A Historical Profile of the Irish Economy and Irish Government Economic Policies with regard to the Enterprise Sector.

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A Review of Irish Government Economic Policy for the Enterprise Sector since Independence

In an informative review of economic policies in the Republic of Ireland, since the granting of independence to the country from British rule in 1922, two noted Irish economists, Walsh and Leddin (2000), pp. 32 conclude:-

' An important lesson to learn from [Irish] economic history is that policies matter'.

During the first decade after Independence, agriculture was viewed as the engine of economic growth and a free trade environment operated, allowing cheap imports of raw materials and open access to export markets. The role of the state in the economy remained relatively limited during this time. With the Great Depression and the collapse of the global free trade system in the early 1930's, liberal policies were abandoned not just in Ireland, but throughout the world. A period of protectionism and inward looking policies began, with high tariffs being imposed on imports (to protect anyone willing to manufacture products in Ireland) and foreign investment was virtually excluded through the Control of Manufactures Act (1932-1934).

' the fact that between 1932 and 1966, the Irish economy was one of the most heavily protected in the world is probably the single most important reason for the country's relatively poor economic performance over these years.'

Walsh and Leddin (2000). pp. 34.

After 1932, numerous state-sponsored bodies (or semi-state companies) were created to fill what was regarded as gaps left by enterprise. The areas in which they operated included radio and TV broadcasting, turf development, air, sea, road and rail transport, hotels and food processing, manufacturing steel and chemical fertilisers. These companies enjoyed significant monopoly power and eventually became overmanned and inefficient. They were also asked to achieve a variety of political and social objectives, which burdened them with high-cost operations. A commentary on this era of protectionism is illuminating :-

' by the 1970's, the role of the state in the Irish economy was probably more extensive than in any country that had not adopted socialism… the result was a high tax burden on the economy and a deterrent to private enterprise.'

Walsh and Leddin (2000), pp. 34.

A start was made on dismantling tariffs with the signing of the Anglo-Irish Free Trade Area Agreement (1966), which led to the elimination of tariffs between Ireland and Britain. The phased elimination of tariffs with European countries was negotiated as part of Ireland's accession to the European Economic Community (EEC) in 1973. Effectively, a return to free trade was made in the 1960's and there is agreement among most economists that this factor made the most important contribution to turning the Irish economy around and opening it up to export-led growth. Given that as late as the 1950's, almost 90% of Irish exports went to the U.K. (mainly consisting of live animals and foodstuffs) and that the banking systems and financial markets remained integrated with their British counterparts, it was not surprising that the growth rate of the Irish economy was closer to that of Britain than that of the continental European countries.

Furthermore, the structure and level of investment in a country is a strong determinant of growth and due to the low savings rate in the 1950's in Ireland, a high proportion of the funds available for investment was used by the government to build houses and hospitals, resulting in a low rate of investment in productive assets. In the 1970's, the rate of investment rose, but the government directly or indirectly controlled it and its productivity was low. This was to change for the better, with the incentives introduced by the government to attract Foreign Direct Investment (FDI). FDI was to improve the productivity of the industrial sector and stimulate the economic growth rate. It is discussed below.

As tariffs were dismantled in the 1960's, an elaborate system of industrial grants and tax incentives were introduced. Instead of giving priority to Irish-owned firms willing to substitute for imported goods, the emphasis of economic policy was switched to attracting export-oriented FDI. The Industrial Development Authority (IDA) was established in 1949 with this remit. The incentives used for this purpose included fixed asset grants, generous capital allowances, export sales tax relief (introduced in 1958) but then superceded by a 10% rate of tax on profits in manufacturing and some traded services in 1981. The sectors that were initially earmarked for FDI were high technology electronics, pharmaceuticals, chemicals, software and medical instrumentation to be followed by financial services, teleservices and high tech food industries.

The success of the IDA is notable as shown in the following statistics, adapted from Walsh and Leddin (2000), pp. 40.

- In 1996, it supported 1,040 companies, employing 97,472 people, accounting for 44% of total manufacturing employment.

- In 1996, IDA expenditure (funded by the Irish government and by transfers from the EU budget) amounted to £136 million, resulting in a cost per job sustained, of £11,920, a decrease from £24,952 in 1983.

- In 1996, sales by multinational companies located in the Republic, amounted to £13.058 million (30% of GDP). Of this, £12,570 million (96%) was exported. These firms spent money on sourcing supplies etc in the Irish economy, to the tune of 33.7% of their total sales. This indicates considerable spin-off effects for the domestic economy.

- Productivity (output per worker) in the FDI sectors is much higher than in the rest of Irish industry, but earnings per employee are slightly lower. The FDI sector is thus very profitable and the profits repatriated from the foreign-owned sector amount to about 5% of the value of Ireland's domestic output.

