Macroeconomic policy in the Celtic Tiger: a critical reassessment

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The miraculous turnaround in the fortunes of the southern Irish economy during the 1990s fooled most experts. The upturn began in the early 1990s, following one of the worst economic periods in the history of the Irish state. The economy then 'took off' in 1994 for seven years of sustained high growth that earned the Irish Republic the popular name of the 'Celtic Tiger'.

The Celtic Tiger emerged from a historic expansion in the United States that was centred on the information technology (IT) industry. After the restructuring of the 1980s and a decade of speculation that Japan would overtake the United States as world economic leader, the turnaround in US fortunes was as unexpected as the subsequent associated boom in Ireland. During every quarter of every year since the US expansion began, respected economists predicted its demise. In early 2001, the expansion finally ended and the US economy was in recession by the end of the year. Soon after the US slowdown began, Irish growth also began to wane and turned negative in the second half of 2001. Experts began to pronounce the death of the Celtic Tiger, as suddenly as they had discovered its birth some seven years before.

In the light of this downturn, perhaps we can now step back and assess what this period of growth was all about, and specify how the southern Irish economy and society have changed, particularly from a macroeconomic perspective. Such a broad look at the experience of the 1990s, I believe, shows that the correlation most economists make between macroeconomic stability and economic growth is spurious. Irish economic growth was due to a unique set of (mostly exogenous) circumstances, centred on a massive inflow of US corporate subsidiaries, which cannot be replicated in other countries and possibly cannot be sustained in Ireland. Without those special circumstances, all the macroeconomic stability in the world could not have achieved economic growth rapid enough to promote convergence with the wealthier economies of the European Union

(EU) or of the Organisation for Economic Cooperation and Development (OECD). Moreover, an assessment of Ireland's decade of growth indicates that the objective of maintaining growth actually impeded the achievement of many important social goals, for two reasons. First, since the southern Irish state correctly realised that the main incentive to attract transnational corporations (TNCs) was low corporate taxes, it pursued a neo-liberal growth model that matched low taxes and fiscal restraint with minimal government interference in business. Second, for several reasons, including a spurious association of fiscal restraint with economic success, the state abjectly failed to mobilise the fiscal resources that were created by rapid growth in order to reduce inequality and improve social welfare. Instead, it turned these resources back, through tax reductions that favoured the wealthier members of Irish society.

Some initial observations

At the end of the 1980s, the Irish people suffered a twenty per cent *official* rate of unemployment¹ and the state had one of the highest ratios of debt to national income in the world. The 1980s had been a difficult period of restructuring in the world economy. The southern Irish economy, whose indigenous industrial sector had been in rapid decline since Ireland's accession to the European Economic Community in 1972, already relied heavily on investments by TNCs. One of the features of global restructuring was large-scale disinvestment and relocation of TNC activities. Irish growth rates declined and unemployment rates soared as TNC disinvestments and the failure of new TNCs to invest in adequate numbers complemented indigenous industrial decline. No one knew at the time how a subsequent upturn of foreign investments would affect specific regions like Ireland. Some experts feared that peripheral regions like Ireland would lose out, since the 'new investment' of the 1990s appeared to be based on flexible relations, such as subcontracting, instead of the older practice of sinking big amounts of capital in foreign subsidiaries.

By 1994, however, it was already clear that the southern Irish economy was going to be an important site for the new expansion in the world economy, which was led by economic growth in the United States and, particularly, by expansion of 'modern' sectors like IT. As a result of a huge increase in Irish exports produced by foreign-owned subsidiaries in manufacturing and services, Irish gross domestic product (GDP) growth rates rose to 5.8 per cent in 1994 and remained at least as high thereafter (Table 2.1). Southern Irish per capita national income, which had been barely sixty per cent of the EU average in 1988, reached the EU average by the late 1990s. The Irish economy, now popularly known as the 'Celtic

Table 2.1 Percentage real economic growth rates in the 1990s in the Republic of Ireland

<i>Year</i>	<i>Gross domestic product</i>	<i>Gross national product</i>
1991	1.9	2.3
1992	3.3	2.3
1993	2.7	3.4
1994	5.8	6.3
1995	9.7	8.2
1996	7.7	7.4
1997	10.7	9.3
1998	8.6	7.8
1999	9.8	7.8
2000	11.5	10.4

Source: *National Income and Expenditure* (Cork: Central Statistics Office, various years).

Tiger', was widely regarded as a model to be followed by other countries seeking 'economic success'.

What was the basis of this turnaround? For most experts, the answer seems to be that Ireland had finally achieved rapid economic growth because of several policy factors. Successive Irish governments had persisted with a policy of educating workers in IT skills, even during the bleak years when the local economy had insufficient need for them.² In time this strategy paid off, because Ireland had a surplus of trained IT experts when capital came a-calling to employ them (and it was also serendipitous that capital wanted English-speaking experts). Social partnership agreements assured pay restraint and flexible labour, which were important to the TNCs but even more important to low-profit service companies. And, most importantly for orthodox economists, southern Ireland achieved a generally stable macroeconomic environment through restrictive fiscal policy, stable exchange rates and so on.³

On this basis, economists cite the Irish case to support the orthodoxy of the International Monetary Fund (IMF), the OECD and other international bodies that favour macroeconomic stability over all other social and economic policy variables. The new orthodoxy as the EU enters into a phase of enlargement is to convince the accession countries that they *will* converge if they maximise the openness of their trade, get the macroeconomics right and encourage labour flexibility. Mainstream analysts point to Ireland, the only country that has recently achieved convergence with the EU average, as proof positive of the beneficence of such policies. But is it really true that macroeconomic stability played such a central role in Irish growth and convergence? And at what price was such stability achieved and maintained?

