Irish Tourist Industry Confederation

Budget 2015 Submission

July 24th 2014

CONTENTS

SUMMARY OF RECOMMENDATIONS

1) After one of the longest periods of recession in decades, the tourism industry is finally emerging into a growth period.

2) Lack of investment in recent years has taken its toll on the quality and variety of the Irish tourism experience, giving rise to concern about the sustainability of the new growth.

3) As a result, ITIC is recommending that Government focus measures in the 2015 Budget on supporting longer-term viability rather than on short-term survival measures. In particular, it recommends focussing on two key areas.

   - Improving the cost competitiveness of the Tourism Industry.
   - Increasing investment in Tourism.

4) Fifteen recommendations in total are made in this submission.

Keep operating costs at a reasonable level for the tourism industry by:

Recommendation 1:	Supporting tourism enterprises in moving towards greener energy sources to combat increasing costs in oil and gas that have been underpinning the rise in electricity costs.
Recommendation 2:	Ensuring no further cost increases in water charges and establish an equitable charging system across the country.
Recommendation 3:	Reducing commercial rates so that they are in line with recent economic developments and there is more transparency in their application.
Recommendation 4:	Ensuring easy and cost-effective access to finance for the tourism industry by considering a venture capital style investment fund for innovative tourism businesses.

Keep labour costs competitive for the tourism industry by:

Recommendation 5:	Raising the entry point to the standard tax rate from €32,800 to €34,800 and reducing the higher rate of tax to 40%.
Recommendation 6:	Dropping the private sector pension levy.

Recommendation 7: Reforming the USC structure to deliver an equal marginal tax rate for self-employed and PAYE workers.

Recommendation 8: Increasing the level of take home pay by adjusting tax and USC rates for lower paid workers, rather than increasing the minimum wage.

Recommendation 9: Continuing to support the competitiveness of the tourism industry and employment in the sector by retaining the 9% V.A.T. rate.

Recommendation 10: Continuing to support the competitiveness of the tourism industry and employment in the sector by reducing the excise rate on alcohol.

Support the ability of Irish tourism to offer a high-quality experience by:

Recommendation 11: Allocating an annual capital budget of €50 million to tourism product development over the period 2016 to 2020 inclusive.

Recommendation 12: Providing a capital budget of €15 million in 2015 to support further development of the Wild Atlantic Way, projects already in train, and those that are ready-to-go.

Recommendation 13: Introducing a special capital allowance of 50% of the cost of new and second-hand touring coaches up to two years old for 2015 and 2016 to enable coach operators to renew their ageing fleets for this growing market.

Recommendation 14: Considering a Public/Private Partnership approach to tourism investment.

Recommendation 15: Supporting the international promotion of Ireland as a tourist destination by increasing the current level of investment in the Tourism Marketing Fund.

1. BACKGROUND

Tourism worldwide has been recognised by the World Economic Forum as a sector which can expand economic opportunity, increase competitiveness, and boost prosperity. Irish tourism has long been, and continues to be, a key component of Ireland's indigenous export sector, contributing over €4 billion to the economy and supporting the employment of almost 200,000 people. Unlike other sectors, it is intrinsically tied to the country and cannot be moved off-shore to where labour, energy or other services might be found more cheaply. It also provides a valuable source of employment and revenue in rural parts of Ireland where other opportunities are scarce.

Like other Irish business sectors, tourism has a high proportion of SMEs. These include Irish-owned, family-run businesses that offer high-quality, personal service which further enhance Ireland's reputation not only as a holiday destination but also as a place in which to do business.

It is also a well-represented sector of the Irish economy. The Irish Tourist Industry Confederation, in existence thirty years, includes members from all the major private and commercial tourism organisations as well as from the principal representative bodies in tourism. It is involved in research, communication, partnership building and providing input to Government on key issues which affect tourism.

The business environment over the last few years has been challenging enough for all sectors but it presented particular challenges for the hospitality industry. Although tourism is now seeing a return to growth, it is not without the loss of some of its original core product – an example of which can be seen in the table summarising changes in accommodation capacity below.

Table 1: Accommodation Capacity 2007, 2008 v. 2013

	Premises			Rooms		
Accommodation Type	**2007**	**2008**	**2013**	**2007**	**2008**	**2013**
Hotels	857	907	835	51,322	57,388	57,362
Guesthouses	387	360	253	4,429	4,221	3,119
B&Bs	2,872	2,680	1,616	11,871	11,337	6,896
Self-Catering - units (group schemes only)	3,673	4,153	3,499	9,985	11,586	0
Hostels	138	135	121	7,922	7,754	8,424
Caravan & Camping - pitch	n.a.	n.a.	93	5,769	n.a.	5,519

Source: Fáilte Ireland

Changes in the hotel sector have been well-documented elsewhere (in the annual Crowe Horwath Hotel Survey, for example) and, although the capacity has increased between 2007, 2008 and 2013, there are deeper issues within this particular sector around debt levels, profitability, imbalanced regional performance and the need to refresh older stock.

However, the real loss in the overall accommodation product is in sectors that were already suffering a decline before the recession. The number of Bed & Breakfasts – once the heart of Irish regional tourism – dropped by 44% between 2007 and 2013, and the number of Guesthouses in operation dropped by over a third (35%). Capacity in caravan & camping, already in serious decline since 2000 when it offered 8,405 pitches, also continues to drop. The loss of these businesses, in many cases, means the loss from the industry of Irish people with local knowledge and colour – one of the key strengths of Irish tourism and not as easily replaced as the bricks and mortar components.

Several factors have made the recession particularly difficult for tourism. Firstly, tourism relies heavily on discretionary income for its viability – something which has been singularly lacking over the last few years, not only in terms of consumer expenditure but also in terms of available budgets for travel and related expenses within the corporate market. Secondly, the small scale and seasonal nature of tourism SMEs means that there is little scope for scaling back operations, as there might be in larger enterprises. Moreover, the reliance on labour to provide high-quality tourism experiences means that automation is not usually a viable alternative to employment for the tourism industry, even where it might provide a cost saving. And finally, the inability of the banking sector to maintain the long-established access to short-term credit for daily operations as well as to smooth seasonal variations within the industry has placed many tourism SMEs in a difficult position.

These pressures added to the existing challenges of operating a small business in Ireland. As noted in a recent IBEC report, 'An Ireland that Works', "*Ireland doesn't produce enough start-up firms and not enough small companies make it big. Many EU countries have a much stronger indigenous SME base…Much more must be done to help Irish firms scale up*." We need to create an enabling environment and to better streamline the right supports for SMEs, helping them to compete successfully internationally.

2. CURRENT POSITION

2.1 Tourism Performance

Last year was an encouraging one for those involved in tourism in Ireland, with growth of over 7% in international visitors, and the positive trend has continued into 2014, as can be seen in the table below.

