

Cost of Doing Business in Ireland 2010



Structure

1. Key findings of report
2. Sectoral cost profiles - what costs matter?
3. How does Ireland compare on key business input costs?
 - Labour
 - Property
 - Utilities
 - Business service costs
4. Review of the broader cost environment

Key findings

- ▶ Ireland experienced a significant loss in cost competitiveness 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.
- ▶ 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.
- ▶ 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 2006 price.

Key Findings

- ▶ The drivers of falling prices are also important to consider. For example, the cost of industrial electricity in Ireland decreased by 24 per cent leading to a significant narrowing of the gap between Irish electricity prices and the euro area average. However, these 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.
- ▶ 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.
- ▶ 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.

1. Sectoral cost profiles - what costs matter?



Sectoral cost profiles - what costs matter?

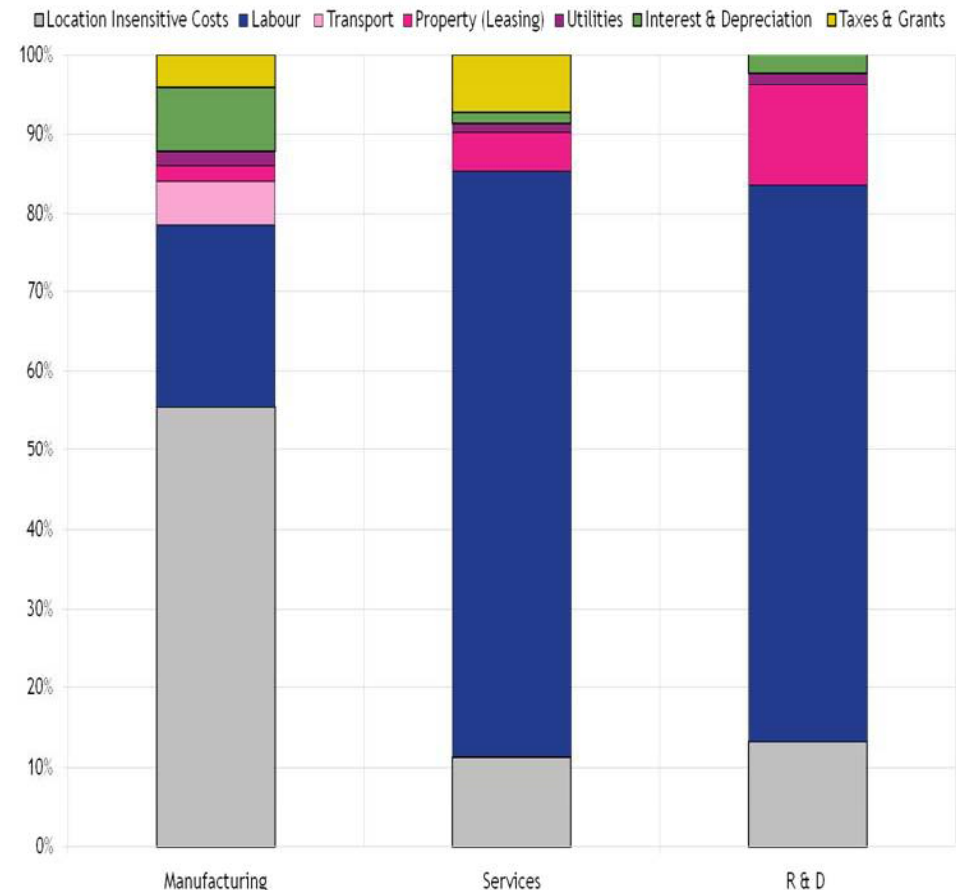
- ▶ Created using KPMG “Competitive Alternatives”
- ▶ Provide **indicative** cost structures using **case study firms**
- ▶ Distinction between location sensitive and insensitive costs
 - Location insensitive costs: Inputs for which the price is set in **international markets**, such as materials and equipment.
 - Location sensitive costs: Inputs for which the price is determined in **local markets**, such as labour, property and locally traded services.

Overview of cost profiles for manufacturing, services and R&D operations

(including location insensitive costs)

- Location insensitive costs form a small component of total costs for services (11%) and R&D (13%). They are more significant for manufacturing firms (56%).
- Labour costs account for 74% of service costs, 70% of R&D costs and 23% of manufacturing costs.
- Transport accounts for 5% of manufacturing costs.
- Property accounts for 13% of R&D costs, 5% of services costs and 2% of manufacturing costs.

Sectoral Cost Profiles



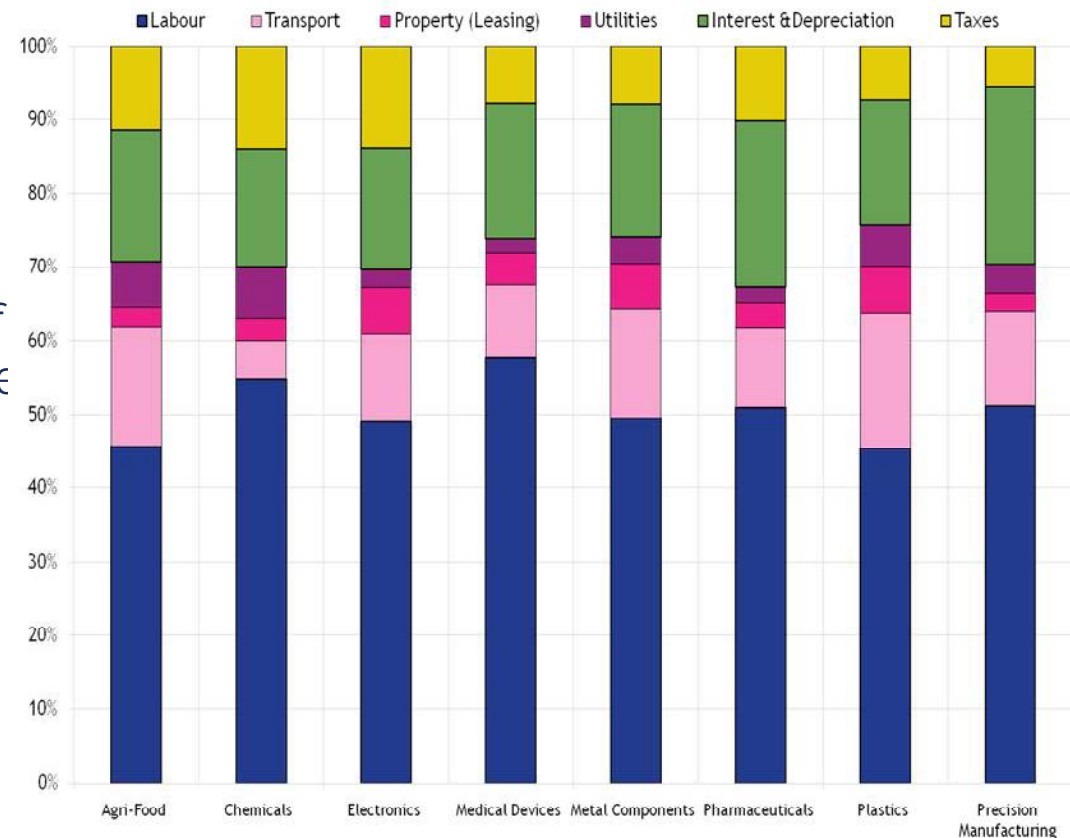
Source: KPMG, Forfás calculations

Manufacturing sector cost profiles in detail

(Location sensitive costs only)

- The significance of **location sensitive costs** varies considerably within manufacturing (62% for medical devices, 32% for chemicals).
- **Labour costs** vary from 45% of local costs for the plastics case study firm to 56% in the medical devices case study.
- **Transport** accounts for 16% of agri-food costs.
- **Utilities** are a significant cost for the case study agri food firm (6%) and the chemicals firm (7%).

