domestically determined such as labour, property, energy, water, waste, communications and business services. Where comparable data is available, costs are compared over time.

The unit cost data reflects current market rates (using the most up to date data available). These costs are accessible to new businesses and to existing businesses where market rigidities do not exist. Market rigidities may exist when firms have contracts or terms of agreement with employees and suppliers that pre-date recent changes in business costs. It is likely that the cost base of existing firms will respond more slowly to cost fluctuations than new firms, however, overtime all firms should realise these changes.

¹⁴ Ireland is not included in the study. The benchmarked locations are Australia, Canada, France, Germany, Italy, Japan, Mexico, Netherlands, the UK and the US.

¹⁵ Details of the data sources used in the completion of this report are included in the appendix to this report.



Where possible, Ireland's cost levels are compared to a relevant peer group average, the OECD-28 and euro area average or else compared to as wide a group of countries as possible. Averages are weighted by each country's GDP where relevant. The report uses the most up to date internationally comparative cost data. As much of the data is collected on an annual basis there may be a time lag in capturing more recent changes in cost levels.

2. Cost Profiles

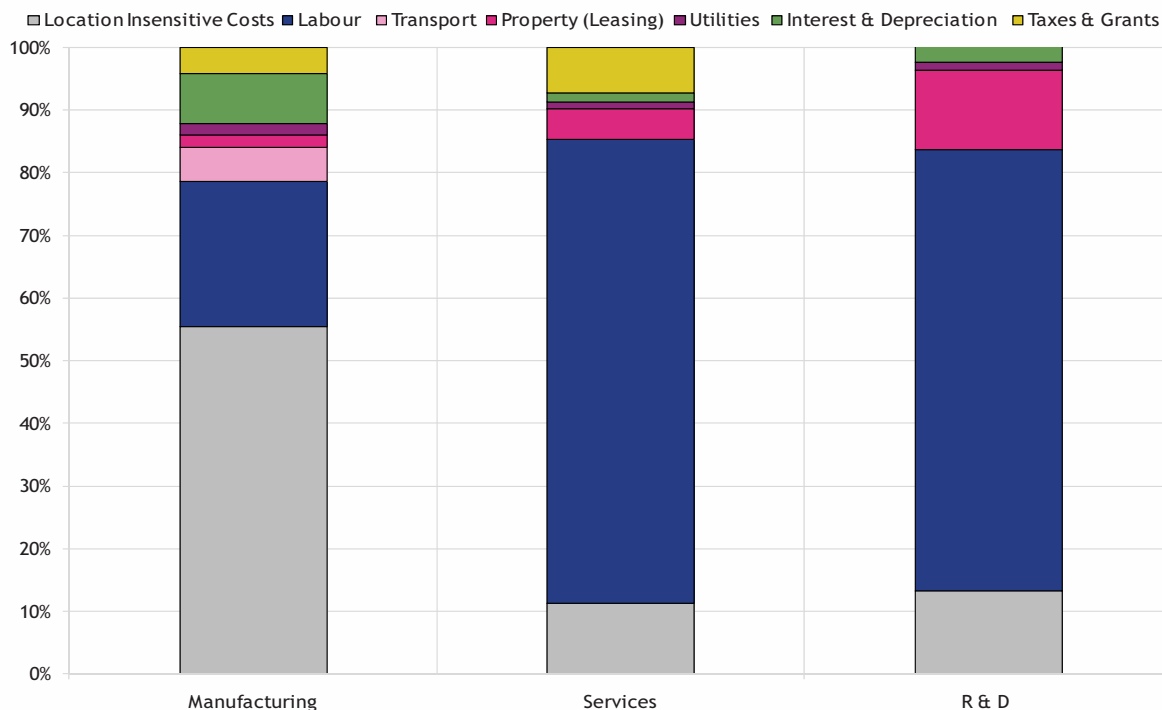
This chapter looks at the relative importance of key business inputs across the main exporting sectors. From a competitiveness perspective, it is essential that public policy focuses on reducing costs that comprise a significant percentage of business costs (as set out in this chapter) and that are out of line with those in competitor countries (chapter three to seven).

The cost profiles have been developed using KPMG’s Competitive Alternatives 2010 report, which uses case study business operations for 17 different sectors and benchmarks the cost of doing business for these model firms in 10 global locations¹⁶.

2.1 Summary Cost Profiles

The summary cost profiles present a breakdown of the cost components for manufacturing, services and research and development (R&D) operations. They illustrate the relative importance of location sensitive and location insensitive costs, i.e. goods and services produced on international markets where the price is determined by global supply and demand conditions.

Figure 2.1: Summary Cost Profiles for Manufacturing, Services and R&D Operations



Source: KPMG, ‘Competitive Alternatives, 2010’, Forfás calculations

A striking, though not unexpected, feature of the comparison of the summary cost profiles is that relative to manufacturing, location insensitive costs form a small component of total costs for services (11 per cent) and R&D (13 per cent). Over half of the total costs in manufacturing (56 per

¹⁶ Ireland is not included in the study. The benchmarked locations are Australia, Canada, France, Germany, Italy, Japan, Mexico, Netherlands, the UK and the US. In past reports, the NCC used internally developed cost profiles. For this report we have adapted KPMG’s profiles as they are more timely and comprehensive. Nonetheless, the profiles are broadly similar.

cent) are accounted for by location insensitive costs. Location insensitive costs include inputs for which the price is set in international markets, such as materials and equipment. As location insensitive costs do not influence decisions on where to invest, these cost elements have been excluded from the more detailed sectoral cost profiles below¹⁷.

Labour costs are the largest cost components for services (74 per cent) and R&D (70 per cent). Labour costs account for 23 per cent of total manufacturing costs. Given their contribution to total costs, the competitiveness of a country's labour costs significantly impact on overall cost competitiveness.

A range of other costs also affect the cost competitiveness of firms. These costs are assessed in detail in section 2.2. At a high level, it is not surprising that transport is a significant cost for manufacturing (five per cent) while not for services or R&D operations. Leasing property is a considerable cost for R&D operations (13 per cent) and forms a smaller portion of total costs for services (five per cent) and manufacturing (two per cent)¹⁸. The depreciation of assets forms a noteworthy element of total costs for manufacturing (eight per cent) and R&D (four per cent). Finally, 'taxes and grants' are calculated as total taxes less total grants. For services (seven per cent) and manufacturing (four per cent), taxes outweigh grants and contribute to total costs. It should be noted that in the R&D sector, the value of grants is higher than the value of taxes across the ten countries benchmarked and provides a cost write off of one per cent.

2.2 Sectoral Cost Profiles

The following sectoral cost profiles provide an indication of the contribution of various location sensitive cost components to total costs in a number of key sectors. As the profiles are based on a single case study firm in each sector, the profiles should be regarded as indicative rather than representative of the structure of costs across sectors.

2.2.1 Manufacturing Sectors Cost Profiles

Location insensitive costs have been eliminated from Figure 2.2.1 to facilitate a more detailed assessment of the impact of various location sensitive cost components for a range of manufacturing operations. As outlined above, location insensitive costs are most significant in manufacturing sectors, averaging 56 per cent of total costs in manufacturing firms. The significance of location sensitive costs varies considerably across sectors within the manufacturing sector. 62 per cent of total costs in the medical devices sector are location sensitive compared to 32 per cent in the chemicals sector.

¹⁷ It should be noted that this assumption may not hold in all cases. For example, peripheral locations may face additional transportation costs on commodity products. Domestic policies such as taxes and tariffs may also impose additional costs on 'location insensitive costs'.

¹⁸ All of the case study firms used in the KPMG report lease rather than buy property.

Figure 2.2.1: Manufacturing Sectors' Cost Profiles (Location sensitive costs)



Source: KPMG, 'Competitive Alternatives, 2010', Forfás calculations

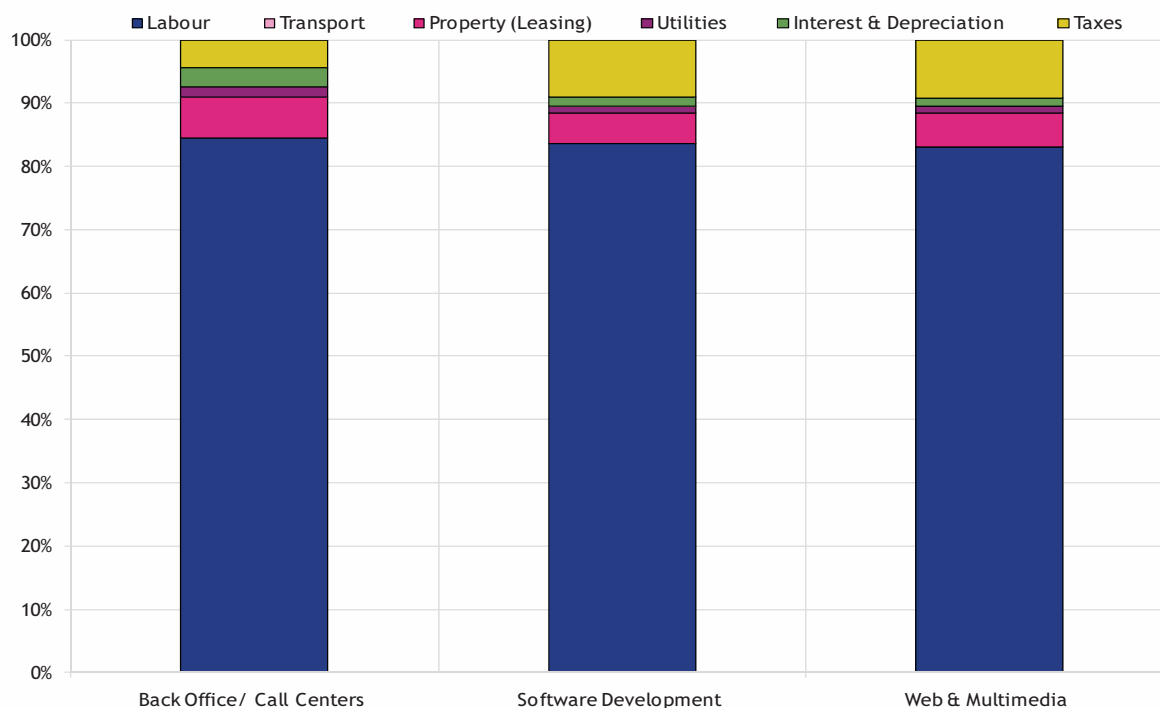
The contribution of labour costs to total location sensitive costs varies from 45 per cent in the case study plastics firm to 56 per cent in the case study medical devices firm. Transport costs are a major component of locally determined costs for the case study plastics (18 per cent) and agri-food operations (16 per cent). This is significant for Irish agri-food firms given the regional dispersion of the sector. Utilities are also an important cost input for the agri-food (six per cent) and chemicals (seven per cent). In light of the importance of these sectors to the Irish economy, measures to bring our relatively higher electricity (Fig. 5.1.1 and 5.1.2) and waste costs (Fig. 5.2.2) into line with our main trading partners must be progressed quickly. Across the sectors benchmarked, taxes are most significant in the chemical and electronics sector (14 per cent) and to a lesser degree agri-food (12 per cent) and pharmaceuticals (10 per cent).

2.2.2 Service Sectors Cost Profiles

On average, location insensitive costs account for just 11 per cent of total cost for the case study services firms, making services operations highly sensitive to locally determined cost. In 2009 services exports accounted for 47 per cent of total Irish exports compared to 25 per cent in 2001¹⁹. Given the increasing importance of services exports to the Irish economy, ensuring Ireland is a cost competitive environment for firms in the services sector to do business should be a policy priority.

¹⁹ CSO Balance of Payment March, 2010

Figure 2.2.2: Service Sectors' Cost Profiles (Location sensitive costs)



Source: KPMG, 'Competitive Alternatives, 2010', Forfás calculations

Location insensitive costs have been eliminated from Figure 2.2.2. As is to be expected, labour costs are the main component of costs in services sectors. They account for 76 per cent of location sensitive costs for back office and call centre operations and 74 per cent for software development and web & multimedia operations. Taxes (less grants) account for nine per cent of costs for software development and web & multimedia, while leasing costs are significant for back office / call centre operations (six per cent). Ireland has seen significant declines in the costs of renting prime office space since 2008 and compares favourably with many of the locations benchmarked (Fig. 4.5).

The KPMG report does not provide a cost profile of the tourism sector, or any of its sub-sectors. However, as part of previous research undertaken on behalf of the NCC a cost profile was developed for a case study business hotel. 59 per cent of location sensitive costs in the sample business hotel firm were accounted for by labour costs, 13 per cent was attributed to property costs and eight per cent to utilities²⁰.

2.2.3 R&D Sectors Cost Profiles

On average 13 per cent of costs for R&D operations are determined on global markets. Of the three R&D sectors benchmarked in this report, clinical trials operations are the most sensitive to locally determined costs (93 per cent).

²⁰ OCO Consulting research for NCC, Cost of Doing Business 2006. The cost profile was based on a case study firm based in Ireland in 2005.

Figure 2.2.3: R&D Sectors' Cost Profiles



Source: KPMG, 'Competitive Alternatives, 2010', Forfás calculations

Similarly to the services case studies, it is unsurprising that labour costs comprise such a large component of location sensitive costs for the case study R&D operations. They account for 91 per cent of costs within the clinical trials firm, 78 per cent within the product testing operation and 73 per cent within the biotechnology firm. The leasing of property of a major cost element for these firms also (18 per cent for biotechnology, 15 per cent for product testing). Due to substantial grants for R&D operations across many countries, taxes amount to less than 0.9 per cent of locally determined costs for the case study biotechnology firm and 0.6 per cent for product testing. For the clinical trials case study operation, on average grants exceed taxes across the ten countries benchmarked and provide a 3.2 per cent cost write off.

3. Labour Costs

As discussed in chapter 2, labour costs are the most significant location sensitive cost for all sectors. This section examines trends in relative labour costs across countries, trends in unit wage costs, and salary levels in range of job categories²¹.

3.1 Labour Cost Growth Rates and Unit Labour Costs

Labour cost growth rates show the change in the cost of employing workers over time. Ireland's growth rates exceeded the EU-15 average between 2004 and 2007. However, growth rates in Irish labour costs slowed significantly in 2008 and the first half of 2009 and were lower than the EU-27 and euro area-16 average (Fig. 3.1.1).

Total labour costs include wages, taxes on income and employer and employee social security contributions. Ireland has the tenth highest total labour costs level in the OECD and is in line with a number of western European countries (Fig. 3.1.2). Ireland has the fifth highest net wage level in the OECD-28, 35.5% above the OECD-28 average. This is due, in part, to Ireland's low tax wedge on labour.

Between 2000 and 2006, the average annual increase in total compensation per employee was significantly higher in Ireland (6.2 per cent) than the euro area (2.3 per cent). However, the rate of increase in average compensation began to slow in Ireland in 2007 (Fig. 3.1.3). In 2009, average employee compensation continued to grow in the euro area (1.4 per cent) while it fell in Ireland (-2.24 per cent).

The Central Bank recently highlighted a number of caveats to be aware of when using compensation levels to review international labour cost comparisons (compensation levels are not adjusted for differences across countries in age, educational attainment and sectoral composition) and advised that such comparisons should be viewed as crude and treated with caution²². The Central Bank found compensation across the economy on a per hourly basis was 12.8 per cent higher in Ireland than the euro area average in 2008. Looking specifically at the industrial sector, however, labour costs on a per hourly basis were 13.4 per cent below the euro area average in 2008. This indicates that compensation levels in the more sheltered sectors of the Irish economy are likely to be significantly higher than those in our main trading partners.

Unit labour costs (ULC) measure the average cost of labour per unit of output. Declining ULC mean that productivity has increased faster than earnings - thus indicating an improvement in competitiveness. In 2005, Irish ULC grew by 5.2 per cent, significantly ahead of both the euro area and OECD averages (1.3 per cent), however, in 2008, Irish ULC converged with the euro area average. During the first three quarters of 2009, unit labour costs fell in Ireland by 1.5 per cent, while the OECD and euro area averages continued to experience slow ULC growth of 0.2 and 0.8 per

²¹ Data relating to job categories is based on the Watson Wyatt Global 50 Planning Remuneration Report 2009. Details of the report and the job categories are included in the appendix.