Table 2: Overseas Tourism to Ireland (000s)

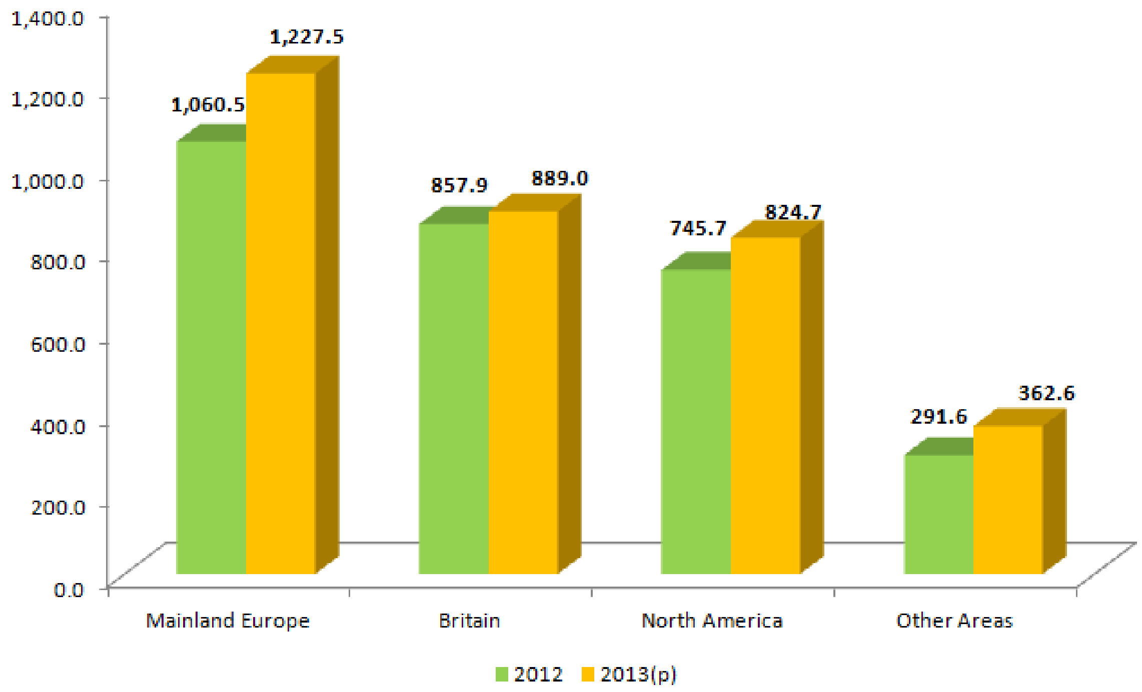
Market	2010	2011	2012	2013	% Change '12 v '13	% Increase Jan-May '14 v '13
Britain	2,739	2,878	2,774	2,929	5.6	13
North America	936	987	1,017	1,158	13.9	8
USA	*848*	*889*	*904*	*1,036*	*14.5*	-
Canada	*87*	*99*	*113*	*123*	*8.7*	-
Mainland Europe	2,045	2,283	2,347	2,463	4.9	4
Germany	*377*	*423*	*448*	*483*	*7.7*	-
France	*343*	*402*	*396*	*434*	*9.4*	-
Benelux	*200*	*235*	*237*	*265*	*11.6*	-
Nordics	*165*	*182*	*191*	*210*	*9.7*	-
Italy	*222*	*220*	*252*	*234*	*-7*	-
Spain	*221*	*245*	*253*	*263*	*3.9*	-
Rest of Europe	*518*	*577*	*570*	*575*	*0.9*	-
Rest of World	318	357	379	436	15	16
Total	**6,037**	**6,505**	**6,518**	**6,986**	**7.2**	**9**

Source: CSO

This performance compares favourably with international tourism trends. Britain experienced a growth of 6.4% in international arrivals in 2013, while Germany and Italy saw growth of 3.7% and 2.9% respectively.

Overseas revenue increased by almost 12%. The economic contribution of the North American market is getting close in value to that of the British market, as can be seen below.

Chart 1: Expenditure by Overseas Tourists in Ireland (€m)



Source: Fáilte Ireland

The domestic travel market remained static at 7.1 million trips, although there was a small growth of 2.5% in holiday trips. Combining the results from the domestic market and international visitors, total tourism revenue for the year is expected to be over €5.8 billion, including carrier receipts and expenditure by visitors from Northern Ireland. This would represent an increase of over 7% on 2012. Of this tourism revenue, a projected €1.4 billion directly benefits the Exchequer through taxation[1].

2.2 Economic Outlook

Following Ireland's exit in 2013 from the Troika bailout programme, it appears that the economy is finally on the road to recovery, with 2014 looking poised to be a turning point for the country. GDP is expected to grow by a low but respectable 2% and GNP by 3.3% during the year. For the first time since the recession started, domestic demand is expected to contribute this year to economic growth, with consumer spending forecast at 1.7% in 2014[2].

[1] Fáilte Ireland and CHL provisional estimates
[2] EY Economic Eye Summer 2014

As an export industry, the economic climate in Ireland's main tourism source markets is also critical for our industry's return to growth. In addition to a positive outlook in Ireland in 2014, it is also expected to be a year of growth in the UK – with GDP growth of 2.9% and consumer spending growth of 2.3%. UK GDP is expected to remain at about 2.3% for the following two years.

More broadly, the Eurozone in general is coming out of its longest period of recession in over three decades, although with a divergence in economic conditions across countries. While Ireland's performance looks positive in the near future, as does that of Germany, conditions in other key tourism markets are not as strong, as can be seen in the following table.

Table 3: Economic Conditions across the Eurozone

Country	GDP Growth 2104	GDP Growth 2015	Inflation Rate 2014-18	Unemployment Rate 2014-18
France	0.7%	1.1%	1.3%	10.0%
Germany	2.0%	1.7%	1.7%	5.3%
Italy	0.3%	1.2%	1.1%	12.2%
Netherlands	0.4%	1.2%	1.1%	7.0%
Ireland	2.0%	2.4%	1.4%	9.8%
Eurozone Avg.	0.9%	1.4%	1.3%	11.3%

Source: Ernst & Young

In the USA, GDP is expected to increase by 3% in 2014 – the largest rise in nearly a decade – and similar annual growth rates are anticipated through to 2017[3]. However, unemployment rates are expected to remain above 6% until late 2016 and growth beyond 2017 is expected to be below average seen over the last few decades.

Despite the optimism in Ireland, a return to recovery across all sectors is not assured and economists have identified several risks that need to be addressed.

[3] Source: The USA Congressional Budget Office

Table 4: Key Risks to Recovery in Ireland

• Continued difficulties within the banking sector and limited private sector lending to spur domestic economic recovery
• Psychological scarring of consumers from the long recession, which could hold back consumer recovery
• Potential pent-up repossessions in the housing market
• Deflation and its associated risks.

Source: Ernst & Young

The first two of these are of particular concern to the tourism industry, which is often reliant on **access to credit** to smooth out the highs and lows of seasonal demand and, as previously mentioned, is reliant on **discretionary consumer spending** for its financial viability. Additionally, overall **cost competitiveness** is now dis-improving and a series of upward cost pressures are emerging, including a strengthening of the euro against the US$ over the past year (although this has ameliorated since April 2014).

Against this backdrop of improving economic conditions and concern regarding the sustainability of the recent growth, economists and the wider business community have identified certain priorities for Government attention. Among them are five identified by IBEC in their 'An Ireland that Works' report and further outlined in their Budget 2015 Submission.

- **Reducing the tax burden** – the high tax burden is a drag on investment, employment and consumer spending.
- **Better government** - Poorly designed policy, legislation, regulation and service delivery add to the cost of doing business and are an obstacle to growth and job creation.
- **Investing in the future** - Capital investment must be ramped up again if we are to avoid the mistakes of the past, when infrastructure gaps were a major constraint on growth.
- **Extending Ireland's global reach** - Investment and trade success will be central to our economic recovery and we must continue to foster effective international links.
- **Promoting enterprise and entrepreneurship** - We need a business environment that supports entrepreneurship and rewards innovation and risk-taking.

Again, these priorities are also important from a tourism perspective in ensuring a return to sustainable growth.

