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Some Political Economy Lessons from Ireland's Boom and Bust[1]

Frank Barry

Even if politicians wished to act solely in the national interest, there are few who are not are powerfully constrained by the need to get re-elected. Putting the national interest above personal advancement is more often asserted than fulfilled. To be re-elected politicians have to pay very particular attention to varying combinations of sectional interests and to swing voters, attention which does not necessarily encourage them to actually act in what they may know to be the national interest. As economist and former Taoiseach Garret FitzGerald has written, 'democratic national governments tend to be subject to such strong pressure from vested interests within their own territories that many of their decisions operate against the interests of society as a whole'.[2]

The term *political economy* is used here to refer to how politics impacts on economic policymaking, though it also takes elements of the behaviour of the bureaucracy into account. A thorough study of these issues, even if only in the Irish case, would be more than a lifetime's work. This paper confines itself therefore to an analysis of a number of historical policy decisions that illuminate some central issues. Some of the policy decisions studied here advanced the public interest and led ultimately to the emergence of the 'Celtic Tiger' era of the 1990s and beyond.[3] Analysis of these decisions, and how they came to be made, illustrates some of the processes by which policy errors can come to be rectified. Equally, however, consideration of how some

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[1] This paper forms part of an IRCHSS-sponsored project on "Turning Globalisation to National Advantage: Economic Policy Lessons from Ireland's Experience".

[2] See Garret FitzGerald, 'Diluting Lobbies and Unleashing Growth', in R. O'Donnell (ed.), *Europe: The Irish Experience, Dublin: Institute of European Affairs* (Dublin, 2000)..

[3] Irish income per capita hovered at around 60 percent of that of the UK for the 60 years up to 1973, and had reached only 65 percent by 1990. Then, in a spectacular reversal of performance over what came to be known as the 'Celtic Tiger' era, the Irish level – measured as GNP per capita (so as to exclude the substantial profits earned by foreign multinationals) and evaluated at purchasing-power-parity prices – shot up to achieve parity with the UK and the Western European EU average by the year 2000. It raced further ahead over the next few years before shuddering into reverse when the economy was derailed by the crisis that began in 2007 with the discovery of the 'toxic' debts that had been accumulated in the US sub-prime lending market.

of the policy errors of the boom period came to be made can shed light on less benign aspects of the policy-making process.

Politics, Economic Policy and the 'Celtic Tiger' Economy

The Irish boom of the Celtic Tiger era is generally agreed to have been facilitated by a number of domestic policy changes that positioned the economy to be able to avail of emerging opportunities offered by developments in the global and European economies over the course of the 1990s.

Ireland had joined the European Economic Community along with the UK and Denmark in 1973, and had been successfully attracting foreign direct investment for an even longer period. Educational attainment levels of the Irish workforce had been steadily improving since the 1960s. The importance of these underlying factors increased with the Single European Market and global high-tech boom of the 1990s. The domestic environment, furthermore, was substantially improved with the sizeable increase in EU regional aid that became available from the late 1980s, and with the successful fiscal consolidation of the period.

Irish decision makers had clearly made numerous policy errors in the past. Chief among these had been the delays in embracing reform – whether of trade policy, competition and tax policy, or of the industrial relations system – along with the fact that the fiscal crisis of the 1970s and 1980s had been allowed to spiral so badly out of control. How did policymakers learn from their mistakes and succeed, ultimately, in implementing reforms in occasionally hostile political environments?

