Review of Competitiveness Frameworks: Submission to the National Competitiveness Council

1. Unite the Union would like to thank the National Competitiveness Council for the opportunity to make a submission on the topic of competitiveness. In this submission we do not proposes to put forward an all-encompassing definition of competitiveness. Most definitions revolve around the ability of an economy to maintain a trade surplus. However, while this is valid for a small open economy like Ireland, it fails in general terms for the simple reason that it is, by definition, impossible for all economies to maintain such a surplus.

In addition, we do not propose to canvas all the relevant inputs. This would be difficult to do in a single submission. We will highlight areas that Unite believes have not been part of the debate, and whose absence has been to the detriment of that debate. We will canvas some of the issues regarding measuring competitiveness and put forward proposals on how the National Competitiveness Council can advance a more sophisticated and wide-ranging, inclusive debate. We believe the Council is the one body capable of achieving this.

2. Narrative Issues

Capturing or ranking competitiveness through a set of measurements is highly challenging. Much depends on the measurements used, the benchmarks, the comparators; this is even more so when considering that the inputs into competitiveness itself are highly contested.

For instance, there is a narrative that states that competitiveness is determined by wage levels, tax levels (especially taxation on firms), labour market legislation (again, utilising the highly contested term 'flexibility'). Therefore, a number of terms are produced: 'wage-competitiveness', 'tax-competitiveness', 'labour flexibility'. That these terms are continually and uncritically reproduced in the popular debate can suggest an ideological bias, or it can suggest something much more mundane: analytical inertia.

Below we subject the issues of wages, taxation, and flexibility to a test. We don't suggest this is conclusive, but hopefully it will be provocative. We compare Ireland with our peer group – other small open economies in the EU (other SOE). This category was defined by the International Monetary Fund (IMF). It shows that the five other SOE have a higher ranking in the Global Competitiveness Index than Ireland – an index used by the National Competitiveness Council and the Department of Jobs, Enterprise and Innovation.

TABLE 1: Rankings in the Global Competitiveness Index: 2015 - 2016[1]

Finland	Sweden	Denmark	Belgium	Austria	***Ireland***
8th	9th	12th	19th	23rd	***24th***

[1] The Global Competitiveness Report 2015–2016, World Economic Forum: http://www3.weforum.org/docs/gcr/2015-2016/Global_Competitiveness_Report_2015-2016.pdf

The other SOE all rank higher in the GCI. Yet, on many criteria they would seem to violate competitiveness tenets that are held by many.

TABLE 2: Comparisons Between Other Small Open Economies – Various Measurements

(a) Effective Personal Tax Rate for Employees: 2012 (% of Gross Wages)

Denmark	Belgium	Austria	Finland	Sweden	Other SOE	Ireland
37.5	35.5	30.2	27.5	25.7	**30.4**	**22.7**

The effective personal tax rate in all the other countries is much higher than in Ireland. Taken together, the effective rate among other SOE is 34 percent higher than the Irish rate.[2]

(b) Effective Corporate Rate: 2012 (% of Profits)

Denmark	Belgium	Sweden	Austria	Finland	Other SOE	*Ireland*
30.4	29.8	25.1	21.7	19.8	**25.6**	***8.5***

The effective corporate tax rate in the other SOE is far higher than in Ireland – three times as high on average.

(c) Employee Compensation per hour in the Market Economy: 2015 (€ per hour)

Denmark	Belgium	Sweden	Finland	Austria	Other SOE	*Ireland*
42.70	41.10	40.10	33.50	32.20	**37.90**	***28.70***

Again, we see that market economy wages in other SOE are far higher than Irish levels – 32 percent higher. A sectoral breakdown (e.g. manufacturing, transport, retail, professional & scientific) will show similar larger gaps.[3]

(d) 'Social Wage', or Employers' Social Insurance, & other Payroll Taxes 2013 (% of Gross Wages)

Sweden	Austria	Finland	Belgium	Other SOE	*Ireland*	Denmark
22.3	19.5	17.7	16.5	**25.1**	***8.0***	Not applicable

The high level of social wages (or employers' social insurance) in other SOE is part of a pattern. They are more than four times as high as Irish levels. Denmark doesn't have a social insurance system.