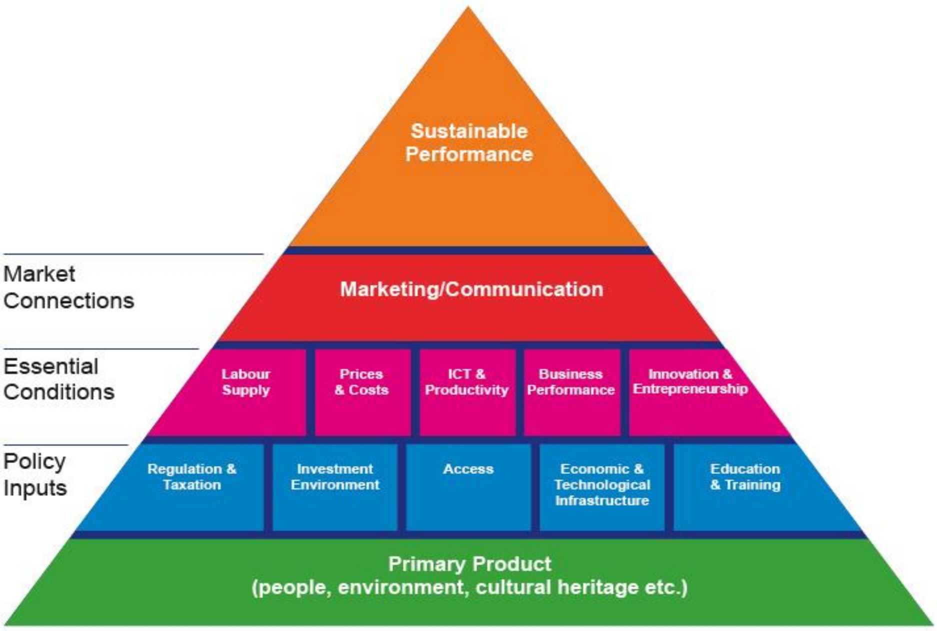
2.3 Key Drivers of Success for Irish Tourism

Competitiveness is a complex concept, encompassing many different drivers and relating more to perceptions of value than to actual price.

> *"Tourism competitiveness for a destination is about the ability of the place to optimise its attractiveness for residents and non-residents, to deliver quality, innovative, and attractive (e.g. providing good value for money) tourism services to consumers and to gain market shares on the domestic and global market places, while ensuring that the available resources supporting tourism are used efficiently and in a sustainable way".*
>
> ***(Source: OECD)***

In the 2007 ITIC report, *'Ireland's Competitive Position in Tourism'*, the National Competitive Council's (NCC) competitiveness pyramid was adapted to specifically reflect the key drivers of success in tourism. It remains an accurate reflection of the broad array of factors that influence the ability of the Irish tourism sector and its businesses to succeed in the international marketplace.

Figure 1: Tourism Competitiveness Pyramid



Source: Ireland's Competitive Position in Tourism, ITIC

As can be seen from Figure 1 above, tourism relies predominantly for its international appeal on assets that are beyond its direct control. Even within the sphere identified as 'primary product' there is much that is outside of ownership/management of the industry and yet on which it relies for competitive positioning – such as people, landscape and culture. This puts the industry at a disadvantage when compared with other sectors, such as manufacturing, where there is more direct control over the production process and where there may be greater opportunity for automation. It also means that, in addition to broader business issues that are of concern to all SMEs, there are other factors that need to be addressed in order to create and maintain a buoyant tourism sector. These are:

- **Primary Product**

Market research over the years has consistently shown that the main attractors for visitors to Ireland and our principal competitive advantages with regard to product are Irish people, scenery, the natural environment and our cultural heritage. These attractors constitute the primary tourism product. They can be defined as Ireland's factor endowments in tourism insofar as they are inherited assets. The national responsibility is to protect and preserve these assets, to enhance them if possible, to educate residents and visitors about them, and to enable access. They are the foundations of the tourism industry and maintaining their integrity will continue to be an essential factor in delivering on Irish tourism's full potential and those that are felt to be at greatest risk are included in the following recommendations.

- **Policy Inputs**

These are key areas in which policy inputs are required to enhance the competitiveness of Irish tourism and are similar for other industries, except that access is highlighted because of its critical importance, and explicit recognition is also given to the investment environment. The latter relates to investment by both the public and private sectors as well as the policy measures required to stimulate and support investment in tourism development.

- **Essential Conditions**

The factors on this layer of the Tourism Competitiveness Pyramid are largely the same as for other, non-tourism, sectors and are considered pre-requisites to successfully competing in business. The use of information and communications technology, however, has been made explicit in the tourism model, as has entrepreneurship and innovation.

- **Marketing/Communications**

A layer of the Tourism Competitiveness Pyramid is allocated to these closely related factors because of their distinctive features in tourism. Firstly, national destination marketing is largely funded by Government through the principal tourism marketing and development agencies, Tourism Ireland Ltd. and Fáilte Ireland and is a profitable activity for the State in terms of the substantial tax revenues earned from tourism. It also fills a large gap which a fragmented industry, mainly composed of numerous small and micro enterprises, cannot fill.

A second distinctive feature of tourism marketing is the physical distance between suppliers and buyers at the initial point of purchase. The 'transactability' of the tourism product therefore depends heavily on the use of various distribution channels, including tour operators, travel agents, global distribution systems and, increasingly, the internet. The importance of distribution channels therefore means that they need to be explicitly featured in the model since they have a significant impact on competitiveness.

- **Sustainable Performance**

This is the apex of the pyramid, and the ultimate objective of national competitiveness in tourism. It is heavily dependent on successful management and delivery with respect to each of the competitive factors highlighted on the supporting layers. Sustainability in this context encompasses economic, social, cultural and environmental sustainability. While it is impossible to insulate Irish tourism against external shocks, such as terrorist attacks, climatic factors or economic upheaval in major source markets, performance and growth are ultimately dependent on the ability of Irish tourism to remain highly competitive in the long term.

3. RECOMMENDATIONS

The impact of the recent recession on the Irish tourism industry was exacerbated by the loss of Ireland's competitiveness in the earlier years of this century and it highlights the ultimate impact of national economic policy on the competitiveness of a tourism destination in the global marketplace. Critical to successful competitiveness in the future, therefore, is the appropriateness of policy responses.

Of key concern to ITIC is that measures should now be taken to strengthen the longer-term viability of the industry after the understandably short-term perspective taken by many in both Government and industry over recent years in response to the economic crisis. It supports IBEC's recommendation that

> *"resources are available to reduce income and consumer taxes (and that) getting more money back into the economy will boost economic activity and support job creation. We also need to boost investment in enterprise and infrastructure..."*

Taking into account the broader economic circumstances outlined previously along with the specific requirements of the tourism industry, ITIC has identified two broad areas which it recommends the Government address in Budget 2015 that will positively influence the key drivers of competitiveness identified earlier. These are:

1) Cost competitiveness
2) Investment in tourism.

Detailed recommendations with regard to each are provided in the remaining sections of this submission.

3.1 Cost Competitiveness

Irish tourism is predominantly an export industry and relies heavily on its ability to compete successfully in international markets. As seen in Figure 1, the competitiveness of Irish tourism relies on a broad range of factors, many of which – including costs - are not within the control of the industry itself.

According to the NCC, Ireland's cost base has improved across a range of metrics over the last four years which has made Irish firms more competitive internationally.

However, Ireland remains a high cost location for a range of business inputs and enhancing cost competitiveness must therefore be a key economic priority for Government. There is also concern that there has been a lack of longer term strategic actions to ensure that recent economic improvements can be sustained.

"The Council is concerned that recent price falls in Ireland are largely a cyclical response to the Irish and international recessions (i.e. reduced demand, spare capacity), rather than a response to structural changes in the Irish economy. It is also not clear that cost gains are being driven across the broad economy. Furthermore, the evidence... suggests that the Irish economy has reached a turning point in terms of cost competitiveness. The trends... indicate that overall relative cost competitiveness in Ireland is now disimproving, and that a series of upward cost pressures are emerging. Marginal improvements in cost competitiveness (resulting from slightly lower inflation in Ireland relative to our competitors and trading partners) have been offset by the adverse impact of the strengthening euro. Low rates of inflation (or possible deflation) across the whole euro area increase the difficulty of extending improvements in cost competitiveness through price reductions."

