The Celtic Tiger

How Did it Happen?

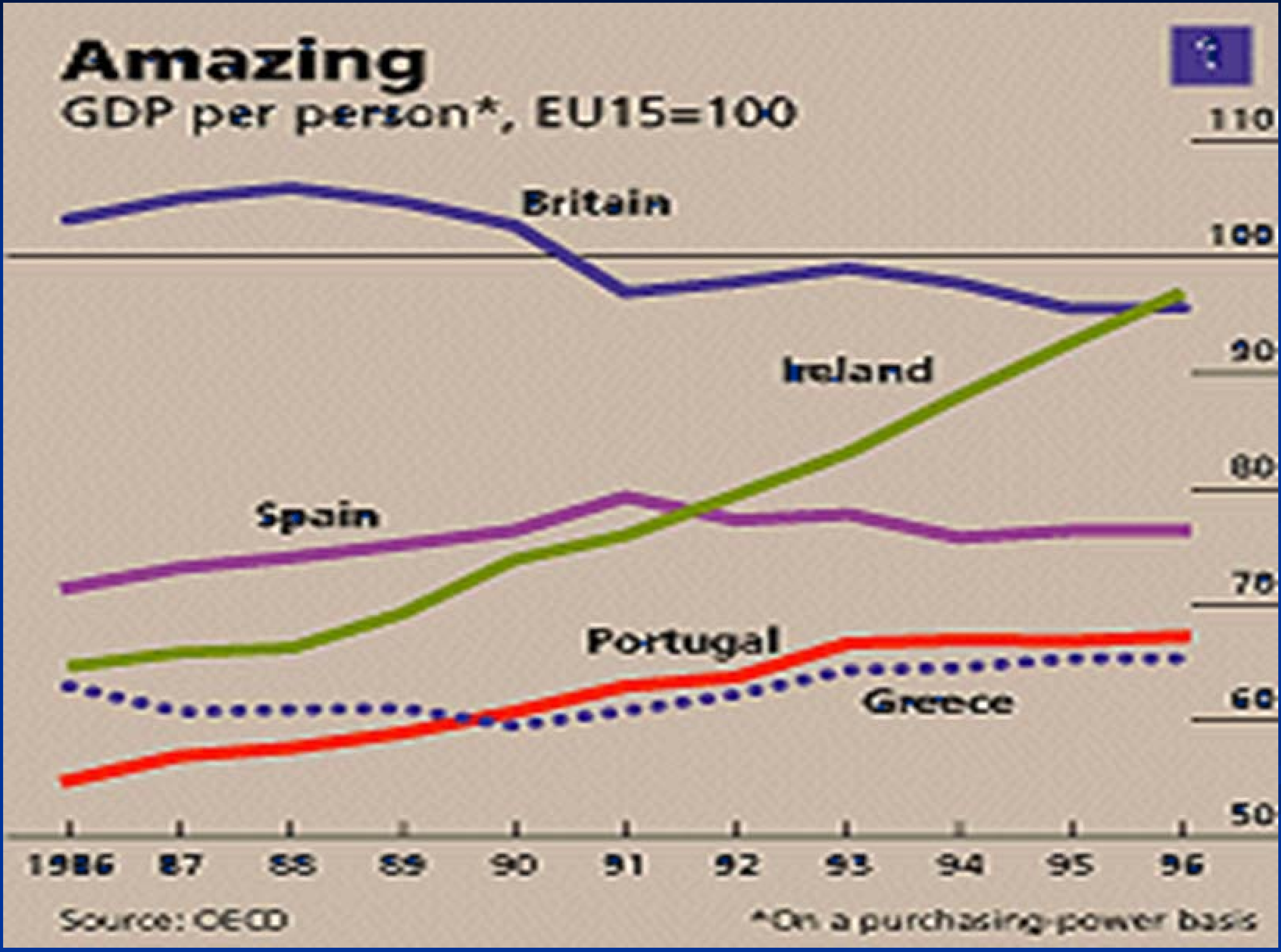

100 km
ATLANTIC OCEAN
Londonderry
NORTHERN IRELAND
Aldergrove
Belfast
Sligo
Dundalk
REPUBLIC OF IRELAND
Dublin
Galway
Leixlip
Dublin
Shannon
Wicklow
Shannon
Limerick
Kilkenny
Irish Sea
Wexford
Waterford
Cork
Cork
Celtic Sea

