

2

Speech by Liam Connellan, Director General, Confederation of Irish Industry, at Meeting of Galway Rotary Club at 1 p.m. on Friday, 10th December 1982, at Great Southern Hotel, Galway.

INDUSTRIAL PROFITABILITY AT DANGEROUSLY LOW LEVELS

The continuation of the international recession is having a serious effect on the small open Irish economy. It is now estimated that the output of the major industrial economies for 1982 has fallen by about 0.3% with a more serious fall of 1½% in the United States and 0.8% in West Germany.

Any recovery in 1983 is likely to be weak. While the output of the United States economy is expected to grow by 2.7%, those of the European Community are now forecast to grow by only 1%.

Manufacturing output in Ireland staged a short lived recovery from the 1980 recession during 1981 but there has been renewed fall in output since February of this year. Between February and August, manufacturing output fell by over 8%. The fall was arrested in September, largely because of the strong performance of the food processing sector but there are as yet few signs of any upturn. Non food manufactured exports have remained buoyant during the year mainly due to the contribution of new electronics firms. Exports from established

industry lost market share in the key British market.
Unless Irish unit costs are restored to the level of our
competitors, further sharp declines in output will occur.
By ensuring that unit costs do not rise during 1983 a further
fall in competitiveness may be avoided and Irish manufacturers
may be able to hold or increase their share of markets at
home and abroad.

The international recession and declining competitiveness
have resulted in falling profitability in the manufacturing
sector. The profitability of the publicly quoted manufacturing
firms has declined sharply during recent years. In 1977
the return on capital employed was 14%. This fell slightly
to 12% in 1979 and then dropped sharply to less than 8% in
1981. There is every indication that profitability fell
even further in 1982. The decline in profitability has been
much more serious in the current recession than in 1975,
when the average return on capital employed never fell below
10%.

Recent studies by the Economic and Social Research Institute indicate that since 1979 there has also been a very sharp decline in the volume of private finance investment.

The decline in investment is a function, not only of the loss of investment confidence because of the recession, but also of the fall in profitability.

Examination of the relationship between profitability and investment over the last two decades shows that they are very closely interlinked. When profitability declined it was followed by lower investment.

Lack of profitability leads to reduced investment and endangers employment. No business can be sustained if its return on

investment fails to cover the cost of capital and generate additional funds for future investment. Lack of retained profits means that additional investment funds have to be borrowed and, therefore, places a limitation on marginal investment projects.

Over the last two decades, there has been a continual shift in the share of national income allocated to wages rather than profits. In the early 1960s the share of national income going to employees' compensation was about 60%. This share increased to 71% in 1975 and by 1980 had increased to 75%. It is likely to be even higher now. This has resulted in a steadily declining proportion of national income to provide for profits and repay debts.

The declining share of profits in national income has lead to a decline in investment and, therefore, in job opportunities. It has contributed to over consumption in the economy and caused unsustainable deficits on the balance of payments.

If the manufacturing base is to expand over the next few years in order to create more sustainable employment opportunities, there must be a restoration of factor income shares in favour of profits. As profitability improves so will investment and competitiveness, with resultant gains in the home and export markets.

Irish manufacturers must compete in extremely difficult international trading conditions. The difficulties have been compounded by the declining competitiveness of the economy. The corrective measures required to bring the economy into balance may erode living standards in the short term but will lead to a higher level of employment. Essential investment will only be made if there is a return to an adequate level of profitability.

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