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The Economic Development of Ireland Since 1870

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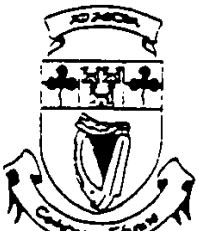

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THE ECONOMIC DEVELOPMENT OF IRELAND SINCE 1870[1]

Introduction

A. 1870-1921:

Few historians deem Irish economic development since 1870 much of a success story. Their gloom is supported by aggregate output and income data, which show Ireland's national income growing more slowly (at less than one percent annually) between 1850 and 1914 than anywhere else in Europe. However, the massive declines through emigration in both the population and the labour force partly explain this snail's pace progress. National income per head grew at a more respectable rate, about 1.5 percent, in that period: enough, indeed, to produce some convergence between living standards in Ireland, on the one hand, and in Great Britain and elsewhere in Europe before the First World War, on the other. Irish income per capita, about two-fifths of British in 1845, had reached about 56 percent of British by 1914 [Kennedy *et al.*, 1988, ch. 1; Ó Gráda, 1994a, ch. 15; Maddison, 1991]. This left the average Irishman and Irishwoman well behind their Danish counterparts in terms of material comforts and slightly behind the Swedes on the eve of the First World War, but well ahead of the Spaniards and Italians. Relative wage movements, spurred on by emigration, also showed convergence between Ireland and its richer neighbours in this period [Hatton and Williamson, 1993; Williamson, 1993]. Within Ireland, wage rate movements implied some convergence too, between the richer east and the poorer west. The rise in living standards brought improved education, better housing, greater commercialization, and big rises in the consumption of everyday comforts such as meat, tea and sugar, shop bread, mass-produced clothes, and travel. In terms of the movement in incomes per head since 1914, Ireland has gained a little further ground on Britain, but fallen behind relative to most other European economies. By west European standards, Ireland remains a poor country. & Before the Tiger boom

Though Ireland's *share* of the United Kingdom's industrial output was probably in decline throughout the nineteenth century, aggregate Irish industrial output continued to rise. The rise was regionally concentrated, but notable in some cases. Thus by the early twentieth century, Ireland was the world's greatest producer of fine linen cloth, it contained the world's biggest

brewery (Arthur Guinness) and the biggest rope factory (the Belfast Ropeworks), and Harland and Wolff were producing the world's most advanced and biggest ships. Engineering and shipbuilding, both concentrated in the Belfast region, were among the most dynamic sectors before 1914. Between 1878 and 1913 Belfast's shipbuilding output rose by an average annual rate of nearly 8 percent [Geary and Johnson, 1989: 45], but advances in other important Irish industries such as brewing, distilling, linen, and butter were far more sluggish, and some industries - notably flour-milling, shoe-making, and tanning - declined [Bielenberg, 1991; Weir, 1980]. Ireland's last major cotton textile producer - the great Malcolmson mill at Portlaw in County Waterford - collapsed in 1876. Industrialization was virtually confined to coastal towns and their immediate hinterlands, and the partition of Ireland in 1920-1 left the newly-constituted Irish Free State[2] with few major industries. Trade data reflect this: industrial manufactures accounted for nearly two-fifths of Irish exports in 1913, but less than one-tenth of the exports of the South in 1924.

Many reasons have been advanced for the failure of most of the island to industrialize [O'Malley, 1981; Ó Gráda, 1994a, Ch. 13; Bielenberg, 1991, ch. 10]. They include the lack of natural resources, peripheral location, external economies, poor entrepreneurs, and even culture or religion. The first two reasons are linked: if imports from Whitehaven or Swansea offered Belfast or Dublin a cheap substitute for Ireland's meagre coal resources, the same could not be said for the Irish midlands or west. Explanations that stress the small size of the Irish market and the distance from other consumer outlets have not been rigorously tested, though they are very much in tune with recent trade-theoretical research. Irish historians have also long stressed the role of external economies, if not in so many words: though difficult to measure, they have been invoked to explain both Belfast's 'success' and Ireland's 'failure'. Finally, not only in Ireland has culture been blamed for poor economic performance. The contrasting economic histories of the mainly Protestant North and the mainly Catholic South would seem grist for the mill of followers of Max Weber and R H Tawney. Weber and Tawney argued that the Reformation had spurred on economic development in Protestant Europe, and the successful industrialization of east Ulster before 1914 would seem to corroborate this.

