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# IRELAND AND EUROPE: CHALLENGES FOR A NEW CENTURY

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Rory O'Donnell



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*LIST OF ABBREVIATIONS*

CEC	Commission of the European Communities
CAP	Common Agricultural Policy
CFSP	Common Foreign and Security Policy
EC	European Community
EFTA	European Free Trade Association
EMS	European Monetary System
EMU	European Monetary Union
EOLAS	Irish Science and Technology Agency
EPC	European Political Co-operation
GATT	General Agreement on Tariffs and Trade
GDP	Gross Domestic Product
GNP	Gross National Product
IPRC	Industrial Policy Review Group
NATO	North Atlantic Treaty Organisation
NESC	National Economic and Social Council
NIESR	National Institute of Economic and Social Research
PESP	Programme for Economic and Social Progress
PNR	Programme for National Recovery
SEA	Single European Act
SFADCO	Shannon Free Airport Development Company
TEPSA	Trans European Policy Studies Association

## GENERAL SUMMARY

### *Background and Objectives*

In 1990 the President of the European Commission, Jacques Delors, established a special unit to assess the European Community's integration process and to establish relationships with research institutes in the member states involved in medium-term forecasting and planning. The first project of this Forward Studies Unit was a 12-country study of the economic, cultural and political factors which will shape the development of the European Community in the years to 2010. The purpose of the study was to move the focus of Community thinking beyond the internal market programme, to the themes, issues and policies which are likely to be important in the years to 2010.

In order to do this, a research institute in each Community country was asked to identify the major factors which will shape the development of their country and the Community, with a focus on factors which will condition economic development. They were also asked to analyse how the European Community could influence its own future and whether it could move from being an "environment taker" to an "environment maker". The Commission's approach to this project was deliberately multidisciplinary and qualitative. It sought a discussion of the interplay between political, cultural and economic forces, rather than a detailed forecast for each country. The aim was to produce a set of short, non-technical, texts setting out the main challenges and strategic issues.

The 12 national reports, and a Commission survey of European business leaders, were discussed at two conferences in Brussels. A number of experts on European integration also participated in these meetings. The Commission's Forward Studies Unit has recently published its synthesis of the "shaping factors" identified by the 12 national research institutes and in the discussions at these two meetings. In *The European Challenges Post 1992: Shaping Factors, Shaping Actors* (Edward Elgar, 1993), Alexis Jacquemin and David Wright compare the perceptions of national social scientists with those of Europe's business leaders. They draw out the implications of these two, contrasting, perceptions for the European Union.

This paper is the Irish contribution to the research project. In undertaking this work, the guiding conception has been the idea that despite the small size and great openness of the Irish economy and Irish

society, the effects of international forces will be mediated by indigenous social, economic and political factors. Likewise, despite the large size of the European Community, and of some of its member states, its development will be significantly shaped by external factors. In recent years, movement towards this "interactive" outlook can be identified in several branches of social science.

#### *International Factors*

The evolution of both the European Community and Ireland will continue to be shaped by a range of international factors. These will include economic, cultural and political forces. The international economic environment is likely to be one of continuing crisis and change. The important factors include technological change, the globalisation of manufacturing, profound changes in international finance and uncertainty about the principles of macroeconomic management. These are a set of interrelated phenomena, reflecting the breakdown of the post-war "golden age" and the failure of a new stable pattern of development to emerge. An important feature common to technological change, financial developments and macroeconomic volatility and uncertainty, is the increase in international interdependence. Other international economic factors which will shape development in both the EC and Ireland are liberalisation of agriculture, EC enlargement and the re-establishment of capitalism in Central and Eastern Europe. An important implication of these economic factors will be increased international competition. From an Irish point of view, a distinction should be drawn between two dimensions of international economic developments: the overall *rate* of growth, and the geographical and organisational *pattern* of production. It seems unlikely that technological change and "globalisation" will reduce the tendency to spatial concentration, though they will force changes in the hierarchy of leading and lagging regions.

Two international cultural factors which may be significant for the Community and Ireland are inward migration into the EC and the question of European identity. While some define European identity in terms of democracy, liberalism and tolerance, it seems more realistic to see the social market economy, in the broadest sense, as the real distinguishing feature of the European model. This raises questions about the Community's willingness and ability to develop a European identity around the truly distinctive feature of its social, economic and political system.

The dominant international political factors are the collapse of the Soviet Union, German unification and EC enlargement. German unification has already had profound effects on the Community; it should

not be presumed that Germany can continue to play the economic and political roles which it has in European integration to date.

*Factors Which are Specific to Ireland*

Perhaps the most important economic factors are the structures of Ireland's industrial and agricultural sectors. The existing structures will shape Ireland's response to international developments; the ability to improve these structures will determine whether Ireland can meet its economic and social goals. Other important socio-economic factors include demographic developments, the emerging social class structure with its high rate of unemployment, the pressure of public finance, and migration.

It is possible to identify a range of cultural factors which will combine to shape the lives of Irish people. While these have an economic dimension, it remains difficult to identify whether that dimension includes causation which runs *from culture to economic performance*. Two aspects of domestic politics may be important: the development of a political process capable of formulating and implementing strategic policies and creation of a more independent system of local government and democracy. A third political factor is the conflict in Northern Ireland.

