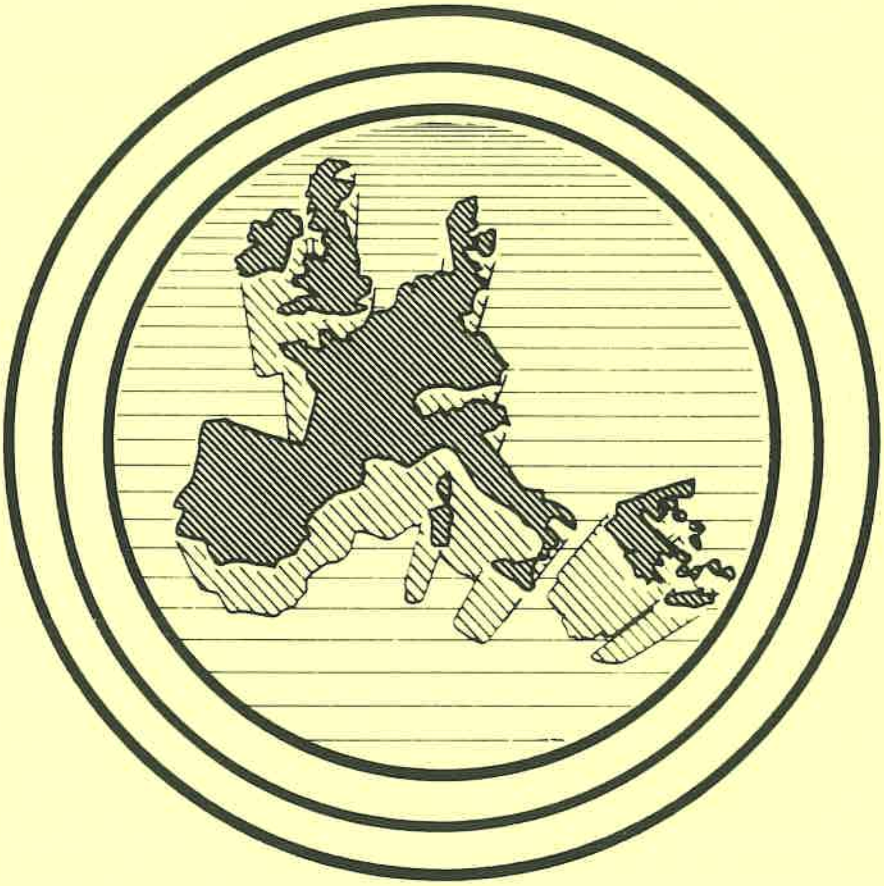
1992

TARGETING THE OPPORTUNITIES



OPENING ADDRESS

Paper presented by

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Address by Mr Liam Connellan, Director General, Confederation of Irish Industry at the Opening of Dublin's First Small Firms Conference "1992 - Targeting the Opportunities" held in the Burlington Hotel, Dublin, on Saturday, 8th April 1989 at 9.00a.m.

Introduction

1992 will be one of the greatest deregulation exercises in modern economic history. The aim is to remove all barriers to trade between the Member States of the European Community so that Member States can concentrate on what they do best, and that European industry be able to compete more effectively on world markets with the United States and Japan.

Many estimates have been made regarding the likely outcome. The most optimistic is that contained in the Cecchini Report which estimates that if Member States adopt coordinated growth policies the European economy would grow 7% faster and create five million more jobs than would otherwise have been the case in the years immediately following the completion of the market in 1992.

There are some indications already that the freeing up of the market has had a beneficial effect. Employment in the European economy last year grew at its fastest rate since the Community was founded in 1957. The attached chart shows the development of employment in Ireland and in the European Community since Ireland joined the Community in 1973.

Forecasts for employment growth in the European Community this year and next year indicate that more than one million additional jobs will be created each year. If the Cecchini projection comes to fruition it is likely that employment will grow by about two million jobs per year from 1992 onwards. This assumes, of course, that there will not be an international recession.

Ireland has held its share of European employment since 1973. Our unemployment rate is very high because our population and labour force grew much more rapidly than the rest of Europe. There is no reason to believe that Ireland cannot increase its share of European employment over the next five years and to steadily improve the rate of employment increase in the economy from a Government estimate of 13,000 net new jobs in 1989 to 20,000 net additional jobs annually.