Sectoral Cost Profiles



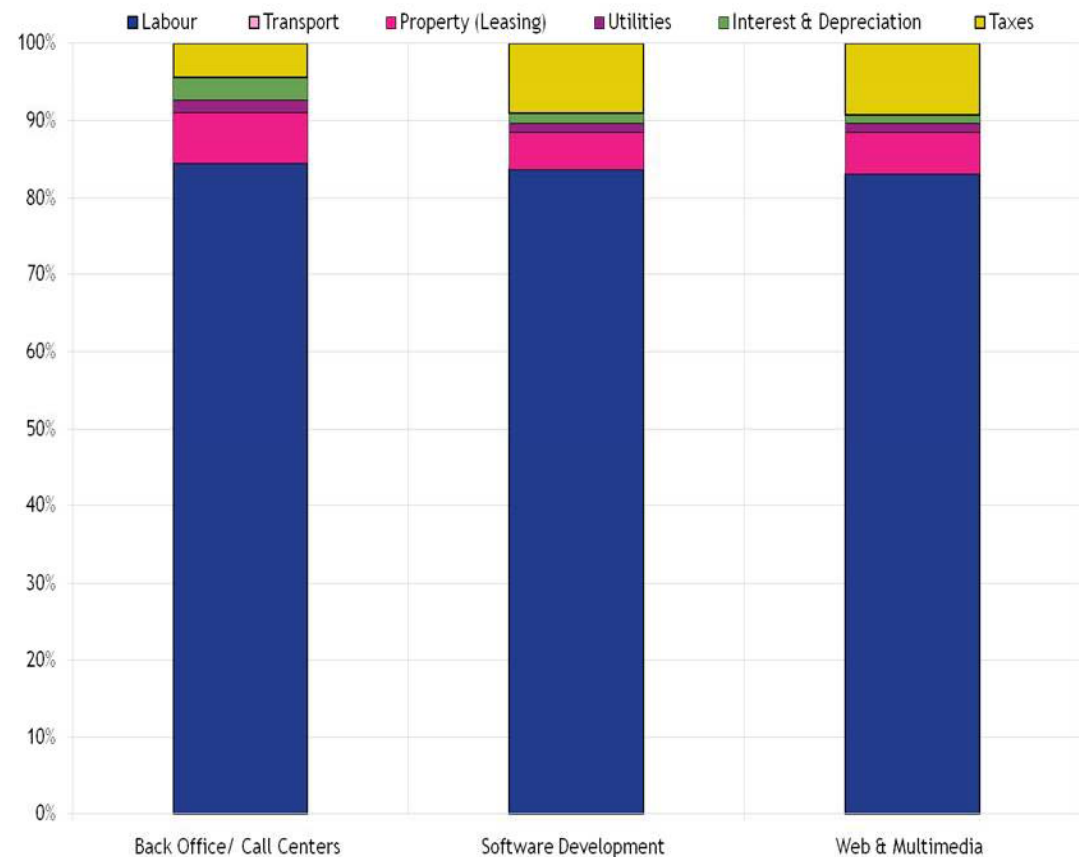
Source: KPMG, Forfás calculations

Service sector cost profiles in detail

(Location sensitive costs only)

- Location insensitive costs account for just 11% of total costs for the case study services firms
- Labour costs account for 76% of local costs for back office operations and 74 % for software development , web and multimedia operations.
- Taxes (less grants) accounts for 9% of costs in the case study software, web and multimedia firms
- Property costs are significant (6%) the for case study back office / call centre

Sectoral Cost Profiles

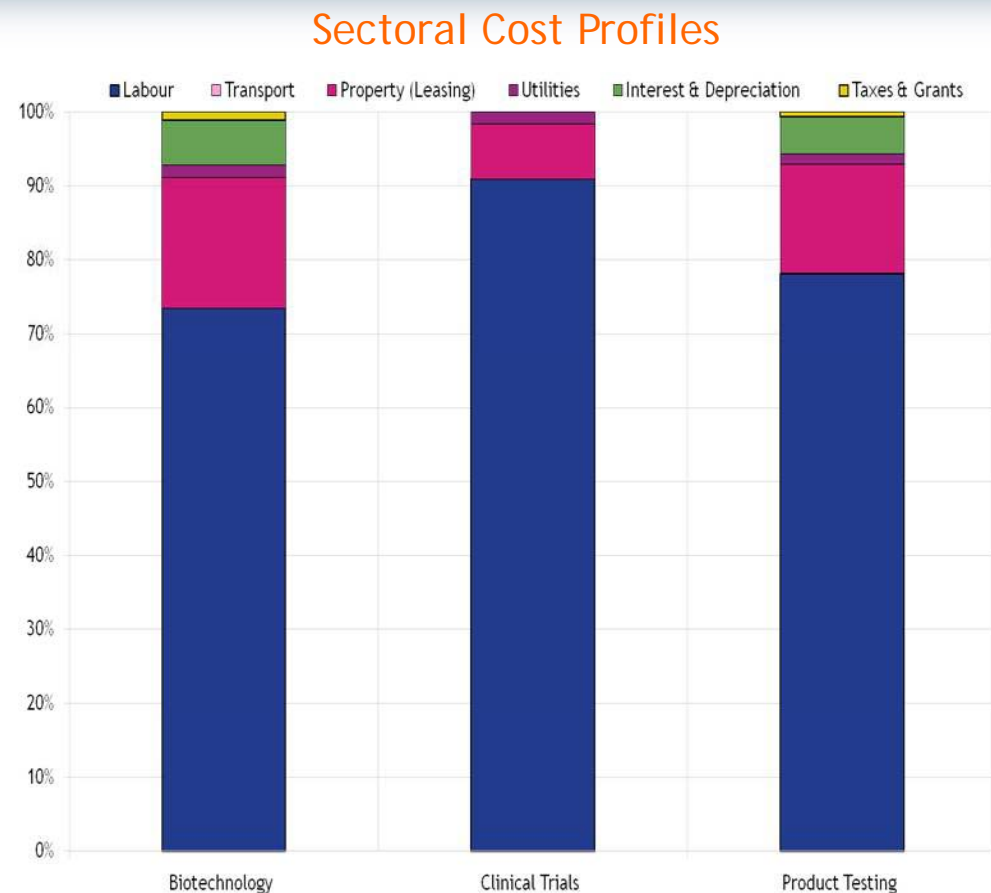


Source: KPMG, Forfás calculations

R&D sector cost profiles in detail

(Location sensitive costs only)

