

**DON'T TURN A RECESSION INTO
A DEPRESSION!**

**THE ROLES OF BOTH CONSUMPTION
AND INVESTMENT IN ENSURING
ECONOMIC RECOVERY**



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INTRODUCTION

It is remarkable how in the space of little more than a month a sense of proportion proposed in one ESRI publication can be totally destabilised by media overreaction to another. The ESRI itself can be absolved from most of the blame for this. Commentators have failed to take account of the fact that, whereas the ESRI Quarterly Economic Commentary of June 23 did forecast a downturn in national output for this year, it also forecast a resumption of growth next year and had very sensible observations to make on the National Development Plan, the need to prioritise investment in training and upskilling and the need to retain a sense of perspective about the overall health of the public finances, showing that a breach in the 3 percent borrowing ceiling of the Stability and Growth Pact for 2009 would not have the negative consequences that might apply in other economies. Far too often the “Growth” component of that pact is forgotten, together with the necessity for fiscal policy to sustain that objective. It is also necessary to recall what might all too easily be lost sight of in the hype of over-reactive commentary, that when the ESRI published its Medium-Term Review on May 14, it carried the following statement:

“Our essential message in this *Review* is upbeat, recognising that there is a danger that Irish society could be transfixed by the current very real difficulties, missing the opportunity to plan and prepare for a better future in the next decade.”

This is not to say that all is well with the ESRI’s own analysis. We believe that the ESRI, in common with the general body of economic forecasters, has seriously underestimated the extent to which the current high rate of inflation is likely to persist well into 2009. And we know that, in common with the general body of economic commentators, the ESRI has also seriously misread the extent to which earnings increases were already falling behind rising inflation last year. It is our view that such existing facts of life regarding declining living standards should require a reassessment not only by Government but also by the ESRI itself of its projections for the introduction of a carbon tax as early as 2010.

In the following pages SIPTU’s Head of Research Manus O’Riordan argues for the placing of the public finances issue in perspective, for more realistic projections on inflation, and for a full realisation of the facts concerning earnings developments to date. The competitiveness of labour costs to meet the export challenge that is required to ride out the current

economic difficulties is also assessed. But no less important is the role that the restoration of living standards needs to play in ensuring that not alone is a collapse in private consumption prevented, but also that this key component of domestic demand is enabled to make its much-needed contribution to a recovery in overall growth next year. A statistical appendix provides further details.

Researcher Marie Sherlock addresses the need to ensure that the National Development Plan provides significant public investment to offset as much as possible of the downturn in private investment, and that investment in training and upskilling will be accorded top priority.

Researcher Loraine Mulligan addresses trade union concerns on energy and climate change, with particular reference to the issue of fuel poverty.

KEEPING OUR HEADS ON BORROWING

The ESRI Quarterly Economic Commentary does indeed seriously address the implications of the current economic slow-down and its impact on Government revenues, which will be significantly lower this year and the next than had been originally envisaged. It forecasts that the General Government Balance as a percentage of GDP will move from a 3.0 percent surplus in 2006 (while just breaking even at 0.3 percent in 2007) to a deficit of 2.8 percent in 2008 and an even larger deficit of 3.9 percent in 2009. The ESRI concedes that this means that Irish public finances will only just about conform to the 3 percent EU Stability and Growth Pact guidelines during the current year and will apparently be in breach of them next year. But it correctly keeps its head as it takes note of the fact that these guidelines can be temporarily breached in order to arrest recessionary developments, arising from exceptional circumstances, which is precisely what is involved in the case of the drastic downturn in house building activity in the Irish economy. In other words, the ESRI perspective is to turn around a GDP/GNP downturn of 0.4 percent in 2008 so as to enable growth of 2 percent to resume in 2009. Were this not to occur, the unemployment prognosis would be far worse than forecast by the ESRI: a rise in the unemployment rate from last year's 4.5 percent to an average level of 6 percent this year, and one of 7.1 percent next year (or even as high as 8 percent, in the absence of net emigration).

Corresponding to this increased borrowing, of course, is an increase in the Gross Debt/GDP ratio, from a little above 25 percent in both 2006 and 2007, to 29.8 percent in 2008 and 34.5 percent in 2009. The ESRI rightly introduces a sense of perspective in this regard, by factoring in both the National Pension Fund and the Social Insurance Fund. On this score, Ireland's Net Debt/GDP ratio is less than half the Gross, rising from 12.1 percent in 2007 to just 13.9 percent in 2008 and 16.1 percent in 2009. Other economies do not have the savings required for such a reduced Net Debt ratio, quite apart from the fact that even Ireland's temporarily increasing Gross Debt ratio is itself significantly below the Euro area average of 65 percent. (See appendix for Table 1). We therefore take issue with those who would criticise the ESRI's assessment in this regard.

ARE OUR LABOUR COSTS COMPETITIVE?

With investment falling, consumption about to do so and public expenditure being squeezed, the one significant demand contribution to Irish growth is that of exports. True, there will be no repeat of last year's 8.2 percent surge in volume. But a 4.8 percent increase this year and one of 4.4 percent next year are indeed significant. While service exports have been to the fore, goods exports will also hold their own in value this year and increase by 1 percent next year, while the ESRI forecasts for the actual volume increases in good exports are 2.6 percent this year and 2 percent in 2009. This is all the more impressive a performance in the light of more depressed foreign markets and the weakening of both the dollar and sterling against the euro.