By the nineteen eighties, it was however clear that the expansion of the role of the state in the economy since the nineteen thirties had not promoted the long-run development of the economy and with an accompanying attitudinal change in Britain and America towards the economic role of the state in these countries, deregulation and privatisation was introduced. Some Irish state companies (e.g. the Irish Life Assurance Company, the Irish Sugar Company) were privatised and the monopoly privileges of those in areas such as health insurance, TV and radio broadcasting and inter-city bus transport were reduced. European Union (EU) regulations for liberalisation of civil aviation, insurance and banking have however, been delayed in their implementation.

The Emergence of the Celtic Tiger Economy of the 1990's

The foundations of the Celtic Tiger [1]Economy were put in place gradually over the nineteen sixties and nineteen seventies, so reversing the stagnation of the nineteen fifties. As discussed above, outward-looking free trade policies, an elaborate system of industrial grants and tax incentives disbursed by the IDA (to attract foreign-owned export-oriented firms) and Ireland's reputation for a highly educated and a young skilled workforce, all contributed to better pre-conditions, as the nineteen eighties dawned.

Ireland joined the European Monetary System (EMS) in 1979, so breaking the link with sterling, just as that currency began to be seriously overvalued. From this fortuitous development, extending all the way to 1998, the country maintained a competitive exchange rate, " through a mixture of good fortune and good policy management", Walsh and Leddin (2000), pp. 47. In particular since the devaluation of sterling in 1992, the Irish currency within the EMS was kept at a level, which enhanced the country's international competitiveness.

In the first half of the nineteen eighties, the growth of the economy was weak. Gross National Product (GNP) grew by 0.2% per year on average in the years 1981-1986, compared to an EU growth average

[1] The phrase "Celtic Tiger " was coined in 1996 by an economist, Kevin Gardner, who worked with London-based stockbrokers, Morgan Stanley Dean Whitter, when comparing Ireland's growth with that of the successful economies of East Asia. The idea was publicised in *Newsweek* (23/12/1996).

of 1.7% per year. Employment levels fell and the rate of unemployment accelerated. The balance of payments was in persistent and substantial deficit. The effects of uncompetitive price performance, high interest rates and a large and unsustainable fiscal imbalance were reinforced by a generally weak economic environment. The country was facing insolvency due to the rising debt/GDP ratio[2] and the exceptional current account balance of payments deficit. The result was a flight of capital from the country and a reluctance by foreign firms to locate in Ireland.

The policy response to this crisis was constrained by the actions needed to rectify the effects of inappropriate economic policies of the nineteen seventies, which were reactive and driven by an overly short-term perspective. These latter policies contributed greatly to a public expenditure burden with substantial carry-over effects up to recent times.

The crisis in public finances reached a peak in the mid-nineteen eighties and forced radical reactive change in a range of public policies to contain the crisis. The need to meet the criteria in relation to public debt, public sector deficits, exchange rate stability and inflation, required for membership of Economic and Monetary Union under the Maastricht Treaty, which Ireland signed in 1992, disciplined the country's economic policies, finances and budgetary measures. Moreover, the substantial financial transfers to Ireland, under the EU Structural and Cohesion Funds, which accounted for circa IR£900 million or circa 2.7% of GNP in 1995, also assisted growth. It is unlikely that the same level of transfers will continue to be available to Ireland after 1999.[3]

The impact of EU aid is often cited as a reason for Ireland's improved economic performance in the 1990's; the timing of the increased inflows was very favourable, because they helped counter the impact on the Irish economy of the world recession of the early 1990's. The money was spent on roads and railways, telecommunications and in aid to industry, agriculture and tourism.

This aid was expected to spur Ireland's growth rate and lead to a convergence in living standards with the richer EU countries, and Ireland did indeed close this gap. Economists may debate about whether foreign aid does really boost investment, as opposed to consumption and about whether its long-term contribution to growth is non-zero, but Walsh and Leddin (2000), pp. 45 note from a recent study that:-

> a high correlation between aid and investment has been found among a few small countries that have received an exceptionally large volume of aid (generally more than 15% of GDP). Such a high level of aid cannot be diverted from uses for which it was provided and is therefore likely to produce the required effect.[4]

In 1988, the standard rate of income tax was 35% and the higher rate 58%; by 1998, these rates had been lowered to 24% and 46% respectively, and the thresholds at which they were applied had been raised in real terms. The reduction in the rates of income tax and corporation tax since the mid-1980's especially in a small open economy, acted as an incentive to economic development. Since the mid-1980's, Ireland has enjoyed a " virtuous circle with faster growth leading to lower tax and public debt burdens, which in turn has reinforced the economy's performance", Walsh and Leddin (2000), pp. 47. Cause and effect may be difficult to disentangle, because faster growth can facilitate tax reductions, while by the same token, lower income tax rates improve the incentive to work and additionally, lower corporate tax rates boost profitability, output, employment and growth.

Rapid reductions in the fiscal imbalance were achieved from 1987. These, together with favourable international developments, supported a fall in interest rates and in inflation. Strong economic growth recommenced, averaging 4.5% per year and significantly higher than the EU average of 3.0 %.

