The National Plan

By Joe Durkan,
DKM Consultants.

There is a general belief among economists that the Irish economy needs no further analysis – what is required is action based on the analysis already done. The difficulty with this is that the people who do the analysis either (i) sometimes shy away from the policy implications and propose a whole set of actions independently of that analysis or (ii) have no role in the formulation of policy so that policy formulation tends to pay mere lip service to the analysis, but effectively ignores it for political or other reasons.

Recent “planning” exercises fall into the second category. We are invited to enchain analysis – after all it has already been done – and the “Plan” is what we are going to do. The implication is that the set of proposals (if any) in the “Plan” follow from the analysis. The strategy is presented as an outcome of the analysis of the causes of the problems identified, the instruments of policy are related to strategy, and all instruments are consistent in their application.

What is the Core Strategy?

The most recent “Plan” – Building on Reality 1985–1987 – differs slightly from previous exercises in that the core strategy is not so readily apparent. In “The Way Forward” the strategy was clearer but not the means by which it was to be implemented. The economy was to be driven by competitive gains leading to a rapid growth in exports, both absolutely and relatively to imports; the balance of payments were to go into surplus; the public finances were to improve mainly because of the growth in the economy; and employment was to rise (with unemployment falls in 1985). The difficulty with the strategy was the reliance on competitive gains since Government has no instrument of policy to vary wage rates. It is of some interest to note that the realisation of the central weakness of “incomes policies” by persuasion led many to advocate tax reductions financed by expenditure cuts as a means of influencing the size of wage settlements through the effects on real disposable income. This is not to be confused with “tax concessions” as an input into centrally negotiated pay agreements – an entirely different concept.
The strategy in "Building on Reality" is very much different. If one were to ask "What is the Government going to do?" it would be very hard to go beyond the general statement that it intends to do very little. It intends to hold the level of taxation constant, and to reduce net expenditure compared to what it otherwise would be by a combination of a fall in the real level of pay expenditure, a reduction in subsidies, increased charges for services, and the natural wastage inherent in the Public Capital Programme when some semi-State investment projects are completed. Essentially this is like saying "we will do nothing". It is a measure of how acutely governments have mismanaged the economy over the past ten years that the most hopeful comment that can be made about this recent "Plan" is that it may not damage the economy too much in the long run. This is a far cry from the strategy adopted by two other countries, Sweden and New Zealand beset by similar problems — though not too different from the "muddle-through" policy of some other countries.

Given that this is the nature of "Building on Reality", it must be said that the document is unexciting. There are one or two innovative ideas but the rest is unremarkable.

Macro-Projections Reasonable

The macro-projections are reasonable, given the assumptions. While the assumptions with regard to the world economy have been criticised as being too optimistic it is clear these criticisms are based on a very short run of recent observations when the world economy was experiencing the deepest recession for decades. I would be more hesitant about the use of world trade, even weighted by our trade pattern, as a measure of growth in markets. Market growth in general is measured by GNP growth; after that it would be useful to look at demand patterns by broad sectors and commodities. Moreover the assumption is really saying that the world economy is likely to grow slowly over the period to 1987 — there will be no major boom or slump. That is the consensus view among forecasters. Nor is the belief that U.S. interest rates are likely to come down unreasonable — indeed recently such a fall has occurred. It would be of interest to know to what extent the interest payments (foreign) implicit in the document would be revised in the light of current rates. The extent of the fall in domestic rates is a different matter and is related to external borrowing targets of Government. It would be a mistake to assume a ready and equal fall in domestic interest rates, given the apparent targets for external debt.

Public Sector Pay

The assumption with regard to public sector pay is too optimistic unless Government is set to trade off public sector employment
against pay increases. The implication from speeches of some Government Ministers is that, if pay differs from that outlined, real tax rates will have to be increased. This would affect real labour costs and employment in the private sector and would weaken the long-term output capacity of the economy – very much as has occurred over the past 3 – 4 years. There is no evidence that Government is aware of the effects of increased real taxes on labour costs, though it does have some notion that taxes are “too high”. The difficulty with unfocussed beliefs is that there are no objective criteria against which to judge the “height of taxes” and this induces the predictable response that taxes are higher elsewhere (without of course bothering to adjust for income, family size, level of services, etc.); or that more could be collected in other forms of taxes (without considering that it is usually the same people who are paying all taxes).

The reality is that the wage bill will be higher than Government has allowed. The difference will be financed by relatively higher taxes (or reduced subsidies or increased charges for services – it matters not). This in turn will impact on wage rates in the private sector – causing them to be higher than they would otherwise be – and this in turn will affect the sustainability of employment in the private sector. This has been our recent experience and there is no reason to believe that it will be any different on the basis of “Building on Reality”. The only positive thing one can say is that the pay bill might be less in 1984 than assumed in the document and this might give some leeway. Obviously the projections would be subject to some change depending on the extent to which pay did grow; but unless the pay settlement in the public sector is grossly excessive, the changes would appear to be marginal over the time period for the broad macro-aggregates – though not for employment.

Fundamental Defects

The issues raised by the deficiencies in “Building on Reality” go far beyond the question of the numbers. It is as if the Government has no conception as to how an economy can function, or of those factors that actually hinder an economy, or indeed of the things a government must do to ensure that the economy functions better. The White Paper on industrial policy is condensed – it apparently is to form the basis of policy, yet most had hoped it could be decently buried once it was published. A document that castigates indigenous firms for their assumed and asserted weaknesses without asking why these weaknesses exist (if at all) cannot be taken seriously. This criticism is independent of that which could arise from a consideration of the deficiencies of those making policy – rarely can enterprises have shown such poor management as government departments.
and agencies. The innovative nadir in our society is surely the public sector.

The most disturbing aspect of "Building on Reality" however is an entirely different issue. It is the apparent failure of the public sector to respond intellectually to the problems of the society. There is no sense of excitement or challenge. By contrast with the first, second and third programmes it is a sorry document. If this is the best the public sector can come up with then we have to start again. If that intellectual response was in fact there, but was stifled by the short-term needs of politicians, then we are in still deeper trouble.