- Location insensitive costs account for just 13% of total costs for the case study R&D firms
- Labour costs account for 91% of costs in the clinical trials firm, 78% in the product testing operation and 73 % in the biotechnology firm.
- Property costs are significant (biotechnology -18%, product testing -15%) for the case study back office / call centre



Source: KPMG, Forfás calculations

2. How does Ireland compare on key business input costs?

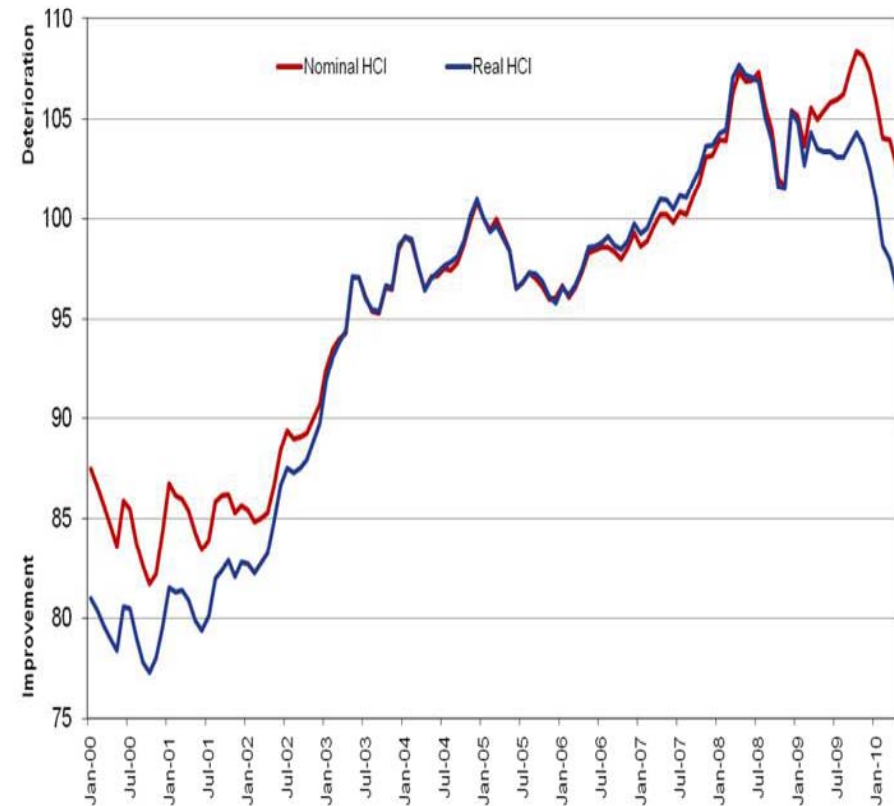
- Labour
- Property
- Utilities
- Business service costs



Harmonised competitiveness index

- Ireland experienced a 7.7% loss in cost competitiveness (real HCI) between January 2005 and April 2008 .
- 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% below the January 2005 value. However, the real HCI remains 19% above the January 2000 level.

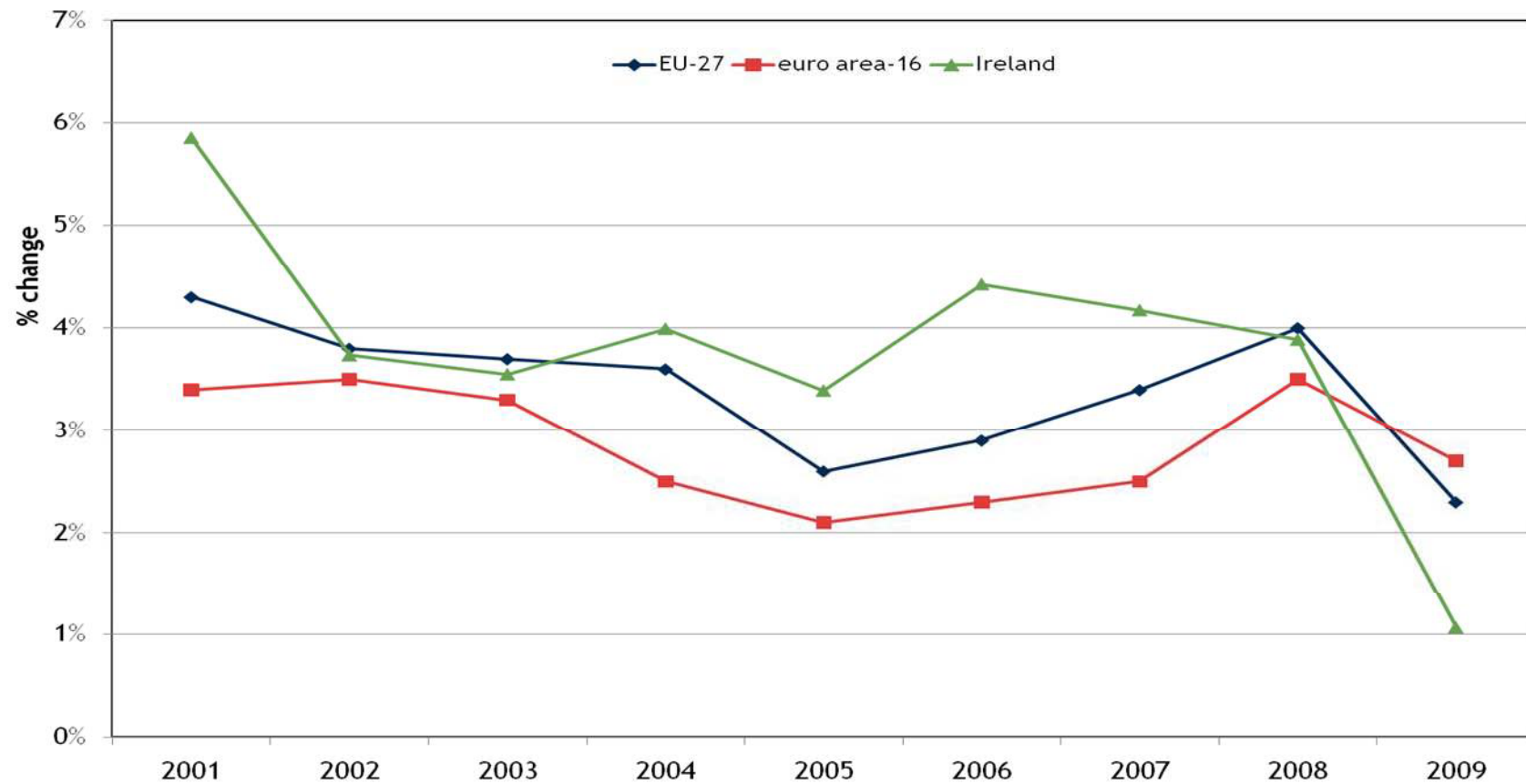
Harmonised Competitiveness Index, 2005 =100



