NERI Opening Statement – Joint Committee on Enterprise, Tourism and Employment

'Views on competitiveness, the cost of doing business in Ireland and related matters'

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Introduction

My name is Tom McDonnell. I am co-director of the NERI, and I am joined today by my NERI colleague Ciarán Nugent.

First of all we would like to thank the Cathaoirleach, and members and staff of the Committee for the invitation to appear before you.

We are grateful for the opportunity to present our views on competitiveness, the cost of doing business in Ireland and related matters. The most important of these 'related matters' is of course productivity because it is productivity that ultimately determines average living standards over the long-run.

Introduction

Competitiveness is a relative concept. It is a function of the economy's underlying productivity and its cost base and, crucially, how economy and firm productivity and cost bases compare to that of competitor countries and competitor firms. We can improve our competitiveness either via productivity increases or via improvements in the cost base relative to competitors. As it happens, Ireland generally ranks as one of the most competitive economies in the world, albeit one with clear weaknesses.

A high road strategy – New Economic Model

Our most notable competitiveness failure is the weakness of Irish infrastructure across a slew of areas including energy, water, transport and housing. This reflects years of underinvestment in the public capital stock and suggests that the budgetary focus over the years ahead should prioritise capital spending over alternatives such as cutting taxes. To complement this focus we will need a medium-term strategy to incentivise workers both foreign and domestic into the Irish construction sector.

Irish labour costs are generally in line with other high income Western European countries. However, there are clear cost issues in a range of other areas. The most notable of these are the cost of energy and the cost of legal and insurance fees. Ultimately, the issue of energy costs will only be resolved by a massive programme of investment (including state investment) in renewable energy supply including battery storage and grid upgrades.

The NERI's view, and one that we explain in the new economic model document referenced in our submission, is that Ireland's competitiveness strategy should be based on a 'high road' strategy of steady improvements in the productive and innovative capacity of the Irish economy. Workers and business owners will both benefit from this in the long-run. On the other hand, the alternative 'low road' strategy of driving down labour costs to improve competitiveness should be avoided. It will simply exacerbate our already high level of in-work poverty and will slow down our economic development.

To achieve a 'high road' outcome we need to:

(A) Meaningfully increase public spending on R&D, and on education and training including supports targeted at adults so that we can respond quickly to technological and other disruptions;

(B) Better design incentives (carrots and sticks) for business to invest in their own research, productivity and innovation including horizontal innovation through worker democracy and collective bargaining;

(C) Develop a set of policy initiatives to attract and retain human capital and diffuse technology more broadly;

(D) Expeditiously reverse our infrastructure deficits and

(E) Pursue inclusive policies that ensure we are utilising everyone's potential – e.g. through policies to end child poverty.

Enterprise policy and return on fiscal investment

Not all enterprise policy is good policy. For example, we do not support calls to reduce the VAT rate for the low value added hospitality sector. Such a policy has very significant fiscal and opportunity costs and will do nothing to improve the long-run well-being of the economy or its citizens and will provide negligible employment growth in what will inevitably be low paid jobs. This is particularly true when the economy is already close to full employment. The fiscal resources are much better used elsewhere - whether the goal is employment in good jobs, productivity, poverty reduction, or even just better fiscal resilience. We can give examples in each area. Not only do policies such as the VAT cut carry fiscal and other opportunity costs, but they are also likely to be counterproductive in the long-run by pushing the economy in a lower value added direction therefore producing slower growth in the long-run.

To be clear we are not against government support for business. We simply believe it should be done in the context of achieving long-term strategic targets. There are many targeted areas where appropriate government intervention could potentially enhance the long-run productive capacity of the economy via supports for enterprise. Three crucial ones are:

1. Policies that increase the economy-wide rate of generation of high potential start-ups (HPSUs) and/or raise equity finance for HPSUs
2. Policies that incentivise private research, development and innovation
3. Policies that attract and retain human capital and diffuse technology more broadly

Department's Action Plan on Competitiveness and Productivity

We should make a quick comment on the *Department's Action Plan on Competiveness and Productivity.* This is broadly a step in the right direction. We note that the very first priority action is to increase expenditure on research activity in the Higher Education sector. This sets a good framing and tone for the overall approach. We need to strengthen our innovative and productive capacities and as such the thematic focuses on innovation and indeed infrastructure are particularly welcome. We do however have concerns about certain priorities such as the ‘SME test’ and the ‘red tape challenge’. We are happy to elaborate upon these concerns in the discussion. We also note with interest Action 24 on the potential of social partners to drive productivity and Action 59 on the development of an action plan on collective bargaining. Collective bargaining has an important role in nurturing horizontal innovation in the economy.

A Productivity Strategy - Policy Proposals

A high-level checklist of appropriate policy reforms to enhance our innovation system might include:

(1) Allocating higher levels of per capita spending on public R&D and providing generous subsidies and tax breaks for private research;

(2) Creating a safety net for entrepreneurship and risk-taking including via social insurance reforms and lenient bankruptcy laws;

(3) Establishing attractive career paths for STEM workers and for other researchers particularly at PhD level and beyond;

(4) Providing fiscal supports for ICT adoption and financial and other supports that encourage the life-long re-or-up-skilling of workers and managers more generally;

(5) Improving infrastructure especially in technologies that facilitate communication and learning such as broadband and artificial intelligence (AI);

(6) Enacting patent reform at EU and UK levels to prevent the monopolisation or mothballing of technologies;

(7) Building out an entrepreneurial state in which the state takes a leading and activist innovation and entrepreneurship role as proposed for example by Mazzucato;

(8) Encouraging inward migration in order to bring in a flow of new skills, new ideas and new perspectives into the economy;

(9) Promoting horizontal innovations from within organisations by encouraging a greater degree of employee voice and autonomy, more active learning by doing, and better communication of internal expertise, and

(10) Ensuring greater economic and social inclusivity including the elimination of child poverty and the other barriers that prevent individuals fully participating and flourishing in the economy. Greater inclusivity allows everyone to potentially contribute to or exploit the sum of knowledge in the economy.

This is what a high road enterprise strategy looks like.

We are happy to take any questions.

Ends.