On closer inspection, however, the Weber-Tawney hypothesis faces many of the same objections in Ireland that have been raised against it in other parts of Europe [Ó Gráda, 1994a: ch. 13].

Agriculture remained Ireland's dominant sector, still accounting for one-third of output and employing half the occupied male population in 1911. However, the sector had been radically transformed in the decades after the Great Famine (1846-50). An important reason for this is that by reducing the reliability and productivity of the potato crop, the fungus that produced the Famine also influenced the course of agricultural change in the longer run [Solar, 1989; O'Rourke, 1991a]. Farmers accordingly cut back on both potato and grain production. In addition, increases in the prices of meat and livestock products relative to that of grain and the rising cost of agricultural labour prompted the shift towards land-intensive agriculture. Farmers came to rely more on their own labour and on machinery; the ratio of farm labourers to farmers fell by almost half between 1850 and 1914. The result was a drop in tillage's share of total agricultural value added from about 60 percent in the mid-1850s to 22 percent in the early 1910s [Crotty, 1966, ch. 3; Solar, 1983: 73; O'Connor and Guiomard, 1985: 93].

Though aggregate output hardly rose, the period between the Famine and the downturn of the late 1870s was a good one for farmers. Rural living standards advanced and rents were paid with little difficulty. The temporary squeeze brought on by a combination of lower prices and poor harvests in the late 1870s focused farmers' attention once more on rents. Nationalist politicians turned the landlord-tenant system into an effective campaign platform in the 1880s and 1890s. Demands for a fairer deal from landlords - the three Fs (fair rent, fixity of tenure, and free sale) - were soon transformed into the successful campaign for peasant proprietorship. Though certainly an important political issue, all sides exaggerated the economic importance of the land question [Solow, 1971; 1981]. Landlord rhetoric repeatedly predicted anarchy and ruin in the wake of peasant proprietorship, while tenant spokesmen exaggerated the expected efficiency gains. Though the shift in tenurial regimes failed to turn sand into gold, neither did the euthanasia of the Irish landlord cost much in terms of foregone output. Comparing output and input trends in Ireland and Britain indicates a reasonable

productivity performance by Irish farmers between the 1870s and World War I [Ó Gráda, 1993: ch. 4; 1994b]. Contemporaries preferred the comparison with Denmark. Using somewhat dubious output estimates, Staehle [1950/1] deemed that contest a draw, though most historians would vehemently proclaim Ireland the loser [e.g. Crotty, 1966: 67-8]. Taking a wider European perspective shows Irish agriculture in a poor light in the pre-1914 period [van Zanden, 1991].

In Irish economic and social history, the role of demography has long been paramount. A low marriage rate, high marital fertility, and high emigration were the key features of the decades after the Great Famine. The three were connected, since the high emigration and low marriage rates were necessary to enable the great majority of the population to pursue something close to a 'natural' fertility regime. The shift to low nuptiality is usually interpreted as a Malthusian preventive check, though recently Guinnane [1991a, 1991b] has claimed that it was a reflection of, rather than a precondition for, higher living standards. On the eve of the First World War, the average age at marriage for Irishwomen had reached nearly thirty years, and the proportion of women never-marrying exceeded one-fifth [Walsh, 1985]. However, high marital fertility compensated for low nuptiality, with the result that the Irish birth-rate was unexceptional by European standards. In the 1900s marital fertility was probably higher in Ireland than anywhere else in western Europe. Nevertheless, recent research indicates that Ireland was a participant in the European fertility decline of the late nineteenth and early twentieth centuries, even though an unenthusiastic one. Already before 1914 family limitation was having some impact on the birth rate, particularly among the urban middle-class [Ó Gráda, 1991a].