Source: Central Bank,

Labour cost index

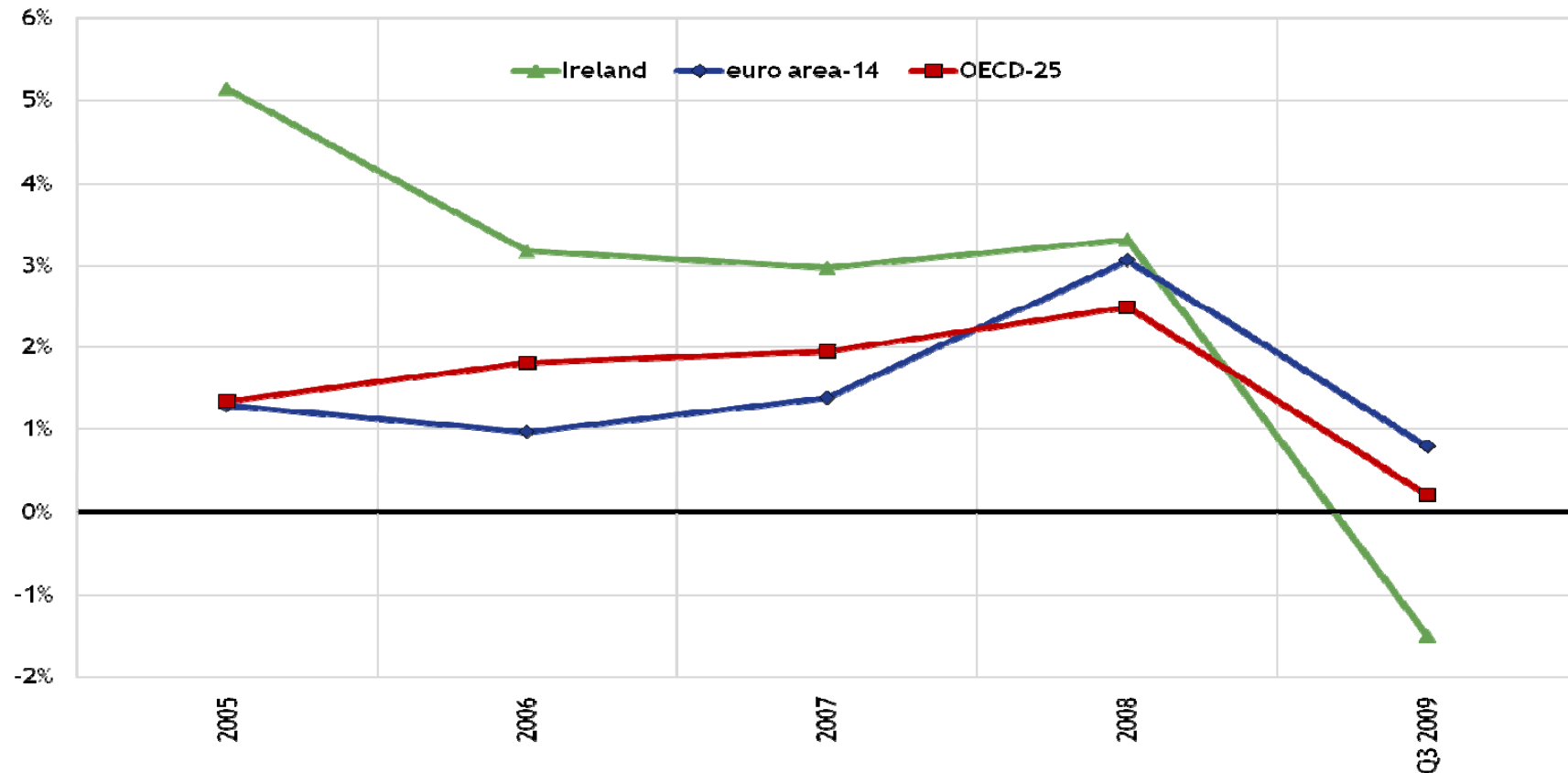
Labour Cost Index- Annual Rate of Change, 2009



Source: Eurostat, CSO

Unit labour costs

Annual Change in Unit Labour Costs



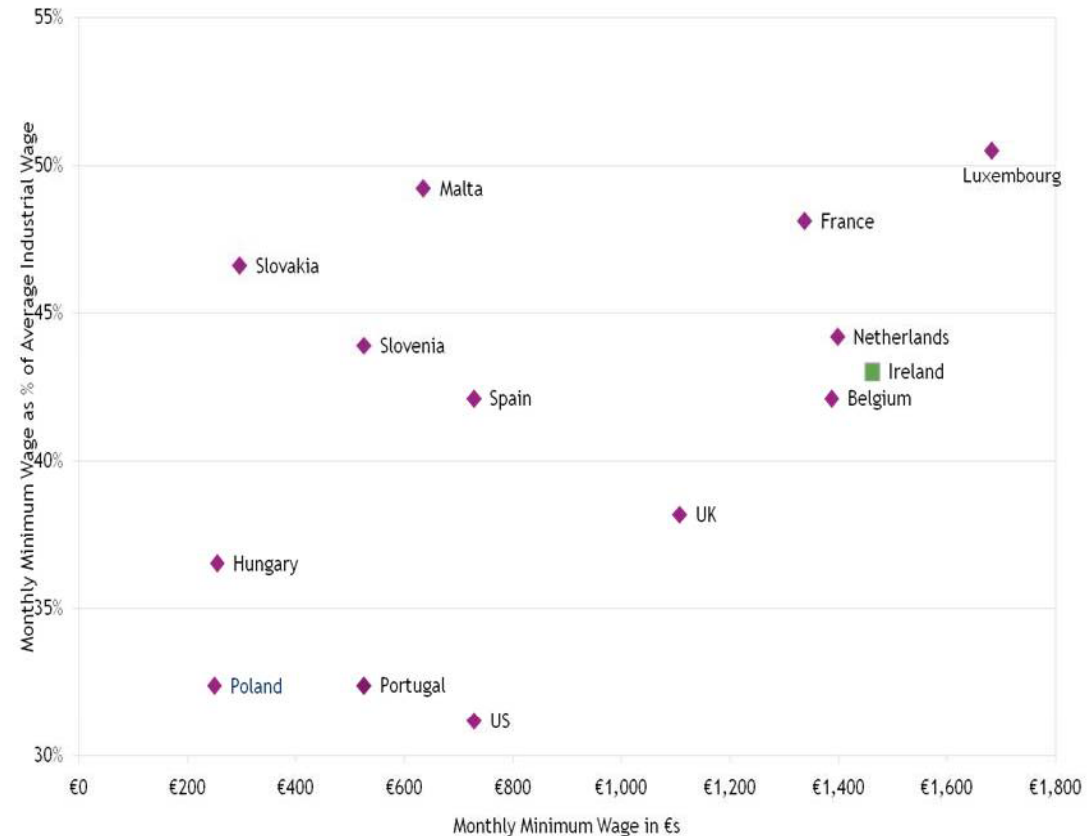
Source: OECD

- ▶ Note: Unit labour costs measure the average cost of labour per unit of output. A downward sloping line indicates an improvement in competitiveness.