The completion of the Single European Market requires the removal of:

1. fiscal barriers;
2. technical barriers; and
3. physical barriers.

1. Removal of fiscal barriers means that indirect tax rates must be similar so that there is not a distortion of competition. Personal tax rates must be similar to avoid loss of more highly skilled people to areas of the Community with lower tax rates. While company tax systems will be similar a variation in company tax rates will be permitted in order to provide incentives for the reduction of regional disparities.

2. The removal of technical barriers will ensure that products which meet national standards can be sold throughout the Community provided health and safety requirements are fulfilled. In the minority of cases such as electrical and telecommunications products they must conform to a European standard.

3. Removal of physical frontiers means that there will be no customs barriers at national boundaries within the Community and that goods will be allowed to move freely between Member States. This will speed up the delivery of products and increase the population which can be served by any firm within a given time period.

Already spare parts for motor vehicles which are ordered by garages throughout Ireland from depots in Britain and the Continent and can be delivered within 24 hours.

We must no longer think of ourselves as islanders but as Irish Europeans who can avail of the opportunities of a large and affluent market of 320 million people.

Role of Small Firms

The structure of industry within Europe has changed significantly over the last few years. Many large firms are concentrating their activities on their core businesses and are buying in products and services which can be made more efficiently by outside contractors. This approach had been adopted for many years by Japanese industry and explains why the output per person in many large Japanese firms is very much higher than in similar European firms. Japanese companies have a tradition of using a much larger number of sub-contractors than their European counterparts, and this has undoubtedly contributed to their success.

Here in Ireland we have seen similar developments. Many large firms have sub-contracted a wide range of operations ranging from component manufacture, computer software, maintenance, cleaning, computer services, financial services, and secretarial services. This has been done in order to improve efficiency, reduce costs, and improve the competitiveness of manufactured products.

The complementary role of large and small firms within the European economy is illustrated by the 80/20 rule. This states that about 20% of firms can be expected to produce 80% of the output of industrial products. These are the large firms which have high volume production lines. The remaining 80% of firms produce 20% of total output represented by a massive array of products and services which cannot be produced efficiently by larger firms although many of these products are essential components for large scale industry.

In Ireland, for every manufacturing firm having more than 100 employees producing high volume products for a European market there are 90 small firms producing a wide range of specialised goods for regional markets or sub-components for their larger counterparts. Small firms play a unique role in the industrial network. Without the well-developed structure of small industries large firms cannot operate efficiently. The existence of a very large number and wide variety of small firms is a hallmark of a highly developed economy. There is still considerable scope for the development of the small firms sector of the Irish economy.

The need for an expanding small firm sector is highlighted by the emphasis now being placed on European content before a product is classified as being of European origin. Before a product is regarded of being of European origin it must have a local content of at least 40% and sometimes more. When the European content is below that level the European Community is likely to regard it as originating outside the Community, and therefore subject to the common external tariff. In some sectors of industry the local content rules are even more stringent.

The more small firms which are available to supply local products and services the easier will it be for foreign companies manufacturing in Europe to meet the minimum European added-value requirement. Industrial firms will be attracted to those regions of the Community which have a large number of small firms capable of supplying sophisticated products and services.

Large high volume firms and small-scale producers and sub-contractors complement one another. Neither can thrive without the other. Every big firm will create the need for a large number of small firms while the lack of a well-developed small firm infrastructure will deter large firms from setting up in many regions. Large firms generate high-volume output from factories which are becoming increasingly more mechanised while small firms fulfill the vital role of producing a wide variety of highly specialised products and services and are much more labour intensive. Put another way, large firms create the output and the wealth and small firms provide the sub-supply infrastructure and the jobs.

Performance of Small Firms

Since 1985 the output of manufacturing industry in Ireland has expanded by an average 8% per annum and total employment in the economy has increased by an average of almost 4,000 per annum.

This increase in employment has occurred despite there being only a marginal increase in direct manufacturing employment. Because of the hiving off of various activities such as transport, cleaning, maintenance, catering and financial services from manufacturing firms many jobs that hitherto have been counted as manufacturing are now classified within the services sector. Since 1985 employment in private services has increased by about 7,000 per annum.