Table 2 in the statistical appendix show the remarkable improvement in Ireland's relative unit wage costs between 1990 and 2003. There was a small reversal of that progress during the following two years. Over the last two years, however, relative wage costs competitiveness has resumed its improvement in national currency terms, although this is being marginally offset in the current year as common currency calculations take account of the adverse exchange rate developments already mentioned.

The April Quarterly Bulletin of the Central Bank has observed:

“While unit labour costs levels are broadly on a par with the EU-15 average, high non-labour cost increases relative to those of our major trading partners also continue to put downward pressure on our international cost competitiveness position ... Unit labour costs in Irish manufacturing relative to main trading partners, expressed in common currency, have been steady in recent years, as adverse exchange rate movements have been in the main offset by productivity increases in manufacturing that, albeit subdued compared with those increases registered in the late 1990s, nonetheless surpass productivity increase in our main trading partners. Since foreign-owned firms import over 86 percent of the materials used in production and export 94 percent on their total output, the negative effects of the recent appreciation of the euro on foreign multinationals margins and competitiveness may be somewhat overstated. Nevertheless, recent relatively high increases in non-labour costs, such as those related to property (purchased or

rented), utilities, waste management, etc., are likely to weigh on the cost competitiveness of Irish manufacturing.”

That rising labour costs have not been aggravating the competitiveness of Irish manufacturing is also evident from OECD data released last month. Ranking the year-on-year changes in industry’s unit labour costs for December 2007, Ireland was in the fourth most favourable position of the twenty OECD economies for which data was available (See Table 3).

But what about labour cost competitiveness for the economy as a whole? The Central Bank states:

“Relative unit labour costs were rising from probably unsustainably low levels at the start of the decade and are now broadly on a par with the average for the EU-15.”

But this is to exaggerate Irish hourly labour costs. Eurostat data for 12 out of the EU-15 countries for whom data is available shows that in the fourth quarter of 2007 Irish hourly labour costs amounted to only 89 percent of that EU-12 average and ranked as low as tenth out of the twelve. Ireland’s hourly labour costs were only 69 percent of Sweden’s, 78 percent of France’s, 80 percent of Germany’s and 81 percent of the UK’s. (See Table 4).

But if Irish wages have not been rising fast enough to threaten export competitiveness, have they been rising fast enough to sustain domestic consumer demand?

WHAT HAS BEEN HAPPENING EARNINGS?

The release of the March Consumer Price Index data also coincided with the end of the last pay agreement in respect of early starters. So the increase in the CPI in the 27 months since the end of “Sustaining Progress” in December 2005 could now be compared with the total pay increases of 10.38 percent over the full 27 months of the “Towards 2016” pay agreement.

Between December 2005 and March 2008 the CPI increased by as much as 11.7 percent. If we take a December 2005 Index as = 100 in respect of both wage rates and consumer prices, the March 2008 pre-tax wage rate index of 110.38 must be deflated by a corresponding price index of 111.7 in order to give us a real value wage rate index of 98.8 – a fall of 1.2 percent in the real value of the wage rate from that December 2005 starting point.

Budgetary tax changes did add somewhat further to take-home pay. So, again taking December 2005 as Index = 100, for the full 27 months of the agreement the take-home pay index in money terms of 112.8 percent for March 2008 must be deflated by the price index of 111.7 in order to give us a real value take-home pay index of 101.0 – a negligible increase of only 1.0 percent. **IN OTHER WORDS, LIVING STANDARDS REMAINED ESSENTIALLY FROZEN AT THE SAME LEVEL BY THE END OF THE PAY AGREEMENT AS WHEN IT COMMENCED.**

That overall outcome for the full 27 months of the pay agreement masks **the actual decline in the real value of earnings that took place during the course of last year** – even for those who received the full terms of that pay agreement, not to mind those workers who did not have access to its terms. “Freeze Wages to Reign In Stagflation” was the shrill Business Analysis headline trumpeted in the Irish edition of the “Sunday Times” of June 22, as it ignored the fact that the real value of wages have not only been frozen but have been declining across the board. While expressed in more sober terms, two successive editorials in the “Irish Times” have hardly been much better informed. The “Hard Landing” editorial of June 14 spoke of “increases in average wages and salaries barely keeping pace with rising prices”, when they haven’t been keeping pace at all. The “Reality of a Recession” editorial of June 24 proclaimed that “the central reality is that living standards cannot continue to grow in the short-run”, when the actual reality is that living standards have been actually falling and the challenge facing us is to prevent them falling still further.

The most recently published CSO data on earnings, released on June 23, are also the least reliable as to their representative character, namely, those for construction earnings in the year to March 2008. “6.4 percent increase in average weekly earnings” is the sub-heading, ignoring the fact that this series only covers directly employed workers, and provides no data whatsoever in respect of those working for sub-contractors. But even here the average weekly earnings increase of 4.4 percent for skilled operatives is dependent on an extra hour being worked, as average hourly earnings only increased by 2.5 percent, or half the corresponding 5.0 percent rate of inflation. Average hourly earnings for unskilled operatives increase at 5.1 percent may appear to have matched inflation. But the extra working time required to bring the increase in average weekly earnings to 6.9 percent only highlights the unrepresentative character of this series, considering that for the same month of March the Index of Employment in Construction showed a year-on-year decrease of 13.8 percent.