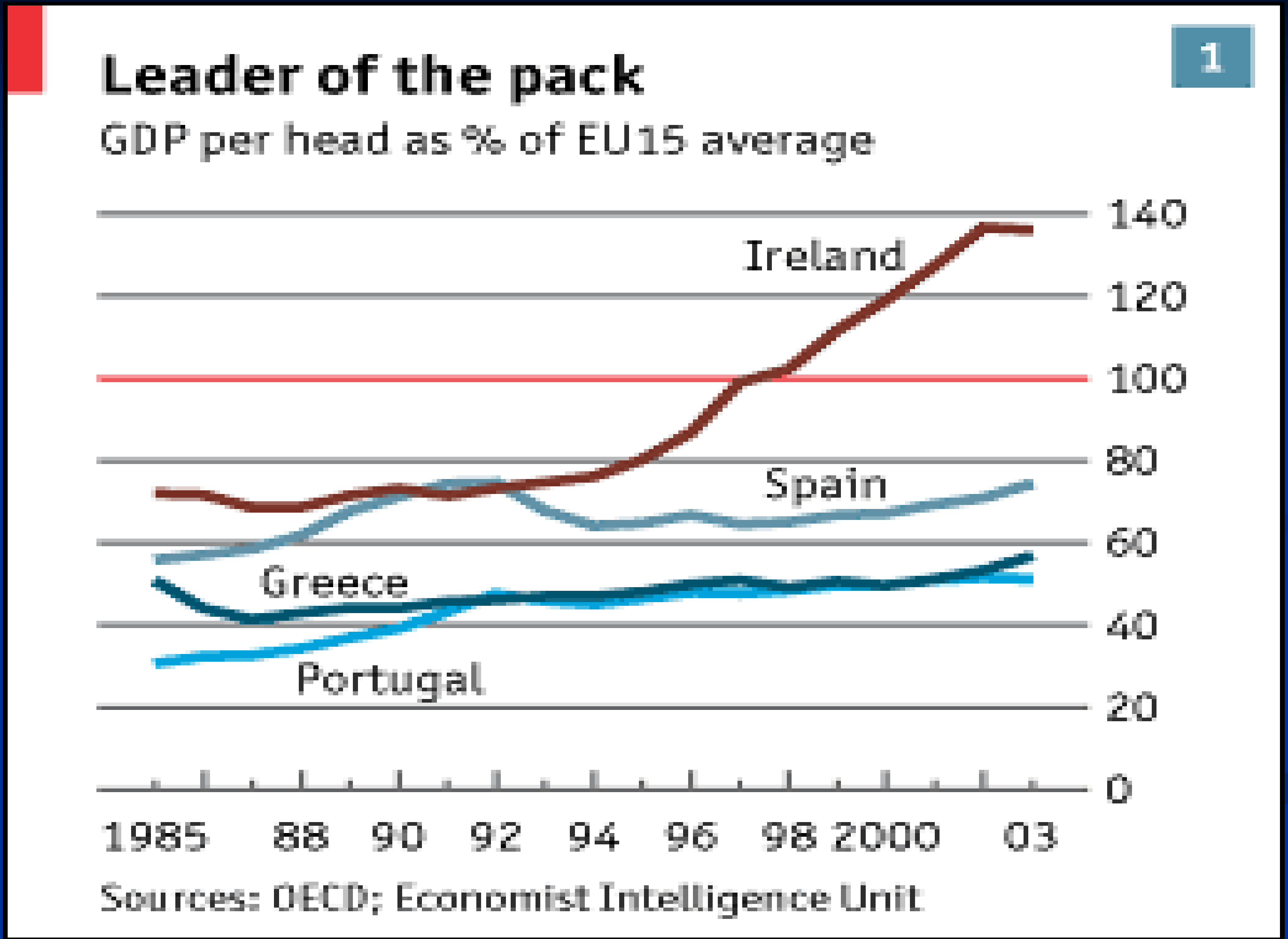
Readings

- A Survey of Ireland, The Economist, 16 October 2004
- A Model of Success: what can central Europe learn from Ireland? The Economist, 14 October 2004
- Green is Good, The Economist, 15 May 1997
- John Fitzgerald, "The Story of Ireland's Failure – and Belated Success", in Brian Nolan, Philip O'Connell, and Christpher Whelan (ed), Bust to Boom? The Irish Experience of Growth and Inequality, Institute of Public Administration, Dublin, 2000
- Paul Sweeney, The Celtic Tiger, Oak Tree Press, Dublin, 1998
- Tom Garvin, Preventing the Future: Why was Ireland Poor For So Long? Gill & Macmillan, Dublin, 2004

The Economic Miracle

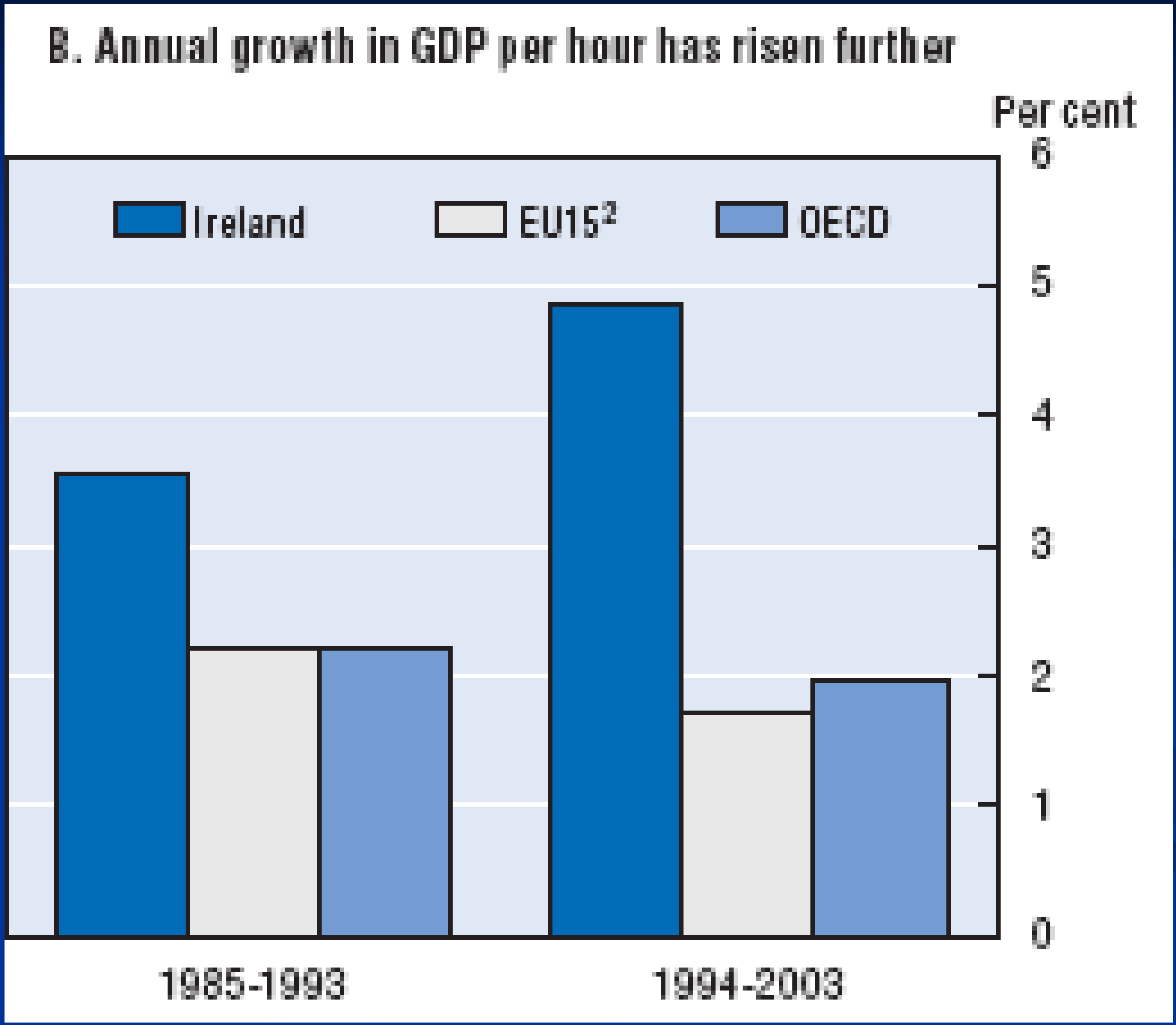
- In 1986, Ireland, along with Portugal and Greece, was one of the three poorest countries in the EU
- Income per person in Ireland was 65% of the EU average
- By 2003, per capita income in Ireland was 40% above that of the EU while Greece and Portugal remained amongst the poorest of the EU countries
- So, how it happen and what can we learn from Ireland?