There has also been a restructuring of employment within the manufacturing sector itself. The number of people employed in grant-aided firms having more than 50 people declined while the number employed in small manufacturing firms has increased. This occurred because large firms, though continuing to increase their output sharply, have found it to be more efficient to sub-contract component manufacture to small firms.

Thus two forms of employment restructuring have been taken place. Firstly, the reclassification of many service activities from manufacturing to the services sector; and secondly the sub-contracting of industrial activities from large firms to small firms. This illustrates clearly that large firms make the main contribution to expanding the output of the economy, and small firms provide sub-supply and support services and account for the greatest increase in employment.

Ireland is now proportionately the third largest exporting nation in the European Community after Luxembourg and Belgium. More than 80% of the output of manufacturing industry is exported mostly to other Member States of the Community. Again there is a substantial and understandable difference in export activity depending on the scale, of firm. Many of our large firms are already of European and world scale and export their products all around the globe. The great majority of manufacturing firms employing more than 100 employees are engaged in exports. On the other hand only one third of firms having between 20 and 100 employees export and about 10% of manufacturing units having less than 20 employees are engaged in exporting. I emphasise that this is not a criticism but rather reflects the complementary role of large and small firms. Most small firms capitalise on their advantage in providing specialised products and services locally. Often these are sold to large companies who subsequently export the finished product.

Obstacles to the Development of Small Firms

Ireland needs more small firms and needs them to grow more rapidly. The small business sector of the economy expands rapidly in response to increased output from the large firm sector. The first requirement for a fast-growing small firms sector is the maintenance of favourable conditions for the expansion of industry generally such as competitive inflation rates, interest rates, taxation rates, and a efficient productive infrastructure including good quality roads, telecommunications, shipping, air freight, education and training networks. The personal and corporate tax regime must encourage people to set up and develop small businesses by providing an adequate reward to the risks undertaken.

Industrial incentives directed towards improving the capacity of small firms to recruit additional staff; to install modern equipment or to develop existing staff make excellent economic sense. The recent report and recommendations of the Advisory Committee on Management Training to the Minister for Labour recognised the resource constraints of small businesses, and recommended that incentives to be provided to help small businesses draw up and implement management programmes.

Technological change particularly in relation to information technology is making it possible for small firms to conduct processes at a level of sophistication and quality which would have been impossible some years ago without massive capital investment. Production schedules can be planned with the aid of computer programmes. Processing times can be reduced and the accuracy and reliability of manufacturing processes controlled within tight margins. It is possible for small firms to have on-line access to data bases in other countries such as Tender Electronics Daily which provides information daily on public contracts open for tendering in many parts of the world. In this way market costs can be considerably reduced, and the investment required to obtain orders held to a minimum.

However while these technological changes have made it easier for small firms to tackle projects which in earlier years had been the preserve of their larger counterparts, large firms are also gaining from new technology.

The division of work between large and small firms will vary from sector to sector. Thus newspapers can be composed and edited centrally, and printed simultaneously at a large number of distribution centres which are franchised locally. Flexible manufacturing systems are making it possible for large firms to manufacture economically small batches of products which heretofore would have required costly production line alterations, resulting in this type of low volume manufacture becoming the preserve of small business.

Outlook

For over twenty five years Irish industry has been increasing its share of the European market . This trend has accelerated in recent years. The structure of industry in Ireland and throughout the Community has become more specialised. This pattern is likely to continue. Irish firms are likely to concentrate on a narrow range of products for the total European market. European industry is likely to expand more rapidly as the benefits of the Internal Market make it more competitive. The faster growth of industry generally will create a more favourable expansion climate for the expansion and creation small firms.

There will be more opportunities for sub-contracting firms to supply sophisticated components to large firms. The growing affluence of the European market will create a greater demand for highly differentiated consumer products ranging from farmhouse cheeses to fashion garments, and specialised computer programmes. The firms most likely to be successful are those which obtain early access to market and technical information; have mastered the most modern and economic production processes and who have the managerial capacity to identify market niches which will make the best use of the firm's resources of manpower, machines, and money.

In summary the Completion of the Internal Market is likely to present far more opportunities than difficulties for firms which achieve substantial improvements in productivity each year through innovation, technological change, education and investment. In this way Irish industry can continue to increase its share of the European market, and small firms can both continue to multiply and to expand.

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