Source: NCC, 'Costs of Doing Business in Ireland', 2014

This concern regarding cost competitiveness is also borne out in the Travel & Tourism Competitiveness Index produced by the World Economic Forum. The Index measures countries against 79 broad indicators of competitiveness and Ireland currently ranks 12th in the listing of European countries, as can be seen in Table 5.

Table 5: Travel & Tourism Competitiveness Index

Rank	2013	2011
1	Switzerland	Switzerland
2	Germany	Germany
3	Austria	France
4	Spain	Austria
5	UK	Sweden
6	France	UK
7	Sweden	Spain
8	Netherlands	Iceland
9	Iceland	Netherlands
10	Finland	Luxembourg
11	Belgium	Denmark
12	**Ireland**	Finland
13	Portugal	Portugal
14	Denmark	Norway
15	Norway	**Ireland**

Source: The World Economic Forum

In the most recent report by the NCC[4], seven trends are identified in Ireland which reflect upward cost pressures at the micro level of business. Of these, four are of specific concern to the competitiveness of tourism enterprises:

1) Labour costs
2) Utility costs
3) Broader cost environment
4) Credit cost.

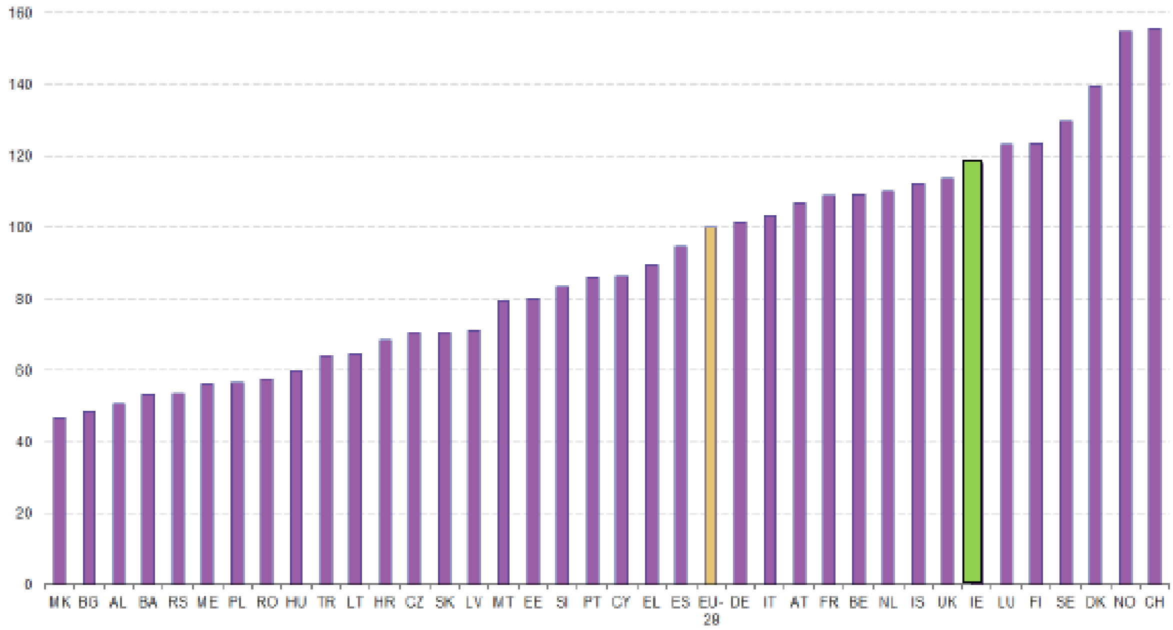
In its June 2014 report, Eurostat ranked costs in Ireland at 18% above the EU average for consumer goods and services – behind the Nordic countries but, more importantly in terms of international positioning for tourism, marginally above Britain and well above the key markets of the Netherlands, France, Germany and Italy – see Chart 2.

These cost pressures make it difficult for Irish tourism enterprises to price themselves competitively in the marketplace, as the price of any tourism experience is a combination of a

[4] NCC: '*Costs of Doing Business in Ireland'*, April 2014.

variety of inputs (as seen previously). They also make Ireland an expensive destination for visitors who come from these countries (see 3.1.5 below).

Chart 2: Price Level Index for Household Final Consumption Expenditure, 2013 EU=100



Source: Eurostat

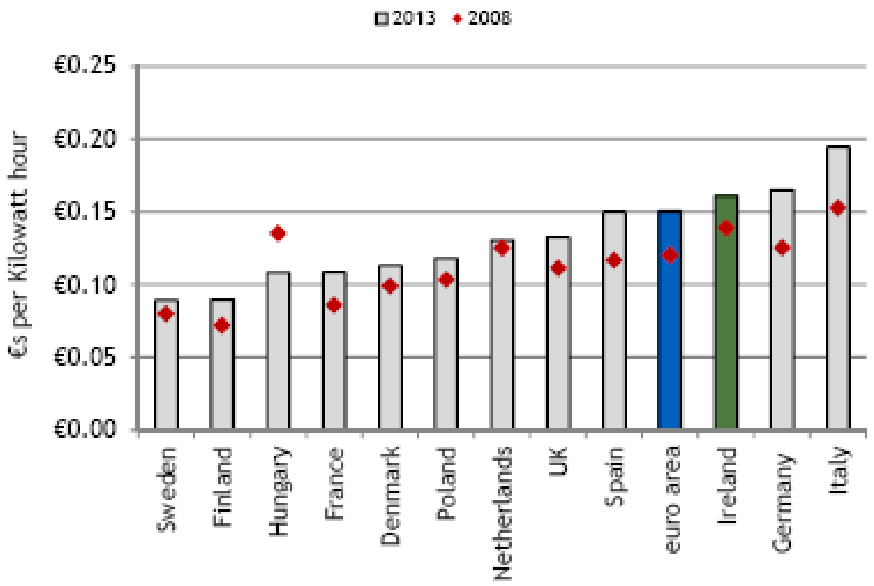
3.1.1 Operating Costs

Utility costs, as well as Local Authority rates and charges, are a significant cost burden on SMEs and many have been increasing at a rate above inflation since the recession began. The cost of operating a tourism business in Ireland continues to be higher than the EU average across a range of aspects, putting the sector at a disadvantage internationally.

Electricity costs in Ireland are relatively high – in the Euro 17 area, Ireland is the 5th most expensive location for SMEs, with prices 8% above average and 10% ahead of the UK. Chart 3 indicates Ireland's ranking against a number of key competitor destinations.