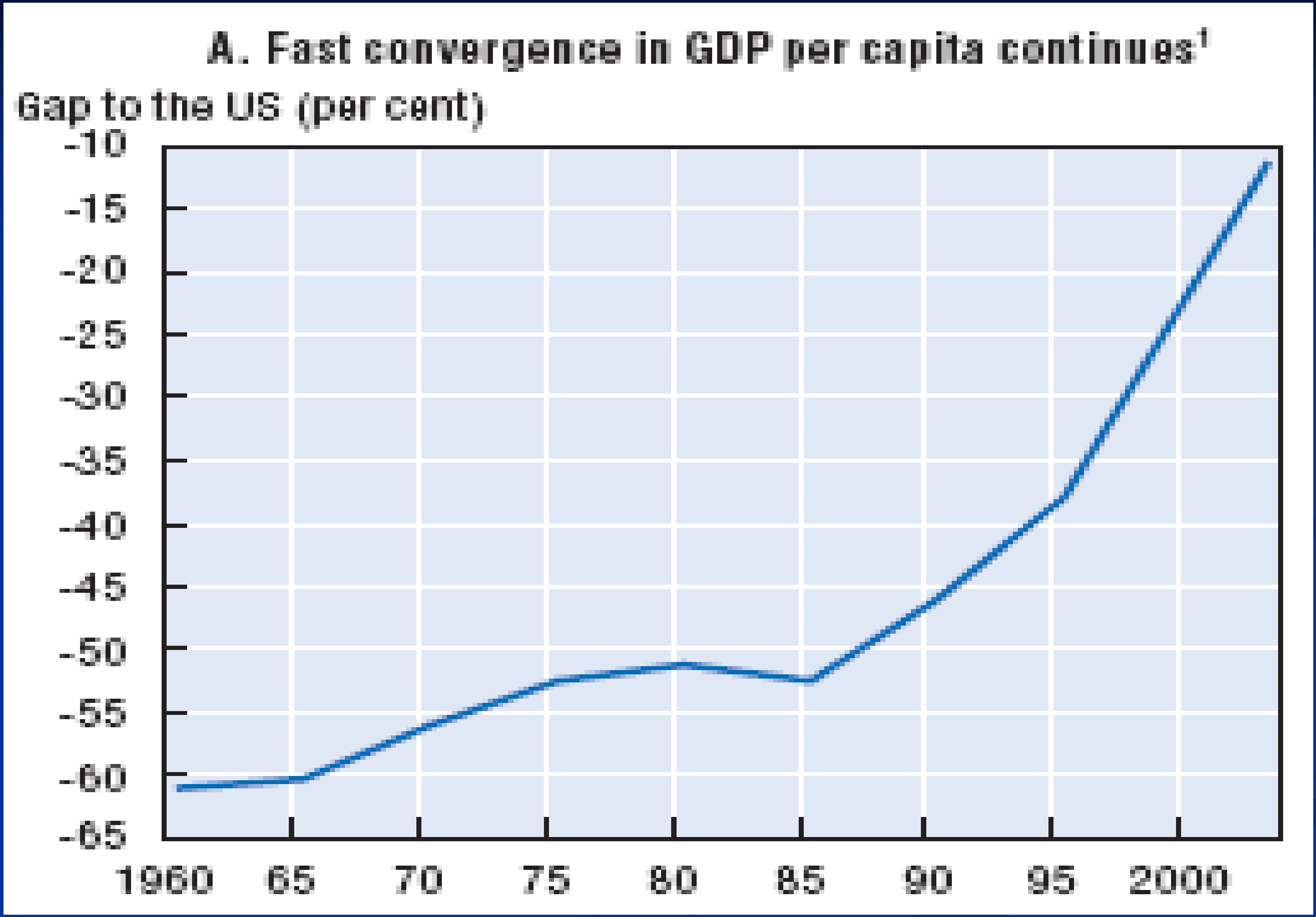

Amazing
GDP per person*, EU15=100
Britain
Ireland
Spain
Portugal
Greece
110
100
90
80
70
60
50
1986
87
88
89
90
91
92
93
94
95
96
Source: OECD
*On a purchasing-power basis


1
Leader of the pack
GDP per head as % of EU15 average
Ireland
Spain
Greece
Portugal
140
120
100
80
60
40
20
0
1985
88
90
92
94
96
98 2000
03
Sources: OECD; Economist Intelligence Unit

The Celtic and Asian Tigers: GDP Growth (% per annum)

	1995	1996	1997	1998	1999
Ireland	11.1	7.4	9.8	9.1	8.3
South Korea	8.9	7.1	5.5	-5.7	0.5
Singapore	8.8	7.1	5.5	-0.8	0.5
Hong Kong	4.6	4.7	5.3	-5.7	1.5
Taiwan	5.9	5.7	6.0	3.7	3.7


B. Annual growth in GDP per hour has risen further
Per cent
Ireland
EU15²
OECD
6
5
4
3
2
1
0
1985-1993
1994-2003


A. Fast convergence in GDP per capita continues[1]
Gap to the US (per cent)
-10
-15
-20
-25
-30
-35
-40
-45
-50
-55
-60
-65
1960
65
70
75
80
85
90
95
2000

Structural indicators

	1990	1995	2000	2003
Trend GDP per capita (% growth rate)	4.8	6.6	6.4	3.8
Trend employment rate	54.2	57.9	63.7	65.8
Trend participation rate	63.3	65.2	68.2	69.8
Structural unemployment rate (NAIRU)	14.4	11.1	6.6	5.7

Source: Estimates based on *OECD Economic Outlook*, No. 76.

Productivity: GDP per person employed per hour (US$)

- **Ireland 48.73**
- France 44.53
- USA 43.22
- Germany 36.17
- Netherlands 35.01
- UK 33.23

  Source - IMD World Competitiveness Yearbook 2005

Policies for Growth

- Opening up of the Irish economy through membership of the European Union
- Active encouragement of foreign direct investment
- Investment in Human Capital
- The Reform of Public Finances

History

- In 1922, Ireland's standard of living was higher than in many Western European countries
- For the next 40 years its economic performance was dismal
- So one way of viewing today's success is a belated catching with past success
- Ireland has worked very hard at failing and, today, even that policy is not working!