Although there is agreement that economic and social factors - such as Ireland's economic structure, unemployment and international trends - will all be important, there is no agreement on *how* they will bear on future development. There is definite controversy on the relevance of the cultural and political factors - reflecting the important debate which has developed in recent years between structural, cultural, economic and political explanations of Ireland's long-run economic failure. These different explanations of Ireland's past tend to suggest different approaches to overcoming current and future problems. In a recent paper commissioned by NESF, *The Irish Economy in a Comparative Institutional Perspective*, the Norwegian sociologist Lars Mjøset presents a synthesis of these different interpretations. This synthesis is made possible by the use of the concept of a "national system of innovation", which is defined as the institutions and economic structures which affect the rate and direction of innovative activities in the economy. Mjøset's central argument is that Ireland's basic vicious circle starts from two facts: a weak national system of innovation and population decline via emigration. Although this work constitutes a considerable advance in our understanding of the interaction of economic, cultural and political factors in Ireland, there remains considerable work to be done. The idea of a national system of innovation has been shown to be a valuable organising concept, but we have little detailed knowledge of the particular system in Ireland in the 1990s.

*Challenges for the European Community*

There is considerable uncertainty about the future of the European Community and Ireland's prospects within it. These uncertainties arise, first, because there is an array of internal and external problems which threaten Europe and, second, because there are severe doubts about whether the Community, with its existing decision-making system and institutional structure, can effectively deal with them. The Community faces a demanding internal agenda, containing the 1992 programme, EMU, cohesion, social Europe, and the formulation of guiding values. It faces an uncertain, and in many ways threatening, external environment because of developments in Central Europe, the Mediterranean, enlargement, North-South relations and environmental decay. This agenda and set of external pressures would be likely to overload even the most authoritative, decisive and legitimate decision-making and administrative system. But the authority, effectiveness and legitimacy of the Community's system of governance are highly problematic.

It is possible to identify four concrete challenges for the Community: change in its decision-making system, development of the European social market model, competitiveness and macroeconomic management. Improvements in the authority, effectiveness and legitimacy of the Community's system of governance are an absolute precondition for facing the other challenges. The social market model is the core of a European identity upon which economic, monetary and political union can be built. But the social market models in place in Community countries are disrupted by economic integration and challenged by neo-liberalism, demographic developments and economic difficulties. Taking a long-term view, one of the major challenges for the European Community is to redesign systems of social rights and welfare in ways which facilitate increased competitiveness and growth.

The third challenge is the competitiveness and economic strength of the Community. A key question is whether the completion of the internal market is sufficient to re-establish the competitiveness of Europe and to unleash long-term forces of innovation and growth.

Fourth, the economy of Europe requires macroeconomic management. The interdependencies between the national economies mean that this cannot be done effectively at national level. It is now clear that the Maastricht Treaty does not provide a system of macroeconomic management for Europe, including a stable transition to EMU. The natural tendency of an intergovernmental system to avoid the political requirements of EMU was reinforced by the prevailing monetary and economic orthodoxy. The establishment of a system of macroeconomic

management capable of facilitating growth and employment will remain a major challenge for the Community in the years to 2010.

### *Challenges for Ireland*

There can be no doubt that the two greatest challenges facing Ireland are the reduction of unemployment and the development of competitive indigenous economic activity on a scale sufficient to meet its social, economic and employment needs. In considering approaches to these two ultimate objectives, attention should be given to two procedural issues: the overall consistency and completeness of Ireland's economic policy and the question of whether centralised income determination and "political exchange" enhances Ireland's ability to formulate and implement strategic policy approaches.

The requirements for a consistent policy framework in a small, open, European democracy have three, interdependent, elements: first, an appropriate macroeconomic framework, second, an income determination system which ensures competitiveness and avoids disruption and, third, policies which promote structural adjustment. Which of these three elements does Ireland have in place? It might be argued that progress has been made towards the first two: the EMS provides the sheet anchor of the macroeconomic approach and national bargaining on pay, taxation, welfare and other policies, determines income growth. Assuming that the macroeconomic element stays in place, the outstanding problems of unemployment and indigenous development suggest the need for further development of the second (income determination) and third (structural) elements of the overall framework.

A second procedural question is: what approach to policy formation will maximise Ireland's ability to identify and implement strategic policies in these and other areas? One view is that the system of centralised bargaining and "political exchange", developed in the Programme for National Recovery and the Programme for Economic and Social Progress, helps progress on the central challenges of unemployment and indigenous development. However, industrial sociologists have raised questions about Ireland's ability to sustain an effective system of tripartite political exchange and some economists have argued that such systems are positively harmful. The latter critics have, however, failed to explain how, freed from centralised and politicised bargaining, party politics will produce better economic management, and how decentralised pay bargaining will give higher priority to the unemployed and other marginalised groups. Nevertheless, the ability of the tripartite system to mount a serious challenge to unemployment and lack of indigenous

development depends on the willingness and ability of the participants to analyse these problems, negotiate serious policy changes and deliver on these. This is a highly demanding task. It implies both a need to learn from the experience of other societies and for institutional and political innovation to address the unique combination of Irish problems and structures.