Abandoning Protectionism and Embracing Foreign Capital

The quote from Garret FitzGerald above suggests that well-functioning societies must develop mechanisms that can provide political cover to help stave off detrimental interest-group pressures. The shift from protectionism to outward orientation that began in the late 1950s provides several examples of where such cover could be found. By that time it had become clear that the protectionist policies followed since the early 1930s had run out of steam. 400,000 people emigrated over the course of the 1950s – the highest level since the 1880s – while the rest of Western Europe boomed on account of post-war reconstruction. Popular history ascribes the subsequent turnaround in policy, and in Ireland's economic fortunes, to T. K. Whitaker, the recently-appointed Secretary of the Department of Finance, whose galvanising report on Economic Development appeared in 1958, and to Seán Lemass, who implemented elements of this new thinking when he took over from de Valera as Taoiseach in 1959. Garret FitzGerald notes how Lemass used the publication of Whitaker's Economic Development alongside that of the government's First Economic Programme to provide political cover for the policy reversal. By doing so, he writes, 'the government made it clear that the Programme was not, and was not claimed to be, a policy prepared by the government party, but was a national programme, prepared by the head of the civil service'.[4] This allowed it to be seen as transcending party politics. Joseph Lee offers a complementary and amusing commentary.

> It may be surmised that Lemass had little ambition to inflict on his backbenchers, or on De Valera, the enlightenment that would be willingly proffered from the opposition benches about the manner in which Fianna Fáil had at last seen the light, and was now reneging on its earlier self. Nor would any astute politician wish to sacrifice the advantage accruing to his party from a 'plan' ostensibly based on the work of a non-party civil servant.The de-politicisation of 'planning' was too useful an asset to be wantonly surrendered to the capricious vagaries of Dáil debates.[5]

The importance of the Export Profits Tax Relief (EPTR) scheme is less frequently remarked upon by historians. Its importance is more obvious to economists, as it marks the genesis of Ireland's low corporation-tax strategy, which – in the words of Padraic White, former Managing Director of the IDA – 'remains to this day the unique and essential foundation stone of Ireland's foreign investment boom'.[6] EPTR was introduced in November 1956 by a short-lived non-Fianna Fáil government, only the second such administration to hold power since 1932.

The Dáil records of the mid-1950s reveal much discussion on both sides of the house of the need to stimulate exports, yet Fianna Fáil thinking remained

[4] See Garrett FitzGerald, *Planning in Ireland* (Dublin, 1968).

[5] Jospeph Lee, *Ireland 1912 – 1985: Politics and Society* (Cambridge, 1989).

[6] See R. MacSharry, and P. White, *The Making of the Celtic Tiger: the Inside Story of Ireland's Booming Economy,* (Dublin, 2000).

sharply divided on the question of foreign capital. 'Since 1948', as Bew and Patterson write, 'Lemass had been prepared to ruminate rather indecisively in public on the possible role of foreign capital in the Irish economy'.[7] His 1953 trip to the US was partly aimed at attracting American investment, yet his Dáil speeches in the summer of 1955, while in opposition, criticise the then Tanaiste's efforts towards the same end. He also criticises the government's acceptance of a proposal from an Anglo-American combine to erect an oil refinery in Cork harbour, which represented the largest sum ever invested in a single private enterprise in the country.[8]

The ambiguity of Lemass's position was motivated both by politics – 'opposition for opposition's sake' – and by a desire to paper over the cracks between his growing acceptance of the need for, and Fianna Fáil's traditional hostility towards, foreign capital. As Bew and Patterson point out, 'foreign capital was, for nationalist ideologues, a far more explosive issue than protection. After all, protection was only a means to an end – the building up of a native Irish industry'.[9] While Lemass was prevaricating, De Valera was railing against handing over Irish resources 'to foreigners "festooned with tax reliefs".'

EPTR, as first introduced 'in the bleak mid-winter' of the 1950s, allowed a 50 percent tax remission on profits earned from increased export sales. The policy was sold in public as a stimulus to exports rather than to foreign capital. Crucially, however, from the political point of view, its introduction by a non-Fianna Fáil government helped the latter party to finally ditch its ideological objections to foreign industry, which responded rapidly to the new tax reliefs. Upon returning to power, Fianna Fáil expanded the tax remission to 100 percent and eased the legal restrictions on foreign ownership that it had enacted in the 1930s.[10] A later Fianna Fáil government minister, Kevin Boland, wrote of his shock and bewilderment 'to find that the principle of Irish ownership of industry – which was central to the Republican policy as I had always understood it – was gone'.