Foreign investment and the Celtic Tiger

Mainstream macroeconomic analyses aside, the single overriding factor in the 'success' of the Celtic Tiger was the arrival of huge clusters of foreign subsidiaries in a few sectors, and predominantly from the United States. The Celtic Tiger has been extremely dependent on foreign activities, particularly on rising exports from Ireland by US computer and pharmaceutical companies. Irish economic growth in the 1990s was dominated by the country's ability to attract investments by TNCs in a changing global environment. If macroeconomic stability played an important role in the creation and maintenance of the Celtic Tiger, it was primarily because a stable environment was more attractive to TNCs. Low corporate taxes were the most important attraction, although they were hardly an innovation, since they had been introduced in the 1950s and extended in the 1970s. Of secondary importance were targeted education policies that created a pool of IT experts (and a small pool, at that, relative to the broad Irish labour market), again a policy feature since the 1960s and 1970s. Finally, the extension of previous corporatist wage agreements into broader 'social partnership' agreements suppressed wages and increased labour flexibility, although the first factor is of relatively minor importance to most TNCs, because their wage bill is extremely low relative to other costs.⁴ None of these policies, however, would have turned around the Irish economy was it not for a single factor: the 1990s was a period of unprecedented boom for the US economy, particularly in computers and health-related technologies. The boom sent US corporations looking for access to new markets (of which the EU was most important) and tax shelters where they could shift unprecedented profits.

After a period of worldwide restructuring in the 1980s and an economic threat from Japan, the United States reasserted its global leadership in high-tech sectors during the 1990s, particularly in IT. US TNCs expanded their IT production and searched for new markets, often by setting up regional hubs to service key markets like the EU. This caused a revival of foreign direct investment, but in new patterns. Investment was more concentrated than in previous decades, with groups of TNCs agglomerated in a key country or region. In this way, they could supply each other as well as supplying the target markets. Cheap labour and government subsidies were less important than labour flexibility and the ability to move commodities and profits freely.

The attraction of the EU as a market for US high-tech products increased further after 1992 with the coming of the single European market. US investments in the EU rose rapidly and they agglomerated in Ireland primarily because of its extremely low tax rates on corporate profits – ten per cent compared with thirty to forty per cent elsewhere in Europe. Low tax rates not only meant that TNCs could retain more of the profits

they received from their activities in Ireland – they also enabled them to shift profits into Ireland by manipulating transfer prices (prices for intra-firm sales), so that they could reduce their overall global tax liability.⁵ While low taxes were the primary attraction, TNCs were also drawn by Ireland's cheap, educated, English-speaking labour force; by its low bureaucratic restrictions on foreign investors; and by a history of close relations with the Irish Industrial Development Authority (IDA).

If a single event can point to the birth of the Celtic Tiger, it was the Irish state's success in attracting Intel to the country in 1990, at a historically high cost to the Irish state. A significant number of IT companies had already located in Ireland during the 1970s and 1980s. But after Intel located its European site for the production of computer chips near Dublin, nearly every major player in the computer industry followed. By the late 1990s, Ireland was home to Gateway, Dell, AST, Apple, Hewlett-Packard and Siemens-Nixdorf in PCs; Intel, Fujitsu, Xilinx and Analog Devices in integrated circuits; Seagate and Quantum in disk drives; and Microsoft, Lotus and Oracle in software. Telesales and teleservicing for these large firms followed, along with hundreds of less well known producers of boards, power supplies, cables, connectors, data storage, printers, networking and everything else that goes into or around computers, as well as services that are connected to or use computers. The Republic of Ireland's share of foreign investment inflows into the EU tripled between 1991 and 1994, as it attracted forty per cent of US electronics investments in Europe. A similar agglomeration of foreign pharmaceutical companies also located in Ireland.

Fixed investments by US firms, which had fallen rapidly during the 1980s, rose dramatically in the 1990s (Table 2.2), while investments by other TNCs and Irish firms declined. As a result, the share of US-based firms in total fixed industrial investment rose from a third at the beginning of the 1990s to two-thirds at the end of the decade.

Because of Ireland's small size, this level of activity directly caused rapid economic growth. TNCs were directly responsible for forty-five per cent of southern Irish economic growth during the first half of the 1990s and were indirectly responsible for additional growth in construction and services. Moreover, the impact of TNCs was rising fast. Between 1995 and 1999, TNCs directly accounted for eighty-five per cent of economic growth in terms of their value added (the difference between their incomes for the commodities they produced and their non-wage costs of producing them). Their rising profits alone accounted for fifty-three per cent of economic growth! Where TNCs' value added was equivalent to fourteen per cent of GDP in 1990, it rose above fifty per cent in 1999.

The effect of TNCs on economic growth was concentrated in exports within three manufacturing sectors that were dominated by US firms:

Table 2.2 Fixed industrial investments in the Republic of Ireland, by country of origin (IR£millions at constant 1990 prices), 1990–98

<i>Year</i>	<i>US TNCs</i>	<i>Other TNCs</i>	<i>Irish firms</i>	<i>US share of total (%)</i>	<i>Irish share of total (%)</i>
1990	68.4	52.0	90.0	32.5	42.7
1991	109.8	114.6	71.6	37.1	24.2
1992	126.7	81.6	60.5	47.1	22.5
1993	175.5	62.2	49.1	61.2	17.1
1994	137.1	48.3	52.8	57.6	22.2
1995	157.9	44.2	56.7	61.0	21.9
1996	252.8	49.9	97.1	63.2	24.3
1997	259.0	51.6	70.3	68.0	18.5
1998	256.0	71.3	62.2	65.7	16.0

Source: Central Statistics Office.

chemicals, computers and electrical engineering. These three sectors alone (and not including software and teleservices) accounted for forty per cent of Irish economic (GDP) growth during the 1990s, including fifty-one per cent in 1998, fifty per cent in 1999 and forty-six per cent in 2000. They accounted for seventy-eight per cent of industrial growth (including construction) in 1998, eighty-five per cent in 1999 and eighty-four per cent in 2000. They were the only economic sectors that exceeded the average GDP growth rate of 6.3 per cent during the 1990s, together growing annually by about fifteen per cent. Even a single product could have a large effect on Irish economic growth, as was the case in 1997/98 when Pfizer introduced its Irish-produced drug Viagra onto the world market and ‘Irish output’ of organic chemical products rose by seventy per cent.⁶

