IRISH HOTELS FEDERATION

Submission to the Low Pay Commission

on the

National Minimum Wage in 2019

February 2018

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1. Introduction

This submission follows the broad approach of previous submissions. As noted in these previous submissions the Irish Hotels Federation (IHF) supports a national minimum wage for all workers but such a rate must be appropriate, competitive and affordable.

IHF agrees with the comment in the 2017 Low Pay Commission (LPC) (page 1) report that

"….minimum wages alone are not sufficient as a poverty alleviation strategy. Other policies are required to deal with items such as exceptional housing and childcare costs"

Consequently, an increased focus should be placed on social policy measures and interventions as opposed to increasing the level of the national minimum wage to deal standards of living impacted by market failure.

The LPC is considering what, if any, changes should be made in 2019 to the current National Minimum Wage of €9.55 per hour and the associated sub-minimum rates for young people and trainees. The current rate applied from January 2018. This followed submissions in March 2017, the LPC report in July 2017 and a Government decision accepting the recommendation resulted in a ministerial order applying the new rate from January 2018. The changes, if any, currently being discussed will apply from January 2019, or later if the IHF recommendations are accepted. Consequently, as previously argued by IHF, the LPC should give a stronger emphasis to future expectations about the national and international economy, other factors such as exchange rates, the labour market performance and rate of inflation in its deliberations. The IHF acknowledges the difficulties of having a very up to date and projected empirical assessment in light of the time lags associated with data availability.

For reasons discussed below in the submission the IHF recommends that there should be no increase in the current rate for 2019. The IHF also recommends that the sub-minimum rates should be retained at their current relativities. The IHF acknowledges that the current implementation of the minimum wage is as a "national" rate. The IHF argues below that specific regional and rural economies and hotel/guesthouse activities and other specific sectors operate in a fundamentally different economic and business environment to the national economy and the economies of the large cities and traditional strong tourism locations. These weaker geographic areas and specific sectors should receive increased emphasis in deliberations and decisions on the national minimum wage rate fixing.

The IHF welcomes the additional data acquisition and analysis which has been done by the LPC in the past year. As argued in this and previous submissions and in the various LPC reports, and as identified in the new data, minimum wage employees have above average representation in certain industries. Certain sectors are also characterised by relatively low earnings primarily because of their business and economic circumstances. Such industries are more vulnerable to labour cost increases than high earnings sectors. The LPC should pay particular attention to the sectoral issues of these industries when deciding on the appropriate minimum wage rate rather than depending on economy wide assessment. A focus on specific sectors would produce better analysis of the effects of minimum wage increases. For example, national productivity levels and international comparisons present Ireland in a good light but this is heavily due to the impact of multinational enterprises. A different picture emerges at the more detailed sectoral level. The particular issues the Commission is obliged by legislation to have regarded in considering its recommendation are:

(a) changes in earnings during the relevant period,

(b) changes in currency exchange rates during the relevant period,

(c) changes in income distribution during the relevant period,

(d) whether during the relevant period— (i) unemployment has been increasing or decreasing, (ii) employment has been increasing or decreasing, and (iii) productivity has been increasing or decreasing, both generally and in the sectors most affected by the making of an order,

(e) international comparisons, particularly with Great Britain and Northern Ireland,

(f) the need for job creation,

(g) the likely effect that any proposed order will have on — (i) levels of employment and unemployment, (ii) the cost of living, and (iii) national competitiveness.

The IHF recognises that it is difficult to make a direct empirical link between the supporting analysis undertaken by the LPC and the specific recommendation on the minimum wage rate. However, there should be a strenuous effort to clearly identify why and how a specific analysis leads to a particular recommendation. In particular, there seems to be very little direct linkage between the detailed analysis of the LPC and its specific recommendation. For example, why was the 2017 report recommendation for a 3.2% increase given the relevant 0.3% increase in the cost of living.