²² Derry O'Brien, Central Bank, "Measuring Ireland's Price and Labour Cost Competitiveness", Quarterly Economic Commentary, January 2010.

cent respectively (Fig. 3.1.3). Therefore, at an economy wide level, Irish labour wage rates - when adjusted for productivity - are becoming more cost competitive.

3.2 Salary Levels

This section compares salary levels across a range of occupations and sectors in Ireland with those in a range of international locations and the euro area average. The data for this section is compiled using the Global 50 Remuneration Survey report, published by Towers Watson Wyatt²³. The salary data represents 12 months' gross salary plus any guaranteed bonuses such as legal holiday pay, extra contractual months, etc. The salary data does not include other non-wage costs such as employers' social welfare contributions.

Irish salary levels are broadly in line with the euro area average across the benchmarked occupations. Irish salaries are higher than those in the US for comparable positions and for most comparable positions in the UK (Fig 3.21 - Fig. 3.2.8). While Irish salary levels remain significantly below those in the most expensive countries (such as Denmark, Germany and Japan), they are generally a multiple of those available in Eastern Europe (Poland and Hungary) and India - countries that we are increasingly competing with for trade and investment. The wage cost differential between skilled and unskilled production operatives is 17.1 per cent in Ireland compared to an average of 16.3 per cent in the euro area (Fig. 3.2.1).

Finally, Ireland has one of the highest minimum wage rates in Europe at €8.65 per hour (€1,462 per month). However, when measured as a percentage of the average industrial wage, the minimum wage in Ireland is seventh highest within the EU. According to the CSO, 1.3 per cent of employees were receiving the minimum wage in Q2 2009²⁴. It is notably however that in hotels and restaurants, wholesale and retail and other locally traded service industries have a notably higher proportion of employees in receipt of the National Minimum Wage or on pay levels determined by it²⁵.

3.3 Social Security Contributions and Labour Taxation


There are significant disparities across locations in relation to the levels of social security contributions and labour taxation. Ireland has one of the lowest levels of employers' social welfare contributions (Fig 3.3.1). The Irish rate (10.8 per cent) is significantly lower than the OECD average (15.2 per cent) and the euro area average (27 per cent), which reduces the total cost of employing workers in Ireland.

Ireland's tax wedge on labour (i.e. the gap between what the employer pays and what the employee receives) for a married couple (with two children) with a combined salary of 167 per cent of the average wage rose from 14 per cent in 2008 to 19.8 per cent in 2009 as a result of increases in income and health levies (Fig. 3.3.2). The tax wedge is significantly higher for higher income

²³ This report is uses a global job-worth hierarchy designed to underpin survey job matching on a consistent worldwide basis. It categorises positions using a number of variables such as tasks, skills, expertise and levels of responsibility. The report provides salary data for 50 generis roles across ten broad job families.

²⁴ CSO, Earning and Labour Costs, Quarter 2, 2009, Preliminary Estimates, 2009.

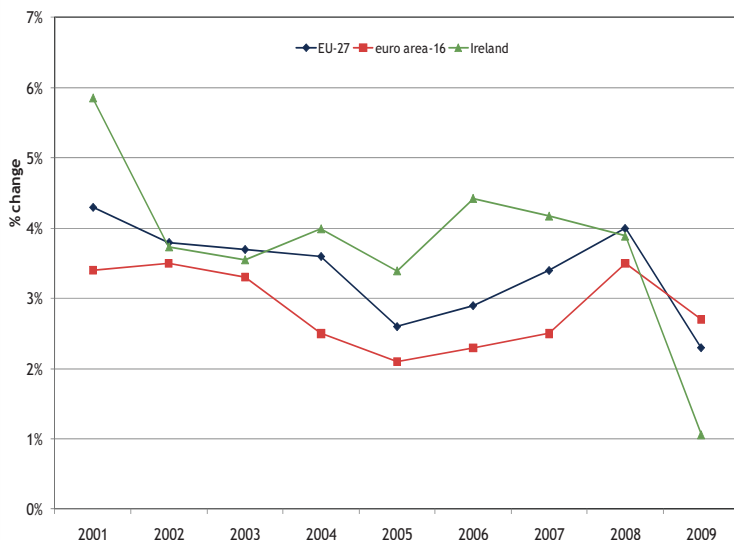
²⁵ CSO, National Employment Survey, 2007.



earners - a potential disincentive for highly skilled internationally mobile workers (Fig. 3.3.3). For a single worker (with no children) on 167 per cent of the average wage, the tax wedge has increased from 34 per cent in 2008 to 39 per cent in 2010.

3.1 Labour Cost Indices and Unit Labour Costs

Figure 3.1.1: Labour Cost Index, 2009

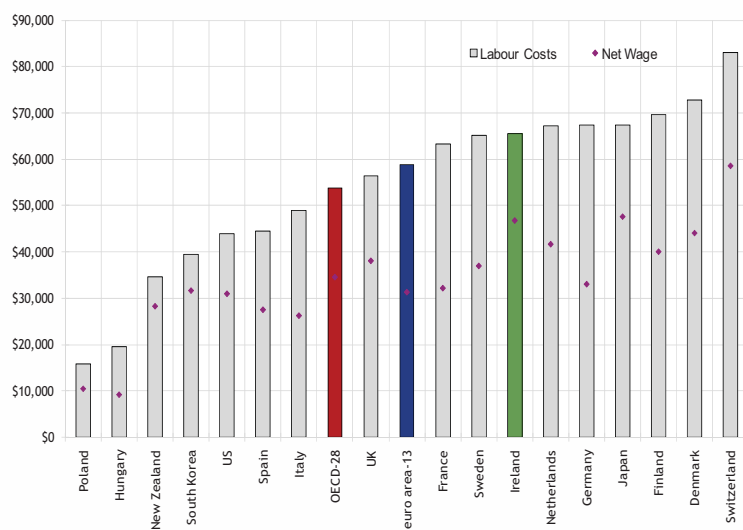


This indicator shows the trend in labour cost growth in Ireland compared with the euro area-16 and EU-27. Data for the euro area-16 and EU-27 is provided to the end of 2009, while the most recent data for Ireland is to the end of Q2 2009²⁶.

The rate of growth in Irish labour costs has fallen from a high of 5.9% in 2001 to 1.1% at the end of Q2 2009. In 2009, the euro area-16 and EU-27 growth rates declined by 1.7% and 0.8% respectively, while within the first six months of 2009 Irish labour costs fell by 2.8%.

Source: Eurostat, Population and Social Conditions, CSO, Labour Cost Index

Figure 3.1.2: Average Total Labour Costs and Net Wages, 2009



This indicator shows total labour costs for a single person with no children earning the average wage. Total labour costs include wages, taxes on income and employer and employee social security contributions. Ireland has the tenth highest total labour costs level in the OECD and is in line with a number of western European countries.

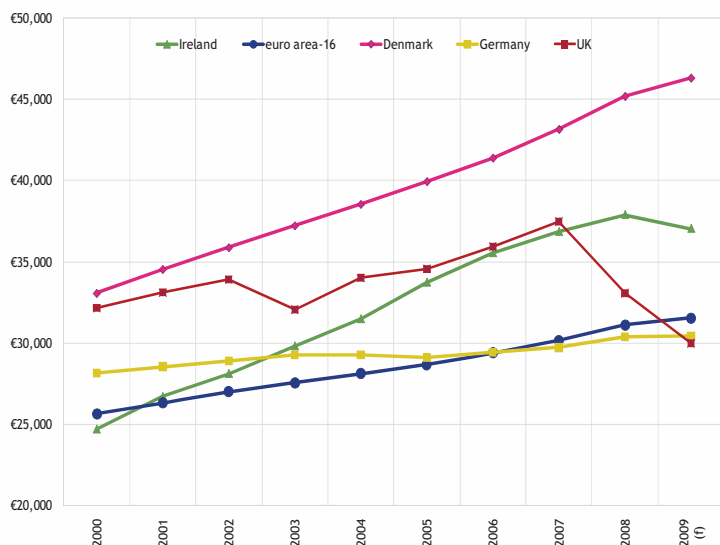
The chart also shows average net wage levels. Ireland has the fifth highest net wage level in the OECD-28, 35.5% above the OECD-28 average. This is due, in part, to Ireland's low tax wedge²⁷ on labour.

Source: OECD, Taxing Wages 2009, OECD, Comparative Price Levels March 2009, Forfás calculations

²⁶ Quarterly data is not available for the EU-27 and euro area 16 group

²⁷ The labour tax wedge is the difference between what the employer pays and what the employee receives.

Figure 3.1.3: Total Compensation²⁸ per Employee Across the Entire Economy, 2000 - 2009f



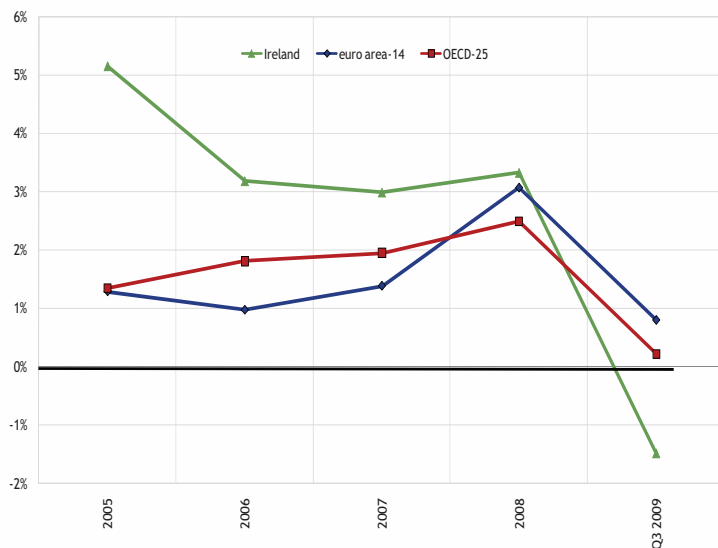
At the beginning of the period, compensation per employee in Ireland was slightly below the euro area average and Ireland had the lowest compensation level of the benchmarked countries.

Between 2000 and 2006 compensation per employee rose rapidly in Ireland (6.3%) compared to the euro area (2.3%).

In 2009, average employee compensation continued to grow in the euro area (1.4%) while it fell in Ireland (-2.24%). The decline in compensation was greater in the UK (9.3%).

Source: Eurostat, National Accounts Groningen, Total Economy Database

Figure 3.1.4: Annual Change in Unit Labour Cost, 2005 - Q3 2009



Unit labour costs (ULC) measure the average cost of labour per unit of output. A downward sloping line indicates an improvement in competitiveness.

In 2005, ULC in Ireland increased by 5.2% compared to an average of 1.3% in both the OECD-25²⁹ and the euro area-14. In 2008, the rate of ULC growth in Ireland (3.3%) was close to converging on the euro area-14 average (3.1%). During the first nine months of 2009 ULC growth was slow in the OECD-25 (0.2%) and the euro area-14 (0.8%). During the same period, ULCs in Ireland declined by 1.5%, indicating an improvement in competitiveness.

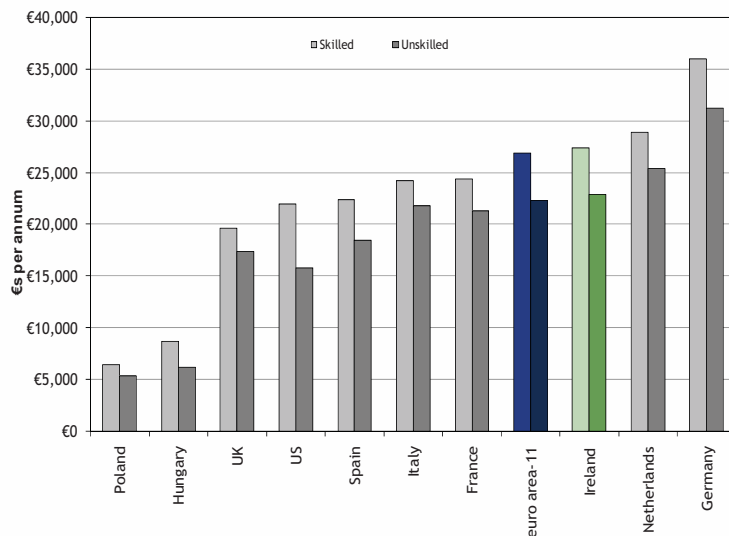
Source: OECD, Unit Labour Cost Quarterly Indicators

²⁸ Total compensation is the total expenditure borne by employers for the purpose of employing staff. It includes employee compensation (including wages, salaries in cash and in kind, employers' social security contributions), vocational training costs, other expenditure such as recruitment costs, spending on working clothes and employment taxes regarded as labour costs minus any subsidies received.

²⁹ The OECD average excludes Iceland and Switzerland, the euro area average excludes Malta and Portugal.

3.2 Salary Levels ³⁰

Figure 3.2.1: Wage Costs for Skilled and Unskilled Production ³¹ Operatives, 2009

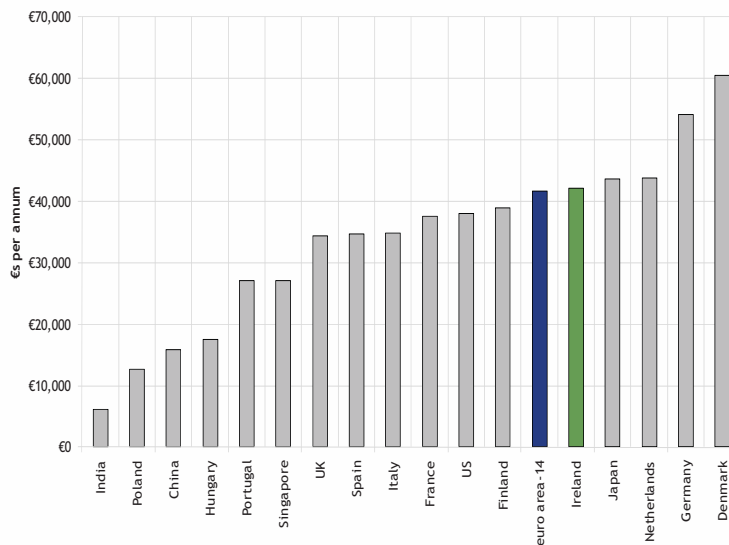


The annual wage cost for an unskilled production operative in Ireland is (2.8%) above the euro area average. Also, the wage cost for a skilled production operative is (1.8%) above the euro area average³².

The wage cost differential between skilled and unskilled production operatives is 17.1% in Ireland compared to an average of 16.3% in the euro area.

Source: Towers Watson Wyatt, 2009 / 2010

Figure 3.2.2: Financial Services - Junior Accountant, 2009



This indicator measures the annual salary for a junior accountant with two to three years experience.

Of the 17 countries benchmarked, junior accountants' wage costs in Ireland are the fifth highest - 23% ahead of the UK (key competitor), 11% ahead of the US (key source of FDI) and 1.3% above the euro area average. Costs are considerably lower in Poland, Hungary and India - locations that are increasingly competing for mobile FDI in financial services.

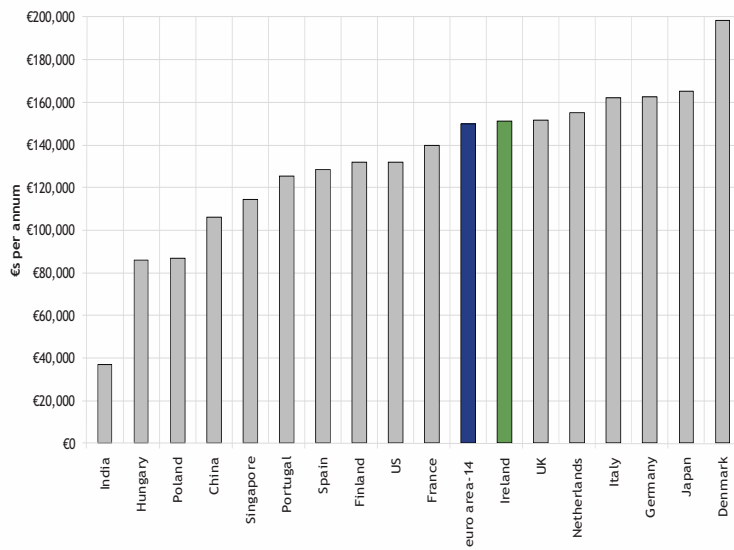
Source: Towers Watson Wyatt, 2009 / 2010

³⁰ The salary data represents 12 months' gross salary plus any guaranteed bonuses such as legal holiday pay, extra contractual months, etc. The salary data does not include other non-wage costs such as employer's social welfare contributions. The euro area-14 averages in these indicators (with the exception on Fig 3.2.1) exclude Cyprus and Malta.