This episode serves to illustrate how changes in government can sometimes facilitate the abandonment of long-held commitments and growth-inhibiting ideologies, much as the Blair government in the UK benefited from the

[7] See P. Bew, and H. Patterson, *Seán Lemass and the Making of Modern Ireland 1945–66* (Dublin, 1982).

[8] See Dáil record of 14 July 1955.

[9] Bew and Paterson, *Seán Lemass and the Making of Modern Ireland 1945–66*, 70.

[10] Fianna Fáil had also embraced upon its return to power the first coalition government's establishment of the Industrial Development Authority in 1949, though it had rejected the move whilst in opposition.

consequences of many of the changes introduced by previous Conservative administrations – changes which a Labour government would not itself, for party political reasons, have been able to introduce.[11]

While EPTR did not directly threaten established (protectionist) interests, it led to a considerable strengthening of the export lobby. This increased the pressure for further liberalisation, of the type represented by the signing of the Anglo-Irish Free Trade Area Agreement in 1965 and EEC accession in 1973.[12] This is referred to in the economics literature as a process of 'cascading' or 'juggernaut' reforms.[13]

One of the unique features of the Irish political landscape since then has been the degree of cross-party support for foreign direct investment. This was apparent in Labour TD Ruairi Quinn's response as Finance Minister in the mid-1990s to European Commission demands for a single corporation tax rate to be applied across sectors. Existing rates were 28 percent for most services and 10 percent for manufacturing. Resenting the windfall gains that would accrue to services, and particularly the banks, his political advisors argued for a harmonised rate of 18 percent. Quinn rejected this advice and instead chose the Industrial Development Agency's preferred rate of 12.5 percent.

By the new millennium, foreign multinationals had come to account for one out of every two jobs in Irish manufacturing and one out of every five jobs in services – far higher proportions than recorded elsewhere in Europe or indeed in most of the world. The inflows of FDI associated with the Single European Market and the global high-tech boom of the 1990s were in turn one of the driving forces behind the 'Celtic Tiger' boom.

The Development of Education

Growing outward orientation in the 1960s was reflected in an increased desire to

[11] 'Blair's generation of Labour politicians felt compelled to accept the Thatcherite settlement on the economy. He, in turn, forced the Tories to accept a new, more social democratic consensus that government had a responsibility to invest in public services and deliver social justice'; Andrew Rawnsley, "The Reckoning", from: *The Blair Years 1997 – 2007*, *Observer* Supplement, April 8, 2007.

[12] Historians have yet to undertake the work of exploring how these political pressures were manifested.

[13] Rodrik's account of how Mauritius came to become one of sub-Saharan Africa's most successful economies is very similar to the Irish experience as recounted here; see 'Institutions for High-Quality Growth: What They Are and How to Acquire Them', *Studies in Comparative International Development* Vol. 35, No. 3 (Fall 2000), 3 – 31.

benchmark against international standards. The desire to perform well in such exercises can be seen today at any meeting of policymakers from Central and Eastern Europe, for example, or from the developing world. The effects were to be seen most dramatically in Ireland in the case of the response to a 1965 survey of the country's education system carried out under the auspices of the OECD. Ireland had been one of only two countries to respond to the OECD's request for volunteers to have their entire educational system surveyed.

The subsequent report, *Investment in Education*, issued in 1965, made newspaper headlines when it reported that over half of Irish children left school at or before the age of thirteen, a far higher proportion than for most of Western Europe. An important feature of the report was that 'technocratic expertise was being given unprecedented attention and might now be heard alongside the political party and denominational interests which had previously dominated ministerial councils'.[14] The report may serve as an example of what is known in the policy-reform literature as 'creating a crisis' in order to weaken the vested interests opposed to reform.[15]

The report paved the way for the introduction, shortly thereafter, of 'free' second-level education and access to school transport networks. Thirty years later the numbers at school had trebled, with 80 percent completing the full cycle (compared to only 20 percent in 1965), while numbers at third-level had increased even more substantially—by a factor of six.