IHF notes, as already mentioned above, that the 2016 and 2017 LPC reports reject the idea of a regionally differentiated minimum wage. However, it is essential that consideration of the size of the national minimum wage should take into account regional economic circumstances which are of great significance in the hotel/guesthouse sector. Increases in the national minimum wage can also generate additional relativity type wage cost increases.

The 2017 LPC report noted that included in the main arguments presented for the "no increase in 2018" case were:

- Brexit and its effects (such as exchange rate of Sterling)
- Regional differences in economic performance
- Competitiveness
- Knock-on pay claims to retain relativities

These issues continue to be valid concerns of the hotel/guesthouse sector for the 2019 minimum wage level.

2. Labour and Earnings Structure of Hotel Sector

The average economy labour and costs situations do not adequately represent the hotel sector. They give a completely misleading impression of the labour costs role in the sector. The hotel sector in Ireland and internationally is characterised by high labour intensity and very high labour cost to revenue and labour cost to gross value added ratios. These factors should be borne in mind by the LPC. The hotel and wider hospitality sector is particularly vulnerable to changes in labour costs. The higher the labour share of overall production costs the greater the burden felt by a sector from a labour cost increase, other things being equal.

The role of labour costs in turnover and gross value added is shown below for a sample of sectors. Official CSO data is used as this allows a comparison between hotels and other sectors and supports transparency. This data illustrates the fundamental difference between the hotel/hospitality sector and several other sectors. The latest CSO data is for 2015 with some sectors available only for 2014. The sample includes indigenous manufacturing sectors such as food, high technology manufacturing sectors such as chemicals and computers and a range of services sectors including retail, wholesale, computer services and accounting.

The CSO sectoral comparative data are shown below and labour costs relative to gross value added and turnover are shown. Gross value added (GVA) refers to the value added generated by the sector. In effect it is turnover less bought in materials. GVA is a more accurate measure of the economic contribution of a sector than turnover. However, the payroll to turnover ratio is also an important business and economic indicator.

Table 2.1 Labour Costs as percentage of Turnover and Gross Value Added 2015

	Turnover	GVA
Manufacturing	4.6	11.3
Food	7.4	22.5
Beverages	7.3	15.7
Chemicals	6.8	18.7
Pharmaceuticals	3.0	9.9
Computer electronic and optical products	9.9	41.7
Retail	14.7	66.5
Wholesale	5.3	51.0
Air transport	9.5	29.7
Hotels	38.4	75.7
Restaurants	36.7	85.7
Beverage serving	33.2	78.7
Computer programming, consultancy	6.2	44.0
Accounting auditing	51.7	71.1

Source: CSO CIP and Annual Services Inquiry, all services refer to 2015, food and manufacturing refer to 2015 and the other sectors refer to 2014. The manufacturing total figures vary greatly between 2014 and 2015 due to the measurement issues in 2015.

The vulnerable position of the hotel sector arising from labour costs is clearly illustrated by the above official CSO data. In manufacturing labour costs amount to 4.6% of turnover. Within manufacturing, the chemicals sector is 6.8%, the pharmaceuticals sector is 3.0%, the food sector is 7.4% and the beverages sector is 7.3%. Within services the ratios also vary, wholesale is 5.3% and retail is 14.7% with hotels at 38.4%. Air transport is 9.5% and computer programming is 6.2%. Of the listed sectors hotels, at 38.4%, have one of the highest labour costs to turnover ratios. Accounting and auditing, at 51.7%, is higher than hotels. Restaurants and beverage serving activities are also high at 36.7% and 33.2% respectively.