The Dismal Years: 1922-1962

- Ireland had a highly protectionist economy with high tariff barriers
- It was isolationist – exemplified by its WW2 neutrality
- It was a rural country dominated by agriculture
- Socially and culturally it was dominated by the Catholic Church with censorship of books
- There was very little recognition of the importance of, or investment in, education
- Emigration in search of job opportunities was a way of life: in 1960, Ireland's population was only 2.8m

Prosperity Delayed

- The most important aspect of Ireland in the period 1930-60 was the important role of the Church in Irish affairs
- The partnership between the Catholic Church and the Irish State was one of the most conspicuous features of Irish society:
  - it was the main provider of education
  - it ran the health system
  - It was the ultimate arbiter of social and cultural affairs
  - It maintained a tight censorship on works of art and literature
  - In effect, it was a "state within a state"

Preserving Ireland

- Both the Church and de Valera wanted to keep Ireland a rural and devoutly Catholic country, even though the rest of Western Europe was becoming more urban and secular
- They saw the spread of education as the biggest threat to the Church
- As the mass of people became educated, particularly in technical subjects, they would become less respectful of the Church
- So, preventing the spread of education in particular, and modernity in general, was a central purpose of Church-supported government policy
- "Picking Ireland" as one commentator described it

Education in Ireland: 1922-60

- A large proportion of children left school at age 12
- Restrictive employment practices discouraged education: for example, banks only hired people below 21 years old
- The age of entry into apprenticeships was below 15-16
- One could not be a graduate and work in a bank
- One could not have a high school leaving certificate and be a skilled tradesman
- Language teaching was a prominent part of secondary education: English, Irish, and Latin
- Vocational schools were frowned upon because:
- Teachers were lay
- Vocational education took people off the land and into cities

Seam Lemass, Taoiseach: 1959-66

- The instrument for change was Sean Lemass who became Taoiseach on 23 June 1959
- Lemass summed up his economic philosophy in one simple phrase: "A rising tide lifts all boats."
- By this he meant that an upsurge in the Irish economy would benefit both the richest and the poorest.
- *First Programme for Economic Expansion* was adopted by Lemass as policy. The programme, involved a move away from the protectionist policies that had been in place since the 1920s

The Opening Up of Ireland: I

- Tax breaks and grants were also to be provided to foreign firms wishing to set up a company in Ireland
- The programme also paved the way for free trade. In 1960 Ireland signed the General Agreement on Tariffs and Trade (GATT), a worldwide agreement to reduce tariffs.
- In 1961 Ireland applied (unsuccessfully) for membership of the European Economic Community
- In 1965, Anglo-Irish Free Trade Agreement between Lemass's government and Harold Wilson's government was signed

The Opening Up of Ireland: II

- There was £220 million of state investment in an integrated system of national development
- The Control of Manufacturers Act, which had been in place since 1932 was abolished.
- The establishment of the state television service, Telefís Éireann in 1962.
- Television programmes, such as *The Late Late Show* and imported American and British ones, had a profound effect on a change in attitude
- Subjects such as contraception, the Catholic Church and divorce were being discussed openly

Education in a New Ireland

- In 1965 a new report called "Investment in Education" was published
- After over forty years of independence the report painted a depressing picture of a system where no changes had taken place
- Every year, 17,000 children left school after finishing primary school
- In 1965, Donough O'Malley announced free education to leaving certificate at age 18 and free buses provided transport for students
- This was "O'Malley's bombshell" because he made this announcement without consulting anyone
- This was followed by the expansion of vocational & technical education through Regional Technical Colleges
- The RTCs were accompanied by two National Institutes of Higher Education (NIHE): now University of Limerick and Dublin City University

Education in Ireland Today

- Even in the 1980s, when the economy suffered cutbacks, education was largely protected
- Of those entering the workforce today (20-29 years):
  - 50% have third-level education
  - 80% have School Leaving Certificates
- By contrast, of the over 65s in Ireland:
  - Only one-third went beyond primary level
  - Less than 10% had third-level education

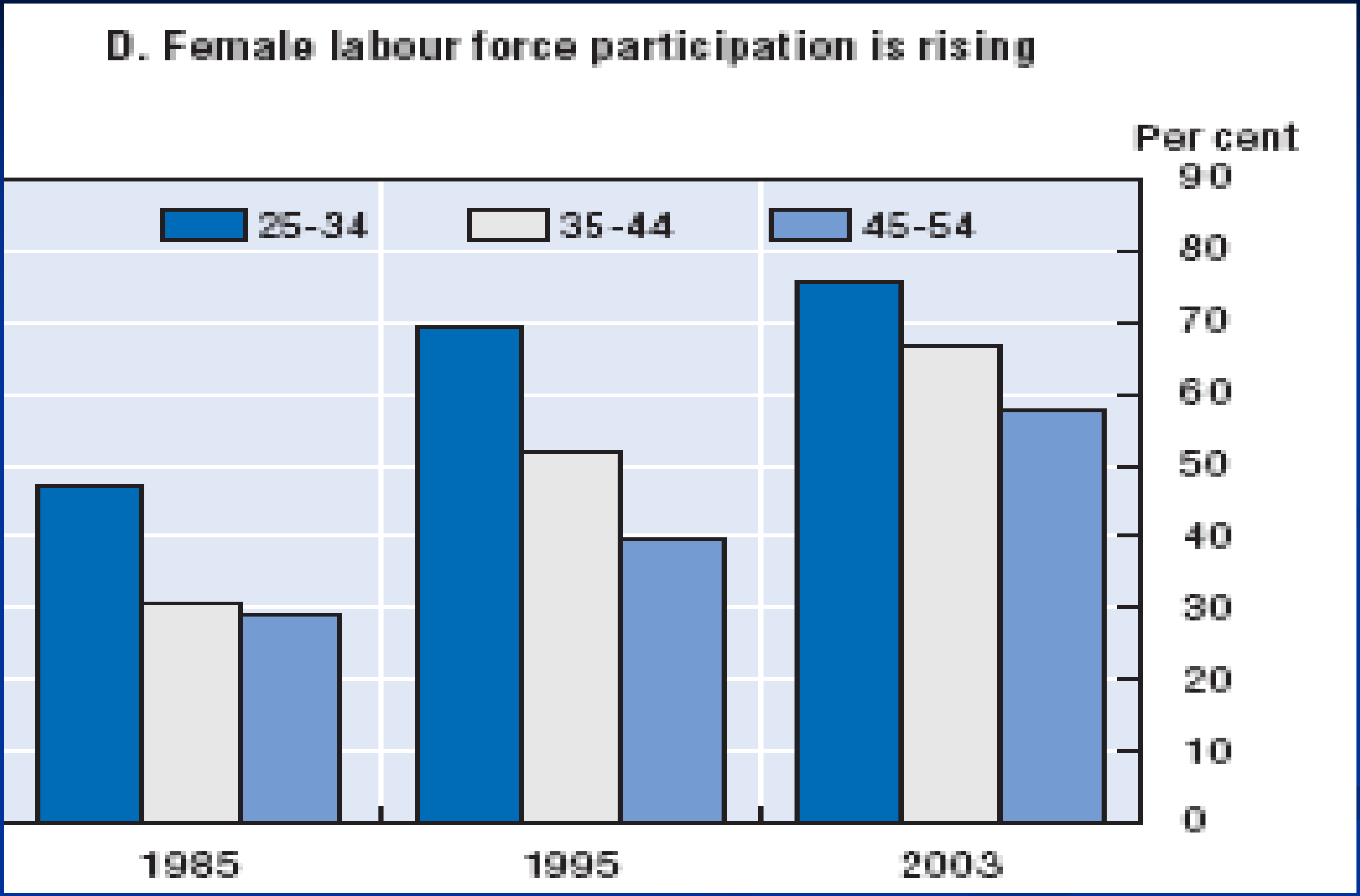
Skilled Workforce:
Science and Technology graduates per thousand in the 20-29 age group.