An unusual feature of the Irish bureaucratic landscape is the degree of 'clout' amassed by the Industrial Development Agency, which is tasked with attracting foreign multinational corporations to the country. The importance of FDI, and the IDA's success, has allowed the agency a voice in areas such as telecommunications and education which are not elsewhere within the remit of investment promotion agencies. A Manpower Consultative Committee had been established in 1978 to provide a forum for dialogue between the IDA and the education system. Through this, the IDA played an influential role in ensuring that tertiary education bolstered competitiveness. Noting a looming disparity between electronics graduate outflows and its own demand projections, for example, it convinced the government to fund a massive expansion in engineering and computer science between 1978 and 1983, as a

[14] See 'All the children: the vocational school and education reform 1930–1990', in J. Logan (ed.), *Teachers' Union: the TUI and its Forerunners 1899–1994* (Dublin, 1999).

[15] See T. Garvin, *Preventing the Future: Why was Ireland so Poor for so Long?* (Dublin, 2004) for a very readable account of the constellation of opposing forces in the educational sphere.

result of which the output of engineering graduates increased by 40 percent over these few years, while the output from computer science increased tenfold.

An unusual feature of the Irish third-level system itself is the relative size of the (sub-university) Institutes of Technology component, which has been of importance in enhancing the environment for foreign direct investment. Ireland now has one of the highest proportions of the cohort aged 25–34 with third-level and specifically with science and engineering qualifications.[16] Furthermore, the country's education system always ranks strongly in surveys of global executives. One recent such ranking of the national educations systems of 60 OECD and medium-income developing countries is provided in Table 1.

Table 1 *Educational Systems ranked out of 60 OECD and medium-income economies*

	"The educational system meets the needs of a competitive economy"	"University education meets the needs of a competitive economy"
Ireland	2	5
Scotland	29	25
UK	36	38

Source: *World Competitiveness Yearbook* (2005)

These various and arguably positive outcomes might be read as resulting from the aforementioned high degree of consensus over the importance of remaining competitive in the global FDI stakes.[17]

Social Partnership and Resolution of the 1980s Fiscal Crisis

Organised interests are known to be most harmful when they are strong enough to cause major disruptions but not sufficiently encompassing to bear a significant fraction of the societal costs associated with pressing

[16] See F. Barry, 'Third-level education, foreign direct investment and economic boom in Ireland', *International Journal of Technology Management*, 38 (2007), 3, 198–219.

[17] See F. Barry, 'Foreign Direct Investment and Institutional Co-Evolution in Ireland', *Scandinavian Economic History Review*, 55, 3 (2007), 262–288.

their own claims.[18] This closely describes the organisation of Irish and UK industrial relations in the 1960s and 1970s. In language reminiscent of Olson, Hardiman notes that over this period 'no single bargaining group believed it had to pay any attention to the impact of its activities on the overall state of economic performance. Yet the cumulative consequences of everyone's bargaining practices were proving more and more harmful to overall economic performance'.[19]

Proponents of the model of social partnership that emerged in Ireland in the mid- to late-1980s argue that participation in this process was sufficiently encompassing that the macroeconomic consequences of the pay deals struck would indeed be taken into account, yielding beneficial employment effects. Whether or not one subscribes to this view of partnership,[20] it was critical along one dimension at least, in that it helped to provide political cover for the fiscal consolidation that was finally implemented in 1987.

Political wrangling had prevented an earlier resolution of the fiscal crisis as trenchant opposition criticism had encouraged the defection of government coalition partners or the withdrawal of support for minority governments over the earlier part of the decade.[21] The newly developed social partnership process helped secure a way out of this prisoner's dilemma, as described by Ray MacSharry, the Finance Minister who implemented the fiscal cutbacks of the 1987–89 period:

> The NESC analysis of what was wrong and the prescription of what needed to be done was agreed by all the social partners – including employers, trade unions, farmers and others – without dissent … It set debt stabilisation as a minimum objective of fiscal policy, while relying

[18] See M. Olson, *The Rise and Decline of Nations* (New Haven, 1982).

[19] N. Hardiman, "Pay Bargaining: Confrontation and Consensus", in D. Nevin (ed.), *Trade Union Century* (Dublin, 1994), 147–158.