The ESRI Quarterly Economic Commentary states:

“The most recent data on earnings that are available from the CSO relate to the last quarter of 2007. Hence they are somewhat dated. They show hourly earnings growing by 5.7 percent on an annual basis on average in construction and weekly earnings growing by 4 percent, 4.1 percent and 4.4 percent in distribution, business services and the public sector (excluding health) respectively. From those figures, we can conclude that earnings continued to grow at a healthy pace in 2007 and our belief is that economy wide earnings will be shown to have grown by 5.5 percent when the national accounts for the year are released”.

This is in fact an unwarranted conclusion based on a very careless, and strikingly defective, reading of earnings statistics released just over four weeks ago in May.

The Consumer Price Index increased by 4.7 percent in the year to December 2007. Yet the CSO data for “Earnings in Distribution and Business Services”, released on May 22, showed that in the year to December 2007 average full-time weekly earnings increased by only 3.4 percent in Distribution and by a mere 2.3 percent in the case of Business Services. In other words, only half the corresponding rate of inflation.

The “Public Sector Employment and Earnings” data, released on May 23, also showed an overall increase of just 3.6 percent in average weekly earnings in the year to December 2007. Even the pay of civil servants alone, increasing by just 4.0 percent, failed to match inflation. But pay in Semi-State companies, increasing by a mere 0.8 percent, actually represented a decline in such workers’ living standards, of the order of 4 percent.

It is, however, particularly inexplicable that the ESRI made no mention whatsoever of the “Earnings and Labour Costs” data released by the CSO on May 21 in respect of the fourth quarter of 2007, during which period the annual rate of inflation averaged 4.8 percent. The fact that aggregate data shows that over the same period average hourly earnings also increased by 4.8 percent - and that this already amounted to an overall real wage freeze – does not, however, lend substance to the IBEC contention in the “Irish Times” on June 25 that “the rise in unemployment is already prompting a greater degree of wage restraint in the private sector through market forces”. Before returning to the detailed breakdown by occupation in respect of manufacturing itself, we will first look at how this **supposed wage restraint is playing out in another private sector – that of **financial mediation**. True, average hourly earnings for **manual workers** only increased by **3.3 percent**, and those for **clerical workers** actually **fell by 0.4 percent**, but **managers and professionals** at the top of the pile actually saw their earnings **shoot ahead by 8.6 percent**. **What was sauce for the goose was certainly not sauce for the gander!****

Turning again to the manufacturing sector, the overwhelming majority of unionised workers received their full pay entitlements under “Towards 2016”. But the increasing substitution of underpaid foreign national workers for Irish workers, a host of them on temporary agency contracts, has undermined the overall earnings performance of manual workers in the manufacturing sector as a whole. Accordingly, while average hourly earnings for clerical and sales staff increased by 5.0 percent, and managerial and professional earnings by 5.1 percent, the average increase in manual workers’ earnings was only half of that, at just 2.5 percent. (See Table 5).

We now refer back to the data for Distribution and Business Services, where the average earnings increase was limited to 2.7 percent overall. Within that overall figure, two of the worst performing sub-sectors were the wholesale trade, where average earnings increased by only 0.7 percent, and land transport, where they actually fell by 0.3 percent. As the

Quarterly National Household Survey has shown, in the year ending the first quarter of 2008 a decline of 1,000 Irish nationals employed in transport storage and communication was offset by an increase of 1,300 foreign nationals. There were 1,400 fewer Irish nationals employed in the wholesale and retail trade, against an increase of 22,500 foreign nationals.

The beginnings of the recession in the construction sector did see a reduction of 1,700 foreign nationals employed, but a much sharper fall of 8,100 in the number of Irish nationals at work in that sector. (The decline in the total number of construction employees was more dramatic still, at 16,900, being partly substituted for by an increase of 7,100 in those classified as self-employed).

But the most numerically significant sectoral decline in the employment of Irish nationals was in the manufacturing sector, which saw their numbers reduced by 10,000, while the employment of foreign nationals increased by 2,500. It is in order to ensure that the underpayment of such workers does not accelerate a race to the bottom that SIPTU is so insistent on domestic legislation being enacted in order to give effect to the collective bargaining rights provided for under the EU Charter of Fundamental Rights, and why it also insists on speedy implementation of the Temporary Workers' Directive so as to ensure that agency workers receive full parity of pay with permanent employees doing the same work.

The ESRI's overestimation of earnings developments to date has led it to underestimate the role of an actual decline in the real value of wages during 2007, thereby failing to recognise it as being the most significant causal factor in rolling back consumer expenditure. Against that background, the ESRI's further underestimation of the rate of consumer price inflation in the year ahead also leads to an inadequate understanding of the important role required of such consumer expenditure in order to ensure a resumption of economic growth.

WHAT IS HAPPENING CONSUMER PRICES?