Emigration was much more important than either fertility or mortality in accounting for shifts in population, being truly massive by international standards [Ó Gráda and Walsh, 1992; Hatton and Williamson, 1993]. However, except for an important blip in the 1880s, the emigration rate showed a long-term downward trend, reflecting (as well as causing) a relative improvement in living standards. Irish emigration was special for its high proportion of women, and its low proportion of return migrants. Though a link between emigration and declining population on the one hand and poor economic performance on the other has long been asserted, specific evidence in support

is lacking [Commission on Emigration, 1956; Ó Gráda and Walsh, 1993]. In fact, it has recently been argued that the marked improvement in Irish living standards relative to those of Britain and America would not have been possible without large-scale emigration.

B. 1921-1956:

Ireland was partitioned in the wake of the War of Independence of 1916-1921. The antipathy of Northern industrialists to the protectionist rhetoric of nationalism provided an economic rationale for partition, though history had much more to do with the outcome than economics. Economic growth in the South continued to be slow, though how slow is controversial [Lee, 1988; Johnson, 1991]: for a comparative assessment see Table 2 below. In Northern Ireland the 1920s and the 1930s were also difficult decades, due largely to the decline of the staple industries of linen and shipbuilding. In the 1930s Belfast's shipbuilding output was less than half its pre-war level, while the export of linen piece goods stagnated and their price fell [Black, 1957; Ollerenshaw, 1991; Geary and Johnson, 1989]. Nevertheless, over the long haul incomes in the North of Ireland have risen faster than in the South, though both still lag considerably behind Britain.

In the South, the economic policies of the first independent administration emphasized continuity, stability, and comparative advantage. This ruled out monetary or fiscal experimentation, and meant soft-pedalling on the teachings of nationalist thinkers such as Arthur Griffith [Daniel, 1976]. Caution, nationalist ideology (which had long maintained that Ireland was over-taxed within the United Kingdom), and the emphasis placed on minimising costs, supported low taxation in the 1920s. In agriculture, the policy emphasis was on helping farmers emulate Danish success by aiming at the high quality end of the British market for meat, eggs, and dairy products. This policy, always associated with Agriculture Minister Patrick Hogan, had yielded few dividends by 1932; perhaps Ireland's Stolypin was given insufficient time to assert himself [O'Brien, 1937]. Hogan's Cumann na nGaedheal lost to de Valera's Fianna Fáil in the watershed general election of March 1932[3] [Lee, 1989: 176-8]. The new regime, initially both populist and radical, had little sympathy

with the stronger farmers who had supported Hogan's policies, and sought to shift the balance in favour of the smallholder and tillage farmer and against the 'rancher'. However, the smallholder and the rancher complemented each other in the cattle trade, so these efforts were only partially successful.

Rising protection abroad in the wake of the world recession and an 'Economic War' between Ireland and Britain over the repayment of land annuities (1932-8) only intensified the hardships facing all Irish farmers [Neary and Ó Gráda, 1991]. On the whole, Southern agriculture performed poorly relative to Northern for several decades after independence. In the South, gross farming output managed to rise by only a quarter between the mid-1920s and the early 1960s, while in the North it more than trebled. The Southern lack of dynamism has been put down plausibly to low prices and weak, or indeed perverse, incentive structures [Johnston, 1937; Gillmor, 1989; Kennedy *et al.*, 1988: 103-5; Ó Gráda, 1991b].

The 1930s introduced a period of economic experimentation in the South. The 'Economic War' with Britain, the general prevalence of protectionist policies in Europe, and the Second World War gave the Irish economy ample scope to try protectionism. Ireland had moved from being virtually a free-trading economy to being a highly protectionist one in the mid-1930s [Ryan, 1948/9]. In the context of the general trade destruction of the 1930s, the experiment was not so costly in the short run [Neary and Ó Gráda, 1991; O'Rourke, 1991b]; the real policy mistake was not to revert to a more open economy after 1945.

The Census of Industrial Production data reveal an initial 'great leap forward' in employment lasting for a five-year stretch after 1932. Both output and employment rose by about one-third, and hundreds of new plants, widely spread throughout the twenty-six counties, began production. Some analysts [e.g. FitzGerald, 1959] view the industrial growth as a statistical mirage, the outcome of more effective data-gathering, but others have contested this interpretation [e.g. Daly, 1988]. In any event industrial expansion came to a halt in the late 1930s, mainly because the home market had been saturated and small-scale Irish industry was predominantly dependent on the home market. Both output and productivity stagnated during the War years. Industry case-studies are unfortunately few. An exception is Press's analysis of the heavily-protected shoe industry, which pays due attention to the constraints

facing Fianna Fáil's efforts at job-creation in the 1930s [Press, 1986; 1989; see too Kiernan, 1927]. However, the import-substitution experiment produced few firms that could survive the shift to freer trade in the 1960s - the multinational Jefferson Smurfit Corporation, originally a Dublin cardboard packaging company, is one well-known, exceptional, example - and assessments of the performance of the protected industries in general have been very negative [O'Malley, 1988].