³¹ Towers Watson Wyatt defines grade five production operatives as skilled workers. The wage costs of unskilled operatives are captured using the data for grade three positions. Grade three operatives require assistance from more senior positions in order to contribute to the organisation.

³² As the Towers Watson Wyatt database does not provide data for unskilled workers in Cyprus, Finland, Luxembourg, Malta and Slovenia are excluded from the euro area average.

Figure 3.2.3: Financial Services - Head of Finance, 2009



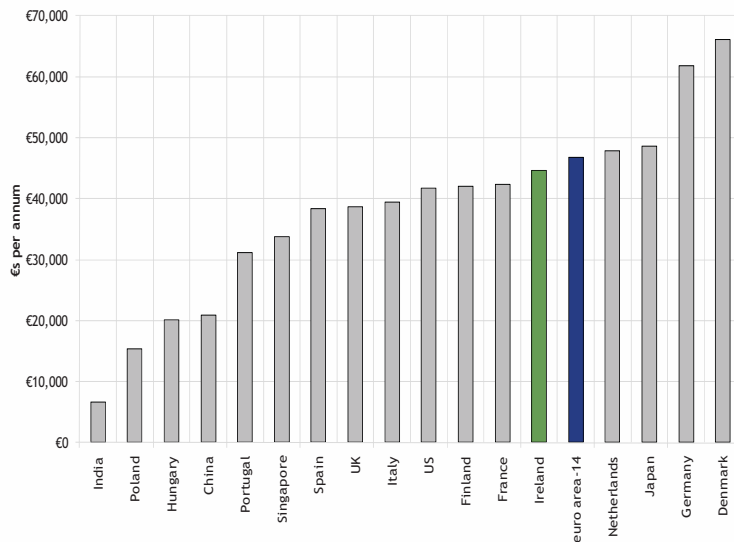
This indicator measures wage costs for heads of finance, defined as someone that controls the financial function within small-to-medium sized firms.

Of the 17 benchmarked locations, Ireland ranks as the seventh most expensive.

Ireland remains relatively cost competitive compared with the euro area average but is 14.5% more expensive than the US. Ireland is 24% cheaper than Denmark, the most expensive location.

Source: Towers Watson Wyatt, 2009 / 2010

Figure 3.2.4: ICT - Systems Analyst, 2009

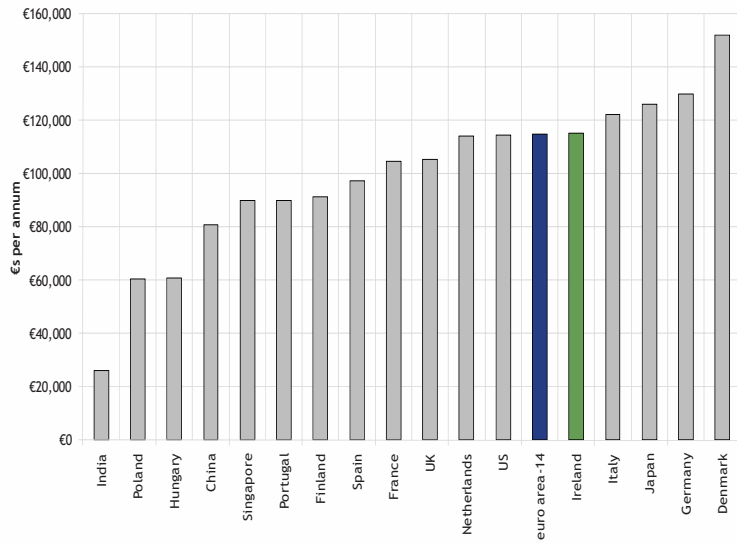


This indicator measures the wage costs for a systems analyst/ programmer, defined as someone who has between three and five years experience and works under the guidance of a senior analyst.

The wage costs for a systems analyst in Ireland are below the euro area average. However, Ireland is a significantly more expensive location for employing systems analysts than the UK where wage costs for comparable positions are 13.5% lower. Costs in India, Poland and Hungary are substantially lower.

Source: Towers Watson Wyatt, 2009 / 2010

Figure 3.2.5: ICT-Senior I.T Manager

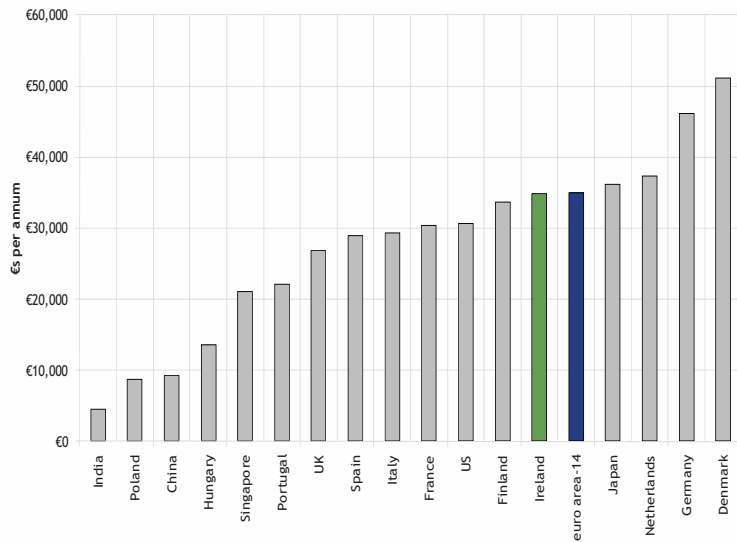


This indicator measures the wage costs for a senior IT manager, defined as someone that is responsible for a number of teams involved in a range of information technology activities and reports to a board level director.

Of the 17 benchmarked locations, Ireland ranks as the fifth most expensive for employing senior I.T managers. It is marginally more expensive than the euro area average. Costs in Poland and Hungary, and in particular, India are substantially lower.

Source: Towers Watson Wyatt, 2009 / 2010

Figure 3.2.6: Engineering - Engineering Technician, 2009

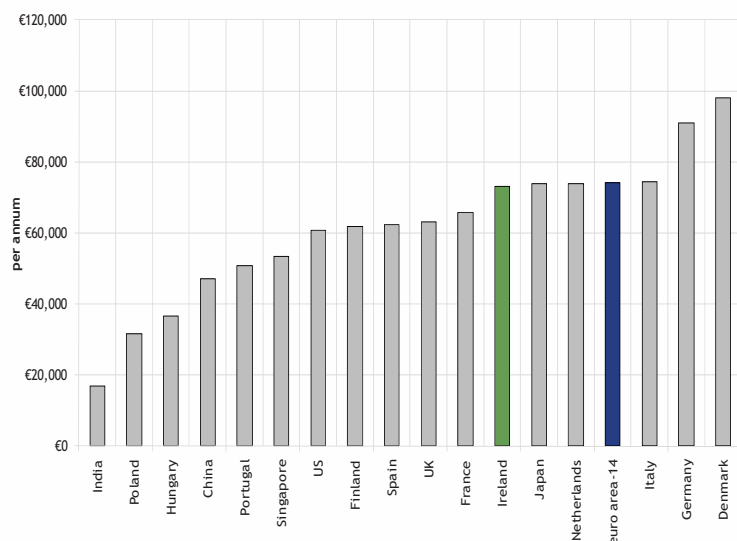


This indicator measures the wage costs for an entry level engineering technician who would typically have a technical certificate with little or no experience and would require close supervision and training on the job.

The wage costs for an engineering technician in Ireland are slightly below the euro area average.

Source: Towers Watson Wyatt, 2009 / 2010

Figure 3.2.7 Engineering - Engineering Manager 2009

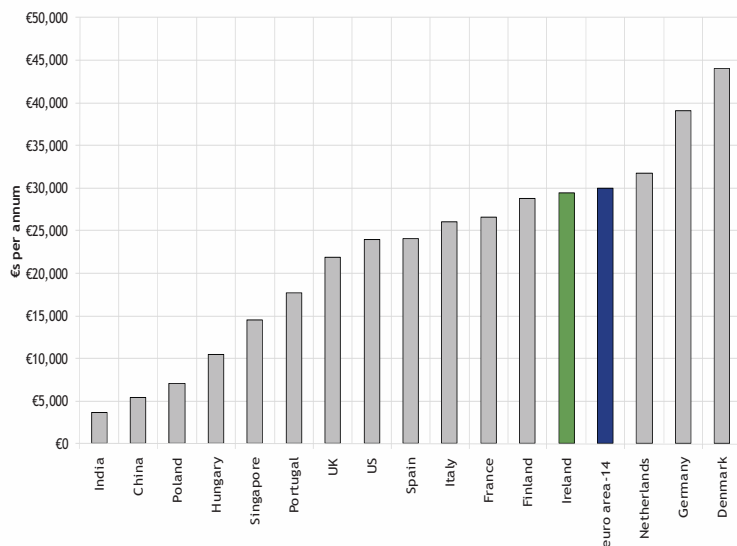


This indicator measures the wage costs for an engineering manager, defined as a qualified engineer responsible for managing a section or project team of more than ten engineers and technicians.

Ireland is 25% cheaper than Denmark, the most expensive location benchmarked and is marginally cheaper (1.3%) than the euro area average for engineering manager wage costs.

Source: Towers Watson Wyatt, 2009 / 2010

Figure 3.2.8: Administration - Department Secretary, 2009

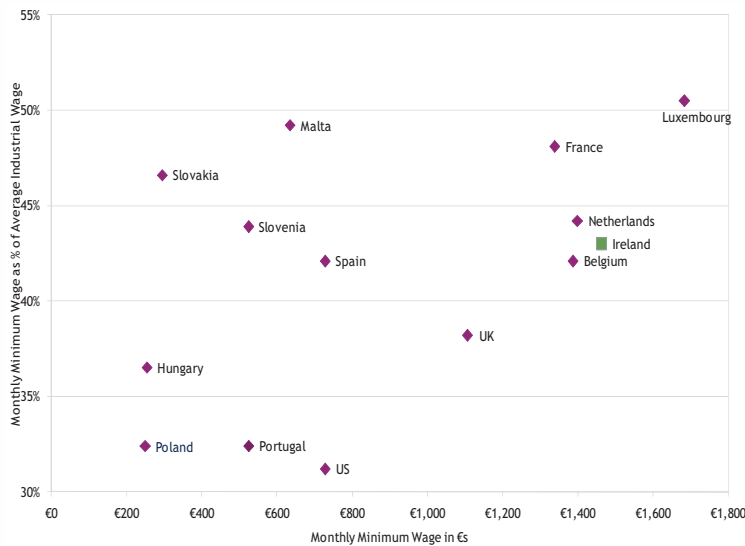


This indicator measures the wage costs for a department secretary, defined as someone who provides administrative support to a number of managers and / or other professionals.

Ireland is the fourth most expensive benchmarked location for department secretary wage costs, but it is below the euro area average.

Source: Towers Watson Wyatt, 2009 / 2010

Figure 3.2.9: Monthly Minimum Wage and Minimum Wage as a % of Average Industrial Wage



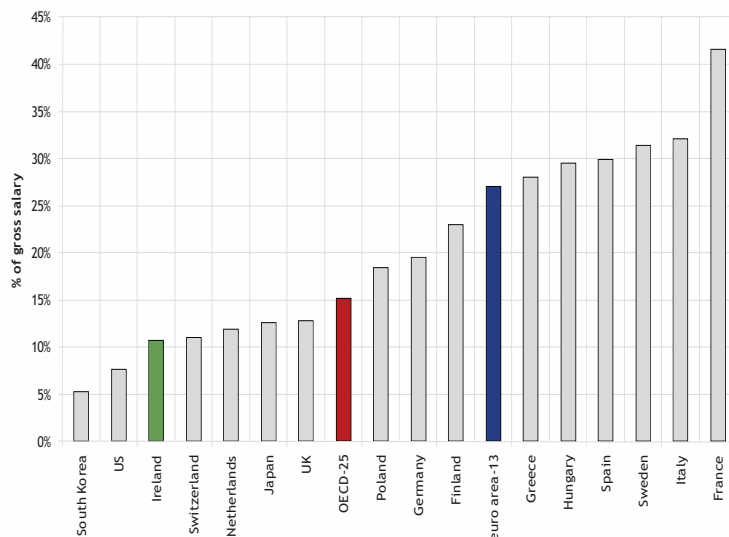
This indicator measures statutory monthly minimum wages and minimum wage as a percentage of the average industrial wage. Ireland has the second highest statutory monthly minimum wage (€1,462). Due to differences in the length of the standard working week, on an hourly basis Ireland (€8.65) has a lower minimum wage than France (€8.82). A number of EU member states³³ operate non-statutory minimum wage rates on a sectoral basis and have rates which are significantly higher than Ireland's.

When measured as a percentage of the average industrial wage, the minimum wage in Ireland is the seventh highest within the EU.

Source: Eurostat, *Populations and Conditions, Eurostat Minimum Wages, 2009*

3.3 Social Security Contributions and Labour Taxation

Figure 3.3.1: Employer Social Security Contributions, 2009³⁴



Social security costs are the statutory contributions that the employer is required to make for employees towards unemployment and sickness benefits.

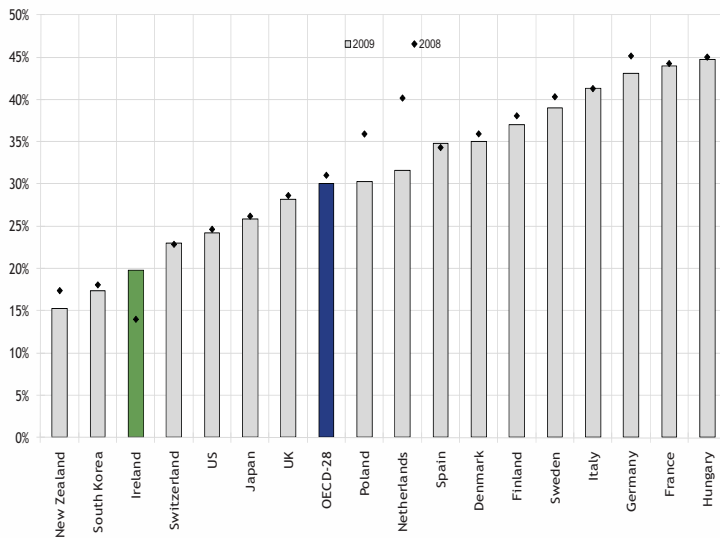
Ireland has the fourth lowest rate of employer social contributions. The Irish rate (10.75%) is significantly lower than the OECD-25 average (15.5%) and the euro area-13 average (27%).

Source: OECD, *Taxing Wages, 2009*

³³ These include Denmark, Finland and Sweden.

³⁴ The OECD-25 average excludes Austria, Denmark and Portugal. The euro area-13 average excludes Cyprus, Luxembourg and Malta.

Figure 3.3.2: Total Tax Wedge on Labour (as a % of Average Earnings), 2009³⁵

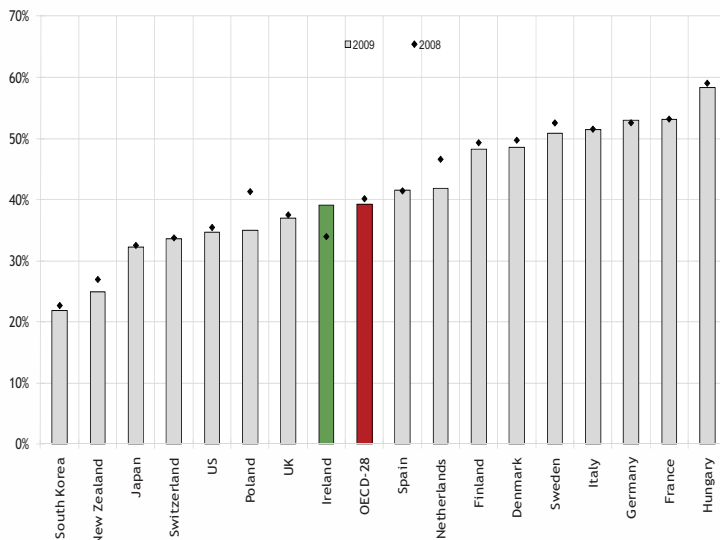


Ireland's tax wedge on labour, i.e. the gap between what the employer pays and what the employee receives has risen significantly since 2008. For a married couple with two children on a combined income of 167% of the average wage the tax wedge is 19.8% in 2009 - an increase from 14% in 2008.