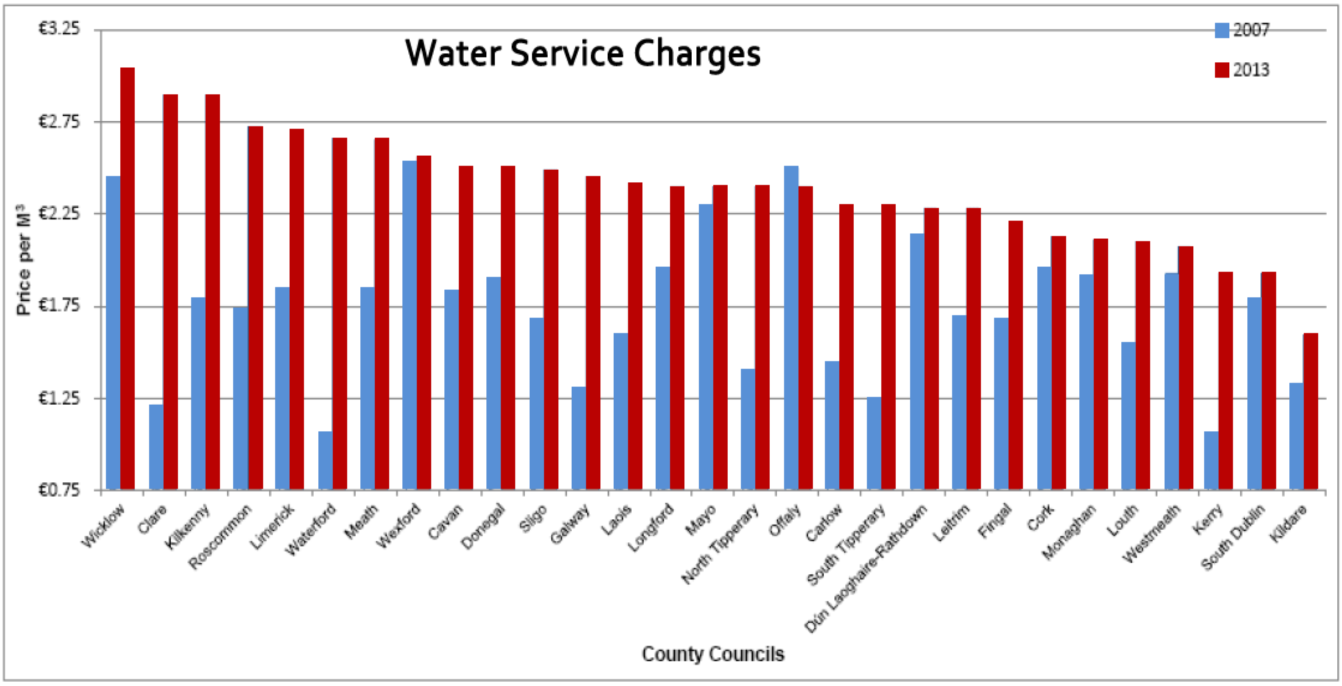
Secondly, **water charges** been increasing over the period since the recession started and have also continued to vary substantially by Local Authority area, with a continuing near two-fold variation between the cheapest tariff (Kildare) and the most expensive (Wicklow).

Chart 3: Industrial Electricity Charges for SMEs (excl. VAT) 2013



Source: Eurostat, Environment & Energy

Chart 4: Comparison of Combined Water Charges by County Council, 2007 v. 2013

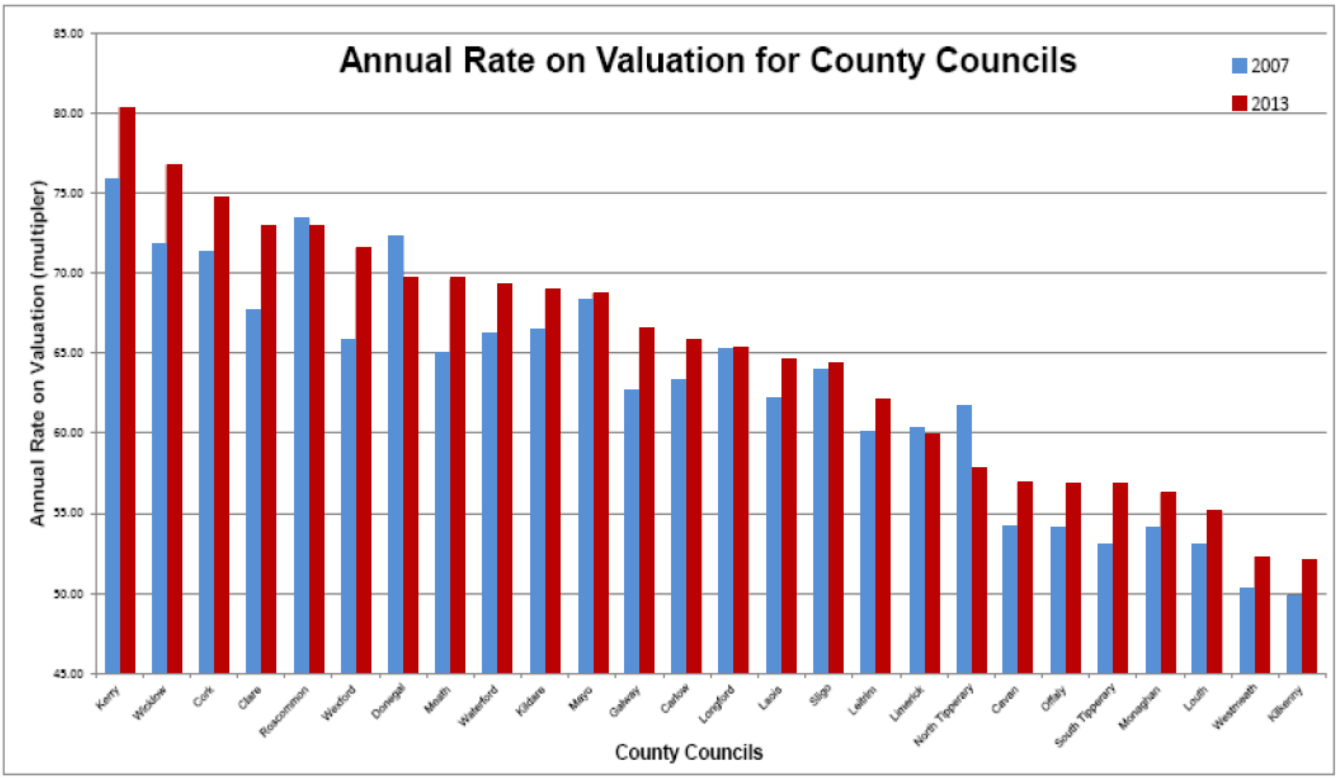


Source: IBEC, Addressing the Issue of Local Authority Costs

The hope is that Irish Water will introduce greater transparency along with harmonised tariffs and that there will be no additional cost increase but the situation in this regard is not yet clear.

Thirdly, the burden of **Local Authority rates** on seasonal tourism businesses is a heavy one. Despite above-average increases up to 2008, there has been little easing of rates across the country since the onset of the recession, as can be seen from Chart 5 (the situation is similar for City Councils, with the exception of Limerick which, in conjunction with Donegal and North Tipperary, seems to be making some progress in reducing the cost burden on businesses).

Chart 5: Comparison of 2007 and 2013 ARV by County Council Area



Source: IBEC, Addressing the Issue of Local Authority Costs

Operating a tourism business is sufficiently demanding - particularly in the current recovery period following a dramatic economic downturn - without the added burden of uncompetitive utility costs and rates. Our recommendations in this area are intended to create a more equitable business environment for the tourism industry and to support the industry in finding more long-term solutions to inevitable challenges.

- **Recommendation 1:**
  Support tourism enterprises in moving towards greener energy sources to combat increasing costs in oil and gas that have been underpinning the rise in electricity costs.
- **Recommendation 2:**
  Ensure no further cost increases in water charges and establish an equitable charging system across the country.
- **Recommendation 3:**
  Reduce commercial rates so that they are in line with recent economic developments and there is more transparency in their application.