The budgetary stances of both Cumann na nGaedheal and Fianna Fáil administrations was rather conservative, and even Fianna Fáil paid no heed to Keynes's call in 1933 for deficit spending on urban renewal and other worthwhile projects [Keynes, 1933]. At the end of the 1930s Ireland's national debt was still relatively small by contemporary European standards. Monetary experimentation was also rejected out of hand, and the Irish Free State's currency could always be readily exchanged into sterling at par. Though the sterling link was not without its tensions, particularly in the wake of the devaluations of 1931 and 1948, it probably boosted investor confidence and ensured the acceptance of the Irish pound. The Irish banking sector, dominated by a cartel of joint-stock banks, may have lacked dynamism, but it proved very stable. The banks vehemently opposed the creation of an Irish central bank, and the Free State survived without one until 1943, when the Central Bank of Ireland was set up. Ireland stands out as one of the few economies free of banking panics or failures during the 1930s [Pratschke, 1969; Ó Gráda, 1994c].

The immediate post-war years brought some respite. Coming after a decade or so of stagnation, industrial output rose by about two-thirds between 1946 and 1951. The increased output was destined mainly for the domestic market. The census of 1951 was the first since 1841 to register an increase in population. Those who believed that growth could last were living in a fool's paradise, however. Indeed, the recovery of the late 1940s concealed for some years the futility of the protectionist strategy adopted in 1932. The measures adopted to right an adverse balance of payments in 1951 introduced nearly a decade of stagnation.

After the general election of 1948, Fianna Fáil were replaced by a multi-party coalition. The first inter-party government (1948-51) re-emphasized the importance of agricultural exports. Ministers set great store by the Anglo-

Irish Trade Agreement of 1948, which removed the quotas on Irish livestock imports to the United Kingdom. An annex to the Agreement outlined (non-binding) Irish livestock export targets. However, the British system of farm deficiency payments depressed prices on the British markets, and the anticipated targets were never met.

In 1948 the new Minister for Finance, Patrick McGilligan, introduced the innovation of separating capital from current items in the budget. McGilligan did not propose to run a current budget deficit, but insisted that a deficit could be run on the capital side, since capital spending would produce dividends in terms of long-run growth. In the memorable words of one economist, "Keynes had come to Kinnegad" [Lynch, 1969: 187]. However, official policy continued to focus far too much on fluctuations in the balance of trade and the balance of payments. Thus the harsh budget of 1952 was aimed at rectifying a huge adverse balance in 1951, prompting economist John O'Donovan to point out that "the subject economics [was] not arithmetic", and that "the theory of economics would have led to the conclusion that imports would have gradually fallen off without any measures being taken to reduce them" [**Evening Herald**, 27 July 1953]. Yet Finance Minister Gerard Sweetman would repeat the mistake, with more serious consequences, in 1956. Thereafter, until the early 1970s, modest deficits and rising expenditure on public capital projects were the order of the day [Kennedy and Dowling, 1975: 215-223].

C. 1958-1992:

This period is better served by reliable macro-economic data than either 1870-1921 or 1921-1958. However, comparative assessments of the Irish economy are quite sensitive to the data used. The Penn World Table Mark V [Summers and Heston, 1991] provides one popular basis for real quantity comparisons both across countries and over time (see Table 1 below). Using the changes in that measure of real GDP per head (GDP/POP) to gauge the trend in living standards, between 1950 and 1988 the Republic recorded one of the worst - if not the worst - growth performances in the whole of Europe [Ó Gráda and O'Rourke, 1993]. As indicated in Table 1, the Heston-Summers data imply a marked deterioration after 1973. The rise in the unemployment rate, already high by

European standards in the 1960s and 1970s, reflects this; in 1984-8 unemployment exceeded twenty percent, a level unequalled for so long anywhere in the EC since the 1940s [EC Commission, 1991: 216]. Focusing on productivity growth (GDP/W) instead of on living standards 'improves' Ireland's relative performance before 1980, though makes it seem worse in the 1980s.