While Ireland still ranks as one of the most competitive countries by this measure, the tax wedge in most OECD countries is unchanged or falling since 2008.

Source: OECD, Taxing Wages, 2009

Figure 3.3.3: Total Tax Wedge on Labour (as a % of Average Earnings), 2009³⁶



Ireland's tax wedge on labour, i.e. the gap between what the employer pays and what the employee receives has risen since 2008. For a single person with no children on 167% of the average wage, the tax wedge is 39% in 2009 (up from 34% in 2008).

This is a potential disincentive for highly skilled internationally mobile workers.

Source: OECD, Taxing Wages, 2009

35 Data based on a two-earner family with a wage level of 100-67% of the average wage.

36 Data based on a single person with no children on 167% of the average wage.

4. Property Costs

This chapter assesses the key property costs for businesses including constructing and renting industrial units and offices.

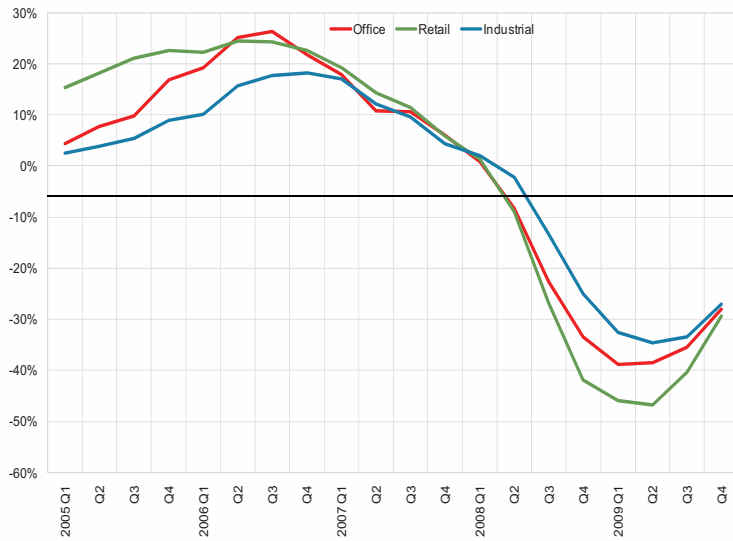
The value of commercial properties in Ireland peaked in Q4 2007. They have been in a steep decline since Q1 2008. While the rate of decline has slowed in the second half of 2009, the value of retail properties fell by 29 per cent, offices by 28 per cent, and industrial premises by 27 per cent between Q4 2008 and Q4 2009 (Fig. 4.1).

The cost of constructing and renting both industrial and office units declined sharply in Ireland during 2009. However, the impact of these decreases on Irish cost competitiveness was relatively muted as there have also been significant cost decreases in many other countries. The main developments include:

- the cost of constructing a prime industrial site fell by 14 per cent in Ireland between 2008 and 2009 - the second sharpest fall across the 13 benchmarked countries. However, Ireland remains the third most expensive benchmarked location (Fig. 4.2).
- the costs of renting a prime industrial unit fell by 18 per cent in Ireland between 2008 and 2009 - the third sharpest fall across the 16 benchmarked countries. With prices falling in 12 of the 16 countries benchmarked, Ireland's ranking improved by just one place. Ireland is still one of the most expensive locations - it ranks third of the countries benchmarked (Fig. 4.4).
- The cost of renting prime office space in Ireland is relatively competitive. Having fallen by almost 25 per cent in 2008, office rental costs fell by another 18 per cent in Ireland in 2009. As a result, Ireland is now a cheaper office rental location than the US and Italy. However, Singapore and Spain both experienced significant price falls in 2009 (49 per cent and 23 per cent respectively) and are now cheaper locations to rent office space than Ireland (Fig. 4.5). The existence of 'upward-only' rent review clauses in Irish rental contracts may have prevented a greater decline in average rental costs. A ban on 'upward-only' rent reviews for all new rental contracts came into effect in February 2010.

There is currently no taxation on property for primary residencies and funding for Local Authorities is drawn from central Government and enterprise. Commercial rates are a form of taxation levied by local authorities on the occupiers of commercial and industrial property. The commercial rate is calculated using the annual rate of valuation (AV). The average AV peaked in 2009 at €64.78 but this decreased by an average of 1.8% to €63.60 in 2010 (Fig. 4.6).

Figure 4.1: Rate of Change for Commercial Property Values in Ireland, 2005 - 2009

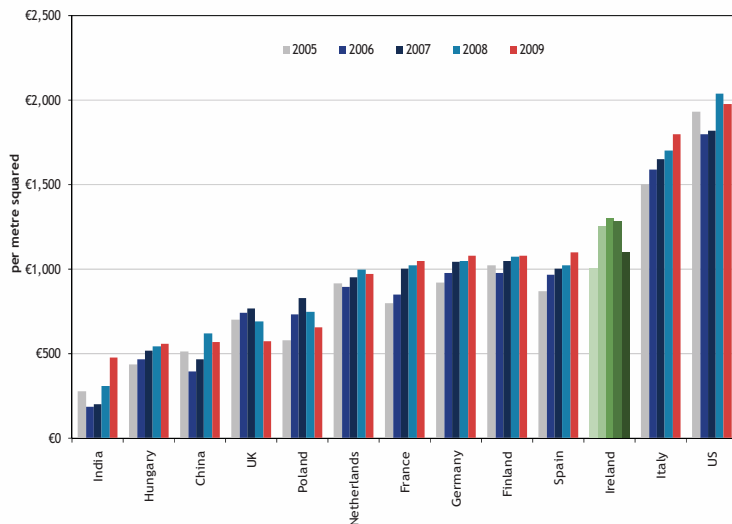


This indicator measures the percentage change in capital values on a year-on-year basis.

The values of commercial properties in Ireland peaked in Q4 2007, but have been in steep decline since Q1 2008. Retail property values experienced the steepest decline. Despite a deceleration in the rate of decline over the year, at the end of 2009, across all three categories, capital values had fallen significantly below the same period in 2008. In 2009, retail values decreased by 29% with office and industrial property values down 28% and 27% respectively.

Source: Society of Chartered Surveyors / IPD Irish Property Index, Central Bank of Ireland

Figure 4.2: Cost of Constructing a Prime³⁷ Industrial Unit, 2005 - 2009



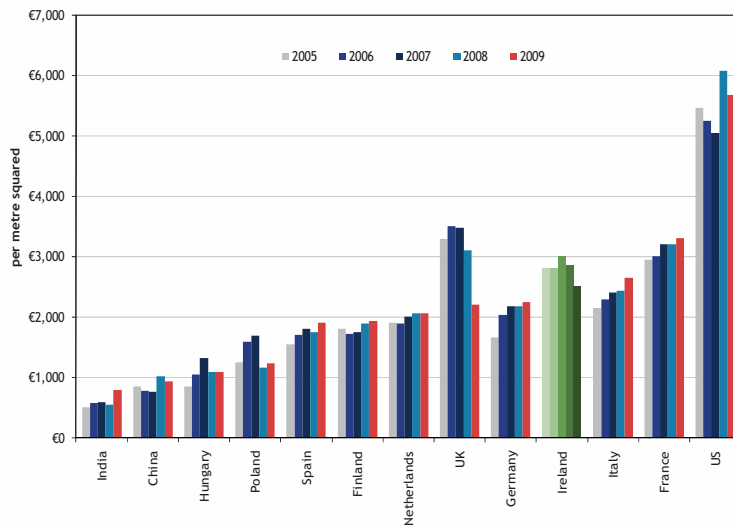
The cost of constructing a prime industrial site in Ireland declined by 14% between 2008 and 2009. Of the benchmarked group only the UK had a larger decline (-17%) in 2009.

Despite the relatively large decline in construction prices, Ireland remains the third most expensive location for building this kind of unit. However, Irish construction costs are now on par with Spain and just 2% above Germany and Finland. Construction costs in the US remain very high.

Source: Gardner and Theobald, International Constructions Costs 2006 - 2010

³⁷ Prime sites refer to those in the most expensive location within each country. Irish figures refer to prime location sites in Dublin.

Figure 4.3: Cost of Constructing a Prime³⁸ Office Unit, 2005 - 2009

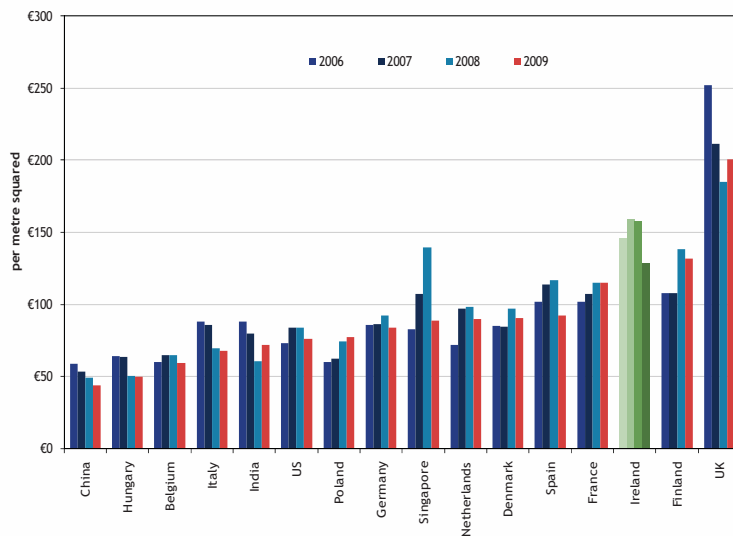


Ireland was one of five benchmarked locations where the cost of office construction declined in 2009.

The cost of constructing a prime office space fell by 13% in 2009 in Ireland. The UK recorded a significantly greater decrease during this period (-29.3%), and is now a cheaper location for building prime office sites than Ireland. Construction costs in the US remain extremely high.

Source: Gardner and Theobald, *International Constructions Costs 2006 - 2010*

Figure 4.4 Cost of Renting a Prime²⁰ Industrial Unit, 2006 - 2009



Ireland is the third most expensive location for renting a prime industrial site. Rental costs fell in 12 of the 16 benchmarked locations in 2009.

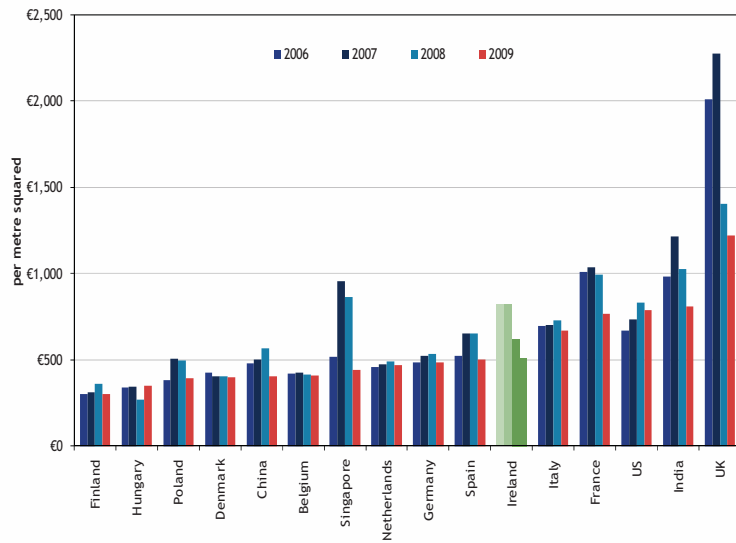
Rental costs for industrial sites fell by 18% in Ireland between 2008 and 2009. Of the benchmarked group only Singapore (-36%) and Spain (-21%) had larger price declines for industrial rental during this period.

Despite the large decline in prices, Ireland's ranking on this indicator, improved by only one place (over taking Finland) between 2008 and 2009.

Source: Cushman and Wakefield, *Industrial Space Across the World, 2007 - 2010*

³⁸ Prime sites refer to those in the most expensive location within each country. Irish figures refer to prime location sites in Dublin.

Figure 4.5: Cost of Renting a Prime³⁹ Office, 2006 - 2009



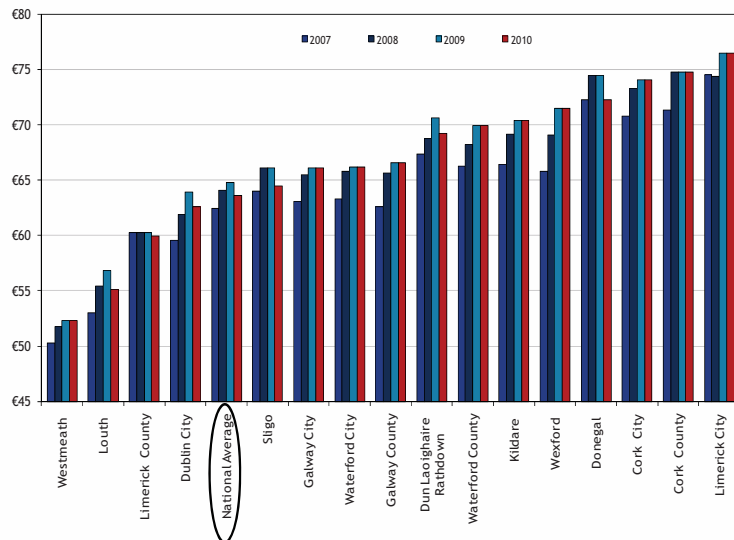
Between 2008 and 2009, office rental costs declined across 15 of the 16 benchmarked locations.

Having fallen by almost 25% in 2008, office rental costs fell by 18% in Ireland in 2009. Ireland is now a cheaper location than the US and Italy. However, Singapore and Spain both experienced significant price falls in 2009 (49% and 23% respectively) and are now cheaper locations to rent office space than Ireland.

While office rental costs in the UK have fallen by over 53% from 2007-2009, they remain the highest among the benchmarked countries.

Source: Cushman and Wakefield, *Industrial Space Across the World, 2007 - 2010*

Figure 4.6: Annual Rate on Valuation by Local Authority⁴⁰, 2007 - 2010



Commercial rates are a form of taxation levied by local authorities on the occupiers of commercial and industrial property. Local authorities determine the annual rate of valuation (AV) and this is used to calculate commercial rates for each eligible property⁴¹.

The average AV peaked in 2009 at €64.78 but in 2010, this decreased by an average of 1.8% to €63.60.

Source: Department of Environment, Heritage and Local Government

39 Prime sites refer to those in the most expensive location within each country. Irish figures refer to prime location sites in Dublin.

40 The listed local authorities are those operating in NSS Gateways with the exception of Fingal and South County Dublin which are not comparable due to revaluation of all commercial and industrial property by the Valuation Office.

41 The annual commercial rate for each property is calculated by multiplying the annual rate of valuation by the rateable valuation (RV) for the property which is determined by the Valuation Office.

5. Utility Costs

This section examines the main utility costs for business – energy, waste treatment, water services and telecommunications.

5.1 Energy and Fuel

The cost of industrial electricity for large energy users in Ireland decreased (-24 per cent) by more than in any other benchmarked location in 2009. The gap between the price of industrial electricity in Ireland and the euro area average has narrowed significantly (from 37 per cent in H2 2008 to five per cent in H2 2009). Ireland is now the sixth most expensive of the 14 benchmarked countries (Fig. 5.1.1)⁴². Although electricity costs for SMEs also fell between 2008 and 2009 (-15 per cent), Ireland is the third most expensive location benchmarked (Fig. 5.1.2)⁴³. However, recent price falls are unlikely to be sustained as they are largely due to the steep decline in global fuel prices (gas and coal) and temporary subsidies which are to be phased out by the end of 2012⁴⁴.

Ireland now has the second lowest industrial gas prices amongst the benchmarked group (Fig 5.1.3). Irish industrial gas prices are 14 per cent below the euro area average. This is a significant improvement for Ireland which ranked as the seventh least expensive benchmarked location for industrial gas in 2008.

