



Confederation of Irish Industry

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Speech by Liam Connellan, Director General, Confederation of Irish Industry, at the Industrial Members Conference of the Leinster Society of Chartered Accountants at the Berkeley Court Hotel, Dublin on Friday, 19 September 1986 at 8.00 p.m.

IRISH INFLATION MUST BE REDUCED BELOW THAT OF OUR MAIN TRADING PARTNERS AND THIS REDUCTION MUST BE REFLECTED IN GOVERNMENT BUDGET ESTIMATES

The reduction in the annual rate of inflation to 3.1% which was announced yesterday brings Irish price increases closer to those of our main trading partners. It results from the 2% annual decline in Irish wholesale prices and the fall in import and export prices. Irish inflation is, nevertheless, still almost three quarters of a percent higher than that of our competitors.

It is essential that Irish inflation falls below the level of our trading partners to offset the competitive losses resulting from the relative strength of the Irish pound. The trade weighted exchange rate of the pound is now about 5% higher than its average value in 1985. This has resulted in

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lower prices for competing imports, and a higher cost of Irish exports. In order to sustain the competitiveness of the economy our inflation rate must be reduced well below the average of our trading partners over the next year.

The cost competitiveness of the economy is determined by the combination of exchange rate movements and domestic cost inflation. When our currency strengthens, costs must be reduced accordingly if competitiveness is to be maintained. When this does not happen, orders are lost for Irish products and industrial production falls. This was one of the main reasons for the slide which occurred in order books, exports and manufacturing output over the last six months.

The currency realignment of early August reduced the degree to which the Irish pound had revalued over its 1985 average level from 10% to slightly less than 5%. This strengthening has to be offset by lower Irish inflation.

In 1987 the EEC rate of inflation is forecast by the European Commission to be 3.1% compared with 3.5% this year.

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On the basis of present exchange rate relationships, the Irish pound will be significantly higher next year than it was in 1985. Irish inflation must, therefore, be considerably lower than average European inflation in 1987 if some of this competitive loss is to be restored.

This is one of the main factors within Irish control which can ensure higher industrial output and employment. No amount of state incentives can substitute for an uncompetitive escalation of domestic costs.

This year we have seen that when too high an inflation rate was assumed in the preparation of the Government estimates, no subsequent downward adjustment in expenditure budgets was made to take account of the lower actual level.

It is therefore of the utmost importance that when preparing public expenditure estimates for 1987, Government, which controls a budget equivalent to two-thirds of national output, should give a clear lead setting an inflation rate standard considerably

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lower than 3%. This approach would demonstrate a
commitment to the creation of the low inflation
conditions which are necessary to maintain
competitiveness.

For the first time in many years, Irish industrial
output this year is growing less rapidly than that
in many other EEC countries mainly because of a
significant decline in cost competitiveness. The
combination of a stable exchange rate and a lower
inflation than our competitors in 1987 would ensure
that the modest recovery in manufacturing output,
which may occur in the fourth quarter of this year,
can gather strength during 1987, and that there
could be a nett increase in employment for the first
time in many years.