Table 1: *IRISH ECONOMIC GROWTH 1960-1988: HESTON-SUMMERS*

(percentage annual rates)

	1960-1973			1973-80			1980-1988		
	GDP	GDP/POP	GDP/W	GDP	GDP/POP	GDP/W	GDP	GDP/POP	GDP/W
Ireland	4.9	4.2	4.5	3.2	1.7	2.0	0.7	0.1	-0.9
Europe	5.3	4.5	4.4	3.4	2.6	2.1	2.3	1.9	1.5

Source: Heston and Summers, 1991: Table III. 'Europe' is defined as the arithmetical average of all twenty-two countries providing information over the three periods. GDP/W is GDP per worker.

However, Angus Maddison's latest comparative assessment of GDP growth rates, based on Eurostat and OECD data, tells a distinctly more cheerful story (see Table 2 below). Ireland's relatively poor performance in 1950-73 in Table 2 can be put down entirely to the disastrous 1950s, but in this league table since 1973 Ireland has performed respectably relative to both advanced and peripheral European economies. On closer inspection, the Heston-Summers and Maddison series differ little for the years before the late 1970s, but the series then begin to diverge, and by the late 1980s the latter estimate puts Irish GDP per head at about twenty-five percent more than the former [Ó Gráda and O'Rourke, 1993].

Two caveats apply to assessments based on either Summers-Heston or Maddison data. First, in the early 1980s the cost of servicing the national debt (on which more below) produced a widening gap between Irish GDP and GNP. As a result, the rise in GDP per head greatly exaggerates the rise in living standards since 1980.[4] Second, both Summers-Heston and Maddison data sets imply that European economies formed a 'convergence club' in the post-war era: poorer economies tended to grow fastest. The growth performance of the Irish

economy fell behind what might have been expected of it in this setting [Ó Gráda and O'Rourke, 1993].

Given Ireland's close economic ties with the United Kingdom, comparativ evaluations of the Irish and British economies since the 1950s are also relevant here. Using GNP per head assessed at purchasing power parities as a gauge, Ferris has shown that between 1971 and 1986 living standards in the Republic deteriorated relative to both Northern Ireland (from 74 to 69 percen and Britain (from 57 to 52 percent). However, labour productivity rose faste in the Republic; by the mid-1980s it was virtually on a par with Northern Ireland's and had reached 89 percent of Britain's. Comparative evaluations o industrial wages show a far smaller gap between Ireland and the UK than do national accounts data. The apparent paradox - high productivity and high wages combined with low GNP per head - is mostly accounted for by differing employment and demographic structures [Ferris, 1989; Ó Gráda and Walsh, 1993; Williamson, 1993]. A recent assessment of manufacturing productivity in Ireland and Great Britain shows that the ratio of manufacturing output per hea in the Republic relative to the United Kingdom rose from 0.79 in 1963 to 1.27[5] in 1984, while the ratio of Northern Ireland to British productivity fell marginally, from 0.84 in 1963-73 to 0.81 in 1973-86 [Hitchins and Birnie, 1991]. Southern agricultural output continued to grow sluggishly in the 1940s and 1950s, but boosted by improved prices and market access in the 1950s and 1960s and further bloated since the mid-1970s by EC subventions, it has also been out-performing its Northern counterpart in recent decades [Kennedy et al. 1988: 104; Ó Gráda, 1991b].

Table 2: *GDP GROWTH IN IRELAND AND OTHER AREAS, 1913-1989*

(percentage annual rates)

Country	1913-50	1950-89	1913-50 Per Capita	1950-73 Per Capita	1973-89 Per Capita
Ireland	0.9	2.6	1.0	3.1	2.9
Spain	1.1	2.4	0.2	5.1	1.8
Portugal	2.4	3.5	1.5	5.6	1.7
Greece	1.4	3.3	0.5	6.2	1.7
UK	1.3	1.8	0.8	2.5	1.9
Denmark	2.5	1.9	1.5	3.1	1.7
Belgium	1.0	3.3	0.7	4.9	2.3

Source: Angus Maddison, 'Explaining the Economic Performance of Nations 1820-1989', mimeo, 1993, Tables 3 and 4. The Irish growth rate for 1913-50 has been adjusted to allow for an Irish GDP level in 1913 ten percent lower than that implied by Maddison.