A significant reduction in unemployment will not occur during the 1990s unless additional policies are put in place. The policies which might be considered capable of reducing unemployment are training and special employment measures, such as labour subsidies, direct job creation schemes and enterprise or self-employment schemes. Although some special employment measures are in existence, there is clearly considerable fatalism – among policy-makers, social scientists and in the society – about the possibility of significantly reducing unemployment. Evaluation studies suggested that labour subsidies have a large *deadweight* effect and direct hiring is both *temporary* and *costly*, and this seems to have undermined faith in the ability of these, and any other public policy, to significantly reduce Ireland's unemployment. It is possible, however, that, properly interpreted, existing evaluation studies do not *dictate* a drift to fatalism and that there are good reasons to continue active debate and experimentation on how to significantly reduce unemployment. The results of evaluation studies can be interpreted as highlighting the need for measures which are *targeted* on the long-term unemployed. The evaluation studies cannot capture the *hysteresis* effects (i.e., the tendency for unemployment to stay low once it becomes low and vice versa) which other research suggests is present. More generally, it may not be correct to use marginal studies of marginal schemes to draw negative conclusions about the possible effects of large scale and multidimensional schemes. While this paper does not make the case for any particular approach, it does seem that the debate on the use of training, labour subsidies and direct job schemes to significantly reduce unemployment, may have been closed prematurely.

There is now widespread agreement that Ireland must develop competitive indigenous industry on a significantly larger scale. There is also agreement on a number of principles and policies: reforms of the tax system, improvements in infrastructure, a switch from grants to equity and greater focus on industrial clusters. There is less agreement on the reforms of education and training proposed in the *Culliton Report*. This suggests three distinct challenges: implementation of the measures which are widely agreed, further exploration of the role of education and training in the Irish economy and analysis of how to use policy selectively to establish clusters around sources of national competitive advantage.

## Chapter 1

### INTRODUCTION

We live out our lives, both individually and in our relationships with each other, in the light of certain conceptions of a possible shared future, a future in which certain possibilities beckon us forward and others repel us, some seem already foreclosed and others perhaps inevitable. There is no present which is not informed by some image of some future and an image of the future which always presents itself in the form of a *telos* – or a variety of ends or goals – towards which we are either moving or failing to move in the present.

Alisdair MacIntyre, *After Virtue*, 1985.

#### (i) The European Commission's "Shaping Factors" Project

The Forward Studies Unit was established at the initiative of President Delors in 1990. The Unit, which works directly to President Delors, has three main tasks:

- the follow-up and assessment of the Community's integration process
- the establishment of relationships with the institutions in the member states involved in medium-term forecasting and planning
- ad hoc mandates given to the unit by the Commission.

Senior officials from this unit visited Dublin in the Spring of 1990 and requested the ESRI to participate in its first research project. The project was to identify the main factors which will shape the long-term prospects of the European Community and its member countries. The purpose of the study was to move the focus of Community thinking beyond the 1992 programme, to the themes, issues and policies which are likely to be important in the years between now and 2010. In order to do this, a research institute in each of the member states was asked to analyse the major factors which will shape the development of their country, with a focus on factors which will condition economic development and business strategies. This involved



- identification of the key general economic, cultural and political factors which will shape the European Community's business environment in the medium and longterm (up to the year 2010), as seen from the perspective of Ireland
- discussion of factors which are specific to Ireland
- analysis of factors which will shape the development of the Community and which could be shaped by the EC.

The Commission's approach to the project was deliberately multi-disciplinary and qualitative. Rather than seek detailed forecasts for each country, the Commission requested a discussion of the interplay between political, cultural and economic forces. The aim was to produce a set of short, non-technical, texts setting out the main challenges and strategic issues. The Commission has recently published its synthesis of the global and national "shaping factors" identified by the national research institutes. In *The European Challenges Post-1992: Shaping Factors, Shaping Actors*, Alexis Jacquemin and David Wright compare these factors with the views of the European business community on the priorities after 1992, and draw out the implications for European union. This paper consists of the Irish contribution to the research project. It is published in order to stimulate thought and debate on the challenges which face Ireland and the Community after the internal market programme.

### (ii) Outline of the Paper

While this document adopts the format suggested by the Forward Studies Unit, it begins with some preliminary material. Chapter 1 (iii) briefly states the major Irish concerns in the coming years. The purpose of this is to establish that the major Irish concerns are economic and, to some extent, cultural, rather than geopolitical, territorial, ethnic or military.

In commissioning the work the Forward Studies Unit adopted a deliberately non-directive approach, in order to draw out diverse national perspectives, rather than diverse national answers to narrowly defined questions. In approaching the task of identifying and discussing the factors which will shape Ireland's evolution in the years to 2010, it was considered necessary to adopt an explicit analytical framework. One reason is the apparent imbalance between powerful international forces and relatively tiny Irish factors. Another reason is to link the, inevitably speculative, discussion of the future to the existing analyses of similar issues which, quite properly, deal with the past. Consequently, Chapter 1 (iv) outlines an analytical framework which informs the substantive material in the paper.

The essence of this framework is the idea that, despite the great openness of the Irish economy and society, the effect of international forces will be mediated by indigenous social, economic and political factors. This "interactive vision" involves rejection of two contrasting approaches which, despite their obvious limitations, have a continuing conscious or subconscious appeal. One view is that the economic and social outcome in Ireland is, and has been, fully determined by external forces – in either a benign or malign way. The alternative view is that the Irish economy or society is an organic entity, contained within itself, to which general laws of economics or society can validly be applied. Although each of these conceptions seems obviously flawed, and an interactive outlook seems clearly preferable, it remains true that in making policy proposals many economists fall back on one or other of them.

It is argued in Chapter 1 (iv) that movement towards an interactive outlook can be identified in several branches of social science, such as international trade theory, regional economics, geography, business theory, the study of technical change and innovation, comparative political economy and development theory – all of which are relevant to the task of identifying the forces which will shape Ireland's future in Europe.