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[2] In 1987, public debt was 130% of national income soaring from 65% in 1977. In 1997, it was less than 80% of GDP. (*The Economist, May 17th, 1997).*

[3] During the 1980's the level of aid under the Social and Regional Funds increased significantly and in the 1990's, a new Cohesion Fund was established to narrow the gap between rich and poor countries. Net receipts reached a peak of 7.3% of GNP in 1991 and total net receipts over the period 1973-1997, amounted to £21,505 million, an annual average of 4.7% of GNP. See Walsh and Leddin (2000), pp. 43 for further details.

[4] Boone, Peter, "The Impact of Foreign Aid on Savings and Growth", London School of Economics, Working Paper, June 1994.

Employment in the non-agricultural sectors of the economy rose by an average of 13, 200 per year. In the private sector, the rate of increase was even faster, at 18,000 per year in the period 1988-1991. These developments were in sharp contrast to the 1981-1986 period when non-average agricultural employment fell by 5,670 per year on average. To date, these positive developments have been sustained. Growth in GNP has averaged 4.4.% per annum during the period 1992-1995, compared with an EU-15 average of 1.5% over the same period. Inflation remains low and the balance of payments is in substantial surplus. Ireland's annual fiscal deficit is now one of the lowest in the EU Member States - a major turnabout from the unsustainably high deficits which persisted for much of the 1980's.

Sensible economic policies and centralised wage bargaining,[5] pursued by successive Governments with the support of the social partners (trade unions, farmers, employers and the community and voluntary sectors) since 1988, but on a generally more systematic basis than was previously the case, have brought about a fundamental strengthening of the economy. A sustained rise in living standards has been achieved and the gap with the rest of Europe has narrowed. GNP per capita has risen from 56.3% of the average of EU Member States in 1980, to 65.2% in 1995 (Forfas Report (1996), pp. 6) and to 111% in 1999 (Sweeney (1999), pp. 56). It is not surprising therefore that the 1990's eventually yielded a net migration to Ireland, as some of the best educated Irish who had emigrated in the bleak 1980's, returned as experienced workers (see Figure 2).

Over the past fifteen years (1980-1995), exports have been the main driving force of economic growth. Their impact however, has been eroded by other foreign transactions, notably interest payments on the foreign component of the national debt and profit repatriations by foreign-owned enterprises. It is estimated that because of this "enclave " of foreign -owned firms within the national economy, that the national economy has been transformed -each year some of its GDP must go to foreign owners in the form of remitted profits, so as a result Ireland's GNP is about 12% lower than its GDP.

Much of the growth in exports has come from the high-technology sectors of industry, generated mainly by the subsidiaries of multinational companies which have successfully invested in Ireland in the past and have provided a net increase of 15,000 in employment in the course of the past fifteen years. These firms have also provided a substantive increase in technology transfer and management know-how to the Irish economy, together with significant sub-supply opportunities for Irish-owned industry. Many of the jobs in traditional, indigenous firms disappeared, to be replaced by jobs with much higher value -added in new high-tech sectors. A smaller, leaner Irish-owned industrial base survived and expanded both inside Ireland and abroad. Walsh and Leddin (2000), pp. 49.

Over the next fifteen years, the number of new entrants annually to the labour-force is projected to reduce from 23,000 in 1995 to 21,000 by 2000, to 9,000 by 2005 and to 8,000 by 2010. The general level of educational attainment will increase. Investment in R and D, as a proxy for innovation, although low by international standards, is increasing slowly throughout the economy, and particularly in the private sector towards the norms of smaller, developed economies. A partnership approach between employers, trade unions and Government on wage restraint has continued. This has contributed to a significant reduction in disruptive industrial disputes, moderate wage increases, the first steps of a moderate tax reform programme and overall policy stability conducive to investment decisions. The new organisational structures for industrial promotion are working effectively and already achieving improved results in promoting employment in both foreign-owned and Irish-owned industry.

Recent economic progress cannot be viewed with complacency, in view of the quite different experience for most of the present century. To gauge the extent of progress without looking at *emigration figures* would be dishonest - see Figure 2 below. In times of deep recession and high unemployment, emigration to the U.S, the U.K. and Australia, has provided a safety valve for an Irish economy, when grappling with a burden of debt and stagnant growth.

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[5] The return to centralised wage bargaining or National Wage Agreements (NWA's) in the second half of the 1980's were an attempt to moderate wage inflation, as the economic recovery gained momentum. In return, the government promised reductions in income tax, improvements in social benefits -for example see the Programme for National Recovery (1988-1990), Walsh and Leddin (2000), pp. 46.