- **Ireland 23.2**
- France 19.6
- UK 16.2
- USA 10.2
- Germany 8.2
- Portugal 6.3
- Netherlands 5.8

Source - Eurostat 2003.

Women in the Labour Force

- There has been a dramatic increase in women’s participation in the labour force
- This increase is for all women, irrespective of education level
- But women’s participation has gone up because Irish women are better educated


D. Female labour force participation is rising
Per cent
25-34
35-44
45-54
90
80
70
60
50
40
30
20
10
0
1985
1995
2003

Migration

- Up to the 1980s, the bulk of emigrants had limited education
- After 1980, emigrants were generally skilled and educated
- There has also been considerable *return* migration to Ireland: Irish men and women living abroad are returning to Ireland
- Most of these return migrants are well-educated and skilled workers

Labour Supply

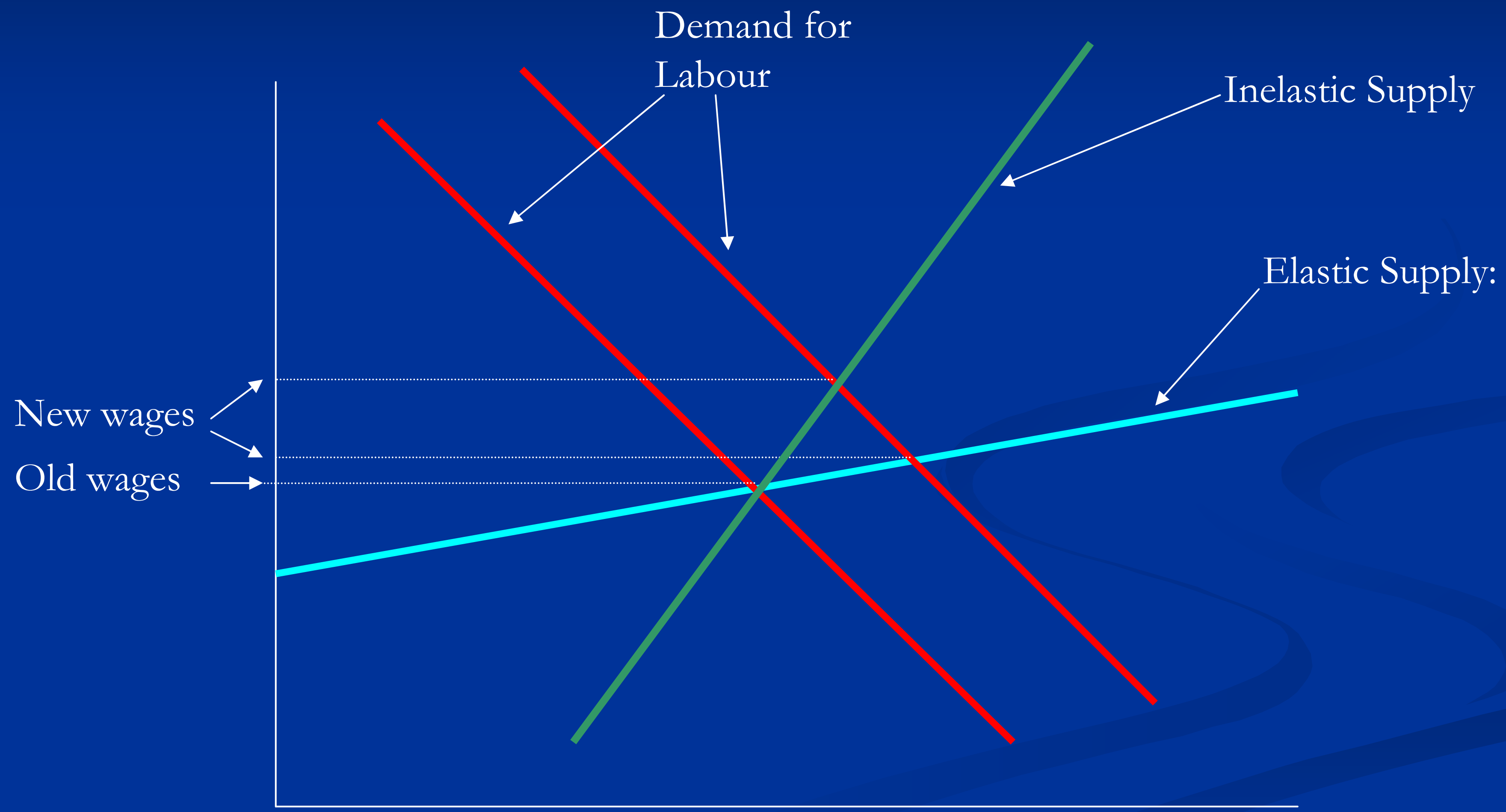
The combination of:

- higher levels of education for all, but particularly for women
- Higher female participation rates, particularly of educated women
- Return emigration, particularly of educated persons

means a highly elastic supply of skilled labour

So, the economy can expand without pushing up skilled wages

Non-inflationary expansion



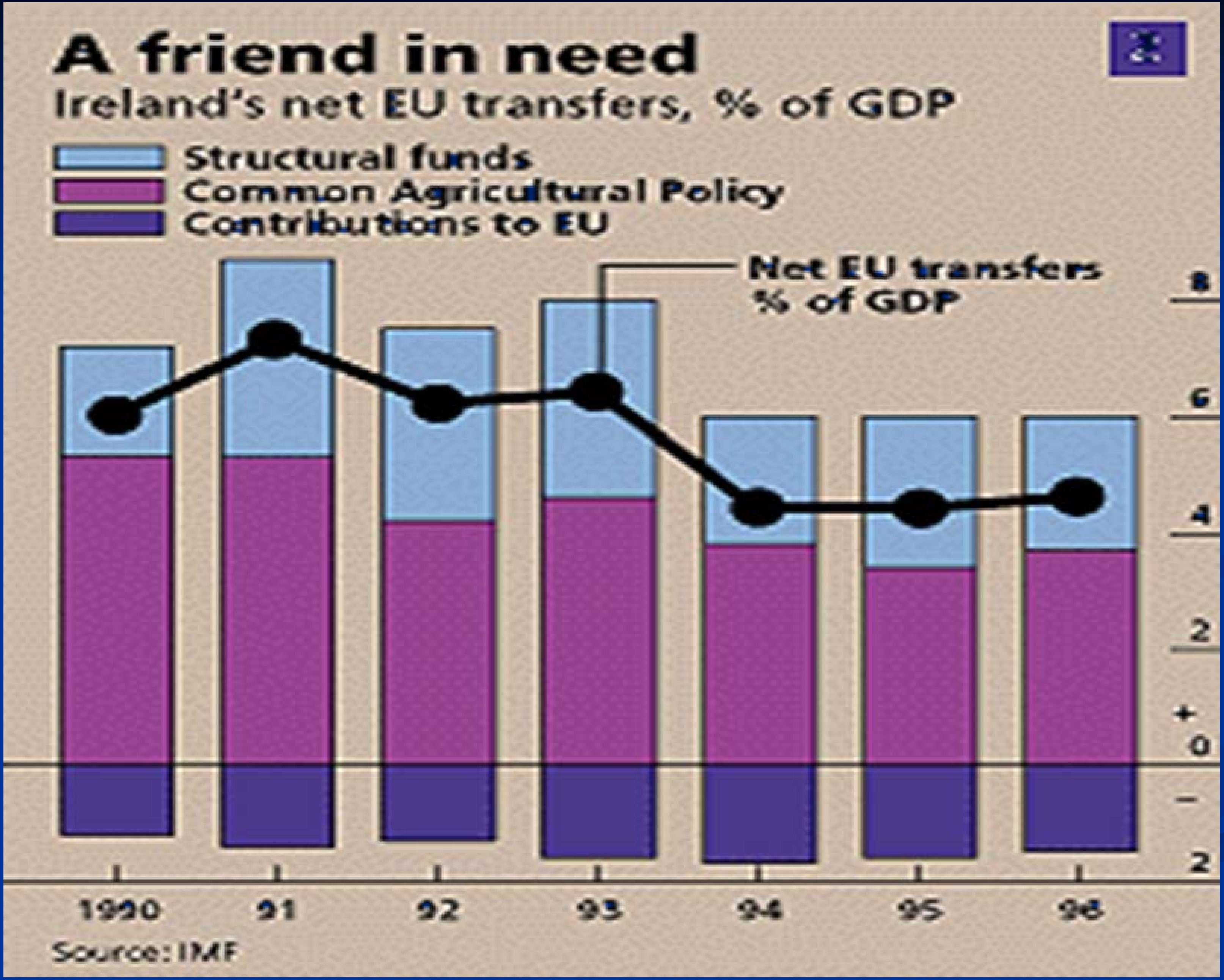
Labour Force Participation

- The numbers in work in Ireland have increased from 1.2m in 1993 to 1.8m in 2003
- This accounts for half of Irish growth in the 1990s

EU Membership

EU membership in 1973 gave Ireland access to:

- ✓ The Single Market: Ireland was an attractive destination for foreign direct investment because it gave access to the EU
- ✓ Structural Funds:
- Underpinned essential public investment in infrastructure
- It forced the introduction of long-term planning and rigorous evaluation procedures in infrastructure investment


A friend in need
Ireland's net EU transfers, % of GDP
Structural funds
Common Agricultural Policy
Contributions to EU
Net EU transfers
% of GDP
8
6
4
2
+
0
–
2
1990
91
92
93
94
95
96
Source: IMF

Foreign Direct Investment

A major plank of Irish economic policy has been to attract foreign direct investment

- This policy has been followed consistently by successive governments over 40 years
- The low rate of corporation tax has been a major incentive
- Another incentive has been the ready supply of skilled labour at reasonable cost

Result

- Today, Ireland takes 25% of all US FDI in Europe, with one-third of all FDI in pharmaceuticals and health care
- One-third of all computers in Europe are manufactured in Ireland
- It is the world's biggest software exporter
- It has 1,100 multinational companies which export $60bn per year

European Corporate Tax Rates for substantial distributed trading profits

Rates of Corporation Tax

Ireland	**12.5%**
Cyprus	10%
Latvia	15%
Lithuania	15%
Hungary	18%
Poland	19%
Luxembourg	23%
Portugal	25%
Slovenia	25%
Estonia	22%
Germany	26%
Czech Republic	26%
Sweden	28%
Finland	29%

US Investment per Head of Population

- Ireland $3,000
- UK $2,000
- France and Germany $500
- Spain $200

Restructuring the Irish economy

The success in attracting FDI has meant that the Irish economy has been completely restructured:

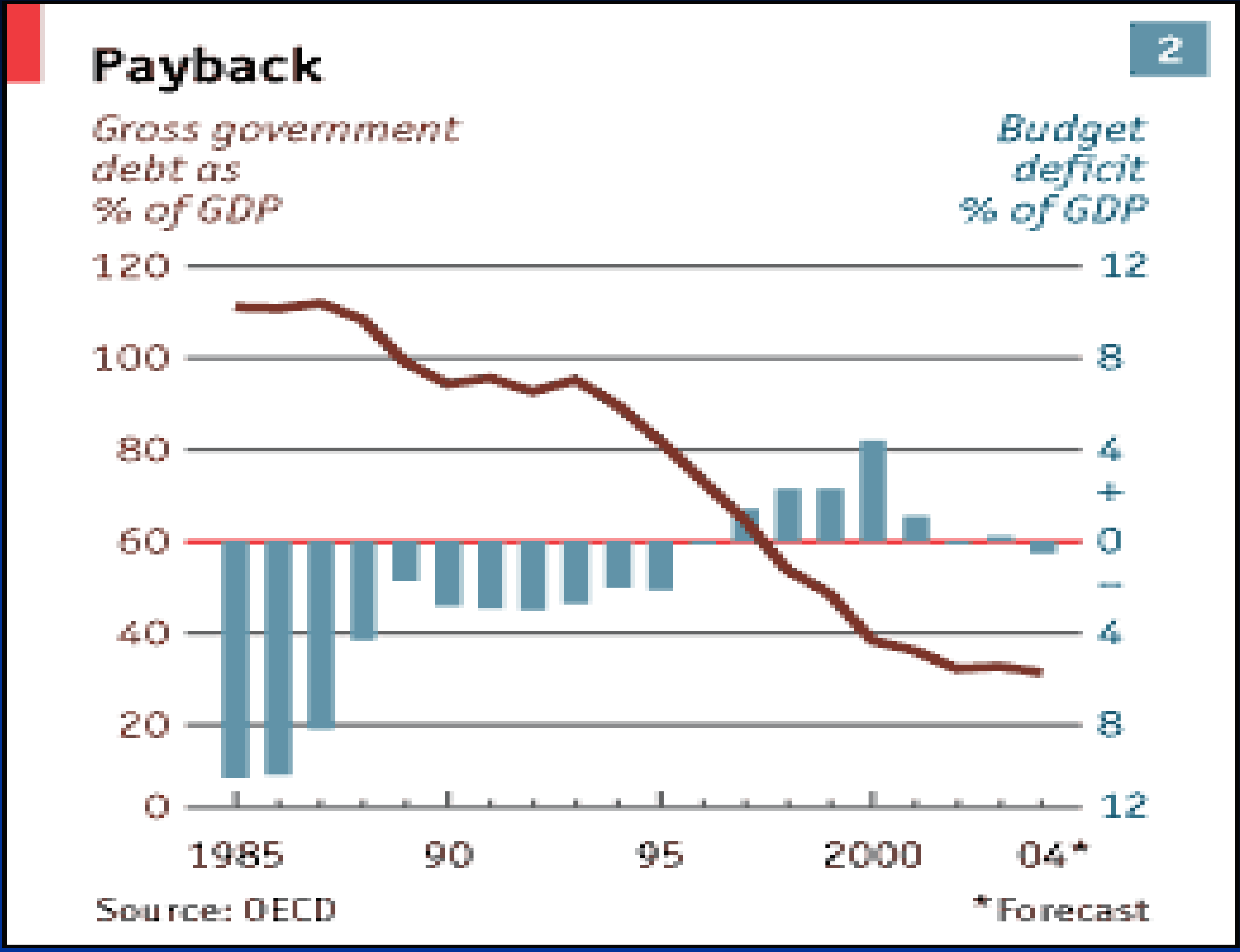
- It has shifted from an agricultural to a manufacturing country
- From a rural to an urban country
- From low technology traditional manufacturing to high technology new manufacturing computers, electronics
- Since 90% of the output of foreign companies is exported, compared to 36% of Irish companies, Ireland has become an export-oriented economy

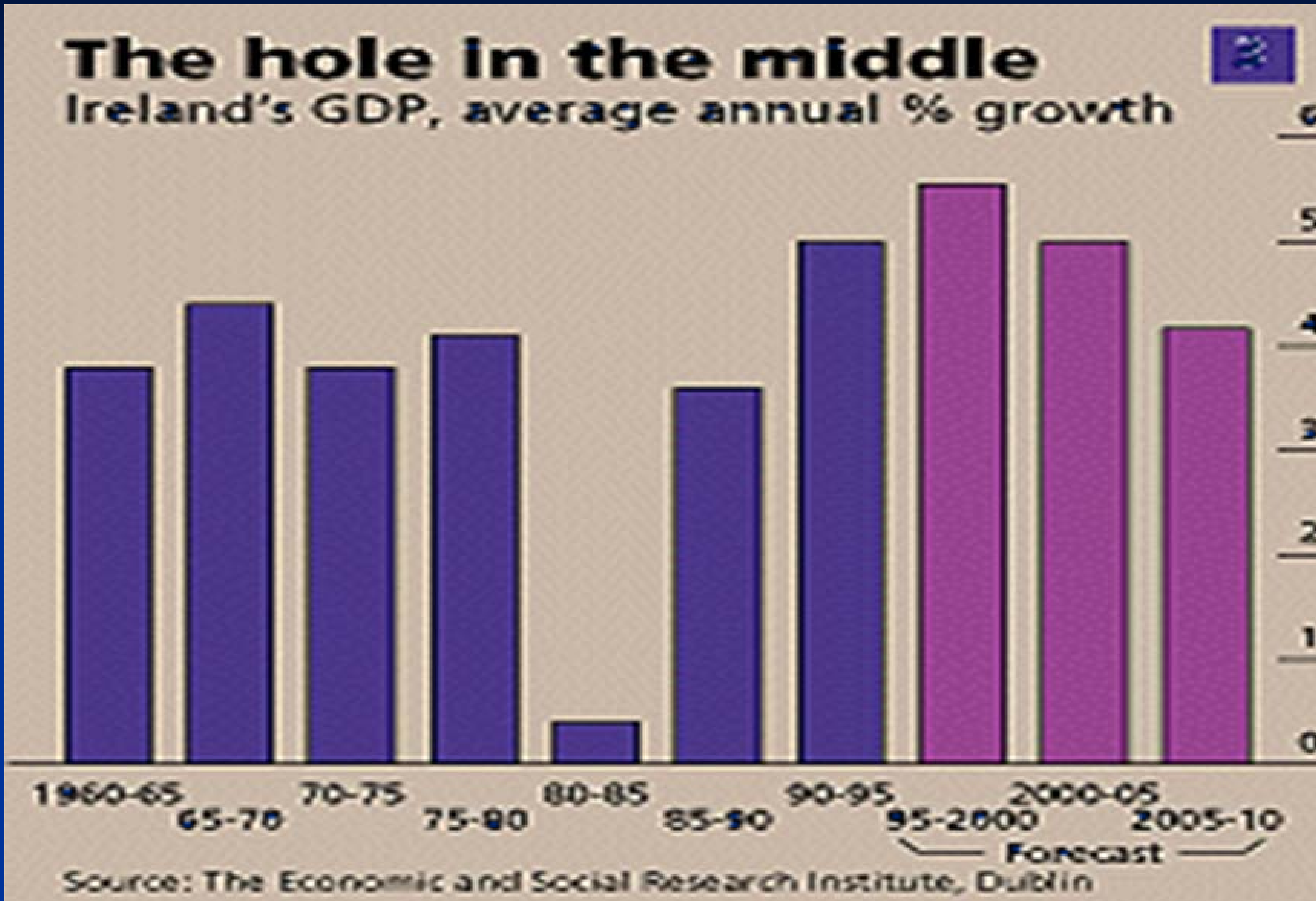
Mistakes Along the Way

- In 1977, the Fianna Fail government decided to make a "dash for growth"
- This involved a huge injection of money into the economy through tax reductions and public expenditure increases
- National debt reached 125% of GDP and interest repayments began to dominate the budget