The cost of diesel in Ireland is in line with the euro area average and unleaded petrol is four per cent cheaper in Ireland than for the euro area.

5.2 Environmental Utilities

Environmental utilities include water and waste water services and waste treatment services.

The average cost of treated water services in Ireland increased by 2.8 per cent in 2009. Ireland is competitive with our main trading partners on this measure (Fig. 5.2.1). However, there was a significant increase in the cost of waste water services of 18.8 per cent in Ireland during 2009. Some local authorities implemented significantly larger increases, for example, Waterford City (100 per cent) and Limerick City (69.5 per cent).

Ireland was the most expensive benchmarked location for the landfilling of non-hazardous waste in 2008 (Fig. 5.2.2). Similarly to water service charges, the cost of waste treatment varies significantly between local authority areas. Proposed increases in waste levies will reduce Ireland's cost competitiveness for these services further.

Flanders in Belgium is the most expensive of the benchmarked locations for thermal treatment at a cost of €110 per tonne including taxes and levies (Fig. 5.2.3). Currently, there are no commercial thermal treatment plants in operation in Ireland. However, the introductory rate of the thermal

⁴² Ireland is the ninth most expensive of the EU-27 in H2 2009.

⁴³ Ireland is sixth most expensive of the EU-27 in H2 2009.

⁴⁴ In 2008, the CER announced a rebate of €315 million (funded by ESB from its carbon windfall gain) to mitigate the impact of the very high global fossil fuels prices at that time for all users. The rebate is to continue for the 2009/2010 tariff year for large users, funded by ESB, in an effort to reduce the effect of the higher electricity prices in Ireland on their competitiveness. It is intended that rebate for large users will be gradually phased out by the end of 2011.

treatment levy currently proposed by the Department of Environment, Heritage and Local Government is €20 - €38 per tonne, with potential for this to increase to €120 per tonne over time. The levy in Denmark is €44 and in Sweden, it is €45 per tonne. The levy is in addition to the operator's fee for the service.

5.3 Telecommunications

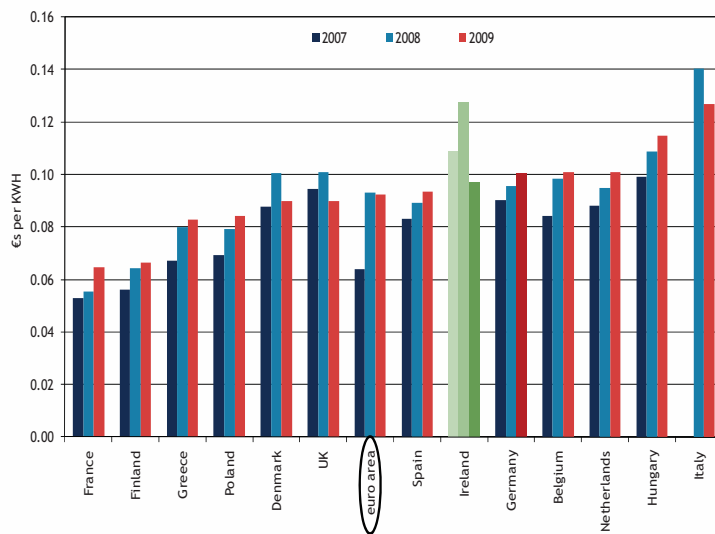
With regard to telephone costs, Ireland is 19.6 per cent more expensive than the euro area average for a business basket of landline calls (Fig 5.3.1). This is due in part to Ireland's low population density which increase the cost of operating telecommunications networks. Ireland is a competitive location for landline international calls and for high usage mobile packages. International business calls cost 18 per cent less than the euro area average (Fig 5.3.2). High usage mobile packages are 30 per cent below the euro area average, however, a number of key competitor locations, such as the UK, are notably cheaper than Ireland.

Ireland is a relatively expensive location for broadband services on a per megabit basis (Fig. 5.4.4). At \$16.31 per megabit, Ireland is significantly higher than the OECD - 28 average (\$7.24)⁴⁵.

⁴⁵ When comparing broadband service offerings across the EU, the Forfás broadband benchmarking study indicates that the incumbent's offering in Ireland costs €1,188 per annum for a 24 megabit connection versus the EU-14 average of €540 for a 17 megabit service. Forfás, Ireland's Broadband Performance and Policy Actions, January 2010.

5.1 Energy and Fuel

Figure 5.1.1: Industrial Electricity Prices for Large Energy Users⁴⁶ (excluding VAT), 2009⁴⁷

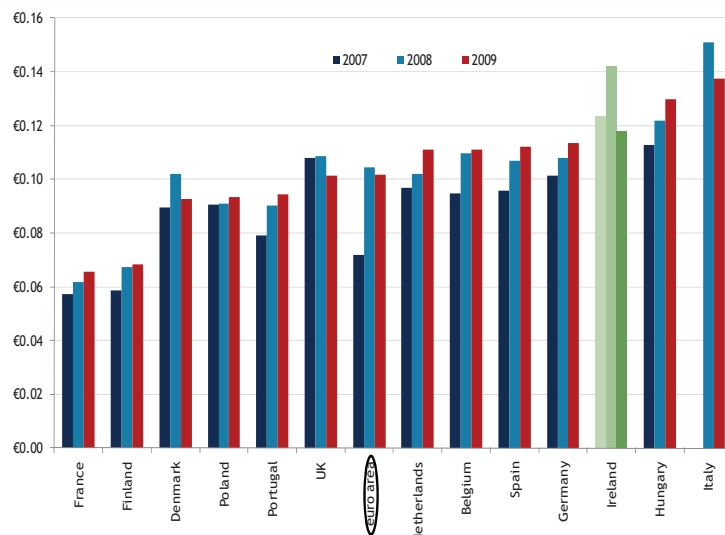


In 2009, the cost of electricity for high energy users in Ireland decreased by 24%, the largest decrease among the benchmarked locations.

The gap between Ireland and the euro area average is now 5% which represents a significant improvement since the second half of 2008 when Irish electricity prices were 37% higher than the euro area average. Countries with high fossil fuel dependencies (e.g. Ireland and Italy) experienced the greatest falls as international fossil fuel prices declined sharply.

Source: Eurostat - Environment and Energy

Figure 5.1.2: Industrial Electricity Prices for SMEs⁴⁸ (excluding VAT), 2009⁴⁹



In 2009, the electricity costs for SMEs in Ireland decreased by 17%, the largest decrease among the benchmarked locations.

Ireland remains significantly more expensive than the euro area average. Between 2008 and 2009, however, the gap between Ireland and the euro area fell from 36 per cent to 15 per cent.

Source: Eurostat - Environment and Energy

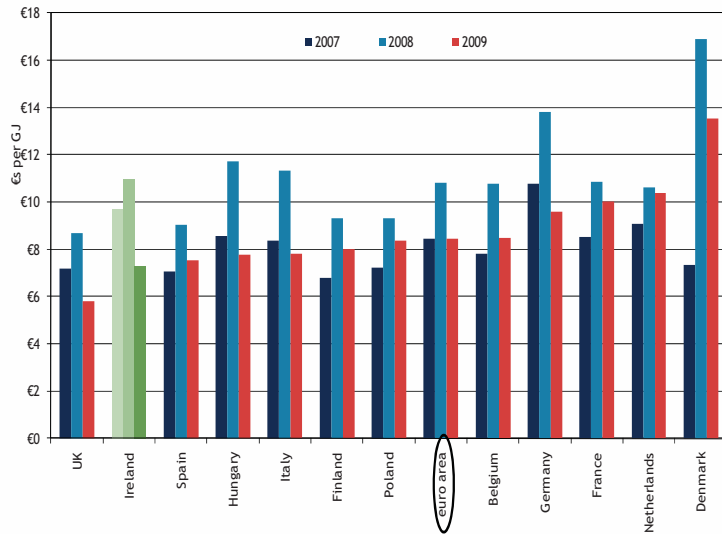
46 Electricity prices for large energy users are based on an annual consumption of 2,000 to 20,000 kilowatt hours.

47 Prices for 2006 are unavailable due to a change in the data collection methodology.

48 Electricity prices for SMEs are based on an annual consumption of 500 to 2,000 kilowatt hours.

49 Prices for 2006 are unavailable due to a change in the data collection methodology.

Figure 5.1.3: Industrial Gas Prices (excluding VAT), 200

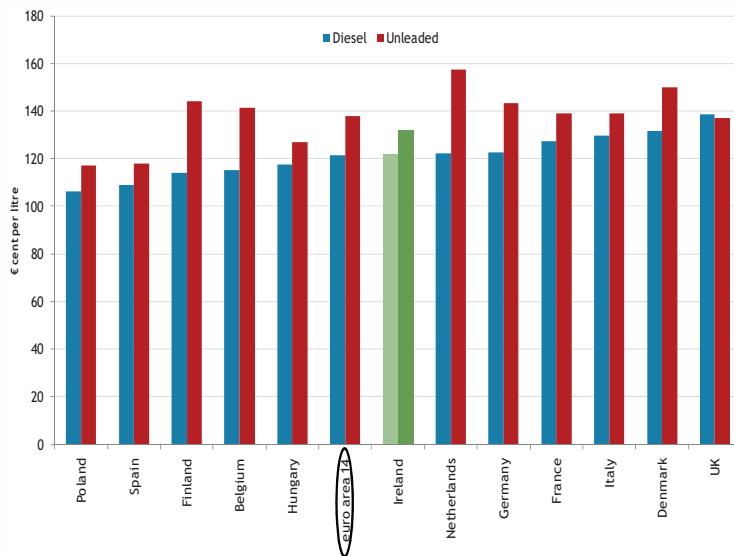


Across all benchmarked locations, the cost of industrial gas fell significantly between 2008 and 2009, reflecting the large decline in international gas prices.

Of the benchmarked group, Ireland has the second lowest industrial gas prices (€7.30 per gigajoule) compared to seventh in 2008. It is 14% below the euro area average of €8.46.

Source: Eurostat - Environment and Energy

Figure 5.1.4: Average Petrol Costs (Diesel and Unleaded) per Litre⁵⁰



The average cost of diesel per litre is Ireland (€1.22) in line with the euro area-14 average (€1.21). The average cost of unleaded petrol (€1.32) is 4 per cent below the euro area average (€1.38).

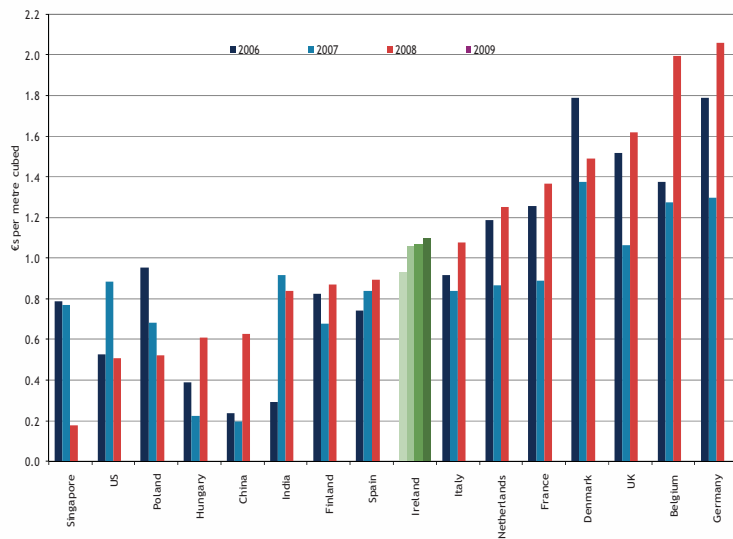
The UK is the most expensive location for diesel (€1.39), while Denmark is the most expensive location for unleaded petrol (€1.50).

Source: AA Ireland, Monthly Petrol Prices, April 2010

⁵⁰ Prices are sorted by the costs of diesel.

5.2 Environmental Utilities

Figure 5.2.1: Water Costs, 2009

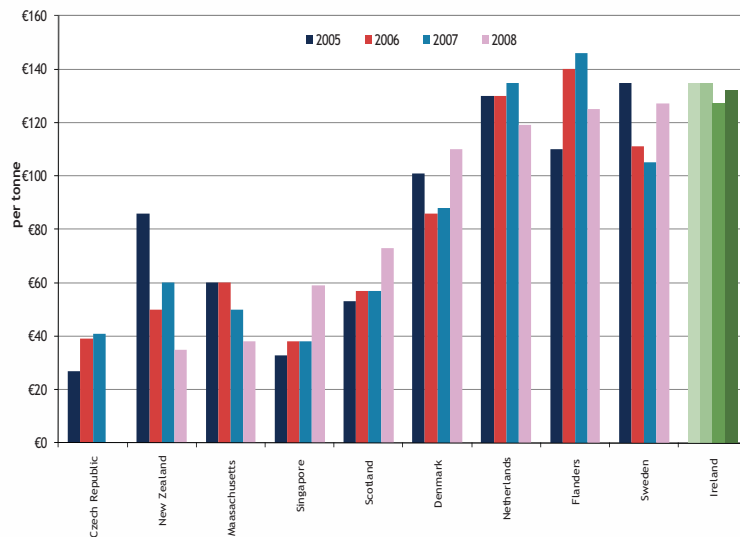


Water costs measure the cost for industrial users per metre cubed. It does not include the cost of waste water services. The average cost of water services rose by 2.6% in Ireland between 2008 and 2009⁵¹.

The average cost of waste water services in Ireland in 2009 was €1.20, an increase of 18.8% on 2008. This brought the average consolidated water services charge per metre cubed in Ireland to €2.29, an increase of 10.5% on 2008.

Source: EIU - World Investment Service, Department of Environment, Heritage and Local Government, Chambers Ireland

Figure 5.2.2: Waste Treatment Costs, 2008



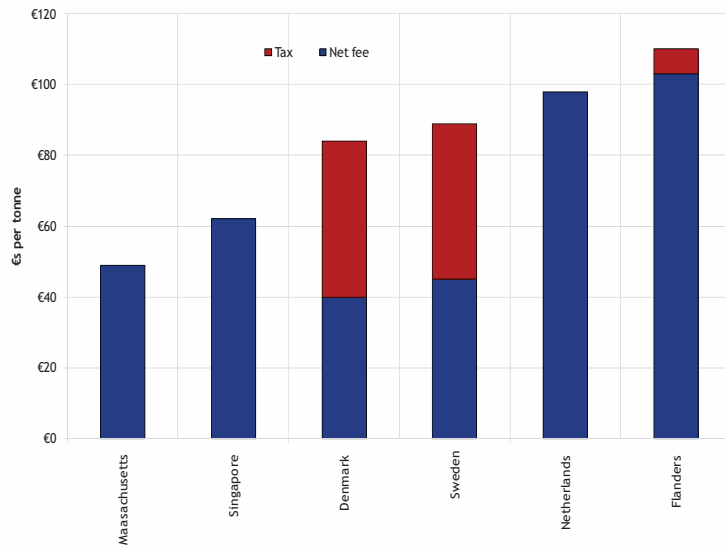
This indicator measures the cost of disposing of a tonne of non-hazardous waste into landfill. The costs shown include the landfill levy.

Ireland was the most expensive of the ten locations benchmarked in 2008. It should be noted that costs within Ireland vary significantly by local authority and that the market prices have fallen recently due to the recession.

Source: Forfás, Annual Waste Benchmarking Analyses, 2006 to 2009

⁵¹ Water costs data for 2009 is only available for Ireland.

Figure 5.2.3: Thermal Treatment Costs, 2008



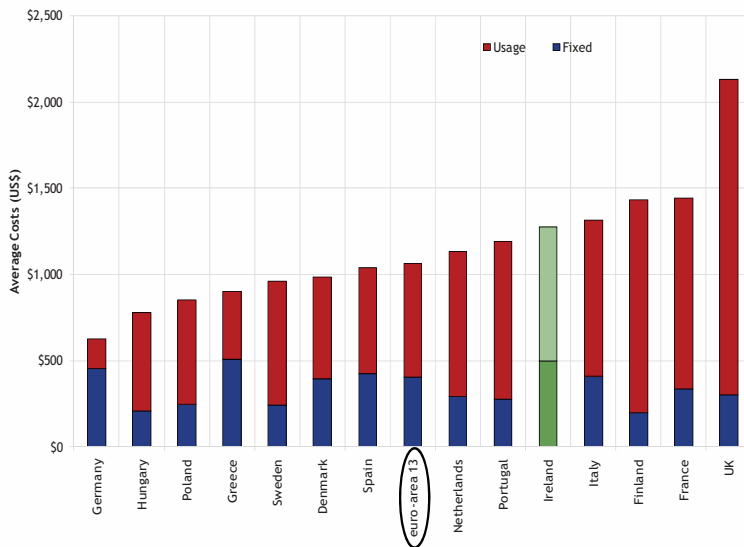
This indicator presents the average cost of treatment for non-hazardous industrial waste. Thermal treatment taxes or levies are included where applicable. Flanders at €110 per tonne is the most expensive benchmarked location. Ireland is not included in the chart as there are no commercial thermal treatment plants currently in operation in the country.