Figure 2. Net Emigration from Ireland, 1850-1998.[6]

1850's (gross outflows)	800,000
1860's (gross outflows)	697,000
1870's net outflows	502,000
1890's ditto	396,000
1900's ditto etc.	262,000
1910's	116,000
1920's (estimate)	136,000
1930's	101,000
1940's	250,000
1950's	409,000
1960's	135,000
1970's	(104,000)
1980's	208,000
1990's	(20,000)

Extracted from Sweeney (1999), pp. 37. based on Central Statistics Office and NESC [7](1991) reports.

Since the Famine ended in 1848, a gross total of over 5 million people have left in over 150 years, with the net figure being over 450 million. In the 1950's, emigration was extraordinarily high at 409,000 (out of a population of 3 million people) people emigrating between 1951 and 1961, compared to a population of 6.5 million people in eighteen fifties.

Between 1986 and 1996 alone, emigration amounted to more than 180,000 people, with a huge exodus between 1986 and 1991. Population growth resumed in the 1990's and is now estimated to be running at 1% a year. If this is maintained, the population will reach 4 million by the year 2010, Walsh and Leddin (2000), pp.23. Even with this massive loss of population, the rate of unemployment had remained high,[8] at 12.9% (1995) of the labour force, compared with an EU average of 11%. In 1996, more than 60% (of the unemployed total) had been unemployed for more than a year and over 41% for more than two years.

Over the next 15 years (by 2010), the government wishes to more than halve the present rate of unemployment to about 6% and to reduce the number of long term unemployed from 127,000 in 1995 to no more than 50,000 in 2010. It also wishes to increase living standards in terms of GNP per capita, to achieve average EU-15 levels and raise the quality of life.

Sustaining the economic and social achievements already gained so far and reaching the ambitious objectives set out above by the year 2010, will require a *dynamic enterprise culture and the further evolution of public policy for enterprise promotion, together with a consistent and systematic implementation of these policies over time.*

The Contribution of the Enterprise Sector to the Irish Economy :

The enterprise sector is defined as the set of Irish-owned and foreign-owned enterprises, based in Ireland, engaged in the manufacture of products or in the provision of marketable services.
It has been central to achieving a level of social and economic progress in future years, greater than that achieved in the past. The sector has faced unprecedented change due to two impacting forces - the presence of technological evolution and the internationalisation of competition.

The manufacturing sector in Ireland is dominated by a small number of sectors (chemicals, computers, instrument engineering and electrical engineering) accounting for over 50% of manufacturing output (gross value added). The indigenous sector (i.e. Irish owned) accounts for one third of gross manufacturing output but about 53% of manufacturing employment. (NDP (2000), pp. 37). The

[6] The figures are all for the island of Ireland until 1924, after which they are for the Republic of Ireland.
[7] The National Economic and Social Council (NESC).
[8] The unemployment rate peaked at 17.1% in 1986 and the net emigration rate at 1.25% in 1989. Walsh and Leddin (2000), pp. 27.

indigenous sector is said to be less productive than the foreign owned plants, with gross output per person in Irish owned manufacturing plants being about 45% of that for workers in foreign owned plants. The average size of plant in terms of persons employed is about 5 times greater in the foreign owned plants, than in the indigenous ones. The indigenous firms tend not to be engaged in the production of high-technology products or use high-technology processes, devote very little resources to research and product development and are the dominant sources of employment in the less developed regions of the Republic.

While most of the traditional indigenous firms that emerged under the umbrella of protectionism have contracted or gone out of business, a core of strong Irish firms have survived and expanded. (Walsh and Leddin (2000), pp. 41). Firms such as Smurfit, CRH, Ryanair, Kerry Group, Guinness Group, Fyffes, Glen Dimplex, Waterford-Wedgewood, Waterford-Avonmore, Independent Newspapers have become increasingly multinational by nature, in their own right and non-Irish investors own significant proportions of their equity. Thus, the Irish economy has become to some extent internationalised, in sharp contrast to the largely self-sufficient, emigration- drained, inward-looking economy of the nineteen fifties.

The growth in employment and in output has largely been in the enterprise sector and specifically, in the internationally traded sector.[9] This can be seen in the following chart - Figure 3.

Figure 3.

Sector of Employment	1989	1995	1998	% Change 1989-1998
Agriculture	162,000	142,000	129,000	-20.3 %
Manufacturing:				
Irish	120,169	129,230	139,687	+16.2 %
Foreign	93,266	110,666	124,480	+33.5 %
Internationally Traded Services:				
Irish	4,135	7,705	14,881	259.9%
Foreign	5,482	15,001	31,441	473.3%
Local Services	608,383	729,294	847,678	+39.3%
Total Services	618,000	752,000	894,000	+44.7%
Other Industries[10]	95,000	105,000	170,000	+80.8%

Of the increase of 24% in manufacturing jobs (being an increase of 51,000, from 213,000 in 1989 to 264,000 in 1998), foreign companies provided 61.5% of this increase (31,200 jobs) and Irish- owned companies provided 38.5% (19,500 jobs). Irish-owned industry consists almost entirely of small and medium-sized enterprises.