The other side of this heavily concentrated growth was that stagnation could also come quickly and in a concentrated form. This appears to have been the case from the middle of 2001 on, after the US IT-based economy went into recession. Within months, there were reverberations within the Irish economy as IT companies began to close or cut back their operations in record numbers. Despite a relatively healthy beginning, the year ended with the IDA announcing record job losses in foreign-owned companies. Due to closures and cutbacks, the numbers employed in the IT sector fell by eleven per cent in 2001, with job losses of 10,792. Some of these were in the most high-profile US companies of the sector, such as Motorola, Gateway and General Semiconductors.⁷

These sector-specific job losses quickly began to translate into a general economic contraction, as the main sources of economic growth dried up. From this point on, the medium-term trajectory of the Irish economy,

including the duration of stagnation and whether stagnation would turn into severe contraction, depended on two things. First, the duration of the US recession would have obvious effects on the duration and depth of Irish recession. And second, the depth of Irish recession would depend on the degree to which the downturn in manufacturing worked its way through other sectors, particularly services and construction. If the 1990s was a period of economic growth, with lagged effects on employment growth and possibly on investment growth, the present decade could easily become one of economic decline, with lagged negative effects on employment and investment.

The extreme relationship between Irish economic growth and the expansion of foreign activity created a number of unique characteristics that set off the Irish economy from others within the EU, including others on the EU periphery. Most distinctly, a gap opened up between GDP and gross national product (GNP).⁸ Ireland is unique in Europe in the degree that its gross *domestic* product exceeds its gross *national* product, because of the profits that are removed by TNCs. In 1983, foreign profit repatriations made up just three per cent of GDP. By 1995, they were nearly nineteen per cent of GDP. In 1999, they had risen to an astounding forty per cent of GDP – forty-eight per cent if incomes from royalties and licences are included! The proportion of TNC profits in GDP began to rise to an astonishing extent after 1997. In 1998, growth of foreign profits was equivalent to eighty per cent of economic growth! During the two years of 1997 and 1999, the rise of TNC profits was equivalent to two-thirds of economic growth. As a result, the gap between GDP and GNP widened. In 1980, southern Irish GDP and GNP were practically equal. In 1990, GDP was eleven per cent higher than GNP. By the turn of the century, GDP exceeded GNP by about twenty per cent. In simple language, GDP overstates by a fifth how much of the material wealth created by the economic activities of the Irish people is available for their own use within Ireland.

Arguably, Ireland's most important function today is as a site where US companies can shift their products into Europe, while accumulating profits in order to avoid taxation. TNCs buy (import) their inputs cheap from other subsidiaries and sell (export) them dear, mainly to Europe but also back to the United States (especially in the case of pharmaceuticals). Significant profit shifting through transfer pricing is indicated by the extraordinarily high TNC profit rates cited above, along with unrealistic output growth and rises of labour productivity in the sectors most prone to profit shifting. According to the US Department of Commerce's *Survey of Current Business*, in the Republic of Ireland US-based TNCs maintained profit rates in the 1990s that were five times greater than those achieved elsewhere in the world (up from two and a half times higher in the 1970s). These uncommonly high profit rates were

accompanied by rapid output growth, beyond what would have been expected from the TNCs' rates of investment.

Growth and employment

Greater optimism about Ireland's economic prospects emerged in the early 1990s. But this optimism was initially restrained by the fact that economic growth and convergence were so disconnected from other policy variables. The main policy target was employment, as the country had continued to endure high unemployment rates even into the mid-1990s. Some observers were concerned at the lack of employment growth that was associated with early output growth. Essentially, the economy appeared to be growing during the first half of the 1990s without employing more people. The unemployment rate actually rose during parts of the early 1990s and this led to a concern that the economy was experiencing growth without gains in employment.⁹

The economy finally began to generate substantial numbers of new jobs after 1994. The growth of employment in the second half of the 1990s was remarkable. Depending on the source of the estimate, unemployment rates still exceeded fifteen per cent and possibly approached twenty per cent in 1994. Yet, by 2000, the number of jobs in the southern Irish economy had risen by nearly a half compared with 1990, with total employment rising by more than half a million during the decade. As a result, official unemployment rates fell to around four per cent at the end of the decade.

As suggested above, however, employment growth was not directly associated with output growth. During the 1990s, output growth was heavily concentrated in manufacturing and, more precisely, in the three US-dominated manufacturing sectors of computers, electronic engineering and pharmaceuticals. Employment growth, however, was clearly concentrated in services (Table 2.3), which accounted for seventy-eight per cent of the net new jobs in the southern Irish economy. There was a clear lag in the employment effect of growth during the 1990s because the companies that were responsible for output growth, US TNCs, did not employ very many people, relative to their economic size. Gains in employment were mostly within the construction and service sectors, which expanded as some of the effects of manufacturing growth finally filtered through to the rest of the economy.

A structural result of the Celtic Tiger growth period, then, was that the southern Irish economy became even more dependent on services for employment, while it became more dependent on manufacturing as a source of growth. In 1990, services made up fifty-seven per cent of total employment. By 1999, they accounted for sixty-four per cent. This also

Table 2.3 Employment (thousands of employees) and percentage employment change during the 1990s

	<i>Services</i>	<i>Industry</i>	<i>Total^a</i>
1990 employment	643	321	1,133
<i>Changes</i>			
1991	13	2	1
1992	15	-5	9
1993	18	-7	4
1994	18	20	36
1995	41	15	57
1996	46	5	45
1997	62	19	80
1998	72	58	130
1999	72	23	96
2000	60	25	80
2000 employment	1,064	476	1,671
<i>Change, 1990–2000</i>	<i>421</i>	<i>155</i>	<i>538</i>

^aEmployment totals in industry and services do not add up to the totals for the economy because of employment in agriculture, which is not included here.

Source: Central Statistics Office.

meant that employment was concentrated in a low-wage sector, although certain of the new services included high-wage jobs. There was also a steady transformation from full-time to part-time employment, as the Irish labour market became increasingly flexible. Seven of every twenty new jobs created in the 1990s were part-time. Where less than eight per cent of jobs were part-time in 1990, seventeen per cent were part-time by 2000. Other forms of casualisation of work, such as fixed-term, temporary and 'self-employed' contracting, also increased rapidly. Wage restraint *and* flexibility were enhanced as a feature of the southern Irish economy by social partnership agreements, where labour moderated its demands over wages and job security in return for concessions on income taxes. Thus, rising employment in the 1990s came at the cost of Ireland having one of the most flexible labour regimes in Europe, with low job security, substantially more workers on low wages and fewer workers' rights.¹⁰

While it took some years for growth to translate into jobs, it also appeared during the early 1990s that growth was taking place without much investment, from either indigenous or foreign sources (TNC-based exports from Ireland grew *much* more rapidly than TNC investments).

