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EXECUTIVE SUMMARY

This document contains the Regional Report developed by Innovate in Ireland. The aim of this Report is to show off a picture of the region and the state of the art on the innovation field. The final objective is to create a image on how creativity techniques can benefit the sme's in the country.

2 PROFILE OF THE REGION

This section of the report describes the Border Midland and Western Region in Ireland. To do thus the following areas are examined: demographic, infrastructure, industrial and technological infrastructure, social and cultural, education and entrepreneurship issues. Each of these aspects is examined in more detail below.

2.1 Demographic aspects

The surface area of the Border Midland and Western Region (BMW) in Ireland makes up 47% of the total surface area of the state but the demography represents only 27% of the population. Urbanisation is relatively low with as little as 32% living in towns with a population of more than 1500 persons. The counties of Mayo, Sligo, Donegal, Leitrim, Monaghan, Louth, Longford, Laois, Cavan, Roscommon, Galway, Offaly and Westmeath make up the BMW Region.

In comparison on a national level to the Southern and Eastern (S&E) Regions of Ireland and other more affluent European Regions, the Border, Midlands and Western (BMW) Region is relatively sparsely populated and rural in nature. Traditionally agriculture has been the main industry within this region. This Region has been something of a black spot and has suffered from high levels of immigration mainly due to lack of employment. The average working age is higher in comparison to the national average indicating that a large percentage of the younger population have immigrated in search of employment. In addition, the population growth for the first half of the last decade is almost half that of the national average.

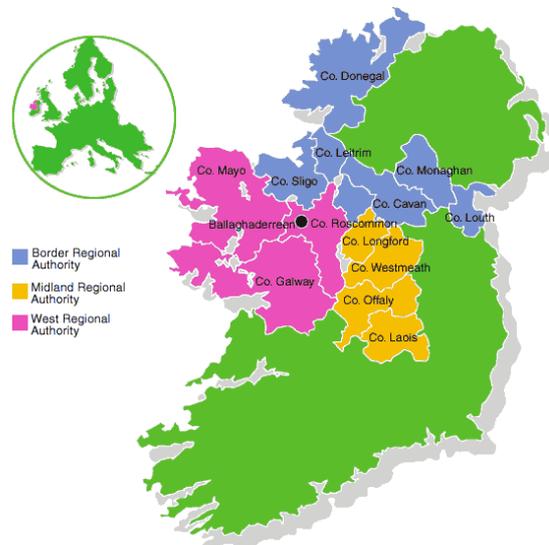


Figure 1-BMW Region of Ireland

2.2 Infrastructure

In comparison to most continental European countries the Irish national infrastructure is poor and undeveloped. The upgrade of all major road, rail, sea and air networks have been of up most importance for the last number of years, especially during the economic prosperity during the late nineteen nineties and the few years of the new millennium. A National Development Plan (NDP) in association with the European Union Structural Funds has been implemented with aim of improving infrastructure nationally. Currently as little as 4% of the population in the BMW Region uses public

transportation to get to and from their place of work again this is less than half the national average of 11% (NDP 2000).

In terms of accessibility, the Region has two fully international commercial seaports in Galway and Sligo, an international airport centrally located at Knock in Co. Mayo and several other small national airports in Galway, Sligo and Donegal. There are minor rail networks running from Dublin to Galway, Sligo and Castlebar in Co. Mayo however there is a definite need for the opening of a rail network servicing Cork, Limerick, Galway and Sligo servicing the western side of Ireland. The road network within the Region is below European standard. Many of the roads are non-national and minor. There is no major servicing of any of the large urban areas with the Southern or Eastern Regions although there are plans to do so under the NDP (2000).

2.3 Industrial and technological infrastructure

In economic terms, the primary production in the Region is agriculture, fishing, aquaculture and forestry. However, according to the department of Agriculture much of the land is classified as "severely handicapped" and the region is dependant on income supports from local and EU government agencies. For the most part all manufacturing and secondary industries are confined to the major urban areas with Galway city and Sligo being the largest. A high percentage of the industry in this sector is in the medical devices and healthcare environments.