There is a difference in the export propensity of indigenous manufacturing versus foreign firms. The Operational Programme for Industrial Development 1994-1999, on pp. 28/9, reported that in 1990, "only one-third of all indigenous firms were exporting compared to 86% of non-indigenous firms".

The Forfas (2000) report, pp.vi also states

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[9] The internationally traded sector includes activities such as information and telecommunications, software, training, financial, healthcare and design and entertainment services.
[10] Other industries include mining, quarrying and turf production; building and construction;electricity and gas and water.

'the export propensity of Irish-owned industry remains vulnerably low and highlights the need for Irish-owned companies to develop non-traditional export markets, particularly if they are to build the scale of operation, needed to compete in an increasingly globalised environment'

Most indigenous firms are in the traditional manufacturing industrial sectors, such as food, clothing and footwear, timber and furniture, paper and printing, clay products, metals and engineering, whereas foreign firms predominate in drink and tobacco, textiles, chemicals, and in the services area, they predominate in electronics (software development and hardware production), telemarketing and international financial services.

The Operational Programme (OP) also notes on pp. 35, that Irish -owned companies must focus on improving their competitiveness, before they can compete successfully on a long-term basis, with international firms both on the domestic and on export markets. The policy effort will be directed at firms in those sectors where "improved competitiveness is expected to yield most in terms of increased output, value added, profitability, employment and wealth generation in Ireland", The deficiencies of indigenous industry noted in the OP, on pp. 36, were researched by Deloitte and Touche consultants and were identified as relating to marketing, technology, skills and finance.

The economic policies that guided the growth trends apparent in Figure 3 above are reviewed in the next section, by means of a content analysis of the groundbreaking Culliton Report (1992) and of the two most recent Forfas reports, of 1996 and 2000 and the National Development Plan (2000). Forfas is the *policy advisory and co-ordination body for industrial development and science and technology in Ireland.* It is also the body in which the State's legal powers for industrial promotion and technology development have been vested. Two other bodies implement the Forfas policies, namely Forbairt, a state body for the promotion of *indigenous industry* and the Industrial Development Authority (IDA Ireland) is the state body responsible for the promotion of *inward investment by foreign firms*.
Much remains to be done, to improve the size and performance of indigenous industry, to international standards.

Review of Culliton (1992) Report

The Culliton (1992) Report was a review of the industrial policy of tax breaks and grants and of the outcome of the FDI policies of the IDA, during the nineteen eighties. At the time of writing the Report, unemployment stood at roughly 260,000 people. Furthermore, the spending approach of the 1980's had not tackled the problem of unemployment, but left the Government with a legacy of debt and growing interest payments.

Instead of trying to create jobs directly through large-scale spending programmes, the Report was radical in suggesting that the approach had to change to one of creating the *conditions in which ability and enterprise could be translated into employment opportunities.* It provided a frame of reference for the subsequent Forfas report of 1996. The main recommendations of the Culliton Report in regard to the promotion of economic development were to reduce reliance on tax breaks and grants and put greater emphasis on creating a *favourable cost and production environment for firms.* In particular, the latter involved four pillars :

- the formation and evaluation of policy needed a broader strategy, to take account of all relevant factors, including taxation, infrastructure, education and training
- the need for more market-led and production-oriented enterprise
- the need to build Irish industrial performance on national sources of competitive advantage
- the need to deliver industrial policy interventions in a more integrated and cost-effective manner

A recognition of the crucial role that economic, administrative and infrastructural environment could play in the development of the enterprise sector marked a *new broader approach to industrial strategy* in Ireland and this change was first called for in the Culliton Report and later referred to the

Government's new approach to industrial policy in the Operational Programme for Industrial Development 1994-1999, pp. 4 :-

> The formation of industrial policy will in future, encompass all areas of public policy which have a significant impact on the creation and maintenance of competitive enterprises in the industrial sector, including internationally trading services in Ireland. These include not only the traditional instruments of policy in the form of direct incentives and advice from State agencies but important areas like : taxation, infrastructure (ports, roads, telecommunications, postal services and environmental services), education and training, competition policy and monetary, fiscal and Government budgetary policies generally.

No simple policy action could ensure a quick and easy solution to the problem of unemployment; there was a need for a structured effort to improve the effectiveness of the economy and to promote active involvement in enterprise throughout the economy, in public and private sectors alike.

The Culliton criticisms of the generous tax and grants package, which was the main focus of previous industrial policy, led to a subsequent reduction in state aid for FDI (through cuts in fixed asset grants and tax concessions) so that the level of state support per job created, fell steadily and is now less than the EU average (Walsh and Ledden (2000), pp. 39). It also recommended a decisive shift by State agencies to equity and venture capital finance, rather than grants, for indigenous industry. This, the authors claimed, should foster a more market-led and product-oriented indigenous enterprise, rather than encouraging a hand-out mentality, Culliton (1992), pp. 10.