3.1.2 Credit

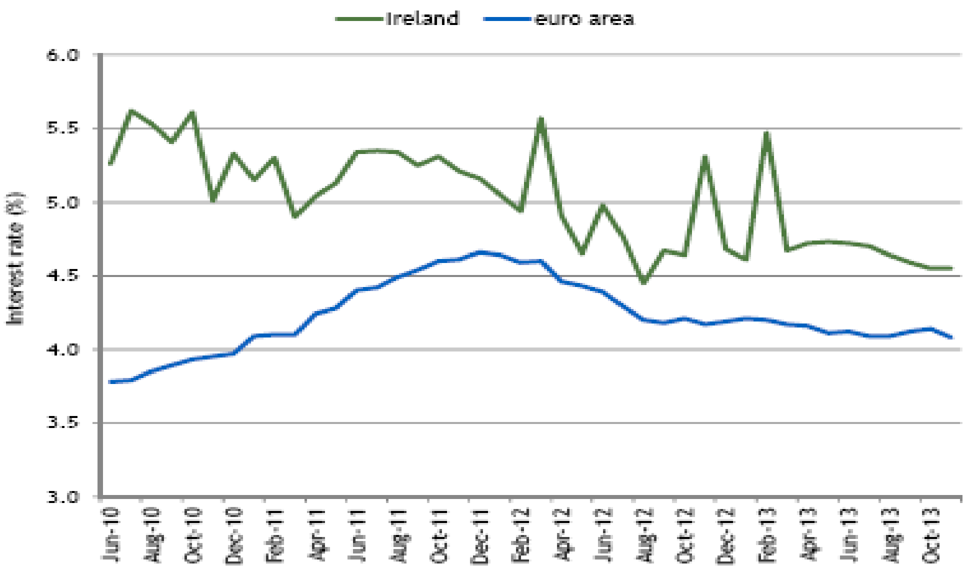
As the banking system has ceased to function effectively, access to finance has been an issue in Ireland since the recession started but is a particular problem for tourism businesses for several reasons. Firstly, the seasonal nature of tourism means that enterprises frequently rely on reasonably-priced and easy access to credit to ensure the smooth, year-round, operation of their enterprises. Additionally - and with a longer term perspective - the lack of access to and higher cost of credit, particularly for the hotel sector, means that there may be insufficient funds to re-invest in repairs, refurbishments and upgrading, leading to the degradation of the tourism experience.

According to the Central Bank, new business interest rates in Ireland for non-financial corporation loans of less than €1 million stood at 5.13% at the end of May, 2014, some 139 basis points higher than the corresponding rate charged by euro area credit institutions, which stood at 3.75%. The average rate for loans above €1 million was 3.04% at the end of May, 2014, compared to a 2.17% euro area average.

Revolving loans and overdrafts are often important sources of credit for SMEs and yet Irish companies continue to experience difficulties in accessing short-term credit and, when they do, they pay more than their European counterparts for the service – as Chart 6 clearly demonstrates.

Although the gap has been narrowing, interest rates in Ireland for these forms of finance are also substantially higher than the euro zone average - rates in November 2013 were 11.5% higher than average.

Chart 6: Interest Rates for Revolving Loans & Overdrafts – Non-Financial Companies



Source: European Central Bank

It almost goes without saying that restoring a vibrant and competitive banking sector is what all sectors of the economy require. However, in the absence of such a medium-term solution, our specific recommendation in this regard is made with the intention of facilitating access to credit for the tourism sector.

- **Recommendation 4:**
  Ensure easy and cost-effective access to finance for the tourism industry by considering a venture capital style investment fund for innovative tourism businesses.

3.1.3 Labour Costs

Labour can account for over 70% of costs in service industries, according to KPMG, and as a labour-intensive service industry, labour regulation and the cost of employing and retaining staff are of crucial importance to tourism businesses. The rate at which taxation is levied on labour is a major determinant of both an employer's decision to retain or hire individuals, and of the take-home pay of workers. As a result of changes in taxation levels, workers increase or decrease the pre-tax wage they bargain for in wage negotiations. The level of taxation in Ireland and costs to employers continue to place Irish tourism at a cost disadvantage when compared to competitor destinations and other industries.

"Following a number of years of marginal decline, labour costs in Ireland are on the increase (2.4% p.a. in 2012 and 0.5% p.a. in 2013)…. Further small increases, which will weaken cost competitiveness, are projected in 2014.

The cumulative impact of increases in income taxes, changes to bands, the introduction of the Universal Social Charge etc. have weakened competitiveness since the onset of recession."

Source: NCC, 'Costs of Doing Business in Ireland', 2014

"Tax on work is now completely out of line with our international competitors: Ireland now has the highest marginal income tax rate at average earnings in the OECD.

The government's pension levy is an inequitable and unjustifiable tax on the savings of private sector workers…"

Source: IBEC, An Ireland that Works

The minimum wage rate in Ireland is the fifth highest in the European Union. Increases beyond its present level would have a serious impact on tourism, primarily because established relativities in pay scales mean that an increase in the minimum wage inevitably leads to increases in all pay rates above the minimum wage.

The focus should be placed on take home pay rather than gross pay, and increases in take home pay can more effectively be achieved through adjustments in the Universal Social Charge and income tax rates for lower paid workers.

It is essential, therefore, that costs which negatively affect the tourism industry's ability to attract and retain suitable staff are addressed and our recommendations are made in this context. It must also be said that any additional measures which might cause upward pressures on labour costs should not be introduced. The recommendations below are consistent with those made by IBEC in its pre-budget submission.

- **Recommendation 5:**
  Raise the entry point to the standard tax rate from €32,800 to €34,800 and reducing the higher rate of tax to 40%.
- **Recommendation 6:**
  Drop the private sector pension levy.
- **Recommendation 7:**
  Reform the USC structure to deliver an equal rate for self-employed and PAYE workers.
- **Recommendation 8:**
  Increase the level of take home pay by adjusting tax and USC rates for lower paid workers, rather than increasing the minimum wage.

3.1.4 VAT Rate

In July 2011, a temporarily reduced V.A.T. rate of 9% was introduced for tourism-related goods and services. The cost of implementing the reduction has been less than anticipated, reinforcing the belief that lower V.A.T. rates stimulate demand, leading to growth in industry and employment.

Reviews of the impact, carried out on behalf of Fáilte Ireland and by ITIC in 2013, suggest that the reduction has had a positive outcome across a number of measures.

- Visitors' perception of Ireland's value for money has continued to improve since 2011.
- Tourism numbers and revenue to Ireland have also continued to rise since the reduction.
- Employment in the accommodation and food services sector rose by 21.5% between Q1 2011 and Q1 2014 compared with an increase in overall employment of just 2.6% for the same period. In total, some 24,100 additional jobs were created in the accommodation and food services sector. As this sector accounts for about two-thirds of total employment in tourism, this implies that in excess of 36,000 jobs have been added in tourism over the past 3 years. The increase in total numbers employed between Q1 2011 and Q1 2014 was 48,700, of which 36,000 or over 70% were accounted for by the tourism sector.

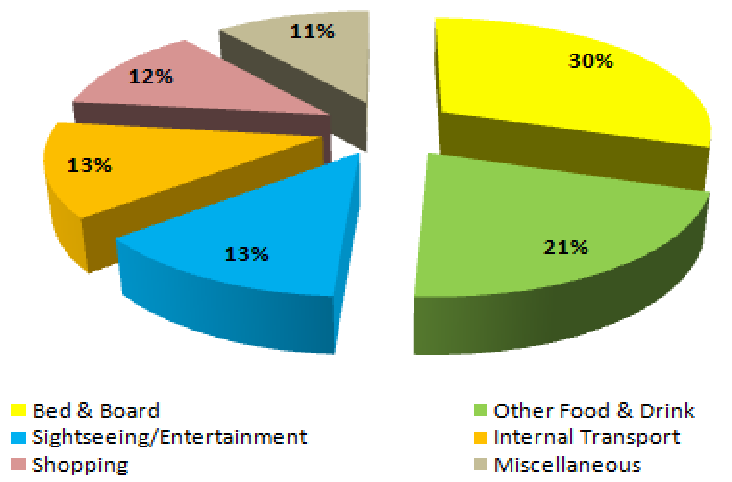
There is also clearly no substantial reason to revert to a higher V.A.T. rate and therefore our recommendation is an obvious one.

- **Recommendation 9:**
  Continue to support the competitiveness of the tourism industry and employment in the sector by retaining the 9% V.A.T. rate.