Labour costs - minimum wage

- Ireland has the second highest monthly minimum wage in euro area (lower than France on an hourly basis).
- As a percentage of average industrial wage, Ireland has 7th highest minimum wage.

Monthly Minimum Wage & Minimum Wage as a % of Average Industrial Wage

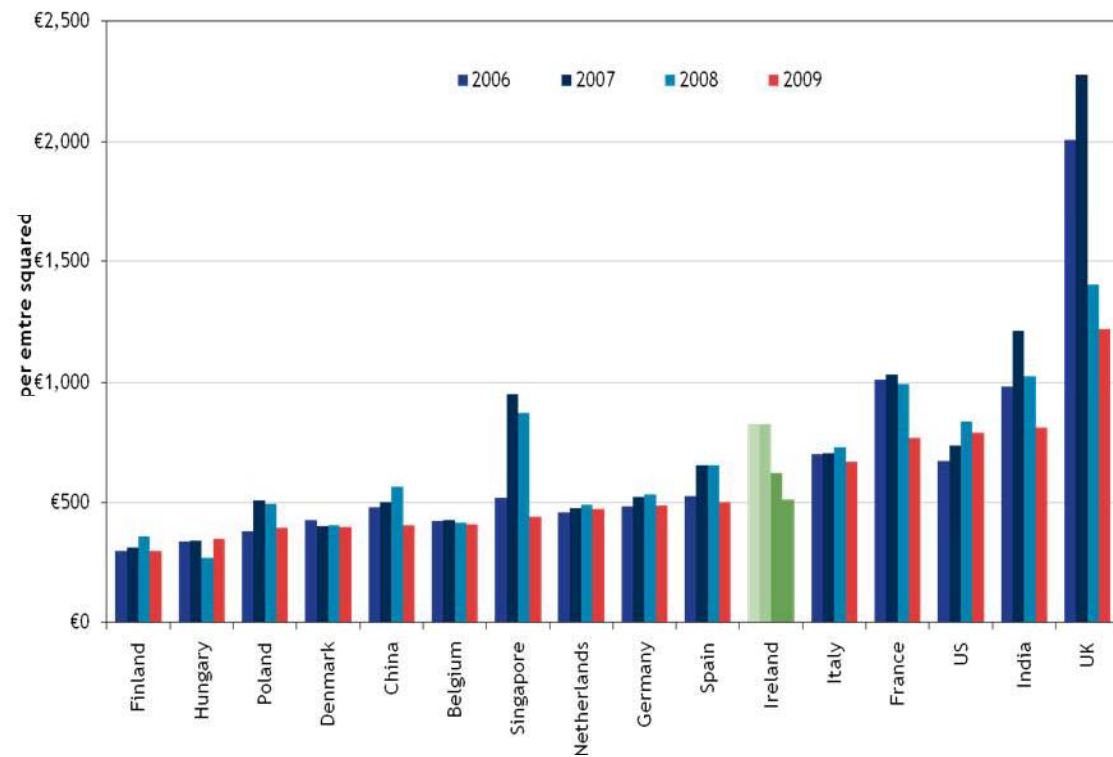


Source: Eurostat, 2009

Prime office rental costs

Cost of Renting a Prime Office, 2006 -2009

- Prices fell by 18% in Ireland in 2009 making us cheaper than the US and Italy.
- However, larger price falls in Singapore and Spain in 2009 mean they are now cheaper than Ireland.