The Report states on pp. 22 :

> in an attempt to boost economic performance over the years, the proliferation of tax breaks and grant assistance has had some unintended negative side-effects, on the structure of industry, on the level of Government borrowing and on the self-reliance of Irish entrepreneurs. In particular, the competitive edge of Irish industry has been blunted as effort and energy have been distracted from the proper emphasis on serving the market and on achieving high productivity, into maximising the grant or tax benefit. Tax avoidance and grant maximisation are directly unproductive activities or "rent-seeking" in the economists' jargon *par excellence* ... tax reform and a reduced emphasis on industrial grants … should help focus entrepreneurial effort.
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> Culliton Report (1992), pp. 22.

An important factor in entrepreneurial effort is that it involves taking risks and therefore the possibility of failure, in that many risky ventures fail. Apart from the above-mentioned point that too little effort was going into directly productive activities, the Report also mentioned a *cultural factor*, namely a negative Irish attitude towards enterprise and a stigma attaching to business failure :-

> Our experience leads us to conclude that an important obstacle to progress on this front is the negative attitude towards enterprise that is prevalent in the country. An important example is the attitude to industrial start-ups and what we would perceive as a deep-rooted prejudice against failure in business. The stigma that attaches to a failed enterprise very often inhibits the individual from ever trying again. We find this to contrast unfavourably to attitudes in, for example, the United States - where many emigrants have shown that to be Irish is in no way inconsistent with an entrepreneurial flair. In the United States, not only is business success respected, but the unsuccessful entrepreneur, who refuses to accept defeat, is given due respect - and represents indeed a kind of folk hero.
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> Culliton Report (1992), pp. 22.

IDA policy had in the past been directed at capturing foreign high-tech and pharmaceutical firms and persuading them to invest in Ireland. It was thought that as these segments were international growth areas or "winners", that linkages would form between the high-tech foreign multinational's Irish branch and local indigenous suppliers. Government expectations that domestic firms would supply most of the service inputs required by the foreign-owned firms, did not materialise and most of the foreign firms sourced most of their materials abroad and "it is only a mild exaggeration to say that most of the newer foreign firms operate [in the Republic] as an industrial enclave", Culliton (1992), pp. 31.

As a policy response to this situation, the reduced grant-aid budget was to be re-focussed on promoting clusters of foreign and indigenous firms in niches of national competitive advantage. The logic was that it was better to promote industry segments which could yield sustainable national advantage, than to simply make the choice based on the criterion of bringing in high-technology "winners".

The high-tech and pharmaceutical "winners" did not build on pre-existing Irish strengths or natural advantages. From this perspective, " the disappointing linkages that have resulted with pharmaceuticals and electronics were not surprising" , Culliton (1992), pp. 74.

Industrial development in successful economies has usually been preceded by the development of clusters[11]. First, one industry emerges from the local environment; soon supplier industries develop to serve it. Investment in education, training, R and D and infrastructure reinforce the process. As expertise further develops, it is spread to other industries that require similar skills, technologies and infrastructure. This process of growth and success of individual firms spills over to other firms and related industries. More effective linkage between the lead firm in the cluster and other small-scale suppliers should follow. There were also regional implications from this cluster policy, as a region with educational institutes and good infrastructure could more readily foster a new cluster of firms, in geographical proximity to these institutes; such proximity often could be decisive to the success of a cluster.

The cluster policy recommended in the Culliton (1992) Report has already been a success in other European countries and on pp. 73, several examples were quoted. Most of Denmark's world class industries relate to agriculture. It is competitive in barley, beer and fermentation equipment, in dairy products and in dairy processing equipment, in insulin and industrial enzymes, which are related to its agricultural industries. The Swiss and German pharmaceutical industries both came out of the corresponding dye industries and the Swedish and Italian packaging machinery industries grew up near, or were closely related to, the food processing industry in each nation.

A Review of the Forfas (1996) Report

Based on Central Statistics Office (CSO) data, an analysis of GDP by sector in 1960 can be compared to GDP by sector in 1994 as shown in Figure 4 below. The nature of trade, work, employment and production has changed , because the industrial and services sectors accounted for over 90% of national output in 1994, compared with 75% in 1960. Into the future, the determinants of economic success will be different to those that were relevant in the past or those that were required as at 1994.

Figure 4. Sectoral Composition of GDP 1960 versus 1994.

	1960	**1994**
Agriculture	25%	9%
Industry	30%	38%
Services	45%	53%
Total GDP	IR£8,313m (at constant 1994 prices)	IR £30,831m. (at constant 1994 prices)

Forfas (1996), pp. 3.

Forces of change that are international and even global in character will impact upon Ireland's enterprise sector over the next 15 years and have been identified in the Forfas Report (1996), pp. 15 :-

- The impact of technological change.
- Trends in the international pattern of economic development and trade.
- The structure and organisation of the workforce.
- The pattern of demographic change.
- The movement towards EMU.

[11] See for example some research evidence of this in Jacobson, D. and Mc Donough, T. (1996/97). "Irish Industry. International Trade and European Integration", Dublin City University Business School Research Papers, No.27, pp.6-9..