(e) Employment Protection

Belgium	Austria	Denmark	Sweden	Finland	Other SOE	*Ireland*
3.17	2.49	2.27	2.18	2.01	**2.42**	***2.07***

Ireland has a low level of employment protection legislation as measured by the OECD Indicators (collective and individual dismissal, regulation on temporary employment). This doesn't capture the full extent of employment protection but should be treated as indicative.[4]

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[2] Eurostat Taxation Trends in the European Union: http://ec.europa.eu/taxation_customs/taxation/gen_info/economic_analysis/data_on_taxation/index_en.htm

[3] See Unite's 'The Truth About Irish Wages', 2016 due to be published. Data from Eurostat Labour Cost Levels: http://appsso.eurostat.ec.europa.eu/nui/show.do

As we stated above, this table is not intended to be conclusive. However, it shows that high employee compensation, high corporate taxation, high personal taxation, high 'social wage' (employers' PRSI) and high levels of employment protection are not bars to a competitive economy.

(a) Childcare

We can see this in the example of childcare. That childcare costs are high by European standards has been well established in the debate. A significant factor in this is the European practice of providing affordable childcare as a public service (either direct provision or in networks with private and non-profit providers). This is essentially a subsidy, or a cost on public finances. Ireland will have to increase public provision for affordable childcare. This will in all likelihood will entail an increase in taxation (given the fiscal rules).

Of course, affordable childcare is an economic good: it reduces upward wage pressures, increases labour supply and removes work disincentives. This should assist in competitiveness. However, if increased taxation is treated as 'uncompetitive', then this creates in, our opinion, an unnecessary contradiction. A similar argument could be made regarding rents and housing shortages in Dublin. It may well be that Irish taxation is uncompetitively low.

3. Structure of Indigenous Business Activity

In assessing competitiveness, it would be useful to disaggregate data on foreign-owned and indigenous business activity; not only because the two sectors face distinct challenges. The development of a strong, value-added, export-facing indigenous sector is vital to long-term sustainable growth as identified in industrial strategy papers ever since the Telesis Report in the early 1980s. By examining the indigenous sector, we may be better able to identify the deficits.

An example of this is the structure of indigenous business activity.[5] Long-term analysis has shown that prior to the recession, the construction sector – primarily indigenous-owned – grew at unsustainable rates. Between 2000 and 2007, construction employment growth comprised 40 percent of all market economy employment growth - and this doesn't factor in other building/property-related employment. In addition, Davy Stockbrokers showed that during the period, investment primarily flowed into residential housing. But there are other structural concerns.

Indigenous Sectoral Employment as a % of Total Indigenous Market Employment: 2012

	EU-15	**Other SOE**	***Ireland***
Manufacturing	19.1	19.0	***9.5***
Accommodation & Food Services	9.2	7.4	***17.1***
Wholesale & Retail	24.5	22.5	***29.3***

[4] OECD Employment Protection Database: http://stats.oecd.org/Index.aspx?DataSetCode=EPL_OV
[5] Eurostat Foreign control of enterprises by economic activity and a selection of controlling countries: http://appsso.eurostat.ec.europa.eu/nui/show.do

In the indigenous market sector, employment in the manufacturing sector is half that of other EU averages. However, there is a disproportionate concentration in the low value-added, low-waged sectors: hospitality and distribution. Over 46 percent of employment is in these sectors. This is mirrored by a similar concentration of investment in these sectors; over 20 percent of total indigenous market investment went into these two sectors – substantially more than European averages.[6]

This is just a sample of the data that is available when we isolate the indigenous sectors. In this example, there is a concern that our competitiveness is being undermined by a strong tendency of indigenous business and capital to seek out low value-added and non-traded sectors.

4. Managerial Quality

Not all important features of competitiveness can be easily reduced to comparative benchmarks. An example of this is managerial quality in the indigenous sector. This is difficult to measure and benchmark against other countries' performance. However, the issue of managerial quality, while not featuring in the public debate, should be addressed given that a number of studies have highlighted serious deficits.