3.1.5 Broader Cost Environment

The price of a trip in Ireland – whether for leisure or business – is composed of a variety of different costs, as has been referred to earlier. Some of these are priced by the tourism industry themselves, but many are part of the broader cost environment as experienced by all who are either resident in or visitor to the country. Chart 7 outlines the main areas of expenditure for overseas visitors during their stay in Ireland.

Chart 7: Breakdown of Visitor Spend in Ireland, 2012



Source: Fáilte Ireland

Of concern to the tourism industry in Ireland is the country's lack of competitiveness in several of these areas, which adds unnecessary pressure to businesses already burdened by other costs identified previously.

"Ireland's current price level and inflation profile can be described as high cost but rising slowly. In 2012, Ireland was the 3rd most expensive location in the euro area for consumer goods and services. Irish prices were 14.6 per cent above the euro area average. Irish price levels remain above the euro area average in 10 of the 12 categories."

Source: NCC, 'Costs of Doing Business in Ireland', 2014

In particular, three areas that are especially relevant to tourism, and where Ireland's prices are significantly higher than the EU average, have been identified by Eurostat. These are Ireland's rating of:

- 17% above average for food and non-alcoholic beverages;
- 78% above average for alcohol and tobacco;
- 19% above average for public transport services.

This means that a substantial share of expenditure by visitors to Ireland is in categories where prices are well above what they could experience either at home or in a competitor destination. Regardless of how efficiently tourism enterprises run their businesses or how competitively they price packages, there is little they can do directly to off-set these higher prices which, in addition to making it difficult to competitively price tourism packages, also portray Ireland as an expensive destination to visit.

The cost of alcohol is of particular concern to tourism given the popularity of the Irish pub experience, the relative lower cost of alcohol in the UK and the centrality of wine to the daily habits of Mainland European visitors. The excise duty on a bottle of wine in Ireland – at over €3 a bottle – is the highest in Europe, and the rate on both beer and spirits is within the top three.

Chart 8: Excise on Standard Bottle Wine

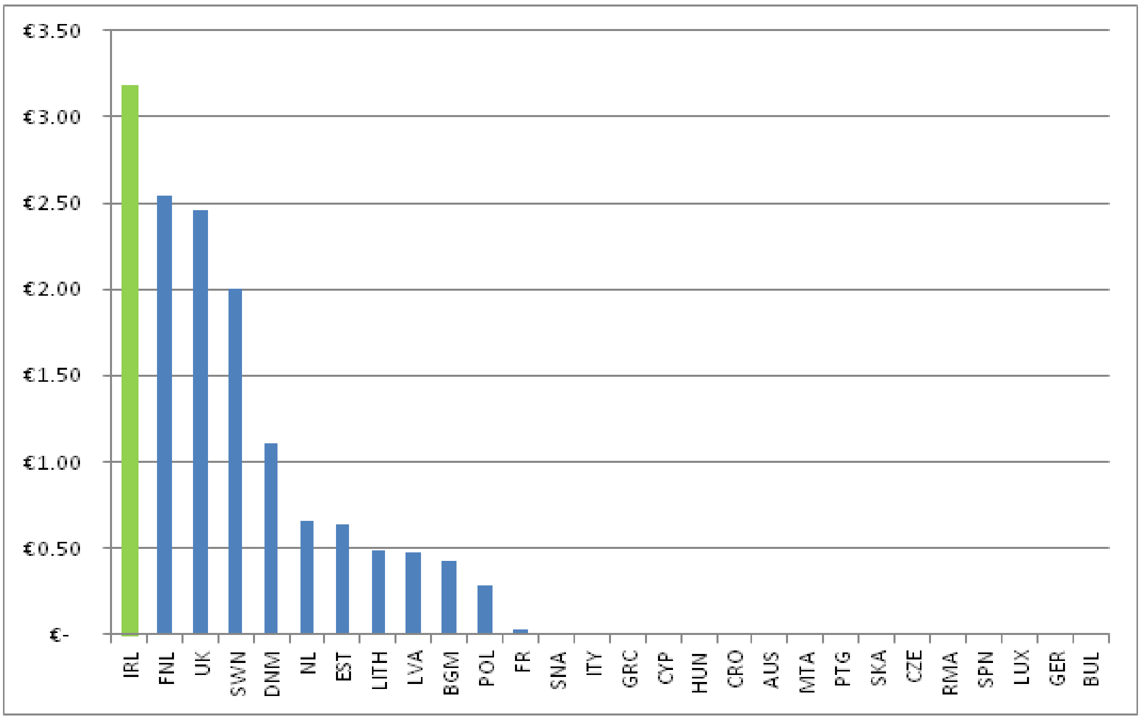


Chart 9: Excise on Standard Pint Beer

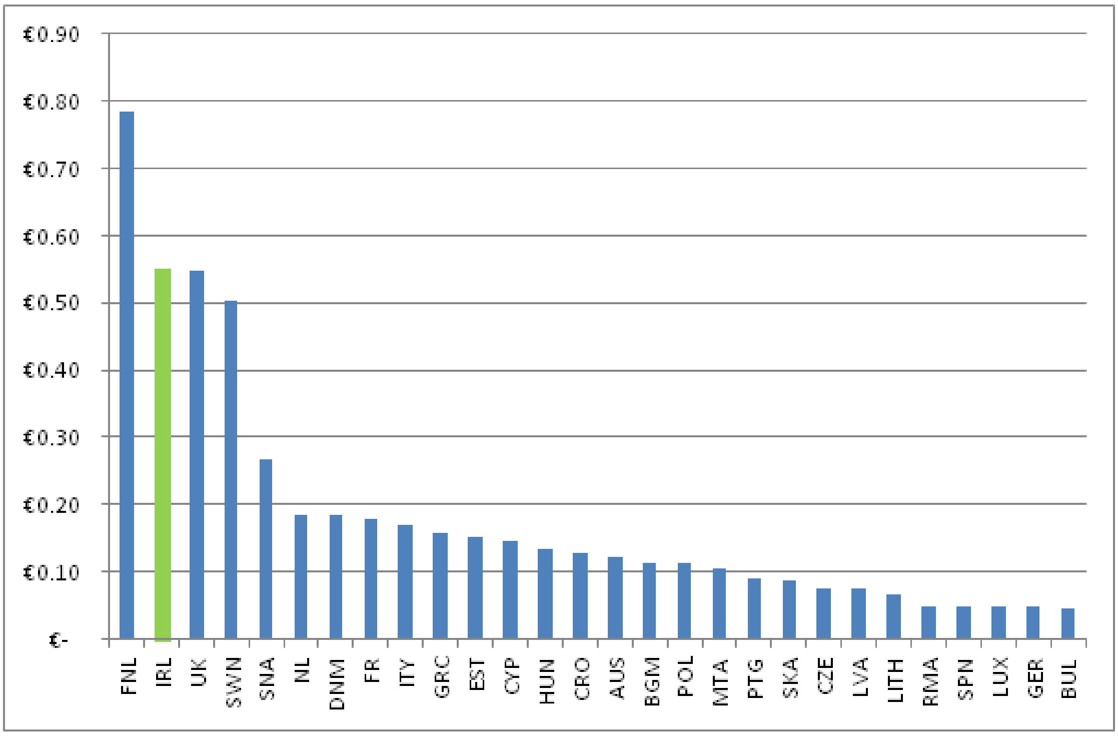
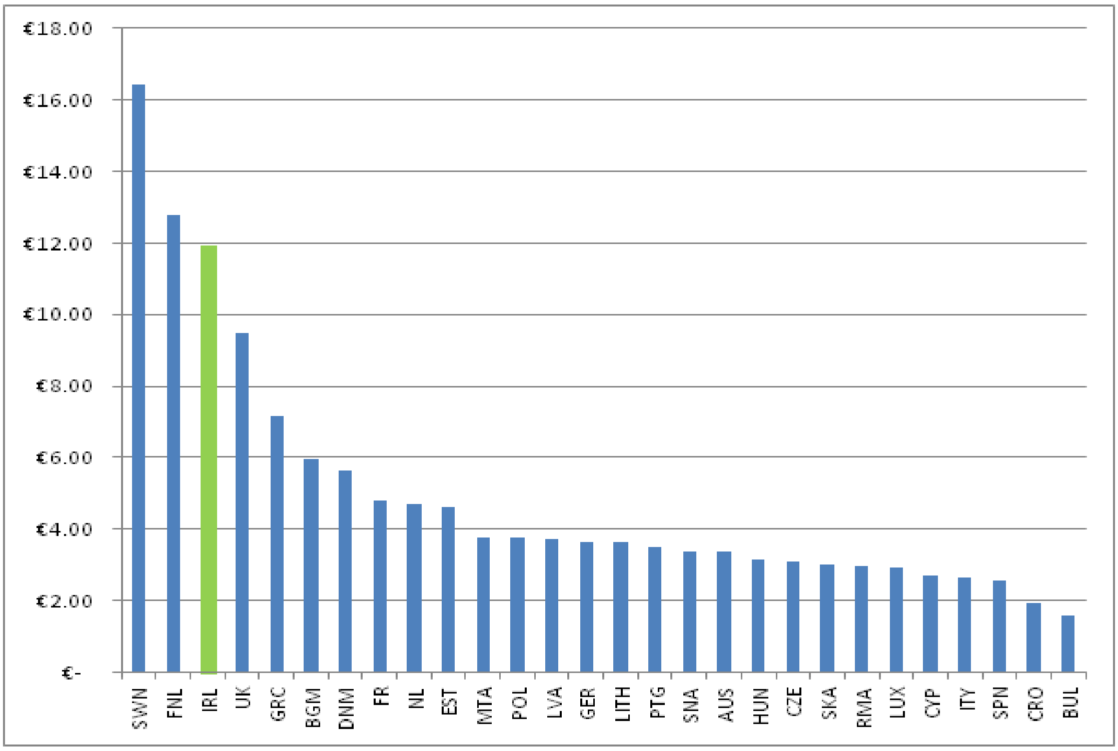