Source: Cushman & Wakefield

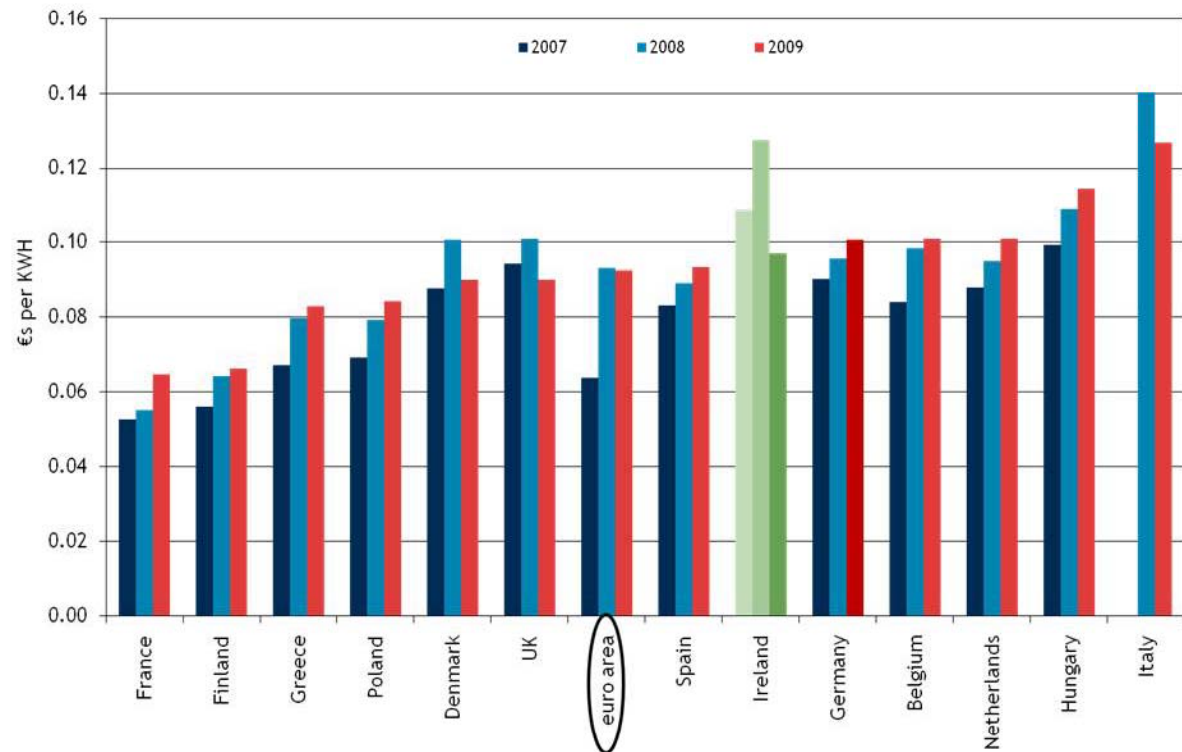
Utilities

- ▶ Significant improvement in cost of electricity for large electricity users (but likely to be temporary).
- ▶ Third most expensive benchmarked location for electricity for SMEs.
- ▶ Treated water remains competitive but large increase in waste water costs, average consolidated charge up 10.5%.
- ▶ In 2008, Ireland had the highest waste costs of the countries benchmarked.
- ▶ Ireland compares favourably on the cost of international telephone calls and high usage mobile packages but broadband costs are the third most expensive (on a per megabit basis) of the OECD- 28. The challenge for Ireland is to deliver higher quality/speed services at existing prices.

Energy

- The price of electricity for large energy users, decreased by more in Ireland (24%) than in any other benchmarked location.
- Electricity costs for SMEs also fell in 2009 (by 15%), but Ireland is still the third most expensive location benchmarked.

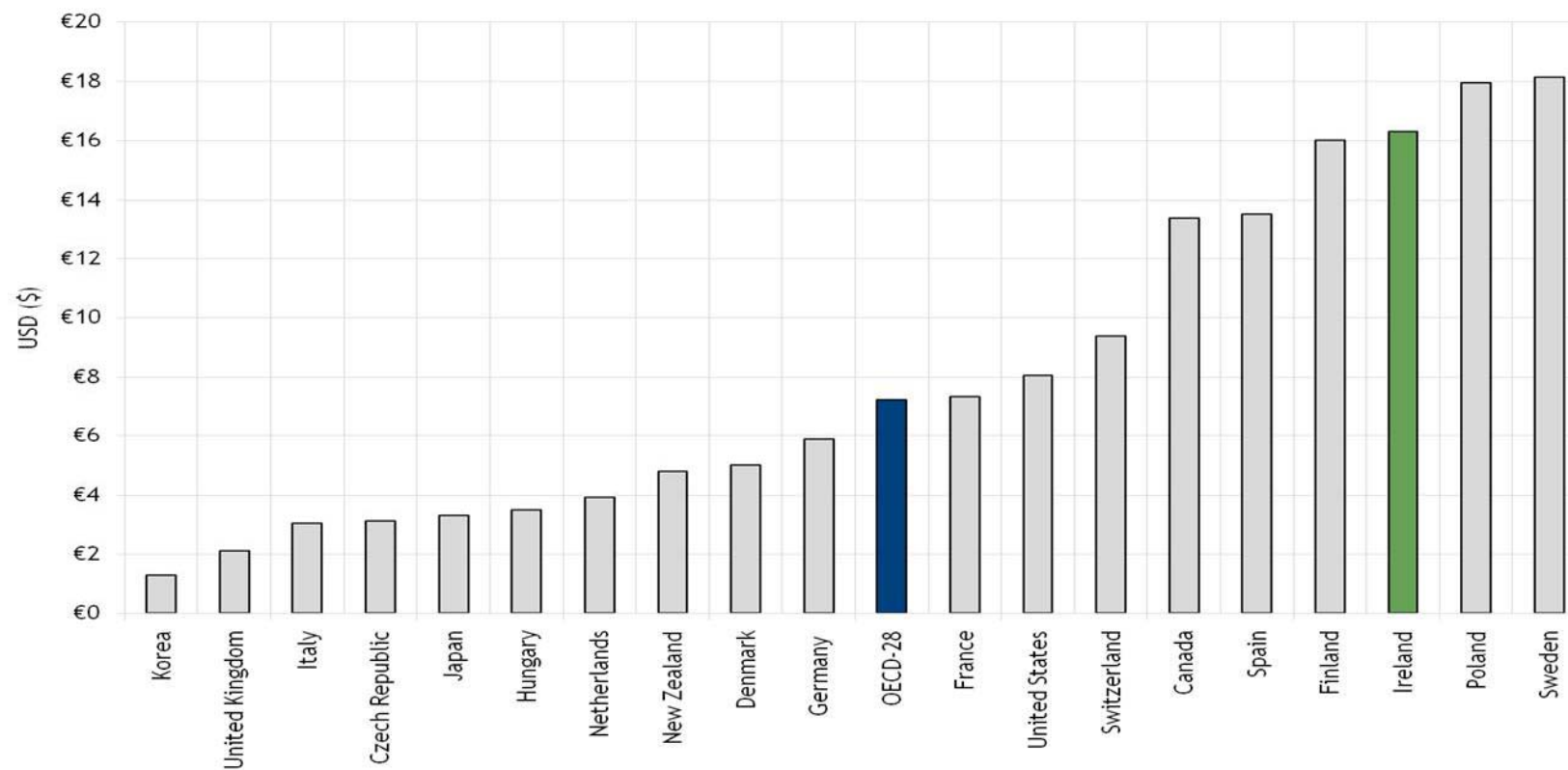
Industrial Energy Prices for Large Energy Users, 2007 -2009