The service industry has been steadily increasing and now represents 51% and is the largest single sector within the Region. This is likely to grow especially within the Tourist industry. Almost all of the landscape is natural and unspoilt with some beautiful and breathtaking coastline and mountainous terrain. The entire Region only generates 19% of the total national GDP.

The Region's labour force represents a quarter of the total national working force. Nevertheless, there are large differences regarding unemployment levels, skilled/qualifications and female participation in comparison to the total labour force. For instance, employment levels rise more slowly than the national average. A smaller percentage of employees have completed second or third level education and the number of unskilled labour is higher than the rest of the country.

Within the Region there has been a reduction in employment in SMEs. Many of the problems facing SMEs in the Region today are as follows:

- Many firms are too small and cannot achieve critical mass or economies of scale
- Need to export earlier
- Devote insufficient resources to Marketing / Sales
- Achieve low productivity / added value levels
- Emerge from product ideas rather than market opportunities
- Are financially undercapitalised or over borrowed
- Only marginally profitable
- Do little product or market research and lack the capacity to innovate
- Short management expertise and resources
- Lack a strategic perspective.

There is strong involvement both locally and nationally from Government and local authority organisations supporting the development and growth of SMEs across the region. These organisations include:

- IDA- Irish Government agency with responsibility for securing new investment from overseas in manufacturing and internationally traded services sectors.
- Enterprise Ireland -is the government agency responsible for the development of Irish industry specifically within the area of Technology Innovation, Business Development and Internationalisation.
- Údarás na Gaeltachta –Responsible for economic development in the Gaeltacht regions
- FÁS – National employment and training agency.
- Bord Bia (Irish Food Board) - acts as a link between Irish food and drink suppliers and existing and potential customers.
- Forfás- The National Policy and Advisory Board for Enterprise, Trade, Science, Technology & Innovation in Ireland.
- City and County Enterprise Boards (CEBs) – These bodies are locally controlled enterprise development companies established in each county and larger urban local authority areas.
- Shannon Free Airport Development Company Ltd- Developed under the NDP, concerned with attracting investment to the Shannon region.
- ISME- An independent voice for SMEs throughout the country.
- Bord Fáilte - The Irish Government Agencies, responsible for the development and promotion of tourism in the Republic of Ireland.

In addition to these organisations and especially in recent years with the information Technology (IT) revolution there is increased involvement and collaboration between third level institutes and industry. All third level institutes within the Region have strong links with local firms and continue to foster and support entrepreneurship and innovation among SMEs. Many serve as incubators, liaison offices and technology transfer institutes for many micro and small enterprises especially those close to the education facilities themselves.

2.4 Social & Cultural

To quote Kottak (2000), "culture is that complex whole which includes knowledge, belief, arts, morals, law, custom, and any other capabilities and habits acquired by man as a member of society". Customs help to tie the Irish together and express their character. Ireland is steeped in traditions, superstitions, customs and tales of old with a rich literary tradition, culture, heritage and history. The culture of Ireland and the Irish people continue to influence all cultures that come into contact with the Irish. Modern Irish culture was formed from a mixture of ancient traditions, religion, and interactions with non-Irish people. The uniquely Irish cultural aspects as listed below:

- **Language:** Irish (Gaelic) and English are the two official languages of the Republic of Ireland and official documents; street and road signs are all bilingual. In Gaeltacht areas Irish is spoken daily, however English spoken throughout the country.
- **Literature** With four Nobel Literature prizewinners in the last century, Ireland's literary pedigree is world-renowned. Past and present Irish writers have inspired audiences through storytelling and the written word.
- **Music:** The Irish have always loved their music and this close relationship dates over the centuries to the present day. The harp, perhaps the most distinctive of all Irish instruments, is a symbol of this harmony of people and music.
- **Sport:** The mainstream sporting and recreational activities in Ireland consist of Gaelic Football and Hurling the two national sports. In addition all major sports

such as soccer, rugby and athletics are also very popular. Ireland is renowned for breathing scenery with excellent fishing and wonderful golf courses. Sport is an important part of the modern Irish social culture.