[20] For references to the debate, see F. Barry, 'Social Partnership, Competitiveness and Exit from Fiscal Crisis', *Economic and Social Review*, 40, 1 (2009), 1–14.

[21] Patrick Honohan, who was an economic adviser to government at that time, notes that 'it was immediate political pressures rather than any intellectual argument that resulted in the choice falling on tax increases rather than spending reductions. In short, it was the familiar consideration that expenditure cuts tend to hit particular identifiable interest groups, while tax increases can be spread more thinly across society'. Even Fianna Fáil, which won the 1987 election and implemented far sharper spending cuts than proposed by the previous government, had campaigned on the slogan that 'health cuts hurt the old, the poor and the handicapped'. See P. Honohan, 'The Role of the Adviser and the Evolution of the Public Service', in M. Hederman (ed.), *The Clash of Ideas: Essays in Honour of Patrick Lynch* (Dublin, 1988).

> on public-spending cuts—not taxation—to achieve that adjustment. This was the most critical part of its overall strategy. The boldness of the NESC approach, the consensus of the social partners in backing it, and Fine Gael's generous promise of political support on fiscal policy all created a new opportunity to tackle, finally, the public finances.[22]

The political cover provided by the 'Tallaght Strategy' of then Fine Gael leader Alan Dukes was the other main factor in facilitating resolution of the crisis. Unfortunately this will prove difficult to replicate in the future, given that Dukes was deposed as party leader shortly afterwards and his stance, which many commentators would regard as patriotic, has by others been ridiculed as politically disastrous.[23]

Political Economy and Maximising the Benefits of EU Regional Aid

Ireland devoted a substantially higher share of its EU regional aid inflows to human capital development than did the other cohesion economies. This was largely influenced by the successful targeting of the much lower pre-1989 aid funds to develop the Institutes of Technology (formerly known as Regional Technical Colleges). Another element that may have entered the mix, however, was the highly centralised nature of the Irish decision-making process. Sub-national governments in the other EU cohesion countries of Greece, Spain and Portugal tended to prioritise spending on roads and other 'hard infrastructure', possibly because 'human capital' is highly mobile and its benefits therefore more difficult to capture by the individual regions undertaking the investments.

The fact that the EU regional aid process requires agreement between Brussels and the national authorities on spending priorities (to the extent that they are co-funded) also served to reduce the extent to which domestic political considerations and interest-group pressures could adversely affect outcomes. FitzGerald suggested, furthermore, that the EU regional aid process had helped embed best-practice monitoring and evaluation procedures within the national public-service bureaucracy,[24] though doubts

[22] R. MacSharry, and P. White, *The Making of the Celtic Tiger: the Inside Story of Ireland's Booming Economy* (Dublin, 2000), 62. NESC refers to the National Economic and Social Council which can be thought of as the secretariat to the social partnership process.

[23] See, for instance, F. Finlay, *Snakes and Ladders* (Dublin, 1998).

[24] J. FitzGerald, 'An Irish Perspective on the Structural Funds', *European Planning Studies*,

have recently been expressed as to whether this has survived the drop-off of EU aid.[25]

McAleese also remarks on the benign effects of EU rules, noting that 'an Irish government untrammeled by Brussels would have found difficulty in turning off the flow of subsidies to several economically weak but politically sensitive companies (Irish Steel, Aer Lingus and the beef processing industry for instance)'.[26] Hence the fact that Irish national investment policy was subject not just to monitoring and evaluation on the part of the EU Commission but also needed EU approval for those elements in receipt of European co-funding helped to keep at bay the localist and clientalist pressures exerted by the Irish electoral system.[27] Eurostat's refusal to allow Kerry and Clare to be included in the (Objective 1) Border, Midlands and West region provides one example of how localist-driven policies have been thwarted by the EU in the past.

Politics and Policy Errors over the Boom Period

In 2009 the Taoiseach, Brian Cowen, admitted that certain policy errors which deepened the subsequent crisis could be seen – with hindsight – to have been made over the boom period. There errors are responsible for the fact that the current Irish recession, triggered as elsewhere by the global financial meltdown of 2008, is one of the deepest in the developed world. The Taoiseach went on to assert however that 'all policy decisions were based on the best advice available at the time'.