There was nothing more irresponsible in the present Taoiseach's approach to the challenge of inflation than his Budget 2008 Financial Statement when, as the then Minister for Finance, he repeated for the second year running his loose definition of inflation. Nowhere in his address to the Dáil did he once refer to the Consumer Price Index. Yet this remains the one measure of inflation that has been agreed upon by all parties in Ireland, a CPI rate of inflation that averaged 4.9 percent for 2007. The only Irish inflation forecast that the Minister was willing to give for 2008 was that for the EU-based Harmonised Index of Consumer Prices which, of course, conveniently excludes mortgage interest payments. The present Taoiseach's forecast was that this Irish HICP could average 2.4 percent in 2008. But that was equivalent to saying that inflation as measured by the Consumer Price Index would still be averaging 3.3 percent next year, even if the Minister wasn't prepared to admit as much. As it happened, Taoiseach Brian Cowen's Budget Speech of December 5 underestimated the increase in Irish HICP itself, quite apart from his total silence on the even faster rising CPI.

In fairness to the Central Bank of Ireland, it has never sought to define the CPI out of existence. But it has been among those underestimating its rate of increase. As recently as its April Quarterly Bulletin its inflation forecasts for this year were for the HICP to average 2.9 percent and the CPI 3.2 percent, while its forecasts for 2009 were for a HICP increase of 2.2 percent and a CPI one of 1.6 percent.

Apart from the overall degree of underestimation, one thing to note here is that this prognosis for a lower rate of CPI inflation in 2009 than that of the HICP was based on the Irish Central Bank's assumption that the European Central Bank would continue to cut interest rates still further. We now know that the opposite will in fact be the case.

So much has changed in the short space of only two months that the ESRI's June forecasts for inflation are very different than those of the Central Bank in April. The ESRI forecasts an average rise in the HICP this year amounting to 3.5 percent, with a corresponding CPI increase of 4.5 percent. As for next year, it forecasts that the HICP and the CPI will increase by 2.7 percent and 3.0 percent respectively.

It is, of course, the acceleration in fuel and food price inflation during the course of 2008 that has led to such revisions in forecasts. There

has also been the phenomenon of profiteering, where the reduction in the euro equivalent costs of goods sourced in the weakening sterling area have not been passed on to the consumer. As a survey released by the National Consumer Agency on June 18 revealed, after accounting for exchange rate differences, the prices faced by customers of Dunnes Stores and Tesco for own brand products were higher in the Republic than those in Northern Ireland by as much as 11 percent and 17 percent respectively. The comparisons were much worse still when it came to branded products, where the differences were 31 percent and 28 percent respectively.

The ESRI takes some account of such phenomena, but only to the following extent:

“Consumer price developments so far this year are not reflecting the recent appreciation of the euro to the same extent as in the past. While further analysis is required, (the ESRI’s own) preliminary finding indicates that the deflationary benefits of a strengthening currency, small though they may be, are currently not being fully passed on to Irish consumers to the same degree as might be expected”.

Such a confession of utter helplessness is the very opposite of policy advice. And the “let the market deal with it” *laissez-faire* approach of the Government amounts to a confession of utter bankruptcy when it comes to the challenge of devising an effective anti-inflationary strategy that would call a halt to such profiteering.

Quite apart from this, even though the ESRI’s inflation forecasts are higher than those of some previous forecasters, one must be concerned that a serious underestimation is involved, even on the part of the ESRI. Previous hopes that rising fuel and food costs would be at least partially offset by further interest rate reductions must now go out the window. The CPI was last affected by the application of a European Central Bank interest rate increase in July 2007, and that particular increase will cease to have an upward effect on the index by this July. But this amelioration will be reversed when the ECB again raises interest rates next month, to adversely impact on the August index. To be fair to the ESRI, it does note that particular change in circumstances.

But when we come to assessing future prospects for consumer price inflation, it should also be realised that at present gas prices are 8.3 percent lower than they were a year ago, and electricity prices are 5.4 percent lower. Consequently, their combined effect is in fact holding the

CPI rate of increase 0.1 to 0.2 percentage points below what it might otherwise be. When these lower prices not only drop out of the system but are actually replaced by significant price increases, such re-emerging adverse developments will have to be further factored into the system. If Bord Gáis succeeds in securing approval for a 17 to 19 percent price increase, this would see an addition of 0.2 percentage points to the CPI from October. And if the ESB also secures a 30 percent price increase, this would see a further 0.5 percentage points being added onto the CPI from January.

For these reasons, we believe that the CPI will average closer to 5 percent for the whole of 2008 than the 4.5 percent forecast by the ESRI. We do not believe that the CPI will dip below 4.5 percent until the latter half of 2009. Average inflation for 2009 as whole is therefore more likely to be above 3.5 percent than the 3.0 percent currently being forecast by the ESRI.

Such inflationary developments have serious implications for the ESRI's consumption forecasts. The ESRI has monitored existing consumer expenditure patterns better than most other commentators. And it does indeed forecast at least one quarter of falling consumption during the course of this year. The end result is that it is only due to a carryover effect from last year that it forecasts a 1 percent increase in the volume of consumption for 2008 as a whole.