The investment share of Irish national income, already low by EU standards, plummeted during the first half of the 1990s. The investment rate (gross capital formation divided by GDP) fell from about twenty per cent in 1990 to fourteen per cent in 1994, which was substantially below the EU average of about twenty per cent. This was considered to be such a problem that the National Economic and Social Council (NESC) carried out a major study into 'investmentless growth' during the mid-1990s. It was only after a lag of a few years that economic growth became associated with rising investment, which recovered during the second half of the 1990s (see Table 2.4, below).

The indigenous economy: following the European path?

Has the rapid growth of the foreign sector spun off into indigenous sectors? Some experts have argued that the 1990s were different from earlier periods because TNC activities encouraged a greater expansion of indigenous companies. O'Malley¹¹ argued that a dynamic indigenous manufacturing sector grew alongside the foreign sector. Others contend that the TNC investments of the 1990s were more strongly linked to indigenous industry than during previous expansions.¹²

Ó Riain¹³ makes a more indirect argument about the effects of the foreign-owned sector on indigenous activity. He argues that there were 'two globalisations' in Ireland in the 1990s. One was the outward movement of US capital through Ireland and into Europe. The other was the development of a dynamic and globally oriented Irish indigenous sector, led by Irish entrepreneurs who were 'globalised' by their connections with TNCs in IT in places like California's Silicon Valley. Ó Riain credits this Irish success to the *flexible* developmental policies of the Irish state, which combined a neo-liberal macroeconomic environment with everyday micro-intervention to identify opportunities for local entrepreneurs.

Accounts of a recent indigenous revival are overstated, however. The Irish state limited its pressure on TNCs to link locally because stronger intervention would have undermined the basic attractiveness of Ireland as a deregulated, hands-off state. In 1996, out of 2,667 indigenous firms that employed ten or more people, only 174 were sub-suppliers to TNCs, mostly providing routine supplies like packaging and printed materials.¹⁴ The proportion of raw materials that were purchased locally by TNCs hardly rose at all during the 1990s, from 18.8 per cent in 1990 to 19.1 per cent in 1996. If we account for the fact that two-thirds of 'local purchases' in the electronics sector actually consisted of one TNC subsidiary buying from another,¹⁵ then TNCs were buying a substantially *smaller* share of their material supplies from Irish firms as the Celtic Tiger developed. While the absolute amount of material purchases by

foreign firms certainly rose by an unknown amount during the 1990s, creating some new opportunities for some Irish businesses, it is important not to overestimate the extent to which this happened.

Ó Riain's second globalisation – indigenous spin-offs that were not directly linked to the foreign sector – appears to be significant only in software. The thousands of engineers and technicians who qualified in Ireland but emigrated, and others who stayed in Ireland but left their TNC employers, were a pool of potential entrepreneurs with knowledge of the software industry and who were eager to set up as small employers. They did so in record numbers during the 1990s. By the year 2000, the media reported that Ireland was the second largest exporter of software, behind the United States, having surpassed Israel and India. They stressed the importance of the indigenous sector in this result. Half of the employment in software was in indigenous Irish firms. Nearly eighty per cent of Irish software companies exported some of their product and nearly half exported most of their product.¹⁶ Yet eighty-two per cent of these firms had no alliances of any kind with TNCs.¹⁷

In reality, however, the indigenous software sector is very weak. The industry is dominated by TNCs in every respect except employment. With only half of software employees, TNCs account for eighty-seven per cent of Irish software sales, ninety-two per cent of software exports and eighty-nine per cent of software revenues. Microsoft alone accounted for forty per cent of exports in 1995.¹⁸ Indigenous software firms are mostly very small, with average employment less than fifteen. According to Ó Riain, their low levels of investment in research and development are 'worrying' and expenditure on training actually fell during the 1990s. This indicates that Irish software, like the rest of the economy, is essentially dualistic – with highly developed TNC giants alongside a scattering of very small and vulnerable domestic firms. The Irish software sector 'cannot bear the burden of the huge expectations which have been placed on [it]'.¹⁹

Overall, the sustainability of Irish indigenous industry had become very questionable by the end of the 1990s. Indigenous exports and profit performance remained weak. While the rise of TNC profits was spectacular between 1990 and 1999, rising more than sixfold, indigenous profits remained stable, even dipping at the end of the decade. Thus, the indigenous share of profits fell from over fifty per cent in 1990 to less than ten per cent in 1999.²⁰ While foreign profits are undoubtedly inflated by TNC profit-shifting behaviour, this does not detract from the fact that indigenous profits were not rising substantially during Ireland's most significant phase of rapid economic growth. This weakness was also reflected in a sharp rise in the numbers of indigenous company failures at the end of the decade.²¹

This duality between a rapidly growing foreign sector and a relatively stagnant indigenous one is shown most clearly in productivity figures

for the 1990s. Output in the three US-dominated sectors of computers, electrical engineering and chemicals grew by 375 per cent during 1990–99, while employment grew by only seventy-three per cent. Thus, output per employee grew by 215 per cent, nearly nine per cent annually. Elsewhere in the economy – mainly Irish-owned services, construction and basic manufactures – output rose by just fifty-five per cent, while employment grew by forty per cent. Output per employee grew by about one per cent annually, which is quite a low figure by international standards. By 1999, the average worker in the foreign sector produced nearly eight times more output by value than did the average worker in the rest of the economy.²² Again, productivity figures in the TNC-dominated sectors are so unreal that comparison with them cannot be taken to imply anything about the productivity growth of indigenous sectors. On the other hand, productivity growth of the indigenous sectors is low by any international standard and challenges the dominant assumption in Ireland that the indigenous sector was a dynamic partner in the Celtic Tiger growth experience of the 1990s.