(a) A study published by the Irish Management Institute[7] concluded that:

> *'Management is a key factor in determining productivity . . .The standard of management in Irish manufacturing firms is not only poor but is losing ground globally.'*

Problems revolve around managerial inability to diagnose weaknesses and lack of evidence-based decision-making.

(b) The Management Development Council – with other agencies - published a survey of indigenous manufacturing firms.[8] After accounting for structural factors (firm size, ownership, etc.) it found:

> *'[Ireland] has a large proportion of lowly rated firms, with 19% of firms scoring less than 2 on a management practice assessment scale from 1 to 5 . . '*

The Council estimated that up to €2.5 billion in value-added was lost due to poor management. Given that in 2012, total manufacturing GVA was €5 billion, this constitutes a considerable loss

(c) Enterprise Ireland and FAS conducted a comprehensive and detailed survey of the Print and Publishing sector – a 200 page report that should be a template for audits on other indigenous sectors.[9] It identified:

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[6] Even when accounting for the large tourism trade, there is an over-concentration of employment in the Irish hospitality sector. Countries with higher levels of tourism as measured by nightly occupancy in the accommodation sector – Greece, Spain, Italy – have much a much lower proportion of employment in this sector relative to Ireland.

[7] Irish Management Institute, Management Makes the Difference, Rebecca Homkes and Eva Maguire, 2011: https://www.imi.ie/wp-content/uploads/2011/12/Management-Makes-the-Difference-2011.pdf

[8] Management Development Council, Management Matters in Northern Ireland and Republic of Ireland,2009: http://i14.archivec.com/files/2012/03/11/20766/01b3e592ff05cd9fe24c7ef2eeaab493.pdf

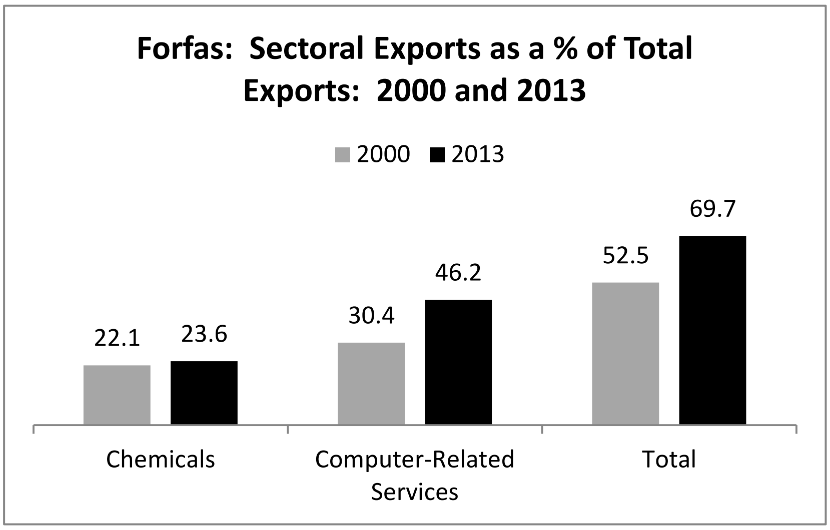
'. . . significant deficiencies in key management and technical skills; a traditional management culture . . . '

(d) Enterprise Ireland and the Expert Group on Future Skill Needs published a survey on SME managerial skills and found that in a range of categories (training, marketing, supply chain, IT, R&D, human resources, new products, planning, project management, innovation) managerial quality was either '*inadequate*' or '*poor*'.[10]

If management is a key factor in determining productivity, then analytical space and time needs to be devoted to this subject. Without such focus, we may be ignoring an important input to competitiveness and, therefore, impeding our ability to address any existing deficits.

5. Export Concentration and Structure

The National Competitiveness Council has referenced this issue previously, but it should be highlighted in the public debate: namely, the concentration of exports in a small number of sectors, driven by a small number of foreign-owned companies.



70 percent of total exports (as recorded by Forfas in their agency-assisted company database[11]) come from two sectors – chemical / pharmaceuticals and computer related service sectors.

While the chemical sector did not rise significantly in overall terms, they do make up nearly half of all goods exports. However, the largest increase has been in the computer-related services sectors.