This conclusion is reinforced by the labour costs share of GVA. Labour costs amount to 11.3% of GVA in manufacturing compared to 75.7% in hotels. The manufacturing figure is, of course, influenced by the accounting practices of the inward multinational sector and also the additional measurement issues of 2015. The food sector has a labour cost to GVA ratios of 22.5%. The other services sectors in the table are above the hotel ratio with the exceptions of the other hospitality sectors of restaurants and beverage serving enterprises. The hotel sector is a very labour intensive industry and is very vulnerable to wage induced cost increases. Three quarters of its gross value added is accounted for by labour costs. The CSO data indicate the very large role of labour costs in the hotel business model.

The hotel sector provides many highly skilled jobs such as managers, accountants marketing executives, HR executives and IT specialists. However, to provide the required level of service, it also employs large numbers of lower skilled occupations. Consequently it has a higher proportion of lower paid persons than other sectors. This means that wage cost is a significant business issue for hotels, unlike many other sectors.

The hospitality sector is of significant strategic importance in the Irish economy and in economic and regional development policy and Government has ambitious growth targets for the hospitality sector.

The new CSO data on the minimum wage (CSO statistical release QNHS – National Minimum Wage Estimates, April 2017) show the regional variation in the role of such employees. While 10.1% of employees are paid the NMW or less, the proportion in Dublin is 8.3% and at the other extreme is 14.3% in the Border region and 13.2% in the South-East region. Increased levels of the NMW have a larger impact on the regions.

The differential regional impacts are further illustrated by the regional breakdown of payroll share data available from the Hotel Industry Survey data. WS refers to Western Seaboard. The CSO estimates refer to "hotels and similar accommodation" and the Hotel Industry Survey refers to "hotels".

Table 2.2 Payroll as % of Revenue by Region

	Dublin	M & E	SW	WS
2016	30.0	37.5	37.1	36.4

Source: Ireland Annual Hotel Industry Survey 2017

The four regional shares range from 30.0% to 37.5%. Labour cost as a share of revenue is much higher in the three non-Dublin regions than in Dublin. It is clear that the three non-Dublin regions are particularly vulnerable to increases in the national minimum wage rate.

3. National and International Economic and Labour Market situation

The international economic situation in 2018 and 2019, with the exception of the UK, is relatively good. The latest Winter EU economic forecasts in February 2018 present a relatively optimistic picture of EU growth despite the impact of Brexit. The economies which are critical for Ireland in terms of both exports and inward tourism are all expected to grow but the UK growth will be low and declining. The EU economy is expected to grow at 2.3% and 2% in 2018 and 2019 respectively. German growth will be 2.2% and 2.1% respectively for the two years. France will grow by an average of about 1.9% in each year. The USA will grow by 2.5 and 2.1% in 2018 and 2019. However, the UK performance is a major problem for the hotel sector and the economy generally. Despite short term resilience related to Brexit the UK is expected to grow by a low 1.4% in 2018 and an even lower 1.1% in 2019. Coupled with the Sterling exchange rate this suggests a continuation of the difficult 2017 for Ireland in the British and Northern Ireland tourism markets.

Table 3.1 Current Expectations of GDP Growth% volume 2017, 2018 and 2019

	2017	2018	2019
USA	2.2	2.5	2.1
EU	2.4	2.3	2.0
Euro area	2.4	2.3	2.0
Germany	2.3	2.2	2.1
France	1.8	2.0	1.8
Italy	1.59	1.5	1.2
UK	1.8	1.4	1.1
Ireland	7.0	4.4	3.9

Source: EU Autumn 2017 and Winter 2018 Economic Forecasts. OECD Autumn Economic Forecasts 2017. Central Bank Jan 2018 Economic Forecasts

On the assumption that there is not a significant worsening of the international economic environment the Irish economy will perform reasonably well over the next two years, but with a much lower growth performance than in 2017, with the Central Bank expecting growth of 4.4% and 3.9%. Consumption will grow by about 2.7% and 2.5% in 2018 and 2019. However, there are significant uncertainties associated with these forecasts, especially with the UK performance. In addition to the general international macroeconomic risks the economy will have to cope with Brexit and the continuing lower value of Sterling. It should be noted that the 2019 growth rate is expected to be substantially below the 7% growth of 2017 although the consumption growth will be close to the 2017 performance.

