

## Press Release

### **Action needed to sustain our strong economic performance into the medium-term - NCC**

#### **Launch of Annual Competitiveness Report and Competitiveness Challenge**

The National Competitiveness Council (NCC) today (Thursday, 14<sup>th</sup> October) launched its seventh **Annual Competitiveness Report** (ACR) and **Competitiveness Challenge** publications.\* The reports were formally received by Mr Micheál Martin, Minister for Enterprise, Trade and Employment.

Speaking at the launch Minister Martin said, “I would like to thank the NCC for its report and recommendations. This report acknowledges Ireland’s ongoing economic success – a success that other countries are trying to emulate – but it also highlights the significant challenges ahead as a result of the changing Irish and global business environments. This Government is not complacent about our future economic well-being and understands that national competitiveness and social progress go hand in hand. For this reason, we have put in place a process to carefully consider the recommendations contained in this year’s competitiveness reports by the NCC”.

This year’s ACR confirms that Ireland’s economic performance has been impressive in 2004. Growth has accelerated, foreign investment is picking up, unemployment remains low and our public finances are favourable. Speaking at the launch, Mr William Burgess, Chairman of NCC said, “At a time of such strong performance, it may seem untimely to focus on emerging threats to our future prosperity. Yet this year’s competitiveness reports show that the pressures on our competitive position going forward are considerable. These include the continued growth in domestic prices and wages and intense competition from EU accession countries and emerging Asia in export markets and for FDI flows. We need to further improve our competitiveness in order to ensure that the current strong economic performance is sustained into the medium-term”.

“Economic growth and social progress are two sides of the same coin and our competitiveness is crucial to boosting living standards and quality of life in our society. This is evidenced by the fact that Ireland scores well not just on most competitiveness indicators but also with regard to broader quality of life measures; Ireland’s score under the UN’s Human Development Index places us third among the 16 countries benchmarked in the ACR on this measure. The NCC believes that the implementation of the recommendations in this report will help safeguard Irish growth, competitiveness and living standards in the coming years. We commend these reports to Government for their consideration,” concluded Mr Burgess.

The reports identify a number of specific competitiveness challenges for Government.

---

\* The Annual Competitiveness Report (ACR) benchmarks Ireland’s competitiveness performance against 15 other countries. Drawing from this analysis, the Competitiveness Challenge report makes recommendations on Government actions that will help improve the competitive performance of Irish-based firms.

## **Developing the Knowledge Economy**

Knowledge and innovation are increasingly central to the competitiveness of Irish-based firms. The NCC applauds the Government's efforts to make Ireland an attractive location for knowledge-intensive business activities. Key initiatives in this regard have been the €2.5 billion public investment in science and technology (R&D) under the current National Development Plan and the introduction of a tax credit for business investment in R&D. There is also evidence from the ACR that the development of industrial clusters – an important element of a knowledge-based economy - has increased in Ireland in recent years. This year's ACR also indicates, however, that more needs to be done. Two concerns stand out:

- First, while the importance of education to economic performance has long been recognised in Ireland, we must aim to be a leader among advanced economies with regards to educational investment and attainment. OECD data from 2002 indicate that only 77 per cent of Irish 17-18 year-olds currently finish secondary-level education, compared with 100 per cent in Denmark, and giving Ireland a ranking of nine out of the 11 ACR countries for which data on this measure was available.
- Second, despite significant improvements over the last decade, our scientific research and innovation efforts must continue to improve compared with other advanced economies. Business investment in R&D measured just 1.0% of GNP in 2002, compared with an OECD average of 1.6% and a Lisbon Strategy target of 2.0%, giving Ireland a rank of 10th out of 15 countries for this measure in the ACR. Public investment in R&D measured just 0.4% of GNP in 2002, compared with an OECD average of 0.6% and a Lisbon target of 1.0%, ranking Ireland 15th out of 15 in the ACR on this measure. Ireland must also improve regarding the application of knowledge for commercial innovation. The ACR gives Ireland a rank of 9th out of 13 countries for both patents granted by the US Patent Office and for patent applications to the European Patent Office.

Mr Burgess said, "Too much of our economy is characterised by low levels of innovation and productivity relative to other industrialised economies". The NCC has set out a number of recommendations in this year's *Competitiveness Challenge* designed to improve Ireland's knowledge-economy performance. In particular, the NCC calls on Government to:

- develop a programme for the roll out of pre-primary initiatives targeted towards areas of social and economic disadvantage. There is strong evidence from abroad that targeted pre-primary interventions could help to address educational disadvantage in Ireland and improve our economic performance. According to Mr Burgess, "We need to do more to maximise the numbers of our citizens that can participate fully in the knowledge economy";
- sustain public investment in R&D at current levels beyond the current National Development Plan (2000-06);
- clarify the respective roles of different public sector agencies in science, research and innovation;
- improve knowledge transfer between universities and industry;
- ensure an adequate supply of qualified scientists and engineers for industry; and
- promote the application of ICT among Irish companies, in part through a better co-ordinated eGovernment programme.