This is concentrated in a relatively few companies. 98 percent of exports in these two broad sectors come from the foreign-owned sector. EU Commission data shows that there are 80 foreign-owned companies in the chemical sector and 472 companies in the broad Information & Communication sector. This high dependency on relatively few companies may even be an under-estimate. Revenue Commissioners' data shows that 7 percent of foreign-owned companies paid over 80 percent of all tax receipts from the foreign-owned sector.

This concentration represents a serious and growing negative impact on our competitiveness.

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[9] Enterprise Ireland and Fas, A Developing Future: A study of the Paper, Print & Packaging industry, 2005: http://www.fas.ie/en/pubdocs/developingfuturereport.pdf

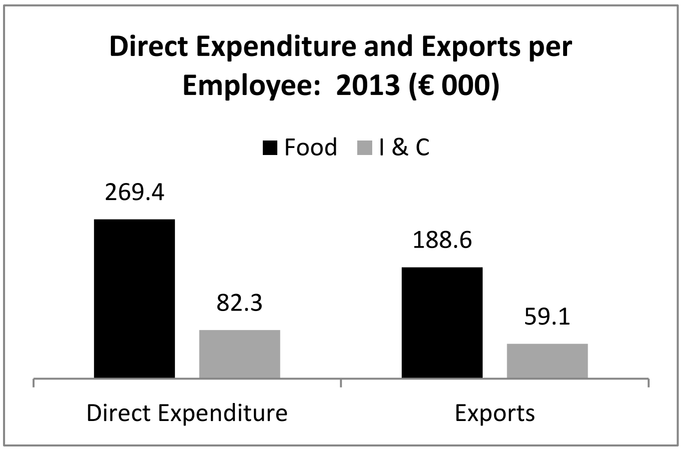
[10] SME Management Development in Ireland', Expert Group on Future Skill Needs, 2004: http://www.skillsireland.ie/media/egfsn060512_sme_development.pdf

[11] Forfas, Annual Business Survey of Economic Impact: https://www.djei.ie/en/Publications/Annual-Business-Survey-of-Economic-Impact-2013.html

(a) Weak Multipliers in Services Exports

In addition to a growing dependency on a relatively small number of companies, we are moving towards greater reliance on service exports. No doubt this will increase given the pattern of global trade and production – especially given the challenges of an indigenous, late-entrant small open economy in developing capital-dense export-facing manufacturing.

If this is the case, then we should be aware that service activity has much lower multipliers than manufacturing. For instance, using Forfas data to compare the food manufacturing and information & communication sector in the indigenous sector, we find the multiplier to be much higher in the former. When direct expenditure (employee compensation, domestically sourced materials and services) and exports per employee are compared, we find the multiplier for the food manufacturing sector to be far higher. In both categories, it would take three people employed in the information & communication sector to match direct expenditure and exports as one person employed in the food sector. In indigenous Business Service exports, the multipliers are slightly better than information & communication but they are still less than half that of the food sector.



This structural shift towards export sectors that have substantially lower multipliers than manufacturing will pose considerable challenges to not only ensure a competitive economy, but to ensure that the benefits of improved competitiveness are shared throughout the economy.

6. Employee Participation and Workplace Democracy

There is a substantial literature that shows that greater employee participation and workplace democracy leads to higher productivity and improved firm performance. The National Centre for Partnership and Performance produced a number of reports on more democratic and cooperative methods of organising the decision-making within firms.[12] One example is that they found that firms with high levels of participation and unionisation experienced a 20 percent increase in productivity over their baseline. All other things being equal, a unionised and high-employee-participation firm achieved twice the level of productivity growth as non-unionised and low-employee-participation firms.

The potential for increasing productivity is, therefore, considerable. This would constitute a cost-less form of increase competitiveness; costless insofar as it doesn't constitute investment or other cost activities (marketing, (re)training, etc). All it involves is what can be considered axiomatic – the more participation in the decision-making process of a firm (just as in society), the more efficient the outcomes.