The 1950s produced a great deal of economic soul-searching. A Bank of England official who visited Ireland in August 1957 was privy to some of the discussion between government officials:[5]

> The fundamental weaknesses remain, namely, that too much has been spent on unproductive capital schemes, particularly building, too little devoted to increasing the productivity of agriculture, and there is too much nationalism as regards the introduction of industry from abroad.. It is impossible to maintain lower wage rates than the United Kingdom owing to the demand for labour in Great Britain: good skilled labour tends to emigrate at once. The result is that the country gives the impression of being an economic slum from which there is a constant outflow of emigrants who have any initiative and any desire to better themselves.

This thinking was embodied in an official 'grey' paper, **Economic Development**, and in the Programme for Economic Expansion, both documents emanating from the Department of Finance in late 1958. The Programme was Ireland's tentative first exercise in indicative planning; it outlined the strengths and weaknesses of the economy, emphasized the importance of farm investment, and held out hopes for some economic growth. The targets set out in that Programme were modest in scope and vague as to the mechanisms for achieving them. A growth rate of two percent per annum over a five year period was anticipated. While the First Programme indicated a commitment to trade liberalization and the re-orientation of industry towards foreign markets, in its emphasis on agriculture

as the engine of growth it was strictly traditional. The economy soon picked up, and the actual growth rate of 4 percent was double the target rate; historians have generally tended to give the First Programme the credit, and the sharp rise in investor confidence (as measured by the rise in Tobin's Q or the relative movement in Irish and British share prices) in the late 1950s suggests that the Programme produced a 'euphoria effect'. However, another view posits that the economy, which was emerging from recession in any case, would have performed just as well in the absence of the Programme.

The First Programme was succeeded by the Second (1964-1970) and Third Programmes (1969-1972). These were far more detailed than the first, and contained specific sectoral projections. In neither case was even the overall aggregate growth rate target of 4 percent met, and both were abandoned before their 'due date'. The Second Programme, formally abandoned in 1967, was laid to rest because of the widening disparity between the projections for employment growth and the year-by-year outturns, and the targets of the Third Programme seemed unrealistic almost from the outset. The programmes were also flawed methodologically [Norton, 1975; Bradley, 1990]. Hardly surprisingly, planning went out of favour for a few years. Yet 1977 saw the creation of the Department of Economic Planning and Development and 1978 the launch of **National Development 1977-80**. That plan's projections proved to be wildly unrealistic. The **The Way Forward** (1982) and **Building on Reality** (1984) followed, both emphasizing budgetary rather than economic growth targets. These documents, better characterized as stabilization programmes than exercises in French-style indicative planning, marked the end of Ireland's experiment with such economic planning. That experiment is a reminder that setting and meeting detailed medium-term growth targets for a small open economy is a difficult, if not pointless, exercise. A looser, milder form of planning has survived to the present, in the guise of tri-partite (government, trade union, and the private sector) agreements about incomes and social welfare policy. So far such agreements seem to have contributed little to solving Ireland's most serious social and economic problem, its high rate of unemployment [Durkan, 1992; Kennedy, 1993].

Irish economic performance during the 1960s and early 1970s kept pace with the European average. Economic growth produced a substantial net

immigration for several years during the 1970s. The result was that for the first time since the before the Great Famine, the population of the Republic began to grow rapidly. It had reached an all-time low of 2.818 million in 1961; by the mid-1980s population had recovered to 3.5 million, and has hovered around that level since then. The population of Northern Ireland (1.6 million in 1991) has fluctuated less in recent decades. However, declining emigration and higher marital fertility have produced a rapid increase in the Catholic share of the total in recent decades. Catholics now constitute about 43 percent of Northern Ireland's population, up from 35 percent in 1961, and probably a bigger share than at any date since the eighteenth century. Northern Catholic fertility remains significantly higher than non-Catholic (Northern Catholic fertility is also somewhat higher than Southern Catholic fertility [Walsh, 1970: 32]), yet both Northern Ireland and the Republic have experienced big declines in fertility in recent decades. By the early 1990s, fertility had fallen to just about replacement levels in the two Irelands.