It is proposed to introduce a levy (€20 - €38 per tonne), with potential for this to increase to €120 per tonne over time. The fee for the service would be charged in addition to this levy, potentially resulting in a cost almost twice that of other countries.

Source: Forfás, Annual Waste Benchmarking Analyses, 2009

5.3 Telecommunications

Figure 5.3.1: Business Basket of Calls - Landline, US\$, 2009⁵²



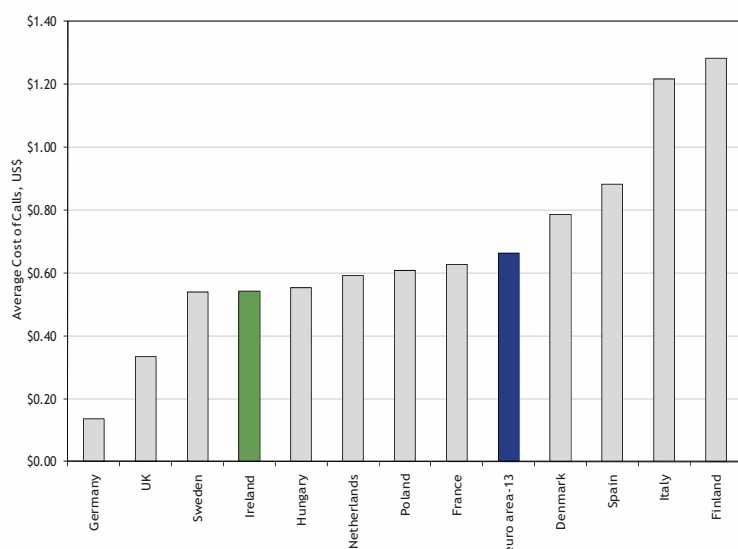
This indicator measures the costs of a business basket of calls from a landline excluding VAT. It does not include the cost of line rental.

Ireland ranks as the fifth most expensive location of the 14 countries benchmarked. Ireland is 19.6% more expensive than the euro area average.

Source: ComReg / Teligen, 2010, Forfás calculations

⁵² The OECD defines the business basket as being comprised of 2,800 calls per year. Of which 224 are international calls and 560 are calls to mobile. The remaining 2,016 are national calls. The euro area-13 is the euro area-16 minus Cyprus, Malta and Slovenia.

Figure 5.3.2: Business Basket of International Calls - Landline, US\$, 2009⁵³

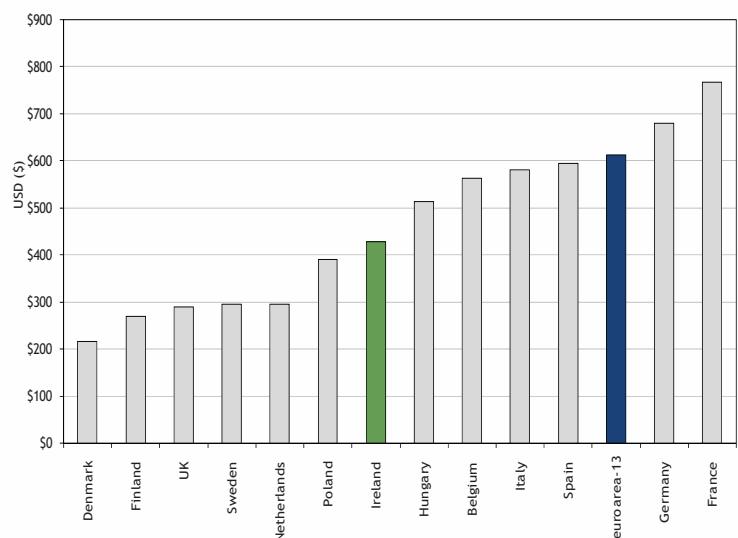


This indicator measures the costs of international calls from a landline excluding line rental and VAT.

Ireland is the fourth cheapest benchmarked location and is 18% cheaper than the euro area-13 average.

Source: ComReg / Teligen, 2010, OECD Comparative Price Levels, March 2010, Forfas calculations

Figure 5.3.3: Mobile Telephone Costs, High Usage Basket, US\$, 2009⁵⁴



This indicator measures the monthly cost charged for a high usage basket of mobile calls including VAT. Mobile voice traffic accounted for 57% of total voice minutes in the last quarter of 2009 in Ireland⁵⁵.

Ireland ranks seventh cheapest of the 13 benchmarked locations and is 30% cheaper than the euro area average. Average revenues per customer in Ireland at €37.20 per month are the highest of 16 European countries benchmarked and are significantly higher than the euro area average (€22.70)⁵⁶.

Source: ComReg / Teligen, 2010, OECD Comparative Price Levels, March 2010, Forfas calculations

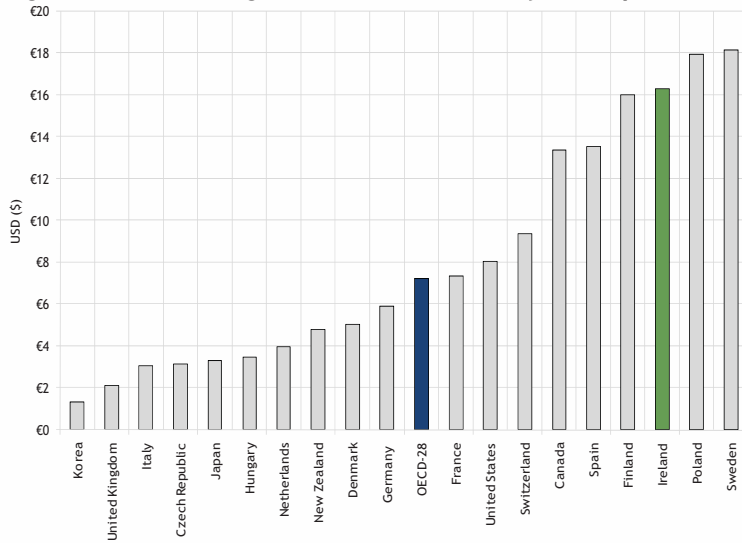
53 The OECD business basket of international calls reflects the cost per minute of an average single international call calculated by weighting the cost with 75 per cent at the peak rate and 25 per cent at the off-peak rate. The euro area-13 is the euro area-16 minus Cyprus, Malta and Slovenia.

54 The OECD high usage mobile monthly basket is comprised of 1680 outgoing calls, 660 text messages and 12 multi-media messages per month.

55 ComReg Quarterly Key Data Report, Q4 2009.

56 ComReg Quarterly Key Data Report, Q4 2009.

Figure 5.4.4: Average Broadband⁵⁷ Monthly Price per Advertised Megabit, US\$, 2009



Ireland is the third most expensive location for broadband per megabit of the benchmarked group of 19 countries⁵⁸. At \$16.31 per megabit, Ireland is significantly more expensive than the OECD - 28 average of \$7.24.

When comparing broadband service offerings across the EU, the Forfás broadband benchmarking study indicates that the incumbent's offering in Ireland costs €1,188 per annum for a 24 megabit connection versus the EU-14 average of €540 for a 17 megabit service⁵⁹.

Source: OECD, Broadband Portal

⁵⁷ Average broadband costs data includes DSL, cable and fibre broadband connections.

⁵⁸ OECD, Broadband Portal.

⁵⁹ In 2009, the fastest DSL business connection (i.e. delivered over the fixed telephone line) offered by the incumbent operator in Ireland was a 24 megabit service at a cost of €1,188 per annum (excl. VAT). However this service is only available in a limited number of locations in Irish cities. A 12 megabit service is more widely available to businesses in most parts of the country at a cost of €780 per annum. The fastest speed available from the incumbent in Sweden is a 24 megabit service at a cost of €881 per annum, which is widely available, while in Portugal a 24 megabit connection costs €343 and 20 megabits in the UK costs €318 per annum. Forfás, Ireland's Broadband Performance and Policy Actions, January 2010.

6. Business Services Costs

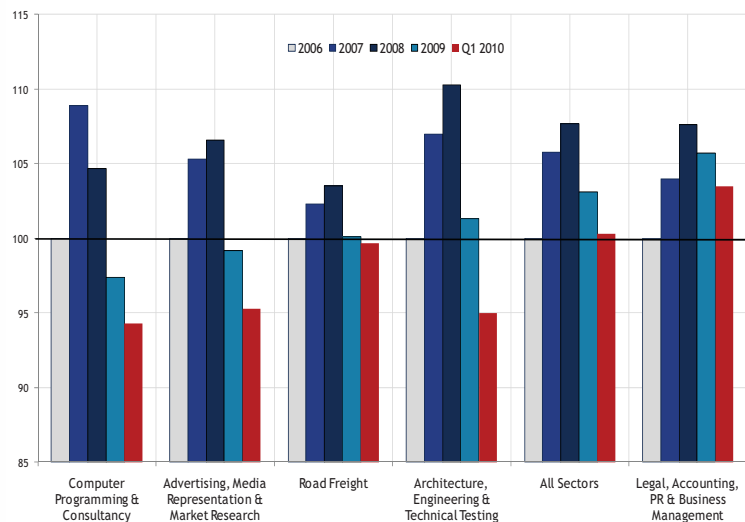
This chapter looks at the cost of key professional services to business such as computer programming and consultancy, accountancy and legal services. It also examines the density of non-life insurance premia.

According to experimental CSO data, (the Services Producer Price Index) the cost of services fell by 4.0 per cent in the year to Q1 2010 (Fig. 6.1)⁶⁰. There were significant disparities in the rate of reduction at sectoral level. For example, computer service costs fell 16.1 per cent between their peak in 2007 and the end of Q1 2010, while legal accounting, PR and business consulting cost fell 5% since their peak in Q2 2008. Looking at this category in more detail, accountancy costs fell from Q1 2008 onwards and by Q4 2009 were 6.8 per cent below 2006 prices. Conversely, the cost of legal services has declined slowly and in Q4 2009, they were 18.5 per cent above the average 2006 price (Fig. 6.2). It is difficult to accurately compare legal costs at an international level due to differences in national legal systems. However, according to the World Bank, the cost of enforcing a contract is notably higher in Ireland than in many of our main trading partners (Fig. 6.3)

There is increasing concern over the costs of insurance in Ireland arising from the financial crises and recent natural events. It is difficult to find reliable data across countries. Data is available on insurance spend per capita or insurance density. High insurance density can reflect both high insurance costs and a requirement for high coverage levels. Among the benchmarked locations, Ireland has the fifth highest density of non-life insurance (motor, property, employer's liability, public liability, travel and other business insurance) per capita but is below the euro area average (Fig. 6.4).

⁶⁰ It is important to note that the experimental publication is based on a relatively small sample size and caution should be exercised when analysing the results.

Figure 6.1: Services Price Index, (2006 =100)

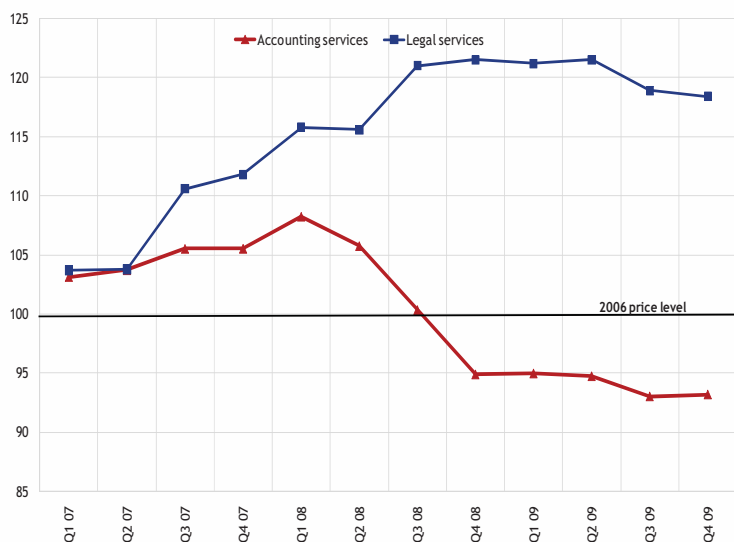


Based on experimental CSO data, this indicator shows the change in prices of key business services. The index shows a total reduction of 4% across services in the year to Q1 2010. Services are now 0.3% above 2006 levels.

Computer services have had the largest decrease in prices, falling by 16.1% since their peak in Q3 2007. Legal, accounting, PR and business management consultancy had the smallest decline in prices, peaking in Q2 2008. By the end of Q1 2010 prices in this sector had fallen 5% from the peak but remained 3.5% above 2006 levels.

Source: CSO, Services Producer Price Index

Figure 6.2: Accountancy and Legal Costs, 2007 -2009, (2006 = 100)⁶¹

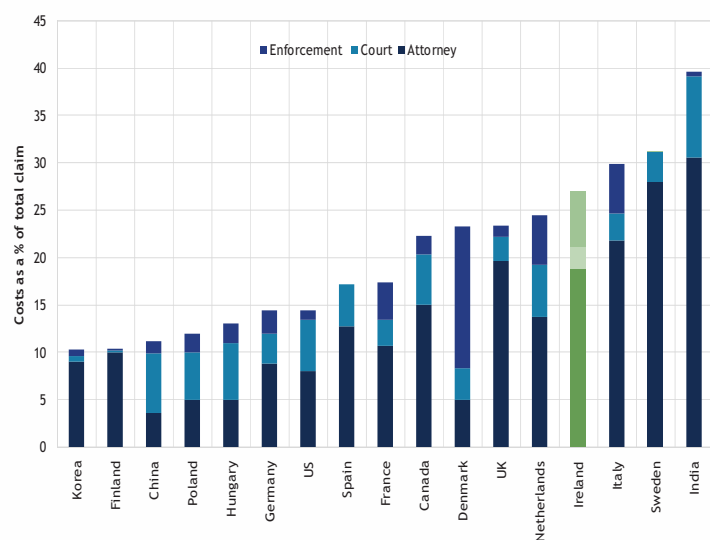


This indicator shows the quarterly change in accountancy and legal services costs between Q1 2007 and Q4 2009. The cost of accounting services peaked in Q1 2008. Since then costs have fallen significantly and by the end of 2009 were 6.8% lower than the average price for accounting services in 2006. Legal fees, having peaked in Q2 2009, took longer to respond to the recession and experienced marginal price falls in the second half of the year (-3.1%).

Source: CSO, Services Producer Price Index

⁶¹ It is difficult to measure professional services costs. The Services Producer Price Index is an experimental publication from the CSO. Given the small sample size used to create the sub-indices for accountancy and legal costs caution should be used when analysing the results.

Figure 6.3: Legal Costs of Contract Enforcement, 2009

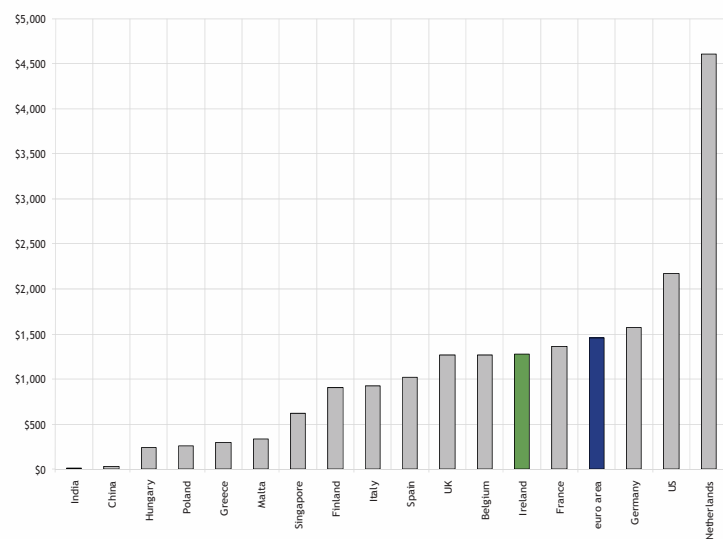


It is difficult to accurately compare legal costs across countries due to differences in national legal systems. This indicator measures the cost of enforcing a contract following a commercial dispute in relation to the sale of goods by one firm to another. The costs are shown as a percentage of the total claim.