- **Customs and Traditions:** Ireland is very much a western civilised democratic republic with first world values. However, tradition still plays an important part in the everyday Irish life. Family values, catholic religious beliefs and community spirit are still very prevalent throughout the country especially in rural areas.

2.5 Education

The quality of Ireland's education system is exceptionally high. The Independent IMD World Competitiveness Report (2003) rates Ireland as one of the top countries in how its educational system meets the needs of a competitive economy (see Table 3). In 2003 55, 374 students sat their Leaving Certificate Examination equivalent to the British A level examinations to obtain entry to third level. The current third level student population has increased by almost 37% between 1992 and 2002. Of the 48,000 graduates in 2004 over 57% were in the Engineering, Computer/Software Engineering, Business Studies and general Science fields indicating the current shift in employment trends towards a knowledge based economy (IDA 2004). Almost 1 million people are in full time education. 60% of school leavers go on to third level education.

In terms of Education the BMW region is successful in producing third level graduates with 11% of the population graduating from a third level institute. This is one percent higher than the national average. However with 28% of the national university students only 13% less than half of all graduates are employed in the BMW Region. Again the lack of employment and lower level of economic and social development are major contributors to the lack of local employment for third level graduates. With respect to Research and Development (R&D) the Region received 12.6% (€80.4M) of funding for its 3rd level institutes between 2000 and 2002 (CIRCA Audit on Innovation in BMW Region, 2004). According to the same report the Region secured only 8.5% of the States national funding for industry related research associations during the same period.

One of the reasons why so many companies choose Ireland is because of the unique workforce - Ireland has the youngest population in Europe with over 40% under the age of 25 years. They are also highly educated and highly motivated. Irelands total investment in knowledge, including investment in public and private spending on higher education increased by an average annual rate of over 10% over the past decade compared with averages of around 3% by the EU and the OECD (IDA 2003). Traditionally it has been shown that foreign investors consider the quality and the 'can do' flexible attitude of Irish people to be two of the country's greatest advantages.

2.5 Entrepreneurship

According to the Global Entrepreneurship Monitor (GEM) report (2007) an average of 2,700 entrepreneurs established new businesses every month in Ireland from January 2004 to June 2007. The authors of the GEM Report state that 'Ireland continues to be to the fore in Europe and the OECD in terms of the numbers among its adult population that are engaged in entrepreneurial activity' (p.13). They note that:

- Ireland ranks 6th in the OECD for nascent entrepreneurs (i.e. people actively planning to start their own business).
- Ireland ranks 3rd in the OECD for new firm entrepreneurs.

This suggests that the Irish, as a nation, have a strong entrepreneurial spirit. A synthesis of many government funded reports (e.g. GEM Report 2007; The Report of

the Small Business Forum 2006; Forfas Report on Entrepreneurial Policy 2007) reveals that some of the factors that facilitate entrepreneurship in Ireland include:

- A strong entrepreneurial culture
- An increasing number of role models
- A pro business government policy
- Positive media
- A growing population

These reports also highlight that some of the obstacles to entrepreneurship in Ireland include:

- Difficult to access early stage finance
- The small size of the home market can limit growth opportunities
- Rising costs and their impact on competitiveness
- Too much regulation
- Slow rate of commercialisation of research from the third level sector
- An educational sector that does little to address the lack of skills

In light of this, it is imperative that Ireland Inc. seeks to optimise its strengths in order to exploit all possible opportunities. This is particularly important in this climate, where competitiveness and productivity are reduced and Ireland is facing into an era of economic uncertainty. It is also imperative for the Irish government and business owners to create policies and procedures in an attempt to alleviate some of the obstacles or limitations to successful entrepreneurship.