- The competitiveness of the Irish economy.

Wisely, the steering committee for the Forfas Report (1996) concluded that there was a need for a *longer-term* framework for the development of economic and enterprise policies for the next 15 years. The framework required was one that

> systematically monitors and anticipates changes in the global markets in which Ireland competes and that identifies the actions required in public policies to support the competitiveness of the *enterprise sector* in the face of these changes. A reactive approach to domestic and external forces of change as they arise will not be adequate in future, if the economic and social progress of recent years is to be sustained over the prolonged period necessary to deal decisively with the unemployment problem and to continue closing the gap in living standards with other EU countries.
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> Forfas Report (1996), pp.9.

Following a wide consultative process, consensus was reached on a proposed 7-point long-term strategy for enterprise promotion.

Forfas (1996) 7-point Long-Term Strategy for the development of economic and enterprise policies for the 15 years to 2010.

- Recognise fully the importance of the *service sector* in the generation of employment and in the development of an enterprise culture.
- Transform Irish industry so it can innovate, re-position and compete.
- Bearing in mind the competition for inward investment, develop Ireland's attractiveness for this, in terms of skills availability, infrastructure and incentives.
- Achieve a reform of the tax system and in national debt, so as to promote private enterprise by establishing an environment conducive to innovation and commercial risk-taking.
- Undertake a major drive to raise the skills profile of people through education and higher investment by firms in training and human resource development.
- Introduce measures to support an Information Society.
- Take early and decisive action to provide a world-class transport and logistics infrastructure in Ireland.

Forfas (1996) Executive Summary, pp.2.

<u>Review of the Forfas (2000) Report</u>

Unprecedented high growth rates in the period 1994-1999 with average GNP growth of about 7.5% per annum in real terms, an increase of 370,000 in the numbers at work and an unemployment rate of only 6% in 1999, compared to 15% in 1993 provided the backdrop to the Report.. The Government deficit was 2.3% of GDP in 1993 and the debt to GDP ratio was 93.1%. The deficit fell between 1994 and 1996, while the budget has been in surplus since 1998. As a result, Government debt fell to 56% of GDP in 1998. NDP (2000), pp. 27. The country is now experiencing significant net inward migration, with the population growing at almost 1% per annum as a result. (Forfas Report (2000), pp. 4.

As a small open economy, Ireland is more exposed than other economies, to changes in the international environment. While the external economic environment has been relatively benign for the past decade, this cannot be assumed for the future. Major changes in technology, markets and business models will lead to considerable structural changes in the decade ahead. Ireland will be particularly affected by these changes as it is highly dependent on industries such as information and communications technologies, pharmaceuticals, healthcare, food and internationally -traded services, where the greatest changes are expected.

These changes include the use of e-business and other Information and Communications Technologies (ICT's). World trading systems are also being transformed with the virtual elimination of tariffs, the gradual opening up of service sectors to international competition and the increasing ability of even

small operators to service global markets, especially with the aid of e-business development. This emerging new business model is leading to a new pattern of international investment, with corporations selecting the best location for each particular activity, rather than necessarily putting integrated projects in a single location. It will also lead to a new definition of peripherality - integration into global information networks will increasingly measure a country's accessibility as much as its links to trade routes and physical market access. Ireland's entry into EMU in 2000 re-inforces the need to remain competitive, since the option of adjusting exchange rates to offset short-term losses in competitiveness is now no longer available. Responsibility for monetary policy has been transferred to the European Central Bank (ECB). Greater flexibility will be required in the economy as a whole and prices and wages must be more responsive to changing economic conditions and fiscal policy must seek to offset excess demand in periods of strong growth and support growth in less favourable times.
There will be a decline in E.U. Structural Fund supports for Ireland, as it embarks on a new century, because of the progress achieved in the last decade; there will also be greater competition from Eastern Europe for mobile FDI funds. The advent of the Single European Market led to significant growth in investment into Europe, particularly from the U.S..

In the period 1986 to 1991, FDI inflows into Europe averaged $63.2 billion with an average of $368 million invested in Ireland (0.6%). By 1997, inflows to the EU had risen to $108 billion, of which Ireland took $4.15 billion (3.8%) … in particular Ireland has been successful in recent years at capturing up to 20% of U.S. manufacturing FDI projects into the E.U. (Forfas (2000),pp.13)

Forfas (2000), pp. 21, anticipates the future effect of these changes on the Irish economy:

> the emergence of global value chains will facilitate the relocation of low value-added, low-skill manufacturing and mobile services jobs to lower wage countries. This will increase the rate at which existing jobs are lost, not just in "traditional" sectors, but also within what are today perceived as high-technology sectors. The jobs that will replace them will be knowledge-based, requiring highly-skilled, creative and flexible people, in operations that are managing global value chains and that are globally competitive. These jobs will be located only where there is a high-quality communications infrastructure, competitive services, and an environment that is attractive to creative people.