But is even this too optimistic a prognosis? The volume of retail sales, excluding motor trades, averaged increases of 6.7 percent and 5.5 percent, respectively, in 2006 and 2007. But the month-by-month year-on-year rate of increase was already declining rapidly from October onwards before turning into a negative in April:

| | Month | % Change |
|------|----------|----------|
| 2007 | October | +4.6 |
| | November | +4.1 |
| | December | +3.9 |
| 2008 | January | +3.0 |
| | February | +2.2 |
| | March | +1.3 |
| | April | -2.9 |

As we have already observed, the ESRI has failed to grasp that real earnings in both the private and public sectors were actually falling during the course of 2007, so that it was not just a question of

consumer confidence, but the far more serious phenomenon of Irish workers' actual inability to pay, that has resulted in such a retail sales setback. The ESRI has forecast a modest return to a 2 percent growth in the volume of consumption for 2009. But if the ESRI has in turn underestimated the rate of consumer price increase for 2009, and has not adequately factored in the rate of wage increase required to ensure that there will in fact be a recovery from the decline in living standards that is not only occurring at present but has been underway since last year, its forecast of a modest consumption recovery will not at all be forthcoming. And yet such a recovery in the volume of consumption is essential for making its contribution to the domestic demand required for overall economic growth to resume in 2009.

The Government must do nothing in 2010 that would choke off the resumption of economic growth. We note that the ESRI Medium-Term Review envisages Budget 2010 increasing the personal income tax burden by 1 percent, while simultaneously introducing a carbon tax with an associated increase in consumer prices of 1 percent. Quite apart from workers being resistant to a further erosion of their living standards from such a double hit, the resulting negative effects on consumption would have detrimental consequences for a recovery of economic growth. Whatever national debate has yet to be concluded on the pros and cons of a carbon tax, 2010 would most certainly not be the appropriate year for any such initiative.

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COMMITTING TO NEW INVESTMENT CHALLENGES

Faced with a drastic fall off in tax revenues, there will be an inevitable temptation, in present times, to cut or postpone what might be perceived as non essential expenditure. If recent reports are anything to go by, a review of all capital projects will be conducted in future weeks.

In seeking to contain the fiscal difficulties that the country now finds itself in, the worst mistake this present Government could make would be to scale back investment in those very areas that are crucial to the long term sustainable growth of the Irish economy.

This means that sufficient funding must be maintained to invest in both the Irish labour market's own workforce and in the physical infrastructure that would ensure the smooth functioning of the economy.

Policy focus must not be blinkered by fiscal containment:

For 10 out of the past 11 years, Irish Governments recorded a general government surplus which allowed capital spending to be funded out of current revenues.

✚ **The need to borrow now seems to be accepted, but the mistakes of 2002 and 2003 should not be repeated,** when a temporary government deficit in 2002 sparked a series of panic cut backs, many of which had a minimal impact on the total government spending but had an adverse effect on those on low incomes. While issues relating to planning were at play in delaying the roll out of certain projects, the fact remains that the funding allocated to public capital expenditure was under-spent for each year between 2002 and 2005.

✚ These infrastructural deficiencies remain, and with GDP forecast by the ESRI to fall by 0.4% in 2008, more doubt will now be cast on the ability to deliver the commitments under the National Development Plan. Clearly, GDP for 2008 and 2009 will fall far below the 4- 4.5% annual average economic growth assumptions of the NDP, but as the ESRI forecasts show, the downturn in investment will be the principle drag on overall economic growth. While volatile fuel prices, a weakened dollar and a global economic slowdown have already adversely affected the traded sectors in Ireland, their overall strength highlights the fact that the **Irish economic downturn is not being felt evenly across sectors.**

- # Notwithstanding the spillover effects of the construction downturn on related services and manufacturing industries, income tax revenues have remained remarkably resilient, demonstrating that the economy is not in freefall. **Comparisons with the 1980s overstate Ireland's economic weakness and fail to acknowledge the sound economic structure of the Irish economy.**
- # **This downturn must be seen as an adjustment phase, shifting from an unsustainably high dependence on construction for employment growth and tax revenues towards a more services oriented economy.** In that context, we cannot afford to be blinkered by what we anticipate will be a short term downturn. Accordingly, the Government's structural policies must maintain some element of independence from the current economic cycle.

Prospects for the Construction Sector

With a 50% increase in planning permissions for non residential projects approved in 2007, there was some hope that other areas of construction would offset the downturn in new house building and absorb some of the lay-offs in the residential sector.

- # However, it now appears **that the downturn is beginning to bite in other areas of that sector**, with the Ulster Bank's Purchasing Managers Index recording accelerating declines in both commercial and civil construction activity since December 2007, albeit at a slower pace of decrease than housing. Similarly, with consumer confidence at its lowest level in well over a decade, it is **difficult to envisage the scale of the upturn in demand for repair and maintenance activity that had been originally forecast.**
- # Just as the boom in residential construction continued longer into 2007 than was expected, the contraction in house building activity at the turn of this year was sharper and swifter than was forecast. **Housing completions now look like being little more than 43,000 in 2008.**
- # Greater uncertainty surrounds forecasts for 2009, **but we would take the view that any pick up in the rate of housing starts is unlikely for the rest of the year. This makes some of the completions predictions of 30,000 or more in 2009 seem unrealistic.** Large volumes of unsold stock will curb further supply, while a continual decline in house prices, along with deteriorating affordability, should

ensure that demand remains flat. Home bond registration data, along with estimates for one-off housing during the first five months of 2008, shows that work began on between 8000 and 9000 housing units across the country. If we assume that these housing units take between 9 and 12 months to be completed, then even the Davy's forecast for 25,000 housing units to be completed in 2009 now appears somewhat optimistic.