With employment growth continuing and unemployment declining. The move towards full employment should ensure that appropriate or commercially justified levels of sectoral wages are realised without increasing the regulated wage level.

4. Exchange Rates

The Brexit-related decline in the value of Sterling has had very significant negative economic implications for the hotel sector in 2017 and this will continue into 2018 and 2019. The sector depends heavily on the British market. Britain accounted for 41% of visitors in 2016. The decline in the value of Sterling has substantially reduced the competitiveness of the Irish hotel sector and this is a factor which is outside the control of both the Irish government and the hotel sector. British visitors declined by 5% in 2017. Other markets performed well and overall there was an increase in international visitors. There was also a decrease in visitors from Northern Ireland and some counties and localities are more dependent on the UK market than the average national position.

In January 2018 the euro was worth £0.88331. In January 2017 the value was £0.86100 and in January 2016 it was £0.75459. This is a substantial loss in competitiveness over two years of 17.1%. There is no expectation that Sterling will recover this lost value in 2018. At best it will experience small changes in either direction. However, poor performance in the Brexit negotiations could result in a further decline in Sterling. It should also be emphasised that the hotel industry has to continue to carry the burden of the decline in Sterling. It is an ongoing burden as opposed to a once-off temporary change. The central bank is assuming a rate of £0.89 for 2018 in its macroeconomic forecasts.

At minimum, however, it is not expected that Sterling will appreciate sufficiently to boost Irish competitiveness in 2018. The Sterling decline has reduced Irish national and tourism competitiveness. The negative effect on the UK market has been seen. The lower value of Sterling will also encourage a switch from Irish domestic holidays and breaks to the UK market and a switch by foreign tourists from Ireland to Britain. It may also result in British tourists spending less on their Irish trips. Irish domestic trips performed poorly in 2017.

As emphasised in our previous submission, the public policy aim should be to find ways to restore the lost cost competitiveness and to avoid additional reductions in competitiveness such as an increased minimum wage.

5. HICP Inflation

The central bank, as of January 2018 reported an average 2017 increase of 0.3% in the HICP and is predicting an HICP increase of 0.7% in 2018 and 0.9% in 2019 but excluding energy the predicted 2018 increase is only 0.3%. Very small overall price increases are expected in 2018.

6. Tourism and Hotel/Guesthouse Performance

Except for the important UK market, Irish international inward tourism performed reasonably well in 2017, but with much lower overall growth than in 2016. Overseas visitors to Ireland increased from 8.036 million in 2015 to 8,742 million in 2016, an increase of 8.8%. In 2017 the increase was only 2.6% to 8.967 million.

The British market was 3.346 million in 2015, 3.632 million in 2016 and 3.387 million in 2017. There was a decline of 6.7% in the GB market in 2017. In addition, trips from Northern Ireland also dropped by 6.7%from 1.356 million to 1,267 million in 2017. We are surprised that the deliberations of the LPC do not reflect the UK position to a greater extent.

The domestic market which supplies the bulk of demand for hotels and guesthouses had a weaker performance. In the first three quarters of 2017 domestic trips decreased by 0.2% compared with the same period in 2016. The growth in inward overseas tourism performance gives an exaggerated positive image of the overall hospitality and hotel/guesthouse performance when the domestic market is included.

The Ireland Annual Hotel Industry Survey reports that in 2016 56.8% of hotel business was sourced from the domestic market with 7.8% from Northern Ireland and 35.4% from overseas. In addition to bed nights the hotel industry depends greatly on the domestic market for a wide range of revenue generating functions.