One important feature of the analytical approach, and of many of the theories which embody it, is that it makes the unit of social and economic analysis the subject of thought, rather than a datum. Chapter 1 (iv) finishes with a brief explanation of this and its relevance to the project.

The remaining sections of the paper follow the format suggested by the European Commission's Forward Studies Unit. Chapter 2 identifies the international factors which will shape Ireland's evolution, distinguishing between the economic dimension, cultural and historical factors, and political issues. The international environment of likely to be one of continuing crisis and change. This will reflect a set of interlinked economic factors, including technological change, the globalisation of manufacturing, profound changes in the structure of finance, changes in patterns of production and organisation and uncertainty about the principles of macroeconomic management. In considering the likely impact on Ireland, a distinction is drawn between two dimensions of international economic developments: the overall *rate* of growth, on the one hand, and the *pattern* of production and location, on the other. The latter is discussed in more detail than other factors in Chapter 2, for two reasons. First, it has, to date, received less attention in Ireland than it might have. Second, it is of particular relevance to Ireland and other less favoured regions of the Community, but is scarcely discussed in some of the national reports. International cultural factors include inward migration into the European

Community and the prospects for development of a European identity. The collapse of communism and German unification are likely to be the dominant international political factors, though EC enlargement will also be significant.

Chapter 3 identifies those shaping factors which are specific to Ireland. Among the economic and social factors discussed are the structure of the Irish economy, demographic patterns, the evolving social class structure and the burden of high long-term unemployment. A range of cultural and historical factors are identified. Three political factors are noted: Ireland's political culture and capacity for strategic policy-making, the question of local democracy and administration, and the problems of Northern Ireland. Attention is given to the varying balance between national and international factors across the Community. It is possible to divide the overall set of factors into two groups: those about which there is a broad measure of agreement and those whose relevance or effects are the subject of controversy. There may be particular controversy about the relevance of a number of the cultural and political factors identified and, in particular, about their influence on economic development. In order to engender discussion of this, Chapter 3 closes with a brief account of various cultural, structural and political explanations of Ireland's long-run economic failure and of a recent synthesis of them in an important study commissioned by NESCI.

In Chapter 4 there is a discussion of how the global and specific factors will affect the European Community. The Community has a demanding internal agenda, containing the 1992 programme, EMU, cohesion, social Europe and the formulation of guiding values; it faces an uncertain, and in many ways threatening, external environment because of developments in Central Europe, the Mediterranean, enlargement, North-South relations and environmental decay. This agenda and set of external issues would be likely to overload even the most authoritative and legitimate decision-making and administrative system. But the authority, effectiveness and legitimacy of the Community's system of governance are highly problematic. This poses severe political, economic and social challenges to the Community. Chapter 4 also contains a detailed discussion of possible medium to long-term approaches to the cohesion issue, since this is an area of Community policy on which Ireland should be expected to lead.

Chapter 5 discusses those factors which will be influenced by policy at national level. An attempt is made to characterise the overall nature of Ireland's policy problem, distinguishing between three requirements of a consistent policy framework in a small open economy: an appropriate macroeconomic policy approach, an income determination system which

avoids distributional conflict and ensures competitiveness and policies which promote structural adjustment. While it can be argued that Ireland has, in recent years, made some headway towards achieving the first two requirements, few would dispute that there is an urgent need for policies for development and structural change. In listing the national political factors which may shape Ireland's evolution (see Chapter 3) we note that Ireland's political culture has a weak capacity for strategic policy making. We also note that the recent steps by the social partners and some political parties to develop a system of tripartite "political exchange" is seen by some as an important attempt to resolve conflicts in the context of coherent strategic approaches. Others doubt that effective centralised arrangements are feasible or desirable in Ireland. Given the importance of this question, Chapter 5 includes a review of the current state of this debate.

Chapter 6 summarises the international and national factors identified in the paper and discusses the major challenges facing the European Community and Ireland, respectively, in the years to 2010.

### **(iii) Major Irish Concerns in the Coming Years**

In viewing the factors which will shape Ireland's development in the years to 2010 it is natural to focus on factors which have a bearing on the central concerns which preoccupy Irish people. Consequently, it may be of help if these concerns are briefly identified here. While these bear a certain similarity to the concerns in other member countries, they may take a particular form in the Irish context. It can be stated categorically that the major Irish concerns are economic and, to lesser extent, cultural, rather than geopolitical, territorial, ethnic, or military. The dominant Irish concern, which is, in fact, acute, is with a set of interlinked economic problems. These include unemployment, poverty and inequality, emigration, Ireland's relative prosperity within the Community, high taxation, the burden and risk of high national debt, and the viability of the Irish rural economy and society.

It is clear that unemployment, poverty, high taxation, emigration, rural decline and public debt are problems which are related to one another in complex ways. They combine to constitute a very considerable overall uncertainty about the economic future which will undoubtedly be the dominant Irish concern in the years between now and 2010. There seems little doubt that Irish people will evaluate the factors that will shape Ireland's future by reference to these problems and concerns.

However, as will be seen later in the study, we do not purport to be able to aggregate the concerns of individuals or groups to represent the

collective concerns of the Irish people. Different groups will be concerned about different problems and these concerns may not be consistent. The issue of finding sufficient consensus, within wider conflicts, is considered in some detail in Chapter 5.