"Many of these recommendations are consistent with those of the Enterprise Strategy Group which published its report in July. The NCC urges speedy implementation of these recommendations," said Mr Burgess.

### **Improving the Regulatory Environment for Industry**

One of the traditional strengths of the Irish business environment has been the light administrative and regulatory burden faced by entrepreneurs and the SME sector, compared with other (particularly EU) countries. According to the ACR 2004, however, Ireland's ranking on the impact of regulation on the creation of firms has fallen to 7th out of 16 countries benchmarked in 2004, down from 1st place in 2003. The deterioration in Ireland's ranking reflects growing concerns about the costs of compliance with national and EU regulation across a range of areas, particularly the area of corporate governance. A growing regulatory burden may explain why the rate of business start-ups in Ireland still lags behind the leading entrepreneurial countries (USA, South Korea, Australia and New Zealand).

A number of actions are needed to sustain Ireland's advantage in this area:

- Government departments should devote greater resources to a system of Regulatory Impact Assessment that tests major regulatory proposals for their impact on competitiveness. Impact assessments from government departments should be published and their quality tested by an independent body.
- More specifically, the Government should instruct the Company Law Review Group to review the Company Law Amendment Act 2001 and the Companies' (Auditing and Accounting) Act 2003 with regard to their effects on entrepreneurship and start-up companies. Both of these Acts are creating significant difficulties for start-up and expanding companies in attracting skilled and experienced non-executive directors.
- There are currently too many government bodies making un-coordinated requests to firms for similar information. In order to reduce 'red tape', information requests to industry from government bodies should be consolidated through the use of technology.

### **Recovering Cost Competitiveness**

The Government's most immediate competitiveness priority should be to slow the growth of prices and costs. Even knowledge-intensive and innovation-driven industries ultimately have to compete on costs. The ACR confirms the widely-held belief that costs in Ireland are out of line with other developed countries. As also highlighted in the recent NCC *Statement on Prices and Costs*, by 2003 Ireland was virtually on a par with Finland as the most expensive country in the eurozone for consumer goods and services.

According to analysis carried out for the NCC, by the end of 2003 Ireland's price level relative to our trading partners (when measured in a common currency) was eight per cent above its long-run sustainable level – the level that keeps the Irish economy competitive enough to sustain full employment. Employment in manufacturing and other production industries – the sectors of the economy most exposed to international competition – has already fallen significantly since 2000 (though it remains at an historically high level). The fact that there has not been an even greater loss of employment in the exposed sectors of the economy to date may reflect buoyant international markets and a willingness of firms in Ireland to absorb a temporary decline in profit margins. But if the decline in cost competitiveness persists, or if the euro appreciates further against the dollar, a lagged response in terms of a much greater loss of employment could still occur.

Speaking about the need to focus on cost competitiveness Mr. Burgess said, "the fall in the cost of insurance for many businesses and consumers over the last year has demonstrated how determined Government actions can lower prices for consumers and improve cost competitiveness for businesses. This determination to improve cost competitiveness now needs to be applied across a range of policy areas".

These are identified in the Competitiveness Challenge, and include:

**Competition and Regulation:** The Competition Authority needs new powers to levy fines on firms that violate competition law. Better regulation is needed in areas such as energy, transport, retailing and professional services in order to stimulate more competition and put downward pressure on prices in these sectors. With regard to retailing, the Government should end the blanket ban on large retail formats for food and non-food shopping, reconsider the ban on below-cost selling and ensure that there is sufficient zoning for new retail outlets in all local area development plans.

**Fiscal Policy:** The government should commit to keeping direct taxes on business low and to further lowering taxation of income by widening the standard rate tax band in Budget 2005. Government should work to reduce inflation and wage demands by avoiding large increases in excise duties, VAT and administered prices in the Budget for 2005.

**Public Sector Efficiency:** The rapid growth in public sector wages agreed by the social partners threatens to lead to a rise in taxes and administrative charges on businesses. To counter this threat, the Government should commission a comprehensive and independent review of government expenditure, finding new ways of providing government departments, their agencies and other parts of the public sector with incentives to exploit opportunities for efficiency savings.

**Incomes Policy and Social Partnership:** The next social partnership wage agreement should make wage growth more sensitive to developments in our international competitiveness. This could be achieved in part by more favourable tax treatment for employee financial participation in firms, such as gain-sharing.

**Infrastructure:** Past under-investment in infrastructure causes unnecessary costs across the enterprise sector. According to the ACR, Ireland's stock of infrastructure now ranks 11th out of the 12 countries for which comparative data are available. Areas of particular concern are transport, energy and communications. The NCC welcomes the commitment from Government to spend five per cent of GNP on capital projects each year into the medium-term, but believes that more analysis and transparency is needed in the allocation of funding for infrastructure projects in order to ensure that funding is allocated to those projects that most effectively support national competitiveness and broader social objectives.

Ends.