3 PROFILE OF SMALL TO MEDIUM SIZED ENTERPRISES (SMES)

Over 97% of businesses operating in Ireland today are 'small' – they employ fewer than 50 people. There are approximately a quarter of a million small businesses in Ireland. This figure represents more than half of the total private sector, non-agricultural workforce. Small businesses are important for a number of reasons:

- They provide regionally distributed employment around the country, deliver a huge range of local services, and contribute to the economic, social and cultural life of the entire population.
- They pay 50% of VAT on services (over €4 billion), 11% of corporation taxes (around €530 million) and 37% of income taxes (€4 billion).
- They form an essential part of the supply chain for larger firms, and in particular are part of the support infrastructure needed to attract and retain foreign investment.
- The performance of the small business sector is thus an important contributor to the overall quality of life and standard of living in the country.

The Irish market has grown very substantially: the population – and particularly the number of people in work – has increased. In short, there are more people with more money to spend. In this positive environment, over the ten years since 1995 the small business sector has flourished: the number of small businesses in Ireland has grown by more than 50%, and employment in small businesses has grown by approximately 79%. Economic growth, however, has created a number of difficulties for businesses in Ireland. Small companies are facing greatly increased competition from companies with lower cost bases; High inflation in recent years has contributed to sharp rises in business costs and small businesses have difficulty finding and retaining suitable skilled staff.

Irish companies are facing increased competition from major international players with highly sophisticated business models, coupled with economies of scale in every aspect of their operation. In this environment, only the strongest and fittest companies will survive. A number of trends have recently emerged that are of particular concern, and that present significant challenges for small businesses in the years ahead. These are discussed in more detail in this document.

As the Irish economy becomes increasingly knowledge-based, and as low value-added activities migrate to lower cost economies, a greater proportion of the country's wealth will have to be generated by indigenous companies. Whereas in the past, Irish indigenous companies have tended to start small and remain small, a new generation of indigenous companies is already beginning to emerge – companies with the potential to grow, and in some cases grow rapidly, to conquer international markets. The small business sector is the incubating ground for these companies. Some of them will be technology-based companies, who will exploit the State's substantial investment in R&D and help to assert Ireland's position as a knowledge creator and innovator. A greater proportion will be in services (reflecting the growth internationally of the services sector). These businesses will use highly innovative business models to grow and deliver internationally, services that were previously the preserve of small companies trading locally. The majority, however, will continue to deliver local services and to play their important role in the supply chain of larger companies. Small business owner/managers with the ambition, ability and potential to grow their companies into strong internationally trading entities must be empowered to reach this potential. Those that continue to trade locally largely determine the cost base for both consumers and other businesses, and these must be encouraged to innovate in other ways, in order to maximise their efficiency, quality of product and service, and productivity.

According to the Small Business Forum the business environment in Ireland has been radically transformed in the last 10 years:

- The Irish market has grown very substantially: the population – and particularly the number of people in work – has increased. In short, there are more people with more money to spend.
- The taxation regime has relaxed – for the vast majority of companies, corporation tax has been reduced to 12.5 per cent; the top income tax rate has been reduced to 42 per cent; and the capital gains tax rate has been halved to 20 per cent.
- Short-term interest rates are considerably lower (currently below 4 per cent, compared with 6 or 7 per cent in the mid 1990s).

In this positive environment, the small business sector has flourished over the last ten years: the number of small businesses in Ireland has grown by more than 50 per cent, and employment in small businesses has grown by approximately 79 per cent. Economic growth, however, has created a number of difficulties for businesses in Ireland:

- With the liberalisation of international trade and globalisation of markets, small companies are facing greatly increased competition from companies with lower cost bases.
- High inflation in recent years has contributed to sharp rises in business costs.
- The labour market is considerably tighter (unemployment is now around 4 per cent); as a result many businesses have difficulty finding and retaining suitable skilled staff, and wage rates are increasing.

In the years immediately ahead, the pressure on Irish companies to perform to the highest international standards will be heightened by intensifying international competition. Irish companies – whether trading locally or in foreign markets – will increasingly face competition from major international players with highly sophisticated business models, coupled with economies of scale in every aspect of their operation. In this environment, only the strongest and fittest companies will survive.