Overall, the industry has performed well over the recent past but with large regional variations. This followed a long period of weak performance since the economic collapse in 2008. Room occupancy has increased from 67.8% in 2014 to 71.1% in 2015 and to 74.0% in 2016. Profit before tax per room (excluding financing costs) has increased from €9,201 in 2014, to €11,990 in 2015 and to €14,558 in 2016. These are average national figures and there are substantial regional variations as shown in the next section of this submission. The national figures exaggerate the strength of much of the rural and regional hotel sector.

7. Regional Issues

As noted in this and the previous IHF submissions to the LPC, the economic recovery is not evenly spread throughout the country. The economic recovery as measured by GDP or GNI modified growth, employment increases and lower unemployment has not been felt evenly throughout the country. This is particularly the case in tourism and the hotel sector. Dublin is performing very well, followed by some other urban centres and traditionally strong tourism locations but there are many hotels and locations in the third group where there has been limited recovery and where hotels and guesthouses struggle. The IHF is concerned that the LPC has not paid sufficient attention to the weak regional and rural economies within the national economy in deciding on the appropriate rate for the national minimum wage.

The LPC has noted that the economic recovery is spreading to the regions. However, there is a wide spread of regional performances. Based on the pre-revision (new Labour Force Survey) employment data, all eight regions experienced increases in employment over the 2012/2017 period. Therefore all regions have shared in the jobs growth. However, the rate of growth is not evenly distributed. The West had the worst performance with only a 4.7% employment increase compared to 16.3% in the Midlands which was the best performing region over the period.

The Mid-West was the only other region to have single-digit growth. The other six regions had growth rates of 11% or higher. Dublin employment grew by 14.5% which was the third highest performance after Midland and South-East.

Table 7.1 Regional Employment levels and changes Quarter 2 2012 to Quarter 2 2017, thousands

Region	Quarter 2 2012	Quarter 2 2017	% change 2012/2017	Rank of regional growth rate
Border	174.6	196.7	12.7	4
Midland	105.2	122.4	16.3	1

West	179.5	187.9	4.7	8
Dublin	547.4	627.0	14.5	3
Mid-East	222.7	247.4	11.1	6
Mid -West	150.1	161.9	7.9	7
South-East	186.0	214.9	15.5	2
South -West	270.7	304.7	12.6	5
State	1836.2	2063.0	12.4	Not applicable

Source. CSO, QNHS

The 2016 Census of Population enables us to look at the county pattern of employment change compared with the previous 2011 census.

All 26 counties experienced employment increases between 2011 and 2016. However, there was a wide range of percentage increases. The highest increase was Louth at 13.8% and the lowest was Sligo at 2.2%. An East-West difference is clear from the figures. The top five percentage increases were all in Leinster, Louth, Dublin, Carlow, Wexford and Kildare. Four of the five lowest increases were in Connacht, Sligo, Mayo, Roscommon and Leitrim. Tipperary completes the bottom five growth performances.

Disposable income per person in 2014 (the latest data available) in the State as a whole was €19.2k. Dublin had an average disposable income of €22.0k while Donegal was at €15.1k. Monaghan was at €16.4k and Roscommon was at €16.3k. Dublin’s disposable average income was 46% greater than Donegal. There are substantial regional differences in disposable income per person.

There is also a substantial regional variation in hotel performance as noted above. The Ireland Hotel Industry Survey divides the country into four regions, Dublin, Midlands and East, South-West and Western Seaboard. A range of indicators is presented for the four regions in Table 7.2.

Table 7.2 Regional Variation in Hotel Performance 2016

	Room occupancy %	Average room rate €	*Profit before Int., Dep, rent & tax per available room €
Dublin	82.3	128.27	20,492
Midlands and East	68.5	91.40	11,821

South-West	68.9	93.25	10,273
Western Seaboard	68.3	79.77	9,479

Source: Ireland Annual Hotel Industry Survey 2017

**Profit before bank loan interest depreciation, rent and taxation*

Room occupancy is much higher in Dublin than elsewhere. The Dublin average room rate greatly exceeds those of the other three regions. Profit before tax per room in the Western Seaboard is less than half of the Dublin level. These regional differences in the hotel sector clearly have implications for the regional impact of a nationally determined minimum wage rate which does not take sufficient account of the regional economic characteristics. The IHF urges the LPC to take account of the evidence based regional business features of the sector.