#### (iv) Analytical Framework

##### *The Interactive Outlook*

This document consists of a discussion of the factors which are likely to shape Ireland's economic development in the period to 2010. In conducting this exercise, the guiding conception is the idea that despite the great openness of the Irish economy the outcome will emerge from an interaction between the international economic forces, the structural characteristics of the Irish economy and society and domestic and Community policy. Recognition of this interaction has recently been described as "central to a balanced assessment of Community membership" (Keatinge, *et al.*, 1991.) This interaction between international and indigenous factors has also been identified as relevant in explaining Ireland's long-run development (Mjøset, 1992). Indeed, at an international level a number of social sciences have, in recent years, each moved towards an "interactive vision" which sees the effect of global of economic forces on a given country or region as contingent on the indigenous economic, social and political structures and policies (Evans and Stephens, 1988). Movement towards this outlook can be identified in international trade theory, regional economics, business theory, geography, comparative political economy and development theory.

Lest this interactive outlook seem empty, it may be useful to briefly illustrate it and draw out some of its implications. The interactive outlook, as stated above in general terms, may seem to be no more than a framework; while what is required (in thinking about the factors which will shape Ireland) are substantive theories and propositions. In fact, the interactive outlook is more than a framework. It has emerged precisely from the development and/or fusion of particular theories. This point, and the meaning of the interactive outlook, can be illustrated by briefly considering the form it takes in each of the subjects listed above.

##### *International Trade Theory*

Recent developments in international trade theory have significantly altered economists' understanding of the effects of free trade on the three main subjects of trade theory: the patterns of trade, the gains from trade and the effects on income distribution. Most of the developments derive from the

introduction of economies of scale. Introduction of economies of scale, and the related phenomena of industrial structures, intra-industry trade and product differentiation, reveals a wide variety of possible outcomes from the integration process. For example, the effects of freeing trade between two countries in a particular industry, is dependent on the market structures (competitive, oligopolistic, or monopolistic), income levels and market size in each country, prior to trade. In addition, economies of scale, though they can be treated in a static analysis, strongly suggest dynamic forces. For example, Helpman and Krugman say that, in practice, "it is likely that one of the most important sources of economies of scale (and imperfect competition) lies in the dynamic process by which firms and industries improve their technologies" (Helpman and Krugman, 1985). This emphasis on innovation suggests the significance of firms' strategies, but also of institutional factors which support or inhibit innovation. Indeed, an important characteristic of the interactive outlook is acceptance of the historical and contingent nature of social and economic processes.

#### *Regional Economics*

In regional economics there has been a distinct move towards recognition that the economic outcome results from an interaction of wider forces of regional specialisation and factors indigenous to a region. While much regional economics has long rejected the neo-classical theory of regional convergence by market forces, it tended to replace this with theories of cumulative causation (Myrdal, 1957; Kaldor, 1970). The focus of these theories on external demand, as the ultimate determinant of a region's prosperity, has now been questioned. The existence of strong tendencies to regional concentration of advanced economic activity is no longer understood as implying that industry will *definitely* concentrate and regional fortunes will *definitely* diverge. One reason is that the process of regional change, just like the process of economic development, is not a steady journey along a path of either concentration or dispersal. It is an inherently uneven process which occurs in bursts of progress and sharp reversals. This unpredictability and contingency suggests that other forces are also very important and, furthermore, that among these might be such factors as political and social structures and economic policies (Albrechts, *et al.*, 1989; Chisholm, 1990; Moulaert, 1991).

#### *Geography*

Similar movement towards an interactive outlook can be identified in geography. The limits of contrasting traditional approaches – such as regional geography and quantitative geographic modelling – have been

identified and, to some degree, transcended (Entrikin, 1991). What is significant for our purposes is that the fusion of these traditional approaches is producing geographical work which strongly embodies the interactive outlook outlined above. The general theme of much of this work is the relationship between social organisation and spatial change. The task is to develop an understanding of both the general economic forces and socio-economic relationships within the world economy and of the unique features that represent local and historical variability (Knox and Agnew, 1989). The approach is one which attempts to explain economic geography by references to a combination or interaction of general processes, differing pre-existing structures and individual responses.

#### *Business Theory*

An interactive outlook is also evident in some recent business theory. Work such as that of Porter (1990), moves beyond management-centred or strategy-centred accounts, to embed firms within the wider milieu of clusters and national institutional arrangements. While the prospects of individual firms are influenced by these factors, the actions of firms also shape the environment to some degree.

#### *Technical Change and Innovation*

Yet another version of the interactive perspective can be found in the growing body of literature on technical change and innovation. It has been recognised in recent years that the current wave of technical and organisational change is essentially, and not just incidentally, *transnational* (Perez, 1983; NESC, 1989). This has prompted some economists to combine an analysis of the pressures within firms to extend beyond national frontiers with analysis of capitalist development at the international or global level (Chesnais, 1988).

#### *Comparative Political Economy*

Finally, an interactive outlook has become important in comparative political economy and the sociology of development (Evans and Stephens, 1988). Its development in this area also highlights the degree to which it can be more than a framework and can arise from the clash of substantive theories. The development of comparative political economy arose out of a rejection of both modernisation theory and dependency theory. The new approach rejected these deterministic theories and argued that the effects of involvement in the world capitalist economy are contingent on a range of national and international factors. Among the factors considered in this

historical comparative approach are the nature and capacity of the state, political mobilisation, the patterns of foreign direct investment and international economic ties, agrarian class relations, working class organisation, the welfare state, industrial policy and geopolitics. As Evans and Stephens say:

The thrust of current work is neither to decry the development costs of engagement in international commerce nor to extol the benefits of openness. The aim is rather to explicate the political and social structural factors that enable individual countries to transform ties to their benefit, while simultaneously analysing the way in which the changing structures at the international level facilitate or limit possibilities for transformation (Evans and Stephens, 1988, p. 757).