Macroeconomic change: components of GDP

How have the dramatic changes of the 1990s affected the overall shape of the southern Irish economy? One of the most dramatic changes during the Celtic Tiger period was a change in the components of GDP/GNP. Indeed, when conservative economists proclaim the success of Irish macroeconomic stability, they are essentially praising a model that has effected a change in the composition of GDP that has entailed a declining proportion going to forms of income and expenditure that benefit the wider population, and a rising proportion being devoted to those that favour private corporations and the rich.

In all the excitement about rapid economic growth, which was certainly spectacular in the latter half of the 1990s, commentators often missed more fundamental changes that were taking place in the distribution of the national product. GDP was growing rapidly, but certain components of GDP were growing especially rapidly while other components changed much more slowly. Moreover, the distinction between what was growing very rapidly and what was growing much less rapidly had a class character and a global character. That is, the components that rose most rapidly favoured the richer segments of Irish and global society alike, while the other components disproportionately affected the wellbeing of the general Irish public.

The changing components of GDP (measured on an expenditure basis) are given in Table 2.4. The most profound increase was in the export surplus, which tripled its share of GDP over the course of the 1990s,

from less than five per cent to over fourteen per cent. The export surplus is practically equivalent to repatriated profits of the TNCs,²³ so it is clear that *transnational capital* was the primary recipient of the benefits of Irish growth. The TNCs' share of GDP rose dramatically, from less than five per cent in 1990 to nearly fifteen per cent in 2000. In other words, their share tripled, while in absolute terms TNC incomes grew many times over.²⁴ This should be hardly surprising if, as I have argued, the overwhelming *raison d'être* of the Celtic Tiger from the global perspective was the creation of a regime that was amenable to the accumulation of profits by US transnational capital.

In return for creating this amenable environment, there were distinct advantages for the Irish state and for *sections* of the Irish public (to which I will return shortly). But, leaving distributional income aspects aside for the moment, what of the general Irish public?

The most striking thing about the changing distribution of southern Irish GDP during the 1990s is the move *away from* consumption, both private and public. Private consumption, which made up nearly two-thirds of GDP in 1990, fell to less than half in 2000. Irish public consumption, which, at sixteen per cent of GDP, was already at one of the lowest levels in Europe in the early 1990s, fell even further, to twelve per cent in 2000. As a whole, the share of GDP represented by public and private consumption fell dramatically, from seventy-seven per cent in 1990 to sixty-two per cent in 2000.²⁵ I will consider the negative consequences of these trends on social welfare below.

Table 2.4 Changing composition of GDP during the Celtic Tiger period (%)

<i>Year</i>	<i>Private consumption</i>	<i>Public consumption</i>	<i>Investment</i>	<i>Export surplus</i>
1990	61.3	15.3	18.7	4.7
1991	61.6	16.1	17.3	5.0
1992	60.0	16.1	16.3	7.5
1993	58.4	15.9	15.2	10.5
1994	58.2	15.7	16.3	9.8
1995	56.3	15.0	17.2	11.5
1996	55.4	14.3	18.6	11.6
1997	53.1	13.9	20.3	12.7
1998	52.6	13.4	22.4	11.6
1999	50.2	12.7	23.4	13.7
2000	49.4	12.2	23.8	14.3

Source: *National Income and Expenditure* (Cork: Central Statistics Office, various years).

Finally, it is worth noting that there was a distinct and rapid recovery of investment, the stagnation of which had exercised many experts during the early part of the 1990s.

The TNC profits explosion, fiscal policy and inequality

These broad changes in the Irish economy during the 1990s are crucial, because there is strong evidence that growth has been associated with inequality under the Celtic Tiger. On the one hand, economic growth encouraged a large rise in profits and unearned incomes, without a corresponding rise in wage levels, so that the class distribution of income moved rapidly away from the working classes and the poor and towards capital and high-income professionals. Rapidly rising outflows of profits to TNCs, combined with inflows of profits and fees to the upper strata of the Irish population, created a level of class inequality that was previously unknown in modern Ireland. Where factor shares of non-agricultural income were relatively stable before 1987, with wages accounting for seventy per cent and profits thirty per cent, they shifted drastically thereafter, until the profits share from non-agricultural activities was virtually equal to the wage share in the year 2000.²⁶

On the other hand, factor income inequality was accompanied by increased disparities in incomes, including wages. The Irish labour market became more segmented during the growth phase of the 1990s, with a clear distinction between high-waged core jobs and low-waged peripheral jobs. As labour market segmentation became more pronounced, income distributions became more unequal. The available data show that both wages and disposable incomes became more unequal after 1987. The disposable incomes of the top forty per cent of households grew *twice as quickly* as those of the bottom forty per cent between 1987 and 1994. They continued to diverge thereafter. The share of the nation's disposable income of the bottom forty per cent of households fell from 16.2 per cent in 1994 to 15.2 per cent in 1998, while the share of the bottom ten per cent fell from 2.3 to 1.8 per cent.²⁷

In terms of the ratio of the income share of the richest ten per cent to the poorest ten per cent, Ireland was, in the mid-1990s, the most unequal country in Europe and second only to the United States in the OECD.²⁸ Barrett *et al.*²⁹ show that the increase in earnings dispersion (ratio of the top to the bottom decile) was greater in Ireland than anywhere else in the OECD in 1994. Nolan and Hughes found that the proportion of Irish workers on low pay in that same year was twice the EU average and five times the Scandinavian average.³⁰ The income data quoted above indicate that this probably got worse rather than better in the last half of the 1990s. Moreover, by some absolute as well as relative measures,

poverty increased along with inequality. By the end of the century, according to the United Nations' *Human Development Report*, the Irish poverty rate, as measured by its Human Poverty Index, was the highest in the EU.³¹

This rising level of inequality and relative poverty during a period of rapid growth was *not* effectively countered by state policies, as one can clearly see in macroeconomic terms by the shares of GDP shifting towards capital and away from public welfare. To what extent was this failure due to policy? On the surface, the changing components of GDP were a combination of two processes: a rapid increase of profit incomes that accompanied the inflow of TNC activities in the 1990s, and a rapid reduction in the share of public consumption/expenditure due to liberalised fiscal policy (i.e., stable macroeconomic policies). The first process is part and parcel of the Celtic Tiger, which is based on foreign activities and foreign profits. It is therefore a *systemic* outcome of the kind of development model that was chosen by Irish governments as far back as the 1950s and which has been adhered to since.