The shift towards an outward-looking policy in the South was reflected in a new attitude to foreign capital in manufacturing. Foreign investors were granted generous incentives to locate in Ireland, and hundreds did so. The remarkable transformation of the economy between the late 1950s and the early 1970s may be largely attributed to their arrival. By 1973 overseas firms accounted for almost one-third of all employment in manufacturing (68,500 out of 219,000). Even in the less propitious climate of post-1973 the number of foreign-owned firms continued to grow. By 1983 there were almost a thousand of them, with a labour force of 87,600, while employment in Irish-owned concerns continued to drop. In the 1980s the newer (foreign) industrial concerns, concentrated in a few sectors, seemed to perform better than the old (indigenous) companies. Baker's division of industry into 'modern' and 'traditional' places pharmaceuticals, engineering, and a category called 'other foods' in the 'modern' sector, and the rest of manufacturing in the 'traditional' sector. The two have differed markedly in terms of performance, judged by criteria of output growth, employment trends, and the movement in unit wage costs [Baker, 1988]. During the 1980s modern - largely foreign-owned - industry trebled its output, while traditional industry barely held its own.

However, observers have increasingly pointed to flaws in government policy towards attracting foreign capital and in the kind of industry attracted [Kennedy *et al.*, 1988, 247-250; O'Malley, 1988]. The record suggests that few overseas firms have generated sustained increases in employment in Ireland, few have delegated entrepreneurial responsibilities here, or have used Irish raw materials. Instead, the grants and tax concessions have encouraged them to be capital-intensive and to use Ireland as a base for transfer pricing. Only a minority of firms have a track record of sustained output and employment growth [compare Bull, 1989]. In other words, foreign-owned firms have tended to be poorly integrated with the rest of the economy. Admittedly, these drawbacks could not have been predicted in the 1960s. Policy in the recent past shows signs of having learnt the lesson, shifting its focus away from attracting ever more overseas firms of the old kind and towards easing the constraints faced by both existing indigenous and overseas firms.

Initially, Ireland's main policy response to the oil crisis of 1972-3 was a succession of large budget deficits. The public sector borrowing requirement (PSBR) rose from 8.6 percent of GNP in 1972-3 to 12.9 percent in 1976-7 [Leddin and Walsh, 1992: 122]. At the time, that rise was rationalized in Keynesian terms. But budget deficits continued to accumulate in the following few years, shielding the Irish consumer for a time from the effects of the oil crisis, but raising the PSBR and the national debt to clearly unsustainable levels. The huge rise in public spending - the PSBR reached 17.3 percent in 1980 and 20.3 percent of GDP in 1981 - failed to generate much productive capital: indeed, despite gross investment rates of over nearly thirty percent of GDP in 1978-81, the economy grew at an average rate of only 2.5 percent in the first half of the 1980s. Economists were quick to criticize the fiscal expansion of those years [Walsh and McCarthy, 1980]; indeed, the tone of some critics soon turned apocalyptic ! Politicians were slow to heed the stream of warnings from economists, and as a result much of the 1980s were wasted undoing the damage of earlier fiscal recklessness, perhaps accounting for Ireland's relatively poor growth record during those years (see Table 1). However the 'delusion' that Ireland could sustain living standards by borrowing in the wake of the oil price disruptions of the 1970s had dissipated by 1983.

The rhetoric of budget-day speeches reflected lessons dearly learned. In

1978 the budget had sought 'to give an impetus to economic activity' that would increase the annual growth rate in GDP to an unprecedented 7 percent, as stipulated in **National Development 1977-80**. The combination of tax cuts and spending would, it was hoped, pave the way for expansion in the private sector. While the budget speech of 1981 derided 'loose comment about so-called disorder in the public finances', by 1983 there was a clear recognition that the cost of servicing the debt had 'preempted resources for the future'. 'Populist quick fixes' have been ruled out in the latest [1993] Budget, and the PSBR has by now been reduced to below 3 percent. The pervasive gloom of economic commentary in the early and mid-1980s, reminiscent of the 1950s, has given way to mild confidence about the future.