A Role for Services in the 21st Century.

As Figure 3 shows, the growth in employment and in output has largely been in the enterprise sector and specifically the internationally-traded services sector. Services comprise local services and internationally traded services, as per Figure 3. Between 1992 and 1997, productivity in manufacturing grew by 41.2%, whereas that in services grew by only 5.3%. Forfas (2000), pp. 27 noted that in 1997, the average GDP per person engaged in the overall economy was IR £26, 260, at constant prices, but in manufacturing it was IR£46,410, in services it was IR£21,040 and in agriculture, IR£17,700. Service exports comprise 11 % of total exports, while in Austria it is estimated at 42% and in Denmark at 21%, Service exports have grown in recent years, primarily driven by the growth in software exports and other internationally- traded services exports.

Services remain the largest part of the Irish economy and the main source of employment growth, but are more labour intensive than other industry sectors. Policy must focus on realising the full potential of the services economy for further employment, productivity and export growth. Regulatory reform and increasing competition in all services market is required. [12]

The Forfas (2000) Report on pp.10, mentions a policy shift in the support provided to projects and firms (in all sectors) by development agencies, from "capacity building" support (i.e. financial support

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[12] Many services markets remain sheltered from international and in some cases, effective local competition, so "this may be a factor in the low levels of internationalisation of Irish service providers and lower productivity; similarly while open market policies have been pursued over the last twenty to thirty years in most industrial sectors, high levels of market regulation remain in a number of key business and consumer services markets." Forfas (2000), pp. 35.

for capital investment and employment grants) to "capability building" support (i.e. support for management development, training, marketing and research and development).

> In the case of Irish-owned industry, the development agencies will work to overcome inherent weaknesses, including lack of scale, low levels of process and product development, low levels of participation in high-growth activities, poor design and innovation capability, and relatively low export propensity. The identification and support of high-potential start-up firms in different areas of the country will be a particular focus of promotional activity.
> In the case of foreign-owned industry, the agencies will promote both new, high-quality firms and the development of foreign -owned enterprises already located in Ireland that provide high value-added employment in manufacturing, services and R and D activities.

Forfas (2000) Report, pp.10

A Possible Research Agenda

It would be an interesting research exercise to test for a cultural difference between the U.S. and Ireland in regard to attitudes to business start-ups, risk and business failure among university students, from which cohort many entrepreneurs eventually emerge. The research could then be extended into a pan-European study, to test whether Irish university students studying a Business degree, would have different attitudes to business start-ups and risk than say Danish, German or French university students of business degrees, assuming that the students have only been educated in their home country.

The existence of many links between Irish, North American and European Business Schools, allows for the exchange of students on Business degrees, between these schools, to form multi-cultural university classes and as such, could provide a convenient sample for contrasting those students educated solely in a university in their home country, with those educated in a university in their home country as well as in a foreign university. Does this variation in educational experience and exposure to another culture influence the student's attitude to starting up their own enterprise and to the risks attaching to same?

It might also be possible to research the question as to whether Irish students who have gained accounting, business or law degrees, eventually set-up the greater proportion of new Irish-owned enterprises or whether Irish students who have gained science or engineering degrees, in fact out-perform their non-scientific counterparts in entrepreneurial endeavour.?

Conclusions - Towards the Future :

Over the first sixty-four years of Independence (1922-1986), little progress was made towards closing the gap in living standards between Ireland and the richer countries of Europe. It is clear that the period since 1986 has been unique in Irish history, because never before did so many favourable factors combine and make it possible to attract a steady inflow of high-quality FDI. The inflow of new firms transformed the country's economic base and raised exports, productivity, living standards and employment to heights that could never have been anticipated in earlier decades.

In the period to 2010, the enterprise sector will continue to be " the main engine of economic growth" Forfas (2000), pp. 24. The forecasted annual rate of growth in GNP over the period 2000 to 2010, will average 5% per year, compared with almost 8% per year, between 1994 and 2000. In order to achieve these growth rates,

- the level of employment in the internationally-traded sector of the economy (manufacturing and internationally-traded services) needs to increase from an estimated level of 310,000 in 1998 to 400,000 in 2010.
- employment in locally-traded services should increase from an estimated 847,000 in 1998 to over 1,150,000 in 2010.

As Ireland embarks upon the 21st Century, it must avoid a dependant mentality : the most productive sector in the Irish economy is composed of dependent branches of foreign multi-nationals as opposed to the indigenous sector, which is less productive and less dominant. This situation cannot be allowed to continue. Irish indigenous industry must seek to become more competitive, through cost reduction, quality improvements and improved product technology in existing firms and segments and move progressively into higher productivity industries and segments. A national evolution in home-managed firms, with deep roots in the Irish economy, to multinational status must be encouraged.
To manage this transition, the lessons of Irish economic history briefly profiled in this chapter, are an indication that "policies will matter."

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