Source: Eurostat, Environment and Energy

Broadband

Average Broadband Monthly Price per Advertised Megabit, US\$, 2009

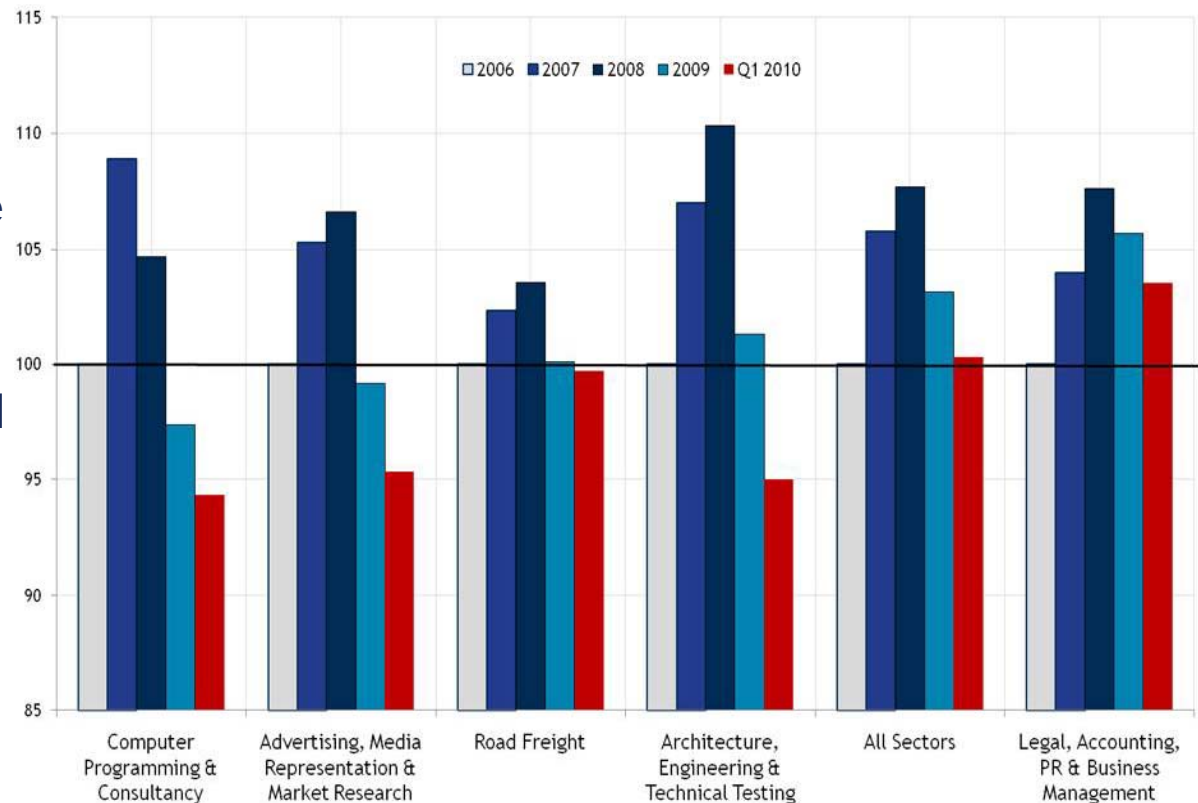


Source: OECD, Broadband Portal

Business services

Services Price Index, 2006=100

- The Services Price Index , which is based on experimental CSO data, 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 just 0.3% above 2006 levels.



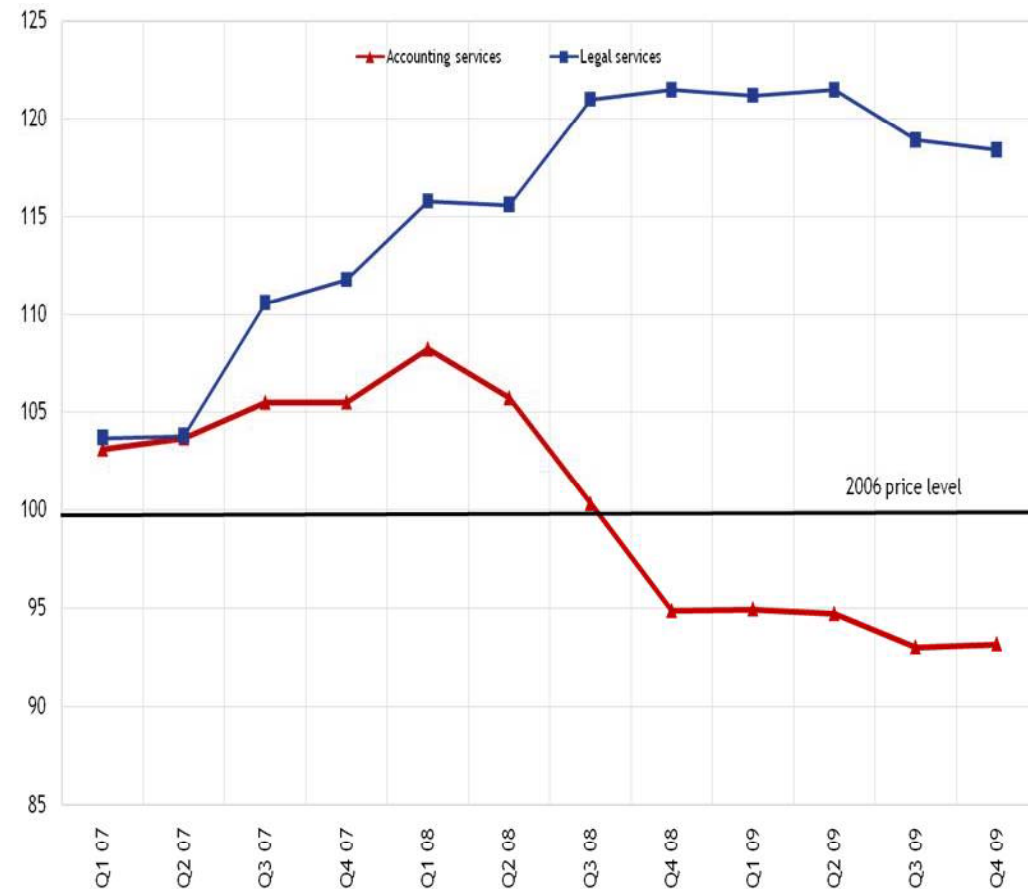
Source: CSO, Services Price Index

Professional services

Differing performances between the professions.

- ▶ The cost of accounting services peaked in Q1 2008, Following a rapid fall thereafter, they were 6.8% below their 2006 level in Q4 2009
- ▶ Legal services costs peaked in Q4 2008. They declined by 3.1% since the peak and remain 18.5% above their 2006 level.

Accounting and Legal Services Index, 2006=100



Source: CSO, Services Price Index

3. Review of the broader cost environment



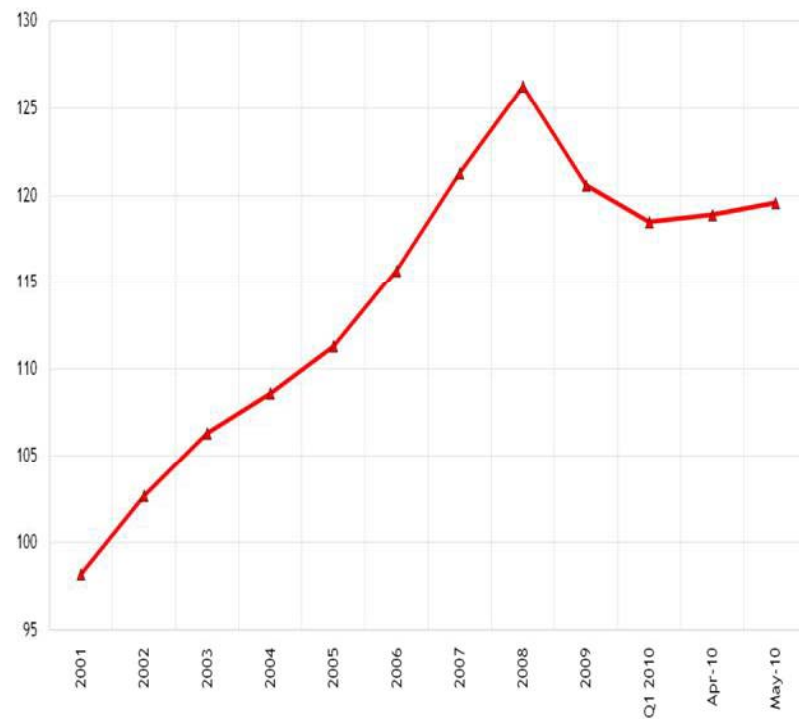
3. The broader cost environment

- ▶ The broader cost environment in which firms operates affects 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.
- ▶ This section of the report looks at consumer prices, accommodation and public and administered prices (e.g. health and education services, public transport and taxis, and public sector wages)