The approach is simultaneously structural, historical and analytical.

These subject areas and theories are outlined here not only to illustrate the interactive outlook but also because they are relevant to the assessment of the factors which will shape Ireland's development between now and 2010. Adoption of this interactive perspective confirms the validity of considering not only economic issues but also social, cultural, historical and political factors. While consideration of this wide range of factors precludes the possibility of exact quantification and prediction, and will therefore be anathema to some traditional economists, it is consistent with the modern post-positivist philosophy of the social sciences (Bernstein, 1983) which does, in fact, have considerable relevance for economics (O'Donnell, 1992). The interactive outlook also confirms the value of seeking to identify those shaping factors that require political initiatives – whether at national or Community level.

#### *Units of Analysis*

An important feature of the interactive perspective, and of many of the theories which work within it, is that it makes the unit of economic and social analysis a subject of thought. It is necessary to ask whether and in what sense we can talk of "Irish society", the "Irish economy", "Irish firms", the "regional problem" and the cohesion objective. These questions have a concrete relevance in the current project because they arise when we assess the effects of international economic developments on Ireland, the relevance of "globalisation", the business strategies of firms and the issue of cohesion. It can also be argued that they have deeper relevance in the resolution of certain key questions in Irish social science.



In regional economics and geography there has, in recent years, been a recognition of the importance of questions raised many years ago by the French economist Perroux. He objected to the treatment of economies as if they were "contained in a container", usually the national territory as defined by political frontiers.

In considering business strategies and the factors which will shape them we face questions concerning units of analysis. Should we assess the competitive advantages of Ireland by considering the business strategies of Irish firms only? Certainly, the dominant tradition is to link the economic prospects of a society and an economy directly to the prospects of national firms. For example, Porter's (1990) *Competitive Advantage of Nations* identifies the advantage of nations with the advantage of its national firms. His work has recently been criticised on the grounds that many firms no longer have a nationality in any meaningful sense and it is important to ask whether these arguments have relevance to Ireland (Reich, 1990; 1991; Thomsen, 1992; see also Graham and Krugman, 1989).

Consideration of business strategies raises another question concerning units of analysis. It is common to see "globalisation" considered as one of the factors which will shape business strategies and national economies. But the idea of globalisation is frequently the sister of the idea of the national firm and the national economy: globalisation arises when firms spill over national boundaries. Consequently, the concept of globalisation also needs to be examined critically (see Chapter 3(i) below and Kay, 1990).

Similar issues concerning the unit of economic and social analysis arise in international political economy. Wallerstein argues that:

. . . it is futile to analyse the processes of societal development of our multiple (national) "societies" as if they were autonomous, internally evolving structures, when they are and have been in fact primarily structures created by, and taking form in response to, world-scale processes (Wallerstein, 1991, p. 77).

It should be clear from what has been said above that units of analysis are problematic within other subject areas and on the basis of other theoretical approaches also. In accepting Wallerstein's scepticism about the concept of German or Irish society, it is not necessary to accept his argument that "it is this world-scale structure and the processes of its development that provide the true subject of our enquiry" (Wallerstein, 1991, p. 77).

Finally, the relevant unit of analysis is a problem in another important theme of this project – cohesion. Recent analytical approaches in geography, and to a lesser extent, regional economics, explore the relationship between regional and social inequality and question the

conventional definitions of regional problems, regional interests and regional policy objectives. Traditionally, the European Community has equated inter-regional equity with inter-regional income equality. But there are fundamental problems in defining and measuring inter-regional equity in this way and these have implications for Community policy.

Furthermore, the case of regions confirms a more general argument concerning units of analysis: that the choice of units of analysis, which might seem merely definitional, actually influences the theories which are then developed to explain the phenomena. The conventional approach to regional disparities in the EC reduces the cohesion question to a purely regional question. It is then a short, and frequently subconscious, step to the assumption that problems *in* peripheral regions are problems *of* peripheral regions, that problems *in* rural regions are essentially problems *of* rural regions. Similar connections between the choice of units of analysis and the choice of theoretical explanation arise in other subject areas.

## Chapter 2

### *INTERNATIONAL FACTORS*

Constant revolutionizing of production, uninterrupted disturbance of all social conditions, everlasting uncertainty and agitation distinguish the bourgeois epoch from all earlier ones.

....The need of a constantly expanding market for its product chases the bourgeoisie over the whole surface of the globe. It must nestle everywhere, settle everywhere, establish connexions everywhere.

The bourgeoisie has through its exploitation of the world market given a cosmopolitan character to production and consumption in every country...it has drawn from under the feet of industry the national ground on which it stood. All old-established national industries have been destroyed or are daily being destroyed. They are dislodged by new industries, whose introduction becomes a life and death question for all civilized nations... In place of the old local and national seclusion and self-sufficiency, we have intercourse in every direction, universal inter-dependence of nations.

Karl Marx and Frederick Engels, *The Communist Manifesto*, 1848.

The evolution of both the European Community and Ireland will be shaped by a range of international factors. These will include political, cultural and economic forces. These international factors are highly interdependent and they can be conceived as operating at four scales: within the European Community, within the wider Europe, between the rich countries of the world's North and the poor countries of the South and at global level. This chapter outlines some of these factors, distinguishing, in so far as this is possible, between the political, the economic and the cultural.