This is a strange claim for a politician to make, in that it seems to deny a role for *politics* in political decision-making. All policy choices have distributional consequences, no matter how much Ireland's political parties seek to portray themselves simply as better economic managers. The Taoiseach's assertion

6, 6 (1998), 677 – 94.

[25] R. Boyle, 'Measuring Public Service Performance and Productivity: how do we know if the Public Service is performing well?', presentation to IPA Annual Conference, September 9, 2009.

[26] D. McAleese, 'Twenty-Five Years a'Growing', in R. O'Donnell (ed), *Europe: The Irish Experience* (Dublin, 2000).

[27] As D. Farrell has noted in *Electoral Systems: A Comparative Introduction* (Basingstoke, 2001), many political scientists accord the multi-seat constituency Single Transferable Vote electoral system a key role in generating 'the heavy emphasis on constituency casework, faction-fighting between candidates from the same party (and) a focus on constituency and localist matters in election campaigns and parliamentary work' (146).

also however seeks to airbrush from the picture the concerns that many economists and others expressed at the time these policy decisions were made. We turn now to a discussion of the political factors behind these errors.

Government stabilisation policy must by definition be counter-cyclical; that is, it must act to dampen rather than accentuate the business cycle. Ireland, however, stands out among OECD countries as exhibiting above-average pro-cyclicality. Nor is this just a recent phenomenon; pro-cyclicality had also been identified in the Irish budget deficits of the 1960s and 1970s.[28] Charlie McCreevy, who was Finance Minister from 1997 to 2004, mocked economists' warnings of the dangers of this stance with his widely-publicised dictum: 'When I have money, I spend it; when I don't, I don't'.

His populist dismissal of ECOFIN's 2001 criticism of Ireland's fiscal over-stimulation represented a tragically missed opportunity to exploit external fiscal commitments as political cover to help overcome the political pressures to act in this way.[29] Instead of tightening fiscal policy, he introduced further income tax reductions along with the profligate SSIA scheme in 2001. While such tax reductions may have helped keep the lid on wage demands in the earlier years of social partnership, their impact increasingly registered as a stimulus to aggregate demand as the responsiveness of labour supply decreased.[30] The legacy of McCreevy's approach, maintained after his departure, was that the country found itself with no stabilising margin when the global recession struck in 2008. The country was then forced into destabilising fiscal contraction.

With monetary policy handed over to the European Central Bank, and with the historically low interest rates that ensued, it became even more important that fiscal policy be used to dampen the property bubble which ultimately burst in 2007.[31] Fiscal policy did the opposite. The construction sector became even

[28] See P. Lane, 'On the Cyclicality of Irish Fiscal Policy', *Economic and Social Review*, 29 (1998), 1, 1–16, and 'The Cyclical Behaviour of Fiscal Policy: Evidence from the OECD', *Journal of Public Economics,* 87 (2003), 2661–2675.

[29] The European Commission raised further concerns about the pro-cyclicality of policy in 2007; it is not insignificant that 2002 and 2007 were both election years in Ireland. On the political pr–essures behind fiscal disequilibria see Schuknecht, 'EU Fiscal Rules: Issues and Lessons from Political Economy', *European Central Bank Working Paper* no. 421 (2004).

[30] F. Barry, F., and J. FitzGerald 'Irish Fiscal Policy in EMU and the Brussels-Dublin Controversy', in *Fiscal Policy in EMU: Report of the Swedish Committee on Stabilization Policy in EMU* (Stockholm, 2001).

[31] Lane had previously warned that the fact that 'fiscal policy in Ireland has in general not behaved counter-cyclically ... imposes costs on the Irish economy that are likely to become more severe in any future European monetary union; see 'On the Cyclicality of Irish Fiscal Policy', *Economic and Social Review* 29, 1 (1998), 1–16.

more bloated by a series of property-related tax incentives, and it had grown to about twice the average size recorded in Europe and the US by the time the bubble burst.