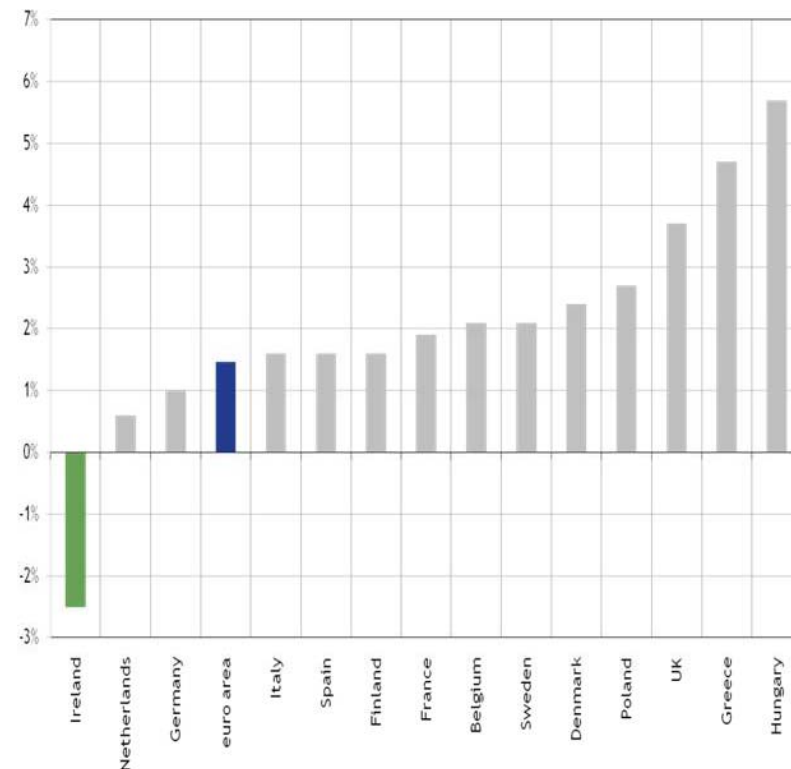
Consumer price index

- CPI has fallen 6.7% since the peak in 2008
- Within the euro area, Ireland experienced the largest decrease in the HICP (-2.5%), in the year to March 2010

Consumer Price Index, December 2001 = 100



Harmonised Index of Consumer Prices,

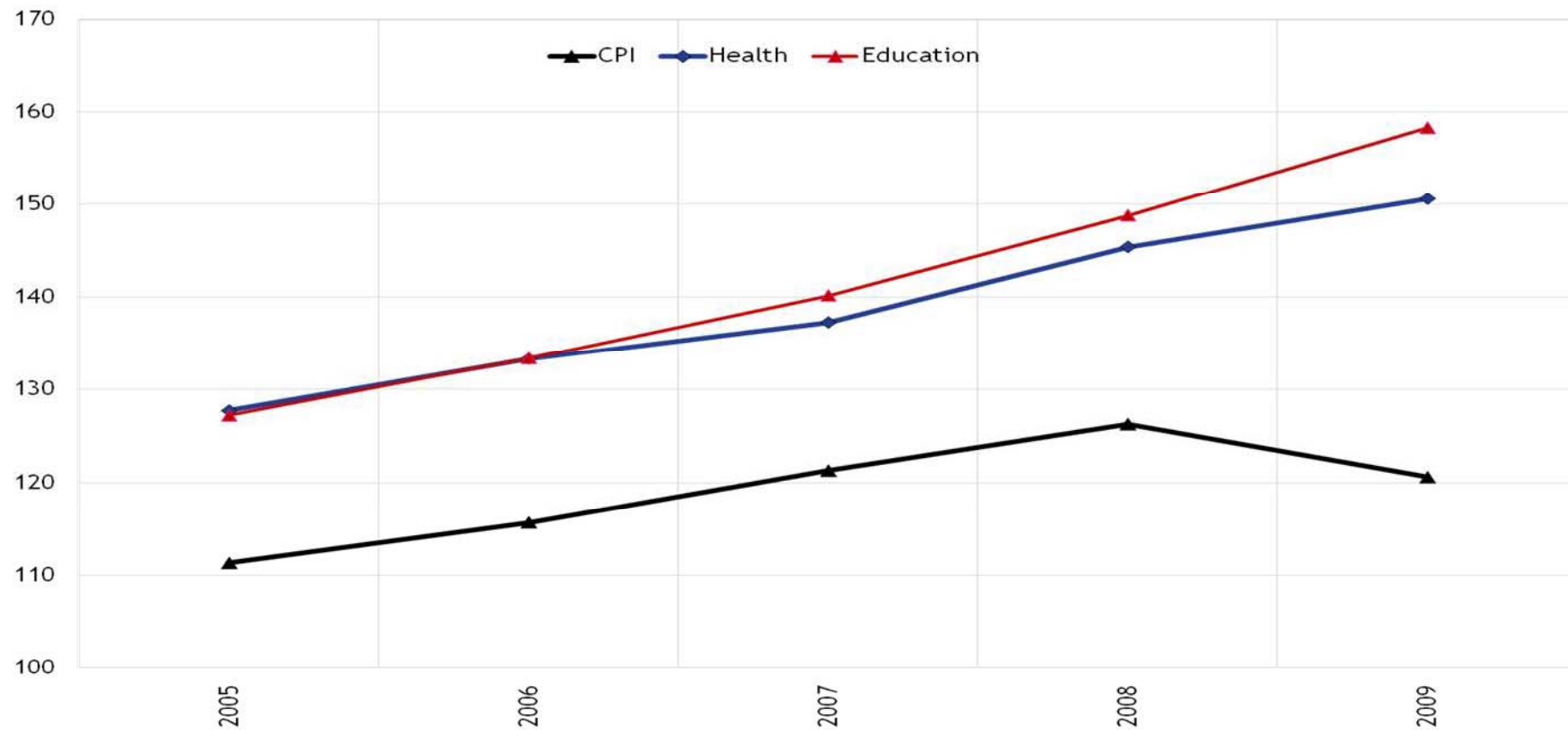


Source: CSO, Consumer Price Index

Public and administered prices

- A range of public and administered prices continue to increase despite price falls elsewhere.

CPI, Health and Education, 2005 -2009



Source: CSO, Consumer Price Index

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www.forfas.ie