The Irish decision in December 1978 to participate in the European Monetary System (EMS) was a landmark in recent Irish economic history, since it brought to an end the monetary union between Ireland and Great Britain that had lasted since 1826. The aim of EMS membership was a monetary discipline which would win Ireland investor credibility, low inflation, and low interest rates. At first, the inconsistent stance of the Irish fiscal policy and repeated realignments of the *punt*'s value within the system's Exchange Rate Mechanism sapped investor confidence in the Irish currency, and interest rates remained high. Such realignments ceased in 1986, and by the early 1990s the Irish yield curve was downward-sloping and the gap between Irish and German interest rates minimal. By 1992 it could be said that the goals of price stability and low interest rates had been reached. This cut the cost of servicing the national debt and thus reduced the fiscal burden facing the economy. The victory was costly, however, in terms of output and employment forgone, and some economists now argue that the exchange rate regime pursued by Ireland under the EMS was unduly deflationary [Dornbusch, 1989; Leddin and Walsh, 1992: 390-3].

Membership of the EMS had aimed to 'free' the *punt* from the shackles of sterling. With a stable *punt*-Deutschmark exchange rate of £1=2.65DM since mid-1986, that goal seemed to have been met by the early 1990s. The crisis caused by sterling's departure from the Exchange Rate Mechanism in September 1992 had therefore not been widely anticipated. Moreover, most commentators initially believed that Ireland would resist the pressure to devalue in order to maintain the credibility that had been so dearly won. The costly and futile battle to

'save' the *punt* against the speculators lasted four months. In January 1993 the Irish currency was devalued by eight percent within the exchange rate mechanism. With the virtual demise of EMS in mid-1993, the Irish currency has become 'one of the smallest independent currencies in the world' [Walsh, 1993]; the search is now on for that golden rule-of-thumb which would yield a *punt* capable of denting Ireland's savage unemployment rate without endangering competitiveness.

The combination of fiscal retrenchment, exchange rate policy, and economic recovery in the 1980s has attracted the attention of outside experts, evoking the admiration of some and confounding others [Dornbusch, 1989; Giavazzi and Pagano, 1991]. Giavazzi and Pagano have proposed the Irish recovery as a classic example of 'expansionary fiscal contraction', a claim denied by Barry [1991; also Barry and Bradley, 1991]. An alternative interpretation of recent Irish macro-economic history has buoyant world market conditions and capital inflows outweighing the deflationary effects of fiscal contraction [Leddin and Walsh, 1993: ch. 13; Barry, 1991].

Cormac Ó Gráda

Dublin, 16 September 1993

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Note: the asterisked items appear in this volume. Volume numbers are given in roman numerals.

KEY:

EJ	**Economic Journal**
ESR	**Economic and Social Review**
IBR	**Irish Banking Review**
IESH	**Irish Economic and Social History**
IHS	**Irish Historical Studies**
JEH	**Journal of Economic History**
JSSISI	**Journal of the Statistical and Social Inquiry Society of Ireland**

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FOOTNOTES

1. Editor's introduction to **The Economic Development of Ireland since 1870** (Edward Elgar, forthcoming). I am grateful to my colleagues Cathal Guiomard, Joe Durkan, Gerard Quinn, and Brendan Walsh for their very helpful comments on an earlier draft of this introduction.

2. The Irish Free State (or Saorstát Éireann) was declared the Republic of Ireland in 1948. In what follows we shall usually refer to either, for brevity, as 'the South' or simply 'Ireland'.

3. Cumann na nGaedheal was the party of those who supported the Anglo-Irish Treaty of 1921; Fianna Fáil, formed in 1926, had the support of a majority of those who opposed that treaty.

4. Real GDP rose by 38.5 percent between 1980 and 1992, real GNP by only 24 percent [Leddin and Walsh, 1992: 69-70].

5. Admittedly some of this rise is probably attributable to transfer pricing (see below).

6. Bank of England Archives, OV81/2, Memorandum on 'The Irish Republic' by J M Stevens (impressions gained during a trip to Ireland in August 1957).