- ✚ Overall, this paints a bleak picture for construction workers, for whom the rate of job losses has so far been slower than the pace of decline in construction activity. Already, over 13% of construction workers in firms of 5 or more staff have been let go and there is still some distance to travel if the Fás forecast of 67,000 jobs losses from the time of the peak of the sector, is to come to fruition.
- ✚ At firm level, there is anecdotal evidence of **site specific redundancies**, where workers are laid off upon completion of a site. **New cost saving recruitment methods have been emerging**, where groups of tradespersons are recruited together, with the knock-on effect of **squeezing individual craftworkers**.
- ✚ There is some evidence to suggest that even these **figures understate the true rate of job loss in the sector**. Although the data are slightly out of date now, construction employment figures for the 12 months to February 2008 highlighted a net loss of 9,800 jobs in the sector, but this masked an even greater loss of 16,900 employees in construction. This fall was partially offset by an **increase of 7,100 self employed persons in the sector, which might point to a gradual shift by some workers into the repair and maintenance sector**.
- ✚ More significantly, a fall of 1,700 workers from the EU new member states in the construction sector was recorded in Q1 2008, at a time where the number of migrant workers in the Irish Labour Market reached an all time high. Given the problems with the registration of workers by firms, together with the phenomenon of bogus self-employment, **there is reason to believe an even greater number of non Irish workers may have been exiting the sector**.

Investing in Ireland's infrastructure

At a time where increasingly congested public facilities negatively impact on the economy's productivity and impose additional costs on private sector activity, investment in Ireland's infrastructure is more important

than ever before. Already we see that Government departments with very large capital expenditure budgets - in areas such as transport, communications, marine and natural resources, environment heritage and local government - have together spent only one third of their annual budget allocation in the first 5 months of 2008.

✚ Amidst the bleak prospects foretold in the ESRI's most recent Quarterly Economic Commentary, there is a welcome support for the maintenance of the capital investment programme. **That all capital projects must be justified on the grounds of Cost Benefit Analysis is a call that we would share, but a note of caution must also be sounded.** It would be a mistake to reject projects on the basis that they do not provide adequate rate of return in less populated, less prosperous areas. The last thing that is presently needed is to devise purely reactive policies to what is anticipated to be a short term downturn, which effectively would concentrate capital investment around the Greater Dublin Area to the detriment of other regional infrastructural needs.

Investing in Ireland's Labour Force -Opportune timing to invest in workers' skills amidst increasing unemployment

With the sudden jump in claimants to over 200,000 on the Live Register, there is a major challenge for the Government to speedily address the skills needs of these persons. There is a **danger now that attitudes toward the labour force will focus on the costs as opposed to the investment in the labour supply**, as increased numbers claiming unemployment benefit impose greater pressure on social welfare expenditures.

Instead, investment in skills enhancement and training is more crucial now than in a period of buoyant employment growth, in order **to prevent redundant workers effectively becoming long term unemployed**. Just as importantly, upskilling and training within the current workforce is vital **if workplace productivity is to be increased and workers own employability and adaptability is enhanced**.

✚ Notwithstanding the net number of jobs created across the regions in recent years, a **serious skills mismatch at a regional level** will now become even more apparent, **with a wide gap in skills between those who have been made redundant from traditional manufacturing and construction industries and the skills demanded by the job generating sectors of wholesale, retail and services**. While, 97,500

jobs were created in the financial and business services and wholesale and retail sectors between the last quarter of 2004 and the last quarter of 2007, these do not easily substitute for the losses of 11,900 in manufacturing.

✚ With particular regard to **construction, the impact of the boom on employment was more a regional phenomena than a nation wide trend, to such an extent that close to one-quarter of all men in counties such as Wexford, Mayo, Donegal and Co. Galway were employed in the construction sector.** The reduced capacity of the construction sector to absorb rural workers presents a distinct regional problem, with serious implications for persons directly employed and the wider indirect multiplier benefits to the local area. Workers made redundant from traditional manufacturing industries face even greater problems of job and location mobility with **little or no alternative, appropriate and decently paid sources of comparable employment available in their counties.**

✚ For those made redundant, **there is a real danger that the longer they remain out of the workforce, their skills will depreciate over time- the so called “hysteresis” effect.** This is particularly the case for manufacturing workers who may have spent a long number of years in the one firm using a very specific skillset. **This is compounded by lower than average levels of educational attainment,** where over one quarter of those employed in industrial production in 2006 had an education level no higher than the Junior Certificate. In the Construction sector, this statistic rises to 38%, raising serious concerns in respect of literacy, (both reading and writing) not to mention the ability to use a computer or digital device.

✚ **The challenge now facing us is to put in place a series of legislative, financial and career guidance mechanisms** to address the skills deficiencies and improve worker’s abilities to compete for new jobs and adapt to new work processes.