Irish banks and Irish tax revenues had also been allowed to become dangerously exposed to the construction sector. When the bubble burst, revenue sources such as stamp duty, capital gains and capital acquisitions tax all but dried up, while the overexposed banking sector had to be bailed out by the taxpayer.[32] As Honohan has pointed out: 'a financial system which reacts quickly to policy deviations can be a great discipline on governments that learn to anticipate these reactions and stay on the straight and narrow path … In moments of dangerous fiscal excess and competitiveness pressures, the financial system did in the past act as a watchdog. If, in the past, the watchdog was prone to bark too readily, thereby creating unnecessary currency crises, it is muzzled today, given EMU membership'.[33] This suggests that careful financial regulation would have been even more important under EMU than it was beforehand. Instead lax regulation allowed huge financial imbalances to emerge.[34] One of the reasons why Ireland and the UK chose 'light-touch regulation' (or, technically, 'principles-based' as opposed to 'rules-based' regulation of the German variety) was because they felt it would offer their substantial international financial services sectors a competitive advantage.

Is there a political-economy dimension to why the property boom was allowed to spiral so far out of control? To answer this, one must ask who gained from the explosion in property prices. The answer is mainly the property developers, even though many of them may have lost their fortunes in the subsequent meltdown. While house prices skyrocketed, the proportion of the price accounted for by the cost of the site rose from around 15 per cent – a level that is apparently normal by international standards – to between 40 and 50 percent.[35] And property developers have

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[32] The social partnership process may have contributed to a shifting of the tax burden away from income tax, as the pay deals typically offered wage moderation in exchange for promised future income-tax reductions.

[33] P. Honohan, "The Role of the Adviser and the Evolution of the Public Service", in M. Hederman (ed.), *The Clash of Ideas: Essays in Honour of Patrick Lynch* (Dublin, 1988).

[34] Honohan notes for example that the ratio of private credit to personal income grew from 48 per cent in 1995 to 132 per cent in 2005, with about 82 percent of the latter figure relating to housing finance; see 'To What Extent Has Finance Been A Driver Of Ireland's Economic Success?', *Quarterly Economic Commentary* (Winter, 2006), 59 – 72.

[35] J. Casey, 'An Analysis of Economic and Marketing Influences on the Construction

long been major contributors to the Fianna Fáil party,[36] a situation which can only be rectified by reform and rigorous policing of the laws governing political contributions.

Another policy error committed over the boom period – though not directly related to the subsequent economic crisis – was the so-called 'decentralisation' programme announced unexpectedly by the Minister for Finance in his budget speech of December 2003. The plan envisaged that up to eight government departments and a number of state agencies, along with roughly one-third of all Dublin-based civil servants, would be relocated from Dublin. The initial timescale for the programme was to be the end of 2006. The process attracted huge resistance from those who were supposed to relocate however, and appears to have been effectively terminated as a result of the 2008 OECD review of Irish public management.[37]

The programme had all the characteristics of a political 'stroke' designed to garner electoral support in the regions. There was no documentation to suggest that any research or analysis of international experience had been carried out. The locations chosen bore no relationship to the National Spatial Strategy which the government had launched a year earlier. The use of the term 'decentralisation' outraged those who had long argued for – and used the term to refer to – the transfer of responsibility to democratically elected lower levels of government. And particularly worrying to many analysts was the threat it represented to the efficiency of the policymaking system.

One of the champions of decentralisation, the then Minister for State at the Department of Finance, Tom Parlon, wrote that: 'the advent of broadband, the internet and e-mail, instant messaging and other advanced communication technologies now means that for many business functions, location is irrelevant'.[38] Research shows however that this assuredly does not apply to strategy and policy development functions, where physical proximity remains crucial.[39]

Industry', *Building Industry Bulletin*, July 2003.

36 A graphic illustration of this is provided by the more than 30 property development and construction companies that took out advertisements in the anniversary publication 'Republican Days: 75 years of Fianna Fáil'.