Fiscal Reform

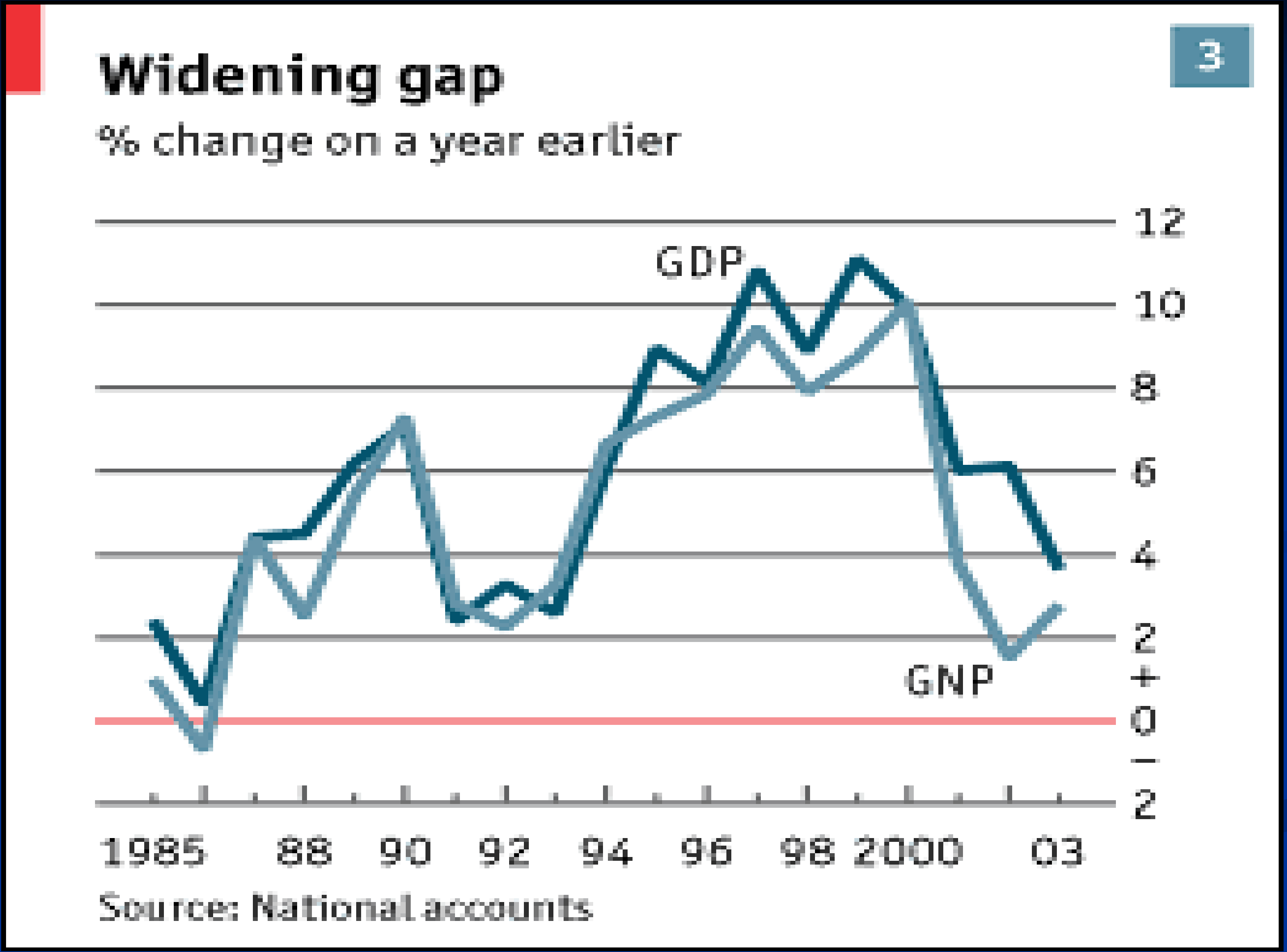
- Fiscal reform was begun by the Fianna Fail government of 1987 with the support of the opposition Fine Gael party
- The budget deficit and borrowing were cut very sharply
- By 1994, the Irish budget was in surplus and debt had fallen as a proportion of GDP


Payback
2
Gross government debt as % of GDP
Budget deficit % of GDP
120
100
80
60
40
20
0
12
8
4
+
0
–
4
8
12
1985
90
95
2000
04*
Source: OECD
*Forecast


The hole in the middle
Ireland's GDP, average annual % growth
6
5
4
3
2
1
0
1960-65
65-70
70-75
75-80
80-85
85-90
90-95
95-2000
2000-05
2005-10
Forecast
Source: The Economic and Social Research Institute, Dublin

Gross Domestic Product versus Gross National Product

- A country's standard of living can be measured either by GDP or GNP
- For Ireland, because of profit repatriation by overseas companies, GNP is a better measure
- GNP does not show Ireland in as good a light as GDP



Widening gap
3
% change on a year earlier
GDP
GNP
12
10
8
6
4
2
+
0
–
2
1985
88
90
92
94
96
98
2000
03
Source: National accounts

Can it Last?

On one argument Ireland's recent success is because it has "caught up" with other countries in:

- Education
- Women's participation

Other advantages are immutable and will not increase:

- English-speaking
- Responsible public finances

Other advantages are temporary:

- Demographics: Ireland has a relatively young population relative to other European countries because its birth rate fell later

Difficult Future

- Ireland needs to continue with fiscal discipline, particular since low European interest rates are heating its economy
- Otherwise higher inflation in Ireland will erode its competitive advantage
- Its needs to beware of the Dublin "housing bubble" and a potential property crash
- In general, construction is overheating: its accounts for 15% of national income and built 80,00 new houses in 2003