The second process, however, may be thought of as a policy variable *within* that developmental system. In other words, the government *could have* held onto its public functions and even increased them as fiscal revenues increased. Alternatively, fiscal liberalisation could be considered to be part and parcel of the neo-liberal model that attracted the TNCs in the first place. In reality, government fiscal liberalisation was probably a combination of the two, that is, both a policy variable and a systemic one. There were strong international pressures on the Irish government to liberalise during the 1990s – a process that was mirrored throughout the EU and, indeed, the rest of the world. But liberalisation was promoted within the twenty-six counties with a relish that was unnecessary, either for Ireland playing its 'proper role' in Europe *or* for maintaining the expansionary phase of the Celtic Tiger. Successive administrations in Dublin drew away from providing public services and public welfare in the 1990s in favour of providing tax breaks that favoured the richer segments of Irish society.

Indeed, the overriding ideological position of the 1990s in the Republic of Ireland was that growth was the result of neo-liberal policies, including privatisation and 'responsible' fiscal policies. Successive state budgets after 1987 favoured tax cuts for the rich and failed to provide the necessary spending to correct Ireland's severe social problems.

According to Eurostat, Ireland in 1997 had the lowest levels in the EU of both government revenues and government expenditures as a proportion of GDP. Sweden raised the most revenues, at more than 60 per cent of GDP, while the Irish state received revenues worth a mere 36 per cent of GDP. Irish spending was even more conservative. It was the only state in the EU whose public expenditures were less than forty per cent of GDP,

at 35 per cent (compared with Sweden at 63 per cent and Denmark at 60 per cent). While these low figures partly result from the fact that Irish GDP was growing rapidly, they nonetheless represent an extraordinarily low level of state spending on basic social programmes. Despite its much vaunted emphasis on educating IT professionals, Ireland had the second lowest per capita expenditure in the EU on primary education, less than forty per cent of the Danish level. And it had the fourth lowest level of per capita spending on health, ahead of only Greece, Spain and Portugal, and only about half the German level.

Due to such government policies, many social services ran down. A populist social housing regime that had provided affordable and reasonable accommodation for successive generations of low-income households broke down. Irish citizens no longer have assured access to affordable housing.³² In health, only three EU member states reduced spending as a proportion of GDP between 1980 and 1996. Ireland's reduction, twenty per cent, was easily the largest of the three. Irish public health spending per capita as a percentage of the EU average remained around seventy per cent, despite Ireland's rapid growth. During the 1990s, the number of hospital beds in southern Ireland fell, even as demand for them rose, leaving the country with the fewest hospital beds per capita in the EU. Even after an increase in health spending in 1998, Ireland still ranked twentieth in a survey of twenty-seven OECD countries, with much of what the government called new 'health' spending actually going on social services.³³ Between 1970–75 and 1995–2000, Ireland's global ranking with respect to life expectancy at birth fell by seven places.³⁴ In the field of education, Ireland has performed poorly, in spite of the public image that growth is due to a highly educated population. Almost twenty-three per cent of the population are functionally illiterate, easily the highest level in the EU. Yet, in the late 1990s, Ireland ranked last in the OECD in terms of investment per pupil as a proportion of per capita GNP.³⁵

One of the most notable economic features of the 1990s was a sustained and rapid increase in fiscal revenues, despite the fact that Ireland was the lowest tax raiser in the EU and despite a falling tax take as a share of national income. This was primarily a result of the large numbers of new employees in the economy after 1995 and of taxes on their incomes and expenditures. Income taxes consistently made up about fifty-four per cent of state revenues from 1995 to 2000, while taxes on expenditures (which are notoriously regressive) rose from forty per cent of revenues in 1995 to forty-two per cent in 2000. It is significant that corporate taxes were not a major source of rising state revenues, despite the fact that trading profits of companies tripled between 1995 and 2000!

Rapidly rising revenues gave the Irish state a historical opportunity to begin making the transition from being one of the low-service economies of the EU to joining the continental social democratic countries

that provide high levels of services and social welfare for their populations. Instead, Irish governments tightened their conservative fiscal policy of spending restraint and ran higher and higher budget surpluses. Where the southern Irish state ran a budgetary deficit of IR£460 million in 1995, rising revenues and spending restraint enabled it to turn this around to a huge budget surplus of IR£5.1 *billion* in 2000. In the period between 1996 and 2000, the government ran budget surpluses totalling more than IR£12 billion. During this period, governments made big announcements about grandiose public programmes to fight poverty and to build infrastructure. Yet their unwillingness or inability to spend money meant that these programmes were, in the end, more words than deeds.

Instead of applying its resources to improving infrastructures and public services, the Irish state introduced a series of 'give-away budgets', which offered tax breaks. These budgets became an annual event in the second half of the 1990s, with the Irish Finance Minister initiating a series of high-profile tax cuts. This publicity was generally geared to give the impression that the reductions in tax were of benefit to most people living in the Irish Republic. Closer inspection, however, consistently showed that the tax packages were heavily weighted towards high-income earners and had marginal effects on the incomes of lower earners. Over the four years from 1997 to 2000, low-income couples (those earning up to IR£12,500 a year) received tax breaks averaging about IR£250 a year, while high-income receivers (couples on IR£100,000 or more a year) received income tax breaks of more than IR£1,600 per year.³⁶

This crude measure of tax breaks, however, hides an even greater bias towards inequality in the state's recent budgetary policies. The Economic and Social Research Institute (ESRI) in Dublin has a tax-benefit model that estimates the distributional impact of Irish budgets on families in different income deciles. The model compares actual budget outcomes against a benchmark, where the percentage change in disposable income would be similar across all income groups. This model found that every budget from 1987 to 1998 was regressive, that is, favoured high-income more than middle- and low-income earners. The 1999 budget was more neutral and perhaps even slightly progressive. And then the budget for the year 2000 was again highly regressive. The 2000 budget gave the lowest decile of income earners a less than one per cent change in their disposable incomes, but gave the top two deciles more than a four per cent increase in disposable incomes.³⁷