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[12] National Centre for Partnership and Performance, Achieving High Performance: Partnership Works — The International Evidence: http://files.nesc.ie/ncpp_archive/research_series/NCPP_Research_1_2003_hpws_full_report.pdf

7. Inequality, Deprivation and Social Exclusion

Since the recession, international bodies have taken a greater interest in the impact of inequality on economic growth. The International Monetary Fund recently wrote:

> *'Earlier IMF work has shown that income inequality matters for growth and its sustainability. Our analysis suggests that the income distribution itself matters for growth as well. Specifically, if the income share of the top 20 percent (the rich) increases, then GDP growth actually declines over the medium term, suggesting that the benefits do not trickle down. In contrast, an increase in the income share of the bottom 20 percent (the poor) is associated with higher GDP growth. The poor and the middle class matter the most for growth via a number of interrelated economic, social, and political channels. '*[13]

The OECD has come to similar conclusions:

> *'Widespread increases in income inequality have raised concerns about their potential impact on our societies and economies. New OECD research shows that when income inequality rises, economic growth falls. One reason is that poorer members of society are less able to invest in their education. Tackling inequality can make our societies fairer and our economies stronger.'*[14]

The OECD is taking this further, by exploring the nexus between inequality and productivity in their integrated framework, New Approaches to Economic Challenges (NAEC) initiative.

Competitiveness and sustainable economic growth are, obviously, inter-related. Therefore, factors that impede sustainable growth will put limits on competitiveness. In this regard, there is serious concern for the Irish experience.

- Ireland has the highest level of market at-risk of poverty in the entire EU – with 37 percent at risk-of poverty compared to an EU-15 average of 26.5 percent.[15] Other SOE is marginally higher at 27.2 percent.
- Ireland's deprivation rate is significantly higher than the European benchmarks. The Irish deprivation rate is 22.6 percent compared to an EU-15 average of 15.5 percent. For the other SOE, that rate is 8.0 percent.[16]
- The Irish rate for social exclusion is, again, higher than the EU-15 average – 27.6 and 23.3 percent respectively (Ireland ranks 4th in the EU-15). The rate for other SOE is 18.5 percent.

Even if one is sceptical about the relationship between inequality, low incomes, social exclusion, and productivity and competitiveness (though we believe this scepticism is shrinking under the weight of

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[13] International Monetary Fund: Causes and Consequences of Income Inequality: A Global Perspective, 2015: https://www.imf.org/external/pubs/ft/sdn/2015/sdn1513.pdf

[14] OECD Focus on Inequality and Growth: https://www.oecd.org/social/Focus-Inequality-and-Growth-2014.pdf

[15] Eurostat At-risk-of-poverty rate before social transfers (pensions excluded from social transfers) by poverty threshold, age and sex: http://appsso.eurostat.ec.europa.eu/nui/show.do

[16] Eurostat Material deprivation rate for the 'Economic strain' and 'Durables' dimensions, by number of item of deprivation: http://appsso.eurostat.ec.europa.eu/nui/submitViewTableAction.do

growing evidence that shows the relationships), it can be easily established that low incomes impede the potential of indigenous firms to enter export markets. This is not only because many firms need to, first, establish a firm foothold in the domestic economy. Even for those indigenous firms that are participating in foreign markets, over 50 percent of sales still come from the domestic market.

8. Measurement Issues

The following canvasses measurement issues in no particular order of importance and does not purport to be comprehensive.

(a) Benchmarking

Current NCC publications benchmark Irish performance with other countries. This is a useful and important exercise. However, there is a question of which countries or group of countries we should be comparing ourselves with. For instance:

- OECD countries and group average: the OECD includes countries which are much poorer than Ireland and, therefore do not constitute a useful comparison. Mexico, Turkey, Chile, Hungary and Poland all have GDP per capita at less than half Irish levels, with Estonia, Slovak Republic, Slovenia and Czech Republic at similar low levels. It is difficult to understand the benefit of comparing Irish performance with these countries.
- Eurozone averages: this comparison omits a significant trading partner (UK) and two out of the five peer group countries (other small open economies: Denmark and Sweden).

While this is not to dismiss such comparisons, they both have defects. Unite proposes that the NCC consider three benchmarks:

- **EU-15**: this category excludes the poorer New Member States of which most do not have a long history of market economies
- **Northern and Central European economies (NCEE**): this EU-15 excludes the poorer Mediterranean countries which do not have the same economic or welfare structures as Ireland.
- **Other Small Open Economies**: referred to above, these are countries with a similar economic structure as Ireland: small domestic markets, reliance on exports.