37 Given that the OECD actually said very little about the programme, this might be taken as another example of the search for political cover to facilitate a necessary reversal of policy.

38 *Irish Times*, June 10, 2005.

39 F. Bannister and R. Connolly, 'Government by Wire: Distance, Discourse and the

Concluding Comments

Democratic electoral systems alone are clearly not sufficient to ensure that growth-enhancing economic policy decisions are always made expeditiously. In some cases unfavourable outcomes emerge through populist or interest-group pressures; in other cases, because governing parties are locked into growth-inhibiting ideologies.

Many of the constraints entailed by EU or WTO membership – what New York Times columnist Thomas Friedman refers to as 'the golden straightjacket'[40] – are designed to address the first set of issues. At the EU level, the Maastricht criteria, the Stability and Growth Pact, restrictions on state aids to industry and the independence of competition authorities all strengthen the hand of government if it seeks to resist detrimental interest-group and populist pressures. WTO rules have played an important role in helping nations to resist populist pressures to turn protectionist in the current crisis, as happened during the Great Depression. EU supervision of national investment planning and implementation in the context of regional aid expenditures has also been seen to help reduce the scope for detrimental outcomes.

The advantage of occasional changes in government appears when we consider the case where governing parties are locked into growth-inhibiting ideologies. The success of the policies adopted by a short-lived non-Fianna Fáil coalition government to attract export-oriented businesses in the 1950s facilitated Fianna Fáil in dropping its ideological objections to foreign industry. Something similar may arguably be seen in the legacy bequeathed to subsequent Labour governments in the UK by the Thatcher administration. The policy learning process may take much longer in non-democratic or effectively single-party systems, as evidenced by the prolonged economic failures of Mao in China or the long stagnation of Northern Ireland under Unionist Party domination.

By strengthening the export lobby, the policy changes of the 1950s facilitated further reforms because these interests favoured EU accession. All astute reform-minded politicians know the importance of assembling a coalition that stands to benefit from the reforms. This alignment between sectional interests and the broader public good is typically only temporary however, and the initial reforms may endow these interests with a privileged position which

Impact of Technology', in A. J. Meijer, K. Boersma and P. Wagenaar (eds), *ICTs, Citizens and Governance: After the Hype* (Amsterdam, 2009).

[40] T. Friedman, *The Lexus and the Olive Tree* (New York, 2000).

can be used to stymie further reforms. While strongly supportive of EU entry, for example, Irish agricultural interests upon accession became highly resistant to further liberalisation at the global level.[41]

Besides the cover available from external commitments, other sources of political cover required for the adoption of reforms might also be available domestically. Social partnership, as we have seen, played such a role in the fiscal consolidation of the late 1980s, while the public service bureaucracy provided cover for the shift away from protectionism in the late 1950s.

Occasionally, of course, politicians choose not to avail themselves of whatever cover against populist pressures might be on offer. Recent Fianna Fáil administrations rejected the cover that Brussels criticisms of Irish fiscal policy would have provided if they wished to move to a more appropriate counter-cyclical stance. Political factors, in the form of forthcoming general elections, were instead allowed to dominate. And the detrimental consequences of being too close to one particular interest group, the construction and property development sector which gained most from the property bubble, are now all too evident.

Of course, not all private-sector lobbying attempts to secure outcomes against the national interest. Some may be to convey genuinely useful information that can, if accepted, trigger beneficial government responses. An efficiently-functioning public-sector bureaucracy can act both as buffer and as channel of communication between the private sector and government, and can assist government in distinguishing one form of lobbying from the other.

The IDA and its sister agencies have played such a role in relation to foreign-owned industry, and it is significant that while Ireland's position in the international-corruption-perceptions-rankings has deteriorated in recent years, the sectors investigated by the various tribunals and inquiries of recent times – property, retail banking, beef, domestic telecommunications – have not been the ones dominated by export-oriented foreign multinational corporations.

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[41] F. Barry, 'Agricultural Interests and Irish Trade Policy over the Last Half-Century: a tale told without recourse to heroes', Working Paper No. 91 (2009), Institute for British-Irish Studies, University College Dublin.