The evidence of the 1990s shows a clear trend towards inequality. This trend is a feature of Irish economic development at all levels. At the macro level, the aggregates of national income have shifted dramatically towards increasing shares for the private sector and capital, while both private and public consumption have decreased their share of national income. At the same time, within these aggregates, there has been widening

inequality among income earners, in terms of earnings dispersion and household incomes. And, far from countering these trends, the state has exacerbated them through its policies of encouraging wage restraint, through its highly regressive tax policies and by its constraints on public spending. As the state's revenues increased in the mid-1990s, it had a choice of continuing its fiscal conservatism or using the resources that it gained from the Celtic Tiger for the purpose of raising public consumption and, hopefully, general levels of wellbeing. It chose the former. And when the state reduced taxes, it had the choice of concentrating tax breaks at the lower end of the income spectrum, thus taking the side of equalisation of incomes, or of giving the largest tax breaks to the wealthiest, thus increasing inequality. It chose the latter.

Conclusions: *recharacterising the Irish state*

The Celtic Tiger boom of the latter half of the 1990s appeared to be coming to an end as the present decade began. In 2001, recession in the United States caused cutbacks and closures of US-owned subsidiaries in the Republic of Ireland, which had been the backbone of the boom. The initial shock created moderate job losses and a strong contraction of growth. It then began to work its way through the rest of the southern Irish economy, particularly in the sectors of high job growth, such as services and construction. Many official economists were optimistic about the economy's future, and assumed that the downturn was short term and that the economy would return to a moderate equilibrium growth path within a year or two.³⁸

Regardless of the sustainability of even moderate growth in Ireland's economic model, which is so dominated by and dependent on TNC activities, the experience of the Celtic Tiger presents us with an opportunity to assess whether such a neo-liberal economic model is desirable on social grounds.

Such an assessment comes in two parts. First, there is the question of whether such a foreign-dependent, and thus neo-liberal, model as Ireland's *can* provide the distribution of growth and the progressive social policies that will enable growth to be translated into general social wellbeing. Second, could the Irish state itself have exercised sufficient autonomy, had it wanted to, to use the resources generated by growth for a more equitable social outcome?

As the evidence of the 1990s shows, the Irish growth model is highly dependent on foreign activities. Rapid economic growth created a dualistic economy. Economic growth, investments, high profits, high-technology products and higher wages were heavily concentrated in the TNC sector. As a result, the continuation of growth required the

maintenance and even the deepening of a regime that was attractive to US capital. The most important characteristics of such a regime are low corporate taxes, low restrictions on business, and especially on the flows of money and commodities, and maximum integration into the EU market, where most US exports were targeted. Such a liberalised regime by definition requires the Republic of Ireland to follow the prescriptions of radical globalisation, including privatisation, liberalisation, wage restraint, flexible labour and fiscal restraint. By adhering to such a regime, the south of Ireland was reckoned in 2001 to be the 'most globalised' country in the OECD.³⁹ Without doubt, fulfilling the conditions that enabled growth by attracting TNCs in the 1990s placed severe constraints on the state's ability to pursue policies that might reduce the negative impact of growth on inequality, combat poverty and allow for greater social provision.

Within these constraints, however, the Irish state had room to manoeuvre. The creation of conditions that favoured the continued entry of and expansion of activities by the TNCs did not require either the severe restrictions on public spending or the highly regressive tax reforms that the state adhered to throughout the 1990s. The windfall of revenues that came to the state in the second half of the 1990s represented a fund that would have enabled it to ease the inequalities that resulted from the Celtic Tiger, while beginning a transformation towards the high-service and higher-welfare models of continental Europe. Instead, Ireland remained, along with the United Kingdom and the United States, one of the most shabby, low-welfare states of the OECD. As a result, Ireland, despite, or perhaps because of, its economic growth, now finds itself at or near the bottom of the OECD on measures of human welfare, such as poverty rates, inequality, infrastructure and the provision of health and general education. It is a sad legacy of what was, after all, *meant* to be an economic miracle.

Notes

- 1 The actual rate of unemployment was certainly much higher than official statistics would suggest.
- 2 In the 1980s, the majority of engineering students emigrated within a year of receiving their primary degree; engineers had the highest rate of emigration of all kinds of students in Ireland. J. Wickham, 'Industrialisation, work and employment', in P. Clancy, S. Drudy, K. Lynch and L. O'Dowd (eds), *Ireland: A Sociological Profile* (Dublin: Institute of Public Administration, 1986), p. 92.
- 3 European Commission, 'The economic and financial situation in Ireland', special edition of *European Economy* (Brussels: European Commission, 1996); J. Bradley, J. Fitzgerald, P. Honohan and I. Kearney, 'Interpreting the recent Irish growth experience', in D. Duffy *et al.* (eds), *Medium-Term*