✚ A question mark must be placed over the current Government’s enterprise and education strategy which seems to have accorded a definite priority to the development of the fourth level and research and development within Irish universities, arguably at a cost to the traditional teaching role of Irish third level institutions. A distinction must be made between policies for developing the “creative economy”, populated by few and focused on product creation, as opposed to a more broad based “knowledge economy”. To put this in

context, the National Development Plan forecasts that by 2010, 62% of all net jobs created will require a third level qualification, yet at the time of the census in 2006, some 64% of the working age population only had an education up to the Leaving Certificate.

- ✚ **For the 92.5% of Irish persons aged between 25-64 years, who did not engage in some form of lifelong learning in 2006, the issue of information, skills identification and course targeting along with a range incentives** must be considered if the number of persons who have some form of contact with the upskilling or training systems is to increase. The National Skills Strategy mooted two types of mechanism (i) Individual learning accounts and (ii) paid learning leave. The Expert Group on Future Skills Needs is due to produce feasibility studies of these, sometime this year. While acknowledging that there are ongoing pilot projects in respect of both of these initiatives, there is a concern that if introduced, they will only ever emerge in a limited application. A comprehensive system of statutory paid learning leave and individual learning accounts must be instituted if workers are to be empowered to take responsibility for their own upskilling.
- ✚ **For those workers with a Leaving Certificate qualification who wish to return to the classroom** and enter third level education, the commitment made under Towards 2106 for the alleviation of fees for part time third level courses for those who had not attended before, must be addressed. To date, progress has paltry with only one course in Institute of Technology in Tallaght funded under this initiative. Implementation must be accelerated and due consideration by the HEA must be given to a broad range of courses. There is a concern that this initiative will be limited to a small number of courses which might be perceived as having a high economic value.
- ✚ **For those wishing to take up part time third level courses**, the issue of fees must be addressed. Ten years after the Green Paper on Adult Education acknowledged the inequity of the fee structure for part time courses. It is now time to give parity of treatment to part time students and equalise the fees charged for full and part time courses.
- ✚ **For the young school leaver**, whose only work experience is with his hands as a labourer, there is a real danger that young men with no more than the Leaving Certificate qualification who spent some years working as construction labourers could well fall through the net during this period of lay-offs. Having been too long out of school to have the confidence to return to formal education and having become

too dependent on the regular income flow to be able to become a full time student again, specific targeting is essential to ensure their range of alternatives are explored. Census 2006 tells us that one in every four young men in the labour force aged 20-24 years were working in construction in 2005 and that of these, a quarter of the men had an education level no higher than the Junior Certificate Over the long term, a dual system of formal academic skilling and on-the-job training must be considered as the way forward to address these issues.

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TRADE UNION CONCERNS ON ENERGY AND CLIMATE CHANGE

One of the main drivers of the CPI is fuel prices. Recent alarming increases in the cost of oil are well known, with the rate currently approaching \$140 per barrel. Moreover, a new report from Sustainable Energy Ireland reveals that, from June 2000 to January 2008, household electricity prices doubled (99% increase). In this context, we are mindful that the issue of fuel poverty arises as a cause for concern.

The SEI report estimates that 1,441,720 homes in 2005 were in a situation of fuel poverty whereby spending on adequate heating and energy accounted for more than 10% of net income. However, the figure may not tell the full picture across the range of income distribution groups. In any event, the situation for many has hardly improved since 2005, given the rising trajectory of fuel prices in the meantime. Low income families spend a larger proportion of earnings on fuel costs than people in higher income brackets. It must be a priority to ease the burden on vulnerable groups such as those with modest incomes, older people and lone parents and to guard against possible negative health consequences. At €18 per week the current weekly fuel allowance is evidently not enough to address the situation of thousands of fuel poor, especially in the light of further expected gas and electricity price increases.

Other state supports aimed at alleviating energy needs – such as the Local Authority Central Heating and Insulation Programme and the Warmer Homes Scheme – are scattered throughout various departments, making them difficult to identify and complex to administer. The SEI report confirms the necessity of improving the energy efficiency of Irish homes, as benchmarked against other EU Member States. Minimizing energy loss is important in tackling fuel poverty over the medium- to –long term. In this regard, low income families in particular require adequate grant aid to upgrade boilers, lighting, heaters etc. We are of the view that more targeted funding is required along with an integrated and consolidated approach to fuel payments and assistance in order to effectively assist those most in need.

It would be unhelpful to aggravate the difficulties that many households are experiencing in relation to fuel costs through the introduction of a carbon tax at this particular juncture. Fuel costs are already prohibitive for many working families and provide ample motivation to reduce wastage in the short term. Imposing a carbon tax risks depressing

consumer confidence and feeding into inflation before the economy has a chance to emerge from the current period of difficulty. Whatever the arguments for and against a carbon tax, the ESRI's suggested timing of 2010 is inopportune.

In the absence of viable alternatives, people cannot in practice change their living patterns without simply incurring unsustainable expense. If Irish people are to have a realistic prospect of making environmentally-friendly choices, infrastructure and social shortfalls must be addressed. Reliance on cars is fuelled to a large degree by a lack of accessible public transport. Funds should therefore be focused on delivering and expanding rail and bus networks.

Moreover, long commuting times increase the carbon footprint of many households. It is crucial to ensure the availability of employment within local areas as well as easy access to schools, sports and recreational facilities within communities. The current necessity for many is to travel to urban centres for work and services. Moreover, the lack of adequate childcare facilities often compels families to drive extra distances for care. Developing an adequate system of childcare would allow households to make choices in their own vicinities. Planning must be centred on such principles if sustainable living is to become a reality.