8. Assessment and Recommendations

- The IHF supports a national minimum wage for all workers but such a rate must be appropriate, competitive and affordable and take account of sectoral and regional factors.

- There should be a greater use of various social policy instruments in addition to the minimum wage mechanism to support standards of living and to deal with specific costs such as housing.

- There should be no increase in the national minimum wage in 2019. The current Irish rate is already higher than the UK. In light of the decline in the British and Northern Ireland tourism markets and the likely continuing low value of Sterling and the uncertainties of Brexit, cost competitiveness is even more critical.

- Public policy decisions should consciously reflect the current and possible future negative direct and indirect economic impact of Brexit.

- The international macroeconomic outlook is reasonably good for 2018 and 2019 with the exception of the UK which is expected to grow by about 1% in 2019.

- While current Irish growth expectations for 2018 and 2019 are relatively good this growth performance will be lower than 2017 and there is a large degree of uncertainty attached to future performance due to Brexit.

- There has been a very small increase (0.3%) in the cost of living as measured by the HICP in 2017 and low inflation is expected in 2018 and 2019 (0.7% and 0.9% respectively).

- The decline in the value of Sterling has significantly lowered the competitiveness of the Irish economy and the hospitality and hotel sector relative to the UK. This will not improve in 2018 and 2019 and may further deteriorate. The sector and the economy have to cope with this structural and long-lasting competitiveness deterioration.

- Public policy should seek to support competitiveness whenever possible and not to worsen it with an increase in the national minimum wage.

- The hotel sector is a labour intensive industry and is vulnerable to wage induced cost increases given the very large role labour costs play in the hotel business model. National level analysis should be supplemented by sectoral analysis in making decisions on the national minimum wage.

- The hotel and wider hospitality sector, as is the case internationally, has very high labour cost to revenue and labour cost to value added ratios which make it vulnerable to minimum wage increases. In addition, the hotel sector is open to severe international competition both for domestic tourism and international inward tourism and has been badly hit by the decline in the value of Sterling. These factors should receive strong consideration in the LPC's deliberations.

- The hospitality sector is of strategic importance in terms of future national and regional economic development and the Government has set ambitious targets for the sector. Its strategic role and the need to support national and regional competitiveness should be recognised in the LPC's deliberations.

- Specific regional and rural economies and very many hotels/guesthouses operate in a fundamentally different economic and business environment to the national economy and the economies of the large cities and traditional strong tourism locations. These weaker areas should receive increased emphasis in deliberations and decisions on minimum wage rate levels. The differential regional performance has been identified in this submission.

- There has been a substantial decrease in inward tourist numbers from Britain and Northern Ireland and the domestic market, which accounts for 57% of hotel business, declined very slightly in 2017.

- The excellent national inward tourism performance and the Dublin hotel performance give an exaggerated image of the overall hospitality and hotel/guesthouse performance and economic position.

- The Dublin average hotel room rate greatly exceeds those of the other three regions. Profit before interest, depreciation, rent and taxation per room in the Western Seaboard is less than half of the Dublin level.

- In light of the existing and likely exchange rate performance, Brexit, the small increase in the price level comparing the average price levels of 2016 and 2017, the decline in the UK inward tourism numbers, the labour cost characteristics of the hotel and wider hospitality sector, the weak economic position of many rural and regional areas and the still uncertain position of many hotels, the IHF recommends that there should be no change in the level of the national minimum wage for 2019.

- The IHF also recommends that the sub-minimum rates should be retained at their current relativities.

- Where increases are proposed in the future the LPC should clearly show the detailed link between its economic and other analysis and its recommendation.