- Review: 1997–2003* (Dublin: Economic and Social Research Institute, 1997); R. O'Donnell and D. Thomas, 'Social partnership in Ireland, 1987–1997', paper presented to a seminar on social partnership in western Europe, Cardiff, 11–13 September 1998; International Monetary Fund, 'IMF concludes Article IV consultation with Ireland', public information notice no. 00/61, 10 August 2000.
- 4 Other factors were also present but less critical, such as demographic change. For one of the most recent and comprehensive discussions of mainstream and critical explanations of Irish economic growth, see P. Kirby, *The Celtic Tiger in Distress: Growth with Inequality in Ireland* (Basingstoke: Palgrave, 2002).
 - 5 Transfer prices are the accounting prices at which a corporation sells things from one of its subsidiaries to another. By selling inputs cheaply to subsidiaries that are located in countries where taxes are low, and selling on the products from those subsidiaries at an expensive price, corporations can shift their profits (the apparent amount of value that is added above the costs of production) from higher-tax countries to lower-tax countries.
 - 6 Central Statistics Office, *National Income and Expenditure: First Results for 2000* (Cork: Central Statistics Office, 2001).
 - 7 M. Caniffe, 'Company failures up 65% in second quarter 2000', *Irish Times*, 19 December 2000.
 - 8 Put simply, GDP is a measure of all of the goods and services that are produced in a country. GNP, on the other hand, is the (earned and unearned) incomes received and retained by the residents of the country, regardless of where the activities occurred that produced the incomes. Thus, unlike GDP, GNP does not include profits, dividends and interest that are removed from a country, for example, by foreign subsidiaries that are located there. GNP is a better measure of the degree to which economic growth benefits a country as a whole, because it measures the resources that remain there as a result of its economic efforts.
 - 9 See the discussion in D. O'Hearn, 'Global restructuring and the Irish political economy', in P. Clancy *et al.* (eds), *Irish Society: Sociological Perspectives* (Dublin: Institute of Public Administration, 1995).
 - 10 Paul Tansey reaches the positive conclusion that part-time work is 'chosen' by most workers who take it because it meets their lifestyle needs, but this is questioned by Phil O'Connell and Peadar Kirby, among others. P. Tansey, *Ireland at Work: Economic Growth and the Labour Market, 1987–1997* (Dublin: Oak Tree Press, 1998); P. O'Connell, 'Sick man or tigress? The labour market in the Republic of Ireland', in A. Heath, R. Breen and C. Whelan (eds), *Ireland North and South: Perspectives from Social Science* (Oxford: Oxford University Press, 1999), p. 228; Kirby, *The Celtic Tiger in Distress*, p. 54.
 - 11 E. O'Malley, 'The revival of Irish indigenous industry 1987–1997', in *Quarterly Economic Commentary* (Dublin: Economic and Social Research Institute, 1998).
 - 12 F. Barry, J. Bradley and E. O'Malley, 'Indigenous and foreign industry: characteristics and performance', in F. Barry (ed.), *Understanding Ireland's Economic Growth* (London: Macmillan, 1999); F. Ruane, 'Whither Ireland's industrial policy?', paper delivered to the conference of the European Network on Industrial Policy, Dublin, 9–10 December 1999.
 - 13 S. S. Ó Riain, 'Development and the global information society', unpublished PhD dissertation, University of California, Berkeley.
 - 14 M. Breathnach and D. Kelly, 'Multinationals, subcontracting linkages and the innovative performance of indigenous firms: some Irish evidence', paper

- delivered to the conference of the European Network on Industrial Policy, Dublin, 9–10 December 1999.
- 15 Forfás, 'Optimising purchasing linkages in the Irish economy', mimeo (Dublin: Forfás, 1997).
 - 16 Forbairt, *National Software Directorate Irish Software Industry Survey 1995: Results* (Dublin: Forbairt, 1996).
 - 17 Ó Riain, 'Development and the global information society'.
 - 18 Forbairt, *National Software Directorate*.
 - 19 S. Ó Riain, 'The birth of a Celtic Tiger', *Communications of the ACM*, 40:3 (1997), p. 24.
 - 20 Author's calculations from *National Income and Expenditure and Balance of International Payments* (Cork: Central Statistics Office, various years).
 - 21 Caniffe, 'Company failures up 65% in second quarter 2000'.
 - 22 Central Statistics Office, *National Income and Expenditure*, various years; Central Statistics Office, *Labour Force Estimates*, various years.
 - 23 D. O'Hearn, *Inside the Celtic Tiger: The Irish Economy and the Asian Model* (London: Pluto, 1998), p. 128.
 - 24 Of course, one must qualify this statement by noting that *reported* TNC incomes are inflated by the profit-shifting mechanisms I have already discussed in this chapter.
 - 25 Of course, both public and private consumption grew over this period in absolute terms. But the rapidly falling shares of consumption in national income indicate how unequally the fruits of growth have been shared. A very small proportion of growth went to goods and services that benefit the wider Irish population. Thus, 'trickle down' is precisely that: a *trickle*. Arguably, a much slower growth strategy could achieve much greater results for the Irish population as a whole.
 - 26 D. O'Hearn, 'Economic growth and social cohesion in Ireland', in M. Dauberstadt and L. Witte (eds), *Cohesive Growth in the Enlarging Euroland* (Berlin: Friedrich Ebert Stiftung, 2001), p. 187.
 - 27 B. Nolan, B. Maitre, D. O'Neill and O. Sweetman, *The Distribution of Income in Ireland* (Dublin: Oak Tree Press, 2000), p. 31.
 - 28 United Nations Development Programme, *Human Development Report 2001* (Oxford: Oxford University Press, 2001), p. 182.
 - 29 A. Barrett, T. Callan and B. Nolan, 'Rising wage inequality, returns to education and labour market institutions: evidence from Ireland', *British Journal of Industrial Relations*, 37:1 (1999), p. 84.
 - 30 B. Nolan and G. Hughes, *Low Pay, the Earnings Distribution and Poverty in Ireland*, working paper no. 84 (Dublin: Economic and Social Research Institute, 1997).
 - 31 United Nations, *Human Development Report 2001*, table 2.4. The Human Poverty Index is based on longevity, life expectancy, standard of living and social exclusion. The data used to construct the index are from various years, mostly in the latter half of the 1990s.
 - 32 T. Fahey, *Social Housing in Ireland: A Study of Success, Failure and Lessons Learned* (Dublin: Oak Tree Press, 1999). The breakdown in social housing was not entirely a discretionary policy variable: increased population and employment led to rising demand. Nonetheless, the crucial point is that the state, having chosen a neo-liberal low-tax, low-spending regime, was unable to do anything effective about the housing problem, which was exacerbated by liberal zoning practices, favourable conditions for speculation and substantial corruption.
 - 33 M. Wren, 'Health system needs urgent funding', *Irish Times*, 3 October 2000.

- 34 United Nations, *Human Development Report 2001*, p. 141.
- 35 OECD, *Education at a Glance: OECD Indicators, 1999* (Paris: OECD, 1999).
- 36 These figures are based upon a household that comprises a married couple, both of whom work.
- 37 T. Callan, 'Biased budget towards better-off marks return to earlier policy', *Irish Times*, 2 December 1999.
- 38 D. Duffy *et al.* (eds), *Medium Term Review 2001–2007* (Dublin: Economic and Social Research Institute, 2001).
- 39 A. T. Kearney, 'Measuring globalisation', *Foreign Policy*, 122 (2001), pp. 56–65.