Ireland is the fourth most expensive location benchmarked. This is driven by relatively high attorney fees.

Source: World Bank, *Doing Business*, 2010

Figure 6.4: Non-Life Insurance Density, Premiums per Capita in US\$, 2008



This indicator shows the value of non-life insurance premiums per capita. It includes motor, property, employer’s liability, public liability, travel and other business insurance.

High insurance density can reflect both high insurance costs and a requirement for high coverage levels. Among the benchmarked locations, Ireland has the 5th highest density of non-life insurance per capita (\$1,278) but is below the euro area average (\$1,455).

Source: Swiss re, *Sigma No 3, Statistical Appendix*, 2009

7. The Broader Cost Environment

The broader cost environment in which firms operates impacts the cost competitiveness of locations as all internationally trading firms procure a wide range of goods and services in the local economy. High and increasing consumer prices act as an upward pressure on labour and other business costs.

7.1 Consumer Price Levels

Following a period of significant increase, the consumer price index peaked in 2008 when prices were 26.3 per cent above 2001 prices. Since then the index has fallen and prices in May 2010 were 6.7 per cent below the peak level (Fig. 7.1.1). Between April 2009 and April 2010, Ireland experienced a 2.5 per cent decrease in the harmonised index of consumer prices (HICP), the second highest decrease in the European Union. During the same period the euro area HICP increased by 1.4 per cent (Fig. 7.1.2).

A comparison of consumer costs between major international cities indicates that Dublin's cost competitiveness improved between 2008 and 2009 as the city moved from third most expensive to sixth most expensive.

7.2 Consumer Product Prices

Irish employees have high purchasing power levels relative to employees in many of our key trading partners. For example, an average worker in Ireland can buy a Big Mac after 15 minutes work and an iPod Nano after 10 hours work. This compares to a group average of 22 minutes for a Big Mac and almost 17 hours for an iPod Nano (Fig. 7.2.1).

Ireland is an expensive location for purchasing groceries. For a comparable basket of food and non-alcoholic beverages, Ireland ranks as the second most expensive European country, 19.4 per cent above the euro area-16 average (Fig. 7.2.2).

7.3 Accommodation


It is difficult to accurately compare the cost of residential property across international locations. However, the affordability of housing has improved for Irish employees since 2007. By the end of Q2 2009, housing affordability for those in employment had returned to levels last experienced in 2000 (Fig. 7.3.1).

In 2009, of the sixteen cities benchmarked Dublin is the sixth most expensive location to rent residential accommodation (Fig. 7.3.2). New York is the most expensive. According to the national rental index, residential rental costs have fallen 24.9 per cent from their peak in 2007 (Fig. 7.3.3).

7.4. Public and Administered Services

The cost of public and administered services affects the competitiveness environment for firms. This section looks at some indicative measures of the cost competitiveness of public and administered services in Ireland.

The cost of health and education services continue to rise rapidly, further increasing the gap between the price of these services and the other goods and services included in the consumer price

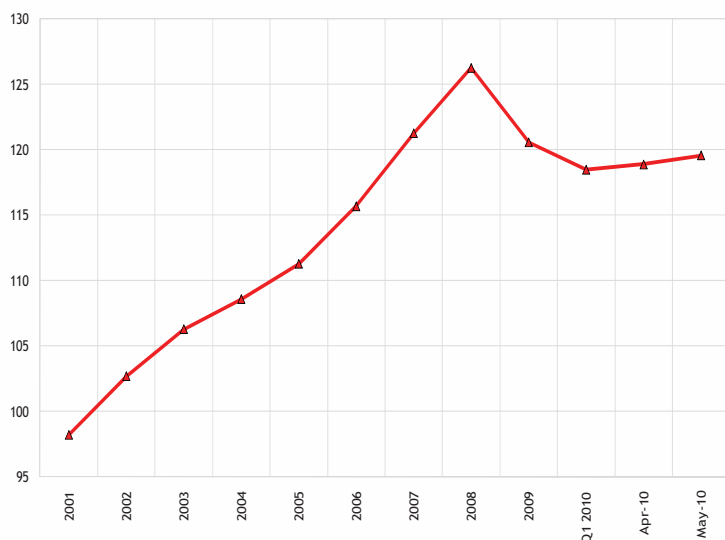


index (Fig. 7.4.1). Urban public transport and taxis are relatively expensive in Ireland compared with our main trading partners (Fig 7.4.2 and 7.4.3).

Although public sector wages do not have a direct impact on the cost of doing business in Ireland, as a significant component of the cost of public and administered services they do have an indirect effect. The starting salary for primary teachers in Ireland in 2010 is 15 per cent above the OECD-25 average, while the top salary scale for primary school teachers in Ireland is 33 per cent above the OECD average (Fig. 7.4.1). Similarly, within the group of countries for which data was available, Ireland had the highest average salary for medical specialists (\$225,000). Ireland has the fourth highest average remuneration level for nurses. While these salary levels reflect the impact of recent public sector pay cuts, they do not capture the impact of the public sector pension levy.

7.1 Consumer Price Levels

Figure 7.1.1: Consumer Price Index, 2001 - May 2010 (December 2001 =100)

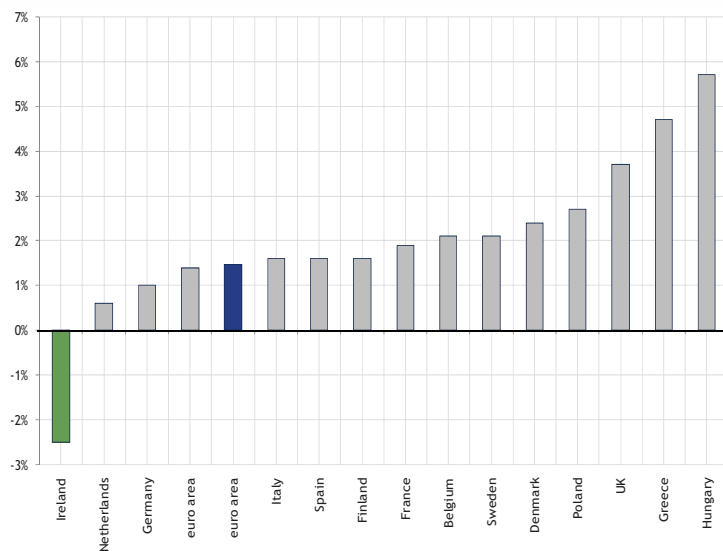


The Consumer Price Index (CPI) measures the change in the average level of prices (inclusive of all indirect taxes) for a basket of consumer goods and services in Ireland.

The CPI peaked in 2008 at 126.3 (26.3% higher than December 2001 prices). Since then the price of goods and services has fallen and by May 2010, the index was 6.7% below the peak. Since 2001, utilities and local charges increased by 44%, health by 51% and education by 68%.

Source: CSO, Consumer Price Index

Figure 7.1.2: Harmonised Index of Consumer Prices, Annual % Change, (April, 2010)

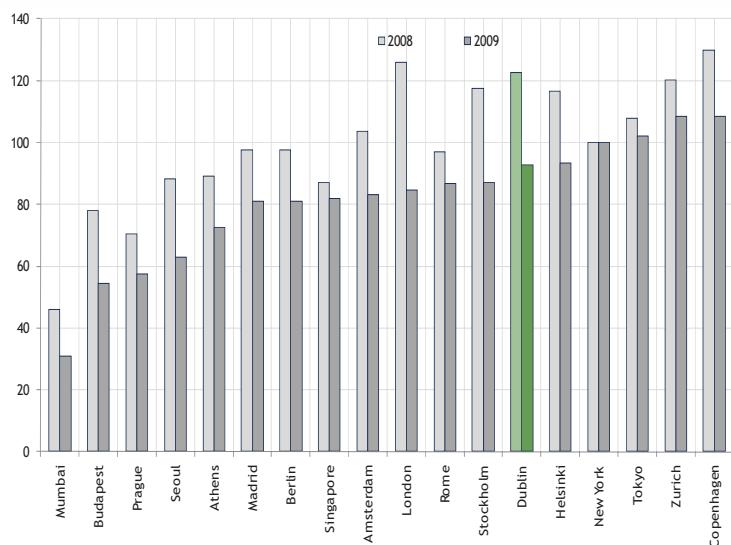


The Harmonised Index of Consumer Prices (HICP) is calculated in each member state of the EU to enable the accurate comparison of consumer price trends.

Of the euro area countries, Ireland experienced the largest decrease in the HICP (-2.5%), during the twelve months to March 2010. The HICP for the euro area increased during that period by 1.5%. This indicates that Ireland's cost competitiveness for consumers is improving relative to the euro area and other European trading partners, such as the UK which increased by 3.7% during the same period.

Source: CSO, Consumer Price Index

Figure 7.1.3: Consumer Price Level Comparison 2008/2009 (New York = 100)



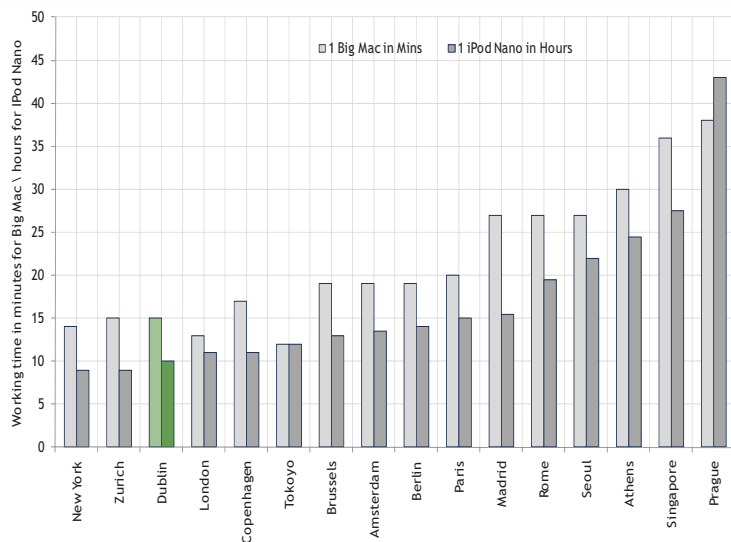
This indicator shows the cost of a weighted basket of 122 goods and services (excluding rent) in a number of large cities.

In 2008, Dublin ranked as the third most expensive location for the basket of goods amongst the group of 18 benchmarked locations. Following relatively large price declines, Dublin was ranked the 6th most expensive location in 2009. London's relative position has improved dramatically following sterling's steep devaluation.

Source: UBS, Prices and Earnings 2008 and 2009

7.2 Consumer Product Prices

Figure 7.2.1: Average Working Time Required to Buy Branded Consumer Goods, 2009

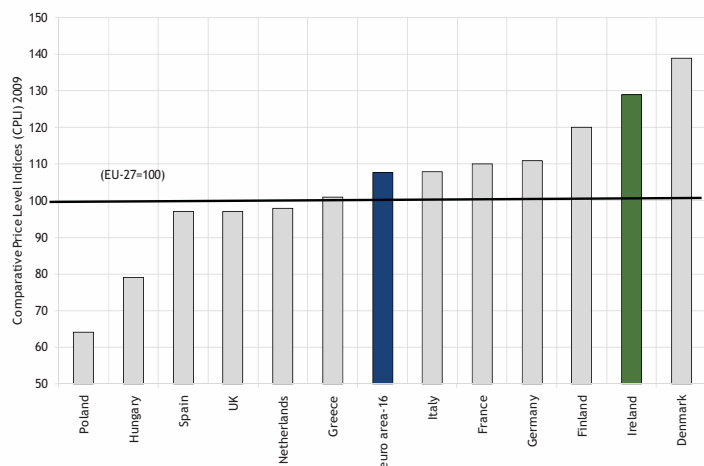


This indicator shows the average working time required to afford a Big Mac and an iPod Nano, a measure of purchasing power.

Irish employees have high purchasing power levels relative to employees in many other key trading partners. An average worker in Ireland can buy a Big Mac after 15 minutes work and an iPod Nano after 10 hours work. This compares to a group average of 21.7 minutes for a Big Mac and 16.8 hours for an iPod Nano.

Source: UBS, Prices and Earnings 2009

Figure 7.2.2: Food and Non-Alcoholic Beverage Indices, (EU-27=100)



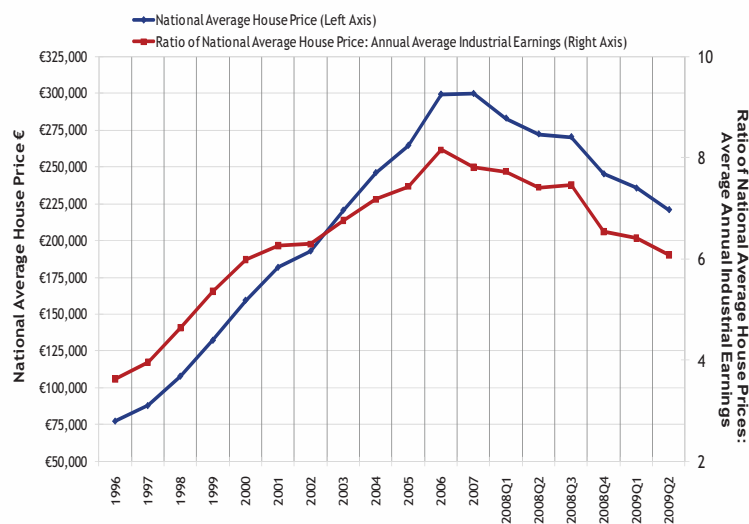
This indicator shows the price level of a comparable basket of food and non-alcoholic beverages. Ireland is the second most expensive country for a basket of food and non-alcoholic beverages after Denmark. Ireland is 29% above the EU-27 average and 19.4% above the euro area-16 average.

At 37% above the EU-27 average, Ireland ranks as the most expensive country for milk, cheese and egg products⁶².

Source: Eurostat, Economy and Finance, 2010

7.3 Accommodation

Figure 7.3.1: Affordability of Housing



In 2007, the average nationwide price for a house peaked at nearly €300,000 or more than eight times average industrial earnings. The average national house price fell by 26% between 2007 and the end of Q2 2009. As of Q2 2009, housing affordability for those in employment has returned to levels last experienced in 2000.

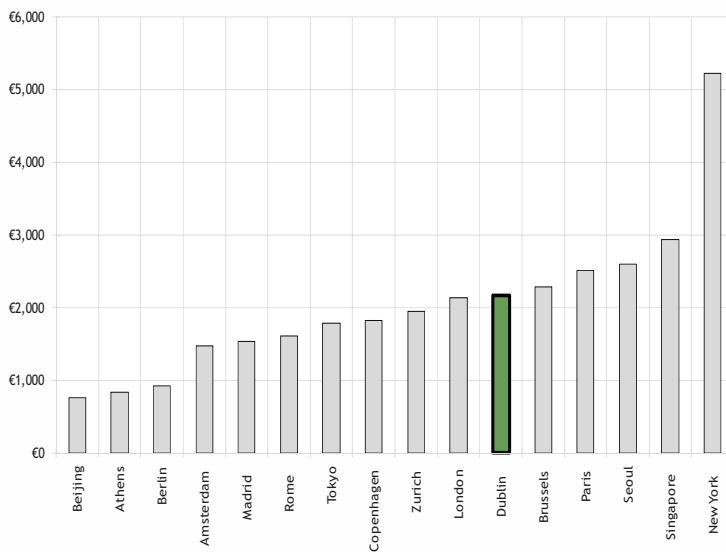
The quarterly EBS / DKM Affordability Index⁶³ demonstrates that in June 2010 the average first time buyer working couple was paying 14.2% of their joint income to service their mortgage compared with 26.4% in December 2006, representing almost a 50% improvement in the past three years.