Chart 10: Excise on Standard Bottle Spirits



While addressing other elements of the pricing of Bed & Board in Ireland can be tackled through operating, labour and other costs, the situation with regard to excise duty on alcohol is more straight-forward and it is with this perspective in mind that the following recommendation is made.

- **Recommendation 10:**

  Continue to support the competitiveness of the tourism industry and employment in the sector by reducing the excise rate on alcohol.

3.2 Investment in Tourism

Investment is an essential component for the development of a country's tourism infrastructure, products and services, and the return on investment – in terms of visitor volume and revenue – is well-documented. The rationale for Government involvement in the tourism sector is founded on several market failures as well the benefits that can be delivered by public intervention. The key to success is a co-ordinated and prioritised approach to investment.

Broadly, Government support for tourism falls into two distinct categories: investment in product/enterprise development and the stimulation of demand (destination marketing).

3.2.1 Capital Investment

According to IBEC, 70% of public expenditure reduction during the crisis was achieved through capital programme cut backs. However, an increase in capital investment is required in order to ensure that Ireland doesn't fall back into infrastructural deficits being a constraint on growth as has been the case in the past.

The Government's capital fund for tourism amounts to about €20 million annually, which is well below the relative value produced by the sector as well as being significantly lower investment than in other industries. A comparison with the agri-food sector, for example – which is a comparable export-led, indigenous industry – reveals a distinct imbalance in support. At present, State support for tourism is one tenth of that for the agri-food sector – a sector which is in receipt of subsidies worth €1.5 billion (less taxes on production), payable by the Dept. of Agriculture, Food & Marine.

Table 6: Agriculture & Tourism – a Comparison

	Agri-Food Sector	Tourism	Ratio
State capital investment, 2014	€168 million	€17 million	9.9:1
Export earnings, est. 2013	€8.6 billion	€4.3 billion	2:1
Employment Q3 2013	110,600	137,700	0.8:1

Source: ITIC

The recent recession has taken its toll on the existing tourism attractions due to the perhaps understandable under-investment of the last five years. Based on the proven appeals of Ireland's natural, heritage and cultural assets, Government has a critical role to play in public sector investment and in creating a pro-business investment environment.

Ireland now requires a prudent and dynamic investment policy for new developments, redevelopments and refreshment of existing tourism infrastructure, products, services and experiences. The policy needs to foster innovation as well as delivering regionally differentiated, market-led products and experiences.

Capital investment from the Exchequer would be used to encourage and support investment in both public and private sector sustainable projects that demonstrate an ability to enhance the appeal and experience for the visitor as well as generating employment and increasing expenditure in the country. Specifically, projects would be required to meet a number of criteria, including:

- enhancement of the local attractions, facilities and amenities in a tourism area;
- the ability to attract additional visitors;
- the ability to operate without operational support funding.

Additionally, the model of the Government's Development Capital Scheme, whereby SMEs in the tourism sector could have access to state-backed investment schemes, could provide a stimulus to investment in export-oriented projects. No such investment funds or access to credit are available at the moment for tourism.

Our long-term recommendation in this area is to support the ability of Irish tourism to offer high-quality experiences by devising a New Product Development Plan with a capital investment budget of at least €250 million/€50 million per year in the period 2016-2020 inclusive. This budget should be made available in the context of a multi-annual framework plan to enable realistic and effective implementation given that the timing of expenditure on capital projects cannot be tied into inflexible annual budgets.

In the short term, we recommend that a capital budget of €15 million be made available in 2015 to support the completion of the Wild Atlantic Way, projects already in train, and those that are ready-to-go.

- **Recommendation 11:**
  Allocate an annual capital budget of €50 million to tourism product development over the period 2016 to 2020 inclusive.
- **Recommendation 12:**
  Provide a capital budget of €15 million in 2015 to support further development of the Wild Atlantic Way, projects already in train, and those that are ready-to-go.
- **Recommendation 13:**
  Introduce a special capital allowance of 50% of the cost of new and second-hand touring coaches up to two years old for 2015 and 2016 to enable coach operators to renew their fleets for this growing market.
- **Recommendation 14:**
  Consider a Public/Private Partnership approach to tourism investment.

3.2.2 Marketing

In addition to support for fresh development/redevelopment, State support for destination marketing is also essential in order to raise awareness and stimulate demand in an increasingly-competitive international marketplace. It has long been established that State support for marketing is not only required on the basis of market failure, but also as a means of harnessing and co-ordinating limited private sector marketing investment. Over the period since 2008, the level of State investment in international tourism marketing has contracted sharply, and this trend should now be reversed.

In the medium term, the focus of marketing resources needs to be on markets with proven potential to yield a return on investment in terms of both volume and value. Britain is by far the most important market in terms of volume, and therefore will remain a priority, as will France and Germany. Long haul markets, including the USA, are high-yield and therefore also a priority for that reason.

In recent years Tourism Ireland has been active in developing new business from emerging markets. This remains important long-term, however, the economic forecasts for some of these countries suggests that the level of investment should remain proportionate to the potential return.

> *"In order to build upon and sustain the recent economic recovery, expanding the Island's export base will be critically important in both the ROI and NI. Given the rising risk profiles and growth forecast downgrades in emerging economies, traditional sources of export success should remain a high priority for exporting businesses, with a more cautious approach adopted towards emerging markets, at least in the medium term."*
>
> ***Source: Ernst & Young***

- **Recommendation 15:**

  Support the international promotion of Ireland as a tourist destination by increasing the current level of investment in the Tourism Marketing Fund.

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