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STATISTICAL TABLES

TABLE 1**IRELAND'S DEBT/GDP RATIO (%) IN PERSPECTIVE**

| EU Spring 2008 Forecasts | 2007 | 2008 | 2009 |
|---------------------------------|-------------|-------------|-------------|
| Euro area average (13) | 66 | 65 | 64 |
| Belgium | 85 | 82 | 80 |
| Germany | 65 | 63 | 62 |
| Spain | 36 | 35 | 35 |
| France | 64 | 64 | 65 |
| Italy | 104 | 103 | 103 |
| Netherlands | 45 | 42 | 39 |
| Austria | 59 | 58 | 57 |
| Finland | 35 | 32 | 29 |
| EU 27 average | 59 | 59 | 58 |
| Denmark | 26 | 22 | 18 |
| Sweden | 41 | 36 | 34 |
| UK | 44 | 46 | 48 |
| Ireland Gross (ESRI est) | 25 | 30 | 35 |
| Ireland Net (ESRI est) | 12 | 14 | 16 |

TABLE 2**IRELAND'S RELATIVE UNIT WAGE COSTS IN
MANUFACTURING INDUSTRY, COMPARED WITH ITS
MAJOR TRADING PARTNERS**

| Relative Unit Wage Costs | | |
|---------------------------------|----------------------------|----------------------------|
| Year | National Currencies | Common Currency (€) |
| 1990 | 100 | 100 |
| 1991 | 98 | 96 |
| 1992 | 91 | 92 |
| 1993 | 89 | 83 |
| 1994 | 85 | 80 |
| 1995 | 74 | 70 |
| 1996 | 73 | 71 |
| 1997 | 67 | 66 |
| 1998 | 59 | 55 |
| 1999 | 54 | 48 |
| 2000 | 52 | 43 |
| 2001 | 50 | 42 |
| 2002 | 45 | 39 |
| 2003 | 44 | 41 |
| 2004 | 45 | 42 |
| 2005 | 48 | 45 |
| 2006 | 48 | 45 |
| 2007 | 47 | 45 |
| 2008 | 46 | 46 |

Source: Central Bank; 1990 index = 100

TABLE 3**ANNUAL CHANGE IN INDUSTRIAL HOURLY LABOUR COSTS
DECEMBER 2007**

| | |
|--------------------|-------------|
| OECD Area | -0.2 |
| Major Seven | -0.6 |
| Euro Area | -0.7 |
| Norway | +8.9 |
| Denmark | +4.4 |
| Australia | +3.9 |
| Sweden | +3.2 |
| New Zealand | +1.9 |
| Hungary | +1.9 |
| Canada | +1.7 |
| Spain | +0.8 |
| Austria | -0.2 |
| USA | -0.6 |
| Finland | -0.7 |
| France | -0.8 |
| Portugal | -1.4 |
| Czech Republic | -1.6 |
| Germany | -2.1 |
| Japan | -2.9 |
| Ireland | -3.1 |
| Korea | -3.3 |
| Netherlands | -5.2 |
| Slovak Republic | -6.9 |

Source: OECD

TABLE 4**HOURLY LABOUR COSTS, FOURTH QUARTER 2007**

| Country | €per hour | Irish costs as % of |
|----------------|------------------|----------------------------|
| Sweden | 36.84 | 69 |
| Denmark | 33.29 | 76 |
| Luxembourg | 32.78 | 78 |
| France | 32.49 | 78 |
| Germany | 31.63 | 80 |
| UK | 31.52 | 81 |
| Finland | 30.12 | 84 |
| Austria | 29.83 | 85 |
| Netherlands | 26.35 | 96 |
| Ireland | 25.41 | 100 |
| Spain | 20.62 | 123 |
| Portugal | 11.67 | 218 |
| EU 12 | 28.55 | 89 |

Source: Eurostat

TABLE 5**ANNUAL % CHANGE IN AVERAGE HOURLY EARNINGS,
FOURTH QUARTER 2007**

| INDUSTRIAL AND FINANCIAL SECTORS | | | |
|---|----------------------|-------------------------------|------------------|
| Occupational Categories | Manufacturing | Mining & Quarrying | Financial |
| All employees | +4.8 | -0.4 | +6.3 |
| Managers and professionals | +5.1 | +12.5 | +8.6 |
| Clerical, sales and service | +5.0 | +1.8 | -0.4 |
| Production, transport, craft and other manual workers | +2.5 | -0.6 | +3.3 |

**ANNUAL % CHANGE IN AVERAGE WEEKLY EARNINGS,
DECEMBER 2007**

| Annual % Change in Average Weekly Earnings, December 2007 | |
|--|-------------|
| DISTRIBUTION AND BUSINESS SERVICES | |
| Total Distribution and Business | +2.7 |
| Distribution | +3.4 |
| of which: | |
| Wholesale Trade | +0.7 |
| Business Services | +2.3 |
| of which: | |
| Land Transport | - 0.3 |
| PUBLIC SECTOR | |
| Public Sector | +3.6 |
| of which: | |
| Civil Service | +4.0 |
| Semi-State Bodies | +0.8 |

Source: CSO