#### **(i) Socio-Economic Factors**

##### *Continuing Crisis and Change*

The evolution of European society between now and 2010 will be profoundly shaped by a set of interlinked economic factors. Although it is possible to identify some of these, it is very difficult to say how they will

evolve and impact on the Community and its member states. The important forces include technological change, the globalisation of manufacturing industry, profound changes in the structure of finance, changes in patterns of production and organisation and uncertainty about the principles of macroeconomic management. It is impossible to predict their impact, partly because these are an inter-related set of phenomena deriving from the breakdown of the relatively stable economic order which prevailed during the post-war "golden age". That order has not been replaced by a new "regime of accumulation" or "mode of regulation". We are living through a period of turbulence and, not surprisingly, it is difficult to get a firm footing or a vantage point from which to gain a perspective on where things are heading. Various interpretations of these changes have been offered in recent years. These include the move from national to global markets, the move from "organised" to "disorganised" capitalism and the idea that the advanced world is at a "new industrial divide" between "Fordist" mass-production and "flexible specialisation". Each of these interpretations contains elements of truth, but it seems too early to synthesise them.

It is also difficult to say which factors are causes and which are consequences. What is certain, however, is that the technological, organisational, financial, macroeconomic and political changes are inter-related. Recognition of this is important in any attempt to harness the forces of change for economic and social objectives or to ameliorate their negative effects. It becomes necessary to think in systemic terms and to recognise the limits of certain piecemeal or local interventions. At the same time, the interactive outlook strongly suggests that local factors matter, but perhaps in new ways which need to be identified.

#### *Technological Change*

Whatever the directions of causality there can be no doubt that technological change will continue to be a major shaping factor. Technological change has lowered the costs and risks of managing at a distance and has altered the scale needed for efficiency. For these reasons, one of the most fundamental features of the current wave of technological change and associated organisational restructuring is that it is *inherently international* (Perez, 1983). This international dimension probably arises in part from the provision of unprecedented data-management capabilities and telecommunications infrastructure, which allows the efficient management of transnational firms. In addition, the radical productivity increases made possible by computer-aided design and manufacturing, mean that for businesses to reach viable size the volume of output and the

range of products of a given plant must serve an international market. The same applies in the production of services, such as information and telecommunications. In short, national markets, particularly small national markets, would be a hindrance to the full deployment of the new technologies.

This technological change and internationalisation have altered the nature of competition and will continue to do so in the future. For each firm, each country and each region, the new rules of the game contain both threats and opportunities.

#### *Changes in Financial Structures*

These changes in technology and production required simultaneous changes in finance in order to be realised in corporate strategy and behaviour. Change in the international financial structure has been identified as creating one of the major economic imperatives which will shape life in the years to come (Stopford and Strange, 1991). The 1980s have seen phenomenal change in the international markets for capital. The independence of banks from national controls on credit creation increased dramatically as a result of technical and structural innovation. These created genuinely global financial markets, greatly increasing the mobility of capital. As a result, capital movements have largely replaced trade as the driving force of the world economy. This increased mobility has, in turn, created more volatility.

These fundamental changes in technology and finance are the background against which the major future concerns of the Community and its member states can be understood. First, they directly and indirectly explain why we can expect intensified international competition. The internationalisation of business, and the increased role of technology and innovation as sources of competitive advantage, directly increase international competition. But, as Fritz Scharf has argued, the changes in the international financial structure reinforce this by undermining the power of national macroeconomic management and forcing governments to seek prosperity through supply-side policies aimed at competitiveness.

This increased international competition will be a shaping factor not only for each member state, but also for the Community as a whole. Every national report in this project has identified intense international competition as a significant factor in the years to 2010. At Community level, there can be no assumption that the internal market programme will, on its own, be sufficient to re-establish the competitiveness of the EC against the US, Japan and other Asian countries. In reporting the views of the European business community, Jacquemin and Wright note "their

growing perception that Japanese and American competitors may be in a position to reap the benefits from the single market more quickly than the Europeans can" (Jacquemin and Wright, 1993, p. 58).

#### *Macroeconomic Volatility*

Macroeconomic volatility will, itself, be a separate and most important shaping factor for the European Community and its member countries. While structural changes may have made abandonment of the Bretton Woods system inevitable, it is now clear that, in a system of flexible exchange rates, rates will change for many reasons apart from differences in inflation, and real exchange rates will be unpredictable. Furthermore, not only does a system of flexible exchange rates and international capital mobility display greater economic instability, but it also robs national governments of the macroeconomic control to deal with the increased risks.

The conduct of monetary policy in a manner which controls inflation and yet avoids recession has become more difficult as a result of enormous international capital flows, financial innovation and deregulation. But these changes also influence the conduct of fiscal policy, since budgetary policy is liable to affect interest rates and, through them, exchange rates. In this context, macroeconomic fluctuations are likely to be a major shaping factor for the European Community. Given the small size and extremely open nature of the Irish economy, this is a particularly important factor in the Irish case.

Quite apart from continued macroeconomic volatility, the changes in the international economy listed above have probably increased the risk of a major financial crash with severe effects on the real economy. While this cannot be discussed as a systematic shaping factor, the possibility of such a crisis, and other unforeseen events, should be noted in any exercise of strategic thinking.