Source: ESRI Permanent TSB House Price Index, CSO, Earnings

62 http://epp.eurostat.ec.europa.eu/cache/ITY_OFFPUB/KS-SF-10-030/EN/KS-SF-10-030-EN.PDF

63 EBS / DKM, Affordability Index, June 2010

Figure 7.3.2: Average Monthly Rental Prices, 2009

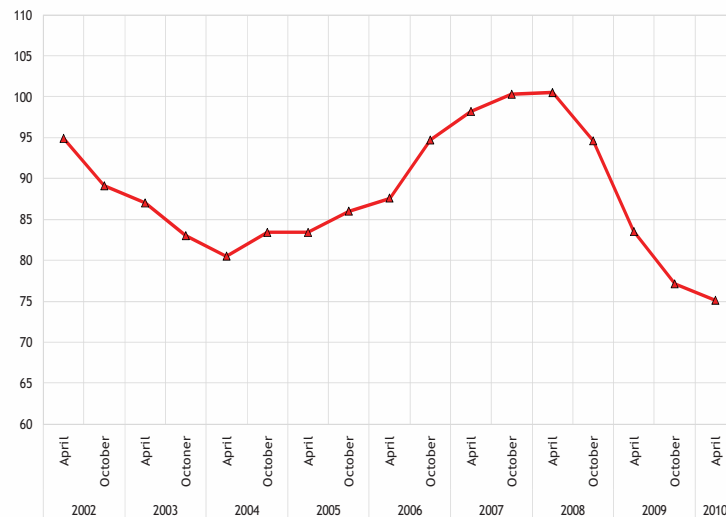


This indicator shows average rental prices for a residential unfurnished three room apartment in each of the cities.

New York is the most expensive location at \$5,220 per month. Of the benchmarked locations, Dublin ranks the sixth most expensive at \$2,160 per month, just slightly above London (\$2,140).

Source: UBS, Prices and Earnings 2009

Figure 7.3.3: National Rental Index, April, 2010, (2007=100)



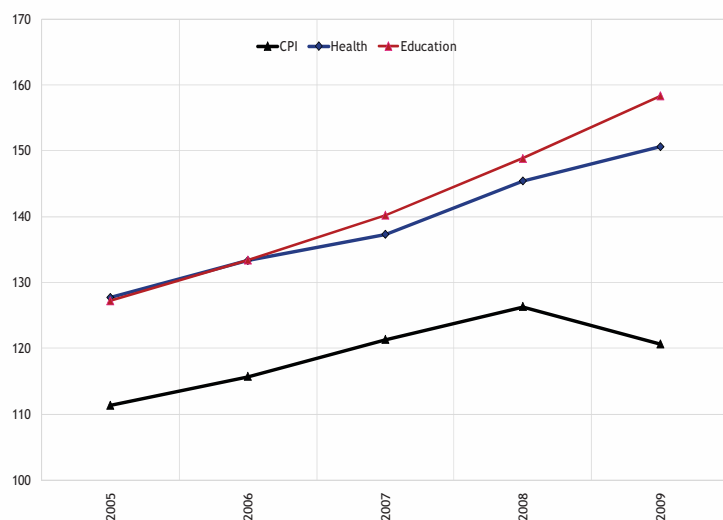
This index shows changes in the average residential property rental cost. In April, 2010 the index had fallen 24.9 points from its peak (and base) in 2007.

While there has been a steep decline in rental costs since 2007, the Daft report notes levels appear to be stabilising, driven largely by the rental market in Dublin and Cork where levels have been static since the start of 2010.

Source: Daft.ie, Rental Report, May 2010

7.4. Public and Administered Services

Figure 7.4.1: Health and Education, 2005 -2009 (December 2001 =100)

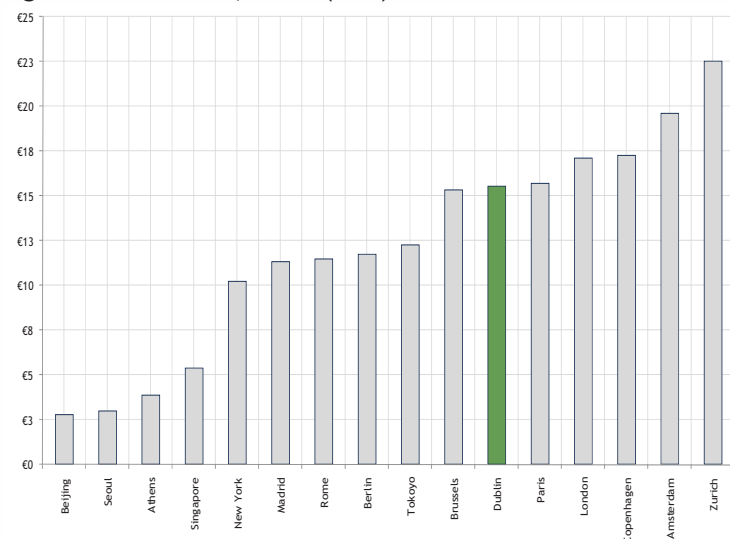


This indicator shows the health and education components of the consumer price index (CPI) and their indexed cost relative to the total CPI basket.

In 2005, health and education, which are largely public sector driven, were 16 index points above the CPI. During 2009, the CPI fell significantly while health and education continued to rise. This widened the gap between the CPI and education to 38 points and CPI and health to 30 points.

Source: CSO, Consumer Price Index

Figure 7.4.2: Taxis, 2009 (US\$)

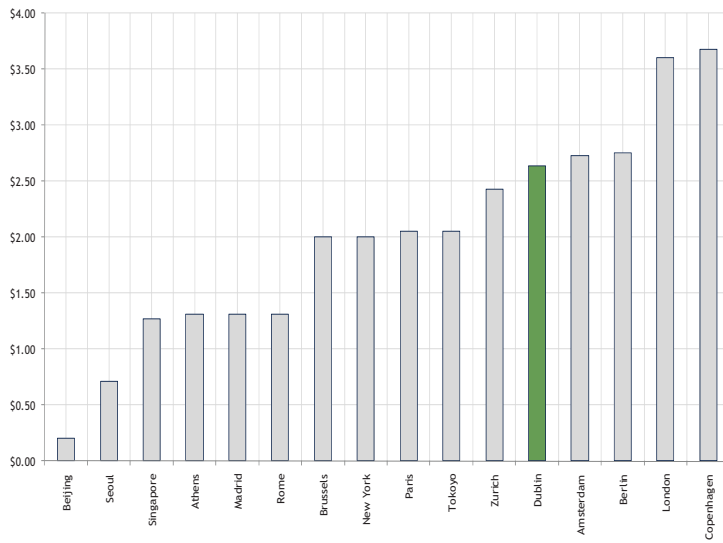


This indicator measures the price of a 5 kilometre fare within the city limits and including service charges.

Of the sixteen benchmarked locations, Dublin ranks as the sixth most expensive location for taxi usage.

Source: UBS, Prices and Earnings 2009

Figure 7.4.3: Public Transport - Urban, 2009 (US\$)

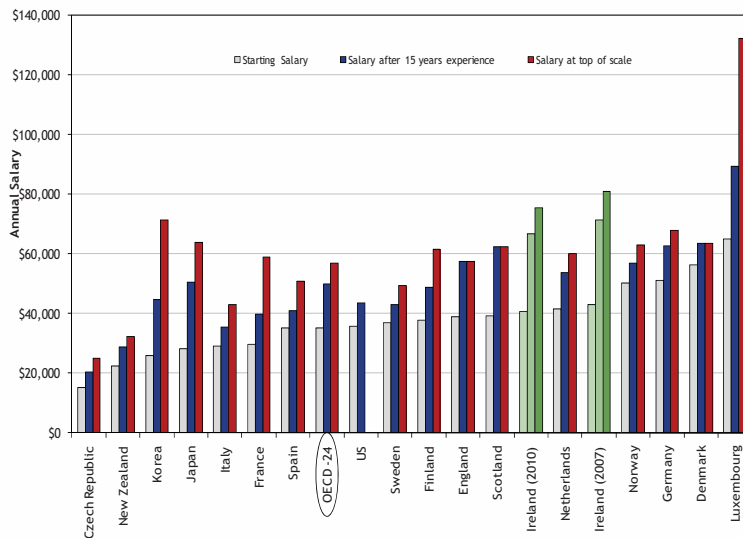


This indicator measures the price of a single ticket for the urban public transport network (bus, streetcar or metro) for a journey of approximately 10 km or at least 10 stops.

Of the 16 benchmarked locations, Dublin ranks as the 5th most expensive on this measure⁶⁴.

Source: UBS, Prices and Earnings 2009

Figure 7.4.4: Primary Teacher Salary, 2007, US\$, 2007



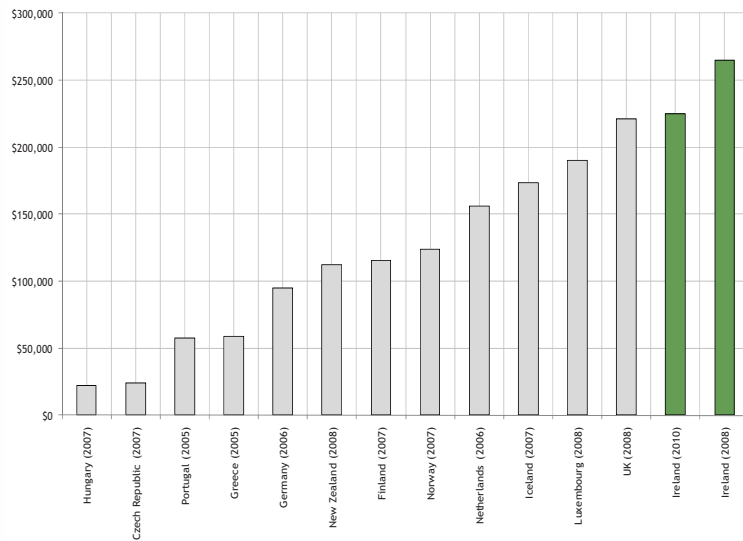
This indicator measures primary teacher salaries across the OECD. It illustrates the salary levels for Irish teachers in 2007 and 2010 to capture the effect of the public sector pay cut in 2010. The starting salary for primary teachers in Ireland in 2010 is 15 per cent above the 2007 OECD-24 average. The remuneration for teachers in Ireland with 15 years experience and for those on the top scale salary is the second highest (after Luxembourg) of the benchmarked group. The indicator does not reflect the impact of the public sector pension levies⁶⁵.

Source: OECD, Education at a Glance, 2009, Forfás calculations.

64 This indicator does not capture the impact of schemes designed to reduce the costs of public transport. For example, in Ireland the Irish Tax saver scheme reduces public transport cost by up to 51% for participating Irish PAYE employees.

65 The public sector pension levy rates range from 3 per cent on salaries of €15,000 to 9.6 per cent of salaries greater than €300,000.

Figure 7.4.5: Specialist Health Professionals Salary, (US\$), 2008 and 2010

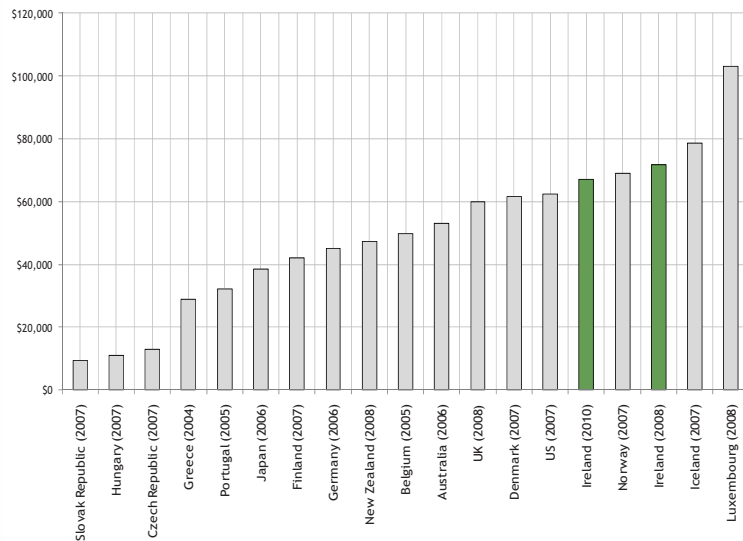


This indicator measures the remuneration of health specialist in a number of OECD member countries. Irish health specialists receive the highest average salary of the group for which data is available,

The 2010 salary level for Irish specialist takes account of the recent public sector pay cuts but does not reflect the impact of the public sector pension levies.

Source: OECD, Health Data, 2009, Forfás calculations.

Figure 7.4.6: Nurses Salary, (US\$), 2008 and 2010



This indicator measures the remuneration of nurses in a number of OECD member countries. Of the group for which data is available, Irish nurses receive the fourth highest average salary (\$67,000).

The indicator does not reflect the impact of the public sector pension levies.

Source: OECD, Health Data, 2009, Forfás calculations.

Appendix - Summary of Specialist Databases

Where possible the OECD, Eurostat and the CSO are used as the data sources for the indicators in this report. In a number of cases, other databases are used to provide comparable data in specialist areas. These are listed and detailed below.

1. KPMG - Competitive Alternatives Report, 2010

KPMG's Competitive Alternatives Report was used to develop the sectoral cost profiles in Chapter 2 of the report. Competitive Alternatives 2010 is an expansion and update of previous KPMG publications, and measures the combined impact of 26 significant business cost components that are most likely to vary by location. The study examines 17 industry operations in ten countries: Australia, Canada, France, Germany, Italy, Japan, Mexico, the Netherlands, the United Kingdom, and the United States. The basis for comparison is the after-tax cost of start-up and operations over 10 years

2. Watson Wyatt - Global 50 Remuneration Planning Report

Data on wage levels by job categories is taken from the Watson Wyatt "Global 50 Remuneration Planning Report" 2009/ 2010. This report uses a global job value framework called Global Grades. The global grades are spread across a 25 level job-worth hierarchy designed to underpin survey job matching on a consistent world-wide basis. It categorises positions using a number of variables such as tasks, skills, expertise and levels of responsibility with regard to leadership, functional and business strategy. Using the global grades as a standardisation tool, the Watson Wyatt report looks at 50 generic roles across ten job families (general management, finance, marketing, sales, human resources, information technology, logistics and purchasing, manufacturing, research and development and administration). This provides a consistent and coherent basis for benchmarking wage levels by occupation in the various locations.

3. Cushman and Wakefield - Global Research Reports

Cushman and Wakefield is the world's largest privately owned real estate solutions firm with offices in 52 countries. The firm performs proprietary research and data-driven analysis using a web-based system, tracks over 10 billion square feet of office and industrial real estate. The annual Cushman and Wakefield "Office Space Across the World" and "Industrial Space Across the World" reports provides a detailed analysis of prime office and industrial property rental performance and occupancy costs across the globe in the previous year.

4. Gardner and Theobald - International Construction Costs Survey

Gardner and Theobald is a worldwide construction consultancy providing services in the areas of project, cost, construction, dispute management, management consultancy and planning. The annual "International Construction Costs Survey" contains data on building cost information (across a variety of unit types), labour rates, material costs and inflation statistics.

5. The Economist Intelligence Unit (EIU) - World Investment Service

The Economist Intelligence Unit is a leading provider of country, industry and management analysis with offices worldwide. The EIU's World Investment Service provides a detailed database containing business costs, flows of investment by country and industry and overseas mergers and acquisitions. The service covers the world's 60 largest economies and provides detailed analysis on

political and economic background, business environment, foreign investment regulations and trends in foreign investment.

6. World Bank - Doing Business 2009

The World Bank publishes the results of its Doing Business survey annually. It looks at domestic small and medium-size companies and measures the regulations applying to them through their life cycle. The report covers ten indicators sets and covers 181 different countries and aims to provide an objective basis for understanding and improving the regulatory environment for business.

7. UBS - Prices and Earnings, 2009

UBS is a financial services firm that offers wealth management, asset management and investment banking services. The study uses a standardised survey to provide a detailed look at the prices of goods and services, wages working hours for 14 professions in 73 cities. The data for the 2009 report was collected in March 2009. All amounts were converted into a single currency (US\$) to ensure that the surveyed prices and earnings could be compared. To compensate for daily exchange rate fluctuations, the average exchange rate over the data collection period was applied.

Forfás

Wilton Park House

Wilton Place

Dublin 2

Tel: +353 1 607 3000

Fax: +353 1 607 3030

www.competitiveness.ie