We would further propose that, where possible, the same benchmark(s) be used consistently throughout measurements. While we appreciate that this is not always possible, the use of different EU measurements (EU-28, Euro-17 or 18 or 19, OECD) can undermine a consistent comparative perspective. The use of our proposed benchmarks could assist in this.

(b) Measuring Irish Data

The problems with Irish data are widely known. There have been debates regarding GDP and GNI; comparisons of productivity are undermined by multi-national tax strategies; recent changes in the Eurostat national accounts classification have thrown up new problems, as has the impact of inversion (on GNP). We raise two issues:

- The NCC uses GNP in many of its measurements. Not only is there no corresponding measurement for other EU countries; there is a strong argument that this is not an adequate measurement for Ireland on a range of issues (any more than GDP). GNP measurements exclude large swathes of production activity that occurs in the state. The NCC should consider using the Irish Fiscal Advisory Council's formulation of a hybrid-GDP as it is a more robust reflection of Irish economic activity and capacity.
- The NCC has correctly highlighted investment as a vital building block in competitiveness. Again, however, it is crucial that we measure actual investment. For instance, in the change-over to ESA 2010, Eurostat included intellectual property in gross fixed capital formation (in the previous ESA 1995, intellectual property was part of intermediate consumption). This is a highly debateable inclusion, especially as in Ireland the import of intellectual property may be driven by multi-national tax strategies, with little impact on the domestic economy.[17]

There are other measurements that would be affected (e.g. current account balance), while other calculations would need to be factored in (e.g. lower GNP due to inversions) in order to get a more accurate picture of the Irish economy.

(c) What Measurements are Supposed to Tell Us?

There are other measurements used by the NCC that should be scrutinised, in order to ensure that it is actually telling us what it purports to tell us. For instance, the NCC uses a measurement 'Average annual gross & net earnings'[18], to describe 'wage levels'. However, gross and net earnings do not speak directly to wage levels. Earnings can also impacted by working hours and taxation. For instance, the wage per hour may fall but, if taxation falls even further, net earnings may rise; this, despite wages actually falling. Or, the same wage level may apply between two countries. However, if there is more part-time work in one country, earnings in that country will be lower; but not their wage level. Annual earnings data tells us about annual earnings; it may not tell us and, indeed mislead us, as to actual levels.

A comparison of wage levels should be done on the basis of employee compensation and labour costs per hour. This reflects the compensation for an hour's work. A comparison of wage increases should be done using robust measurements in the Labour Cost Index.

9. Proposals

Unite believes the National Competitiveness Council is in a prime position to commence a new and comprehensive debate on the issues of competitiveness. Therefore, Unite proposes the following:

(a) The NCC to give active consideration to including new competitiveness criteria in its analysis; for example: structure of indigenous business and export activity, managerial quality, employee participation and workplace democracy, issues relating to equality and social cohesion, etc.

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[17] Eurostat GDP and main components (output, expenditure and income): http://appsso.eurostat.ec.europa.eu/nui/show.do

[18] National Competitiveness Council, Ireland's Competitiveness Challenge 2015: http://djei-competitiveness.ptools.net/Publications/2015/Competitiveness-Challenge-2015.pdf

(b) The NCC to undertake a thorough re-examination of the current criteria and the measurements it uses. To this end the NCC should invite representatives of civil society groups (employers, employees, civil society organisations) to conduct this re-examination through meetings, workshops and public debate.

(c) The NCC to give equal weight to alternative narratives regarding competitiveness in its analysis (e.g. this Submission's discussion of comparative taxation and wage levels in Section 2 above).

(d) The NCC to give consideration to how it can promote the debate on competitiveness. For instance, it could set up a new website (or a page on its current website) devoted to articles and comments on competitiveness from a range of civil society organisations. This would help promote greater public awareness of the different approaches to competitiveness held by public stakeholders.

Ultimately, the issues regarding competitiveness are not fixed; nor are they mechanistic. They are ultimately political in nature and reflect on the type of society we want to create. To promote this debate would be significant contribution by the National Competitive Council.

End