In light of this, a number of issues need to be addressed if the small business sector is to realise its full potential and play the increasingly important role in the Irish economy that will be demanded of it in the years ahead.

This report was compiled by the Small Business Forum, Ireland and it profiles small businesses in Ireland. It examines the growth in small businesses, their contribution to the Irish economy and society, some trends and the performance of the manufacturing sector. Levels of entrepreneurial activity are also presented as well as the importance of indigenous sector. The challenges facing small business in Ireland are also identified. These include; access to finance; management capability; innovation; ICT audits for small businesses; better regulation; balanced local authority charges; access to information and advice as well as infrastructure.

4 CHALLENGES FACING SMALL BUSINESS IN IRELAND

In this changed business environment, there is broad agreement on the challenges facing small businesses today. The main issues identified include access to finance; management capability; innovation; ICT audits for small businesses; better regulation; balanced local authority charges; access to information and advice as well as infrastructure. Each of these is briefly discussed in more detail below.

4.1 Access to Finance

While the problem of funding for small business has eased somewhat over the past decade with the improvement in the investment environment and the drop in short term interest rates, small businesses continue to report difficulties in obtaining appropriate levels of finance for start-up and growth. These difficulties appear to be more pronounced for: Businesses in the services sector, with limited capital assets; and Businesses that are ineligible for support from the enterprise development agencies. In particular, financial institutions are reluctant to lend money to businesses that are perceived to be risky or that have limited collateral, while under the current taxation regime Irish investors are more likely to choose one of the many asset-backed investment options than take equity stakes in small companies. The financial support provided by the enterprise development agencies does address this issue to some extent, but only for the limited number of businesses that are eligible for agency support. A separate issue relates to working capital and cash flow. Small businesses that supply goods and services to large organisations are often compelled to accept long delays in payment, either because of unreasonable contract terms, or because they are afraid to pursue on-time payment for fear of losing business.

4.2 Management Capability

The performance – and even the survival – of a small business depends on the competence and capability of its management. The quality of management affects productivity, profitability and sales growth. Work carried out in Ireland has shown that the level of general management skills in Irish small businesses is relatively poor, particularly in specific functional skills such as human resources, marketing and finance, and in forward planning and strategic management.

Despite these deficiencies, small firms engage in management training and development only to a very limited extent, both for reasons of time and cost, and because the available management training programmes are not perceived to be relevant. Given that economic progress in Ireland in the years ahead will depend heavily on the performance of the small business sector, it is critical that the management of these businesses be equipped with the knowledge and skills they need to make the businesses perform optimally. At present, resource constraints are not the primary barrier to enhancing management competence in the small business sector. Approximately €35 million per annum in public funding is available between 2006 and 2008 to support management training and development (including non-financial supports, such as mentoring), particularly in SMEs.

4.3 Innovation

Innovation is imperative throughout the enterprise sector as Ireland progresses towards a knowledge-based society. The type of innovation most often referred to is technological innovation, which is rooted in scientific research and development (R&D), but other types of innovation are also important, and more relevant to the majority of small businesses, particularly in the services sector.

Very few small businesses have the resources or the expertise to engage in R&D. Those that are unlikely to become R&D performers – and particularly companies in the services sector, should be encouraged to use the best available expertise to help them constantly adapt and be innovative in their businesses. This should help them to bring their operations into line with international best practice, to increase productivity and profitability, and to win new markets. The recommendation proposed overleaf will enable them to develop new service offerings, change their business models, improve their customer interface, cut costs, and adopt new technology.

A number of companies, however, have some in-house scientific or technological capacity, but not sufficient to engage in formal R&D activity. These companies should be encouraged and supported in making the transition to R&D performance. The intermediate step for them is to form significant productive relationships with outside sources of knowledge and technology, and in particular with the Institutes of Technology and other third-level institutions. Support should be made available to help such companies to form these relationships and acquire the knowledge they need to develop new products, processes and designs. These supports should stimulate innovation and awareness of innovation throughout the small business sector.

4.4 ICT audits for Small Businesses

The effective use of ICT by the entire small business sector will be critical to sustained productivity and growth in the years ahead. The Small Business Forum agrees with the assessment of the Government's eBusiness Strategy that many SMEs need to make better decisions about Information Technology (IT) investment, to manage the IT facilities they already have, and to make more and better use of these facilities. The Small Business Forum believes that the low uptake and limited use of ICT by small businesses is due to a low level of awareness of the benefits presented by the technology.

Addressing this issue will encourage businesses to adopt and exploit the available technologies in an optimum fashion, and thereby increase their productivity. The Forum recommends that €2 million be provided per annum over the next three years to meet this requirement. Clearly, such a scheme will be limited in the number of companies supported, but it should be structured and promoted in a manner which will highlight to a much larger number of small companies the benefits of ICT usage to their businesses.

4.5 Regulation

Regulation is necessary and beneficial to society in general, to consumers, to the environment and to businesses themselves. However, regulation carries compliance costs, and much of these are borne by businesses. In recent years, the Government has taken a number of positive initiatives, including the introduction of Regulatory Impact Analyses for new regulations and the establishment of the Business Regulation Forum. However, small businesses are required to bear compliance costs that are disproportionately high, with a resulting loss of competitiveness. The Small Business

Forum found that the most burdensome regulations for small businesses are those relating to health and safety, employment, and tax and VAT administration.

4.6 Balanced Local Authority Charges

The rapid growth in the number of households and businesses in recent years has brought about a greatly increased demand for local authority services. Local authority current expenditure increased by 114 per cent between 1996 and 2004, and to fund this increase, commercial rates were increased by 111 per cent and local charging for goods and services (most of which is contributed by the business sector) grew by 112 per cent.

Continually increasing local authority charges are a significant issue for all businesses, but particularly for small businesses. Increased charges – commercial rates, service charges (water and waste), planning and development fees and development charges – are impacting negatively on competitiveness, and stifling growth. While recognising the Government's reluctance to increase the contribution of households to local authority funding, the Small Business Forum stresses that it is unreasonable – and ultimately economically counter-productive – to expect the business sector to absorb sustained increases in local authority charges.

4.7 Access to Information and Advice

Despite having access to a very wide range of information sources, far too many entrepreneurs and small business owner/managers in Ireland are without a readily available single point of contact to answer the questions that inevitably arise at each stage of business development. As a result, they are frequently referred from one organisation or individual to another, and may ultimately get advice that is inappropriate or sub-optimal. At best, this can lead to frustration and wasted time; at worst it can lead to missed opportunities, poor performance and business failure.

A coherent strategy on information provision would mean that entrepreneurs and small business owner/managers would have a single, well-publicised point of contact to deal with all their enquiries at each stage of developing their business.

4.8 Infrastructure

The very success of the Irish economy over the past ten years has put a huge strain on our physical and social infrastructure. The National Development Plan (2000-2006) has played a significant role in closing many infrastructure gaps, but despite these investments, deficiencies remain. Infrastructure developments continue to lag behind demand in many parts of the country, particularly in four key areas:

- **Broadband:** while the Forum recognises that broadband connectivity and penetration are increasing and costs are falling, broadband take-up in Ireland is significantly slower than in many other OECD countries.
- **Transport:** An efficient transport infrastructure is essential for enterprise development. The Forum welcomes the Government's Transport 21 plan. However, components contained in the Plan's framework will require prioritisation and must be subject to cost-benefit appraisal to ensure that value for money is achieved.
- **Energy:** Noting that electricity costs increased by 40% between 2001 and 2004, the Forum is concerned that liberalisation of the energy market is not having the

desired effect in reducing prices or improving quality of service. It also notes that very significant investment is needed in order to cater for predicted economic growth.

- **Waste management:** Waste costs are a major issue for Irish business; the total cost of waste disposal for business in Ireland has risen from €32 million in 1995 to over €800million in 2004. Lack of access to suitable recovery and disposal outlets has a negative impact on every enterprise in Ireland.