Of course, identification of continued, or increased, macroeconomic volatility and the risk of severe crisis, as factors shaping the future of Europe and its member states, highlights the need for action by the Community. Minimisation of macroeconomic volatility requires advances in macroeconomic management, while reduction of the risk of financial instability requires financial regulation. In both cases it is likely that action will be necessary at both EC and global level (see Chapter 4).

#### *International Economic Development: Patterns of Production and Location*

While it is widely agreed that Ireland's prosperity is dependent on sustained international economic growth it has not, until relatively recently, been recognised that Ireland's evolution is also shaped by the

*pattern* of international economic development (O'Malley, 1989; NESC, 1989). Indeed, this has been the case for well over a century: Ireland's current economic and social structure was, to a large extent, determined by the place which it assumed in the international division of labour in the eighteenth and nineteenth centuries, i.e., Ireland's specialisation as a producer of grass-based agricultural commodities for the British domestic and imperial markets (O'Malley, 1989). Likewise, Ireland's evolution in the years to 2010 will be very significantly influenced by the changing international patterns of production and location.

The global patterns of production and location will, of course, be influenced by a complex set of factors including:

- the rise and decline of particular industries and firms
- the pattern of industrial and corporate organisation
- technical change
- transport, telecommunications and social infrastructure
- energy and environmental developments
- GATT.

It should be emphasised that Ireland's fate will not be inevitably shaped by the global forces in a deterministic way. The essence of the interactive perspective which informs our approach is that these forces are mediated by local economic and social structures and policies.

In this context an important question is the role of transport and telecommunications, and technical and organisational change, in shaping the location of economic activity. For a number of reasons this is a subject which must be considered when assessing the factors which will shape Ireland's evolution. First, it has figured in a number of important Commission documents, including a paper by President Delors published with the Delors Report on economic and monetary union (Delors, 1989), and in *One Market, One Money* (CEC, 1990). The central thrust of those discussions was that changes in technology and demand make geographic concentration less likely, because transport costs are becoming, on average, less important in the location of industrial production. Second, the implications of technical, organisational and infrastructural development on the location of activity do not figure prominently in the reports on other member countries. Third, the issue is closely related to, and can throw some light on, certain other concepts which do figure in various national reports. The most significant of these are the concept of *globalisation*, and its relation to *development*, and the relationship between economic development, on the one hand, and socio-cultural development,

on the other. Fourth, this overall set of issues are ones which may require Community policies.

Some of the general claims concerning the effect of new technology and infrastructure on the scale of firms and patterns of location were examined in the NESC report *Ireland in the European Community* (1989). There it was argued that the effect of technical and organisational change on scale economies was much more complex than allowed for by those who believe that scale economies are becoming uniformly more rare and distance is becoming uniformly less significant (NESC, 1989, pp. 245-247). A number of arguments were outlined which suggest that current technical and organisational change may reinforce the tendency to spatial concentration (NESC, 1989, pp. 324-326 and see O'Donnell, 1991a). The conclusion of that analysis was that "overall then, it seems too simplistic to infer that radical technical, telecommunications and transport improvements, because they technically reduce the significance of distance, also reduce its overall economic significance, or cause a wider dispersal of activity and a convergence of regional economies" (NESC, 1989, p. 325).

Very similar conclusions have since been reached by regional theorists and students of technical change. Storper and Walker note that:

It was common in the 1970s to hear predictions that improved telecommunications would lead to a decentralization of information-based industries. Yet for the most part this has not happened. The reason can be found in the countervailing force exerted by dynamic external economies in the organization of production in these industries. Moreover, the general ease of modern communication actually facilitates the growth of the function basic to central city agglomeration, by making possible even larger multinational corporations, bigger banking networks, more international securities transactions. The same technologies also stimulate the invention of any number of new producer services, such as computerized securities trading, and these specialized activities are themselves often carried out through an elaborate social division of labour. Thus, there is no end to the interaction of scale and specialization in the industrial economy, and there is no reason, in principle, to expect an end to agglomerative forces, even with continued improvement in transport and communications technologies. (Storper and Walker, 1989, pp. 196-7).

In his analysis of the relationship between new information technologies and urban and regional development, Castells says:



As in previous historical instances of major technological transformation, prophecies tend to take the place of analysis in efforts to comprehend the emerging social and spatial forms and processes. Futurologists predict the evolution of society on the basis of linear extrapolation of characteristics of new technologies ... We are told, for example, that telecommunications allows work at home in "electronic cottages", while firms become entirely footloose in their location, freed in their operations by the flexibility of information systems and by the density and speed of the transportation network.

In fact, none of these prophecies stands up to the most elementary confrontation with actual observation of social trends. Telecommunications is reinforcing the commanding role of major business concentrations around the world (Castells, 1989, p. 1).

In this he relies precisely on the argument that the effect of new technologies "vary according to their interaction with the economic, social, political and cultural processes". Finally, in his recent study, *Technological Innovation and Multinational Corporations*, Cantwell concludes that the:

....intensification of international competition is argued to enhance a pattern of cumulative causation in which centres of innovation enjoy a virtuous circle, while certain other locations are as part of the same process locked into a vicious circle of declining growth and diminishing local research...

Where it exists, this tendency towards virtuous circles in some locations at the expense of vicious circles in others can be explained in part by the requirements of technological accumulation in the MNCs of a global industry. The technology accumulated by firms producing in each location is to some extent specific to that location (Cantwell, 1989, p. 161 and p. 139).

Cantwell's analysis, based on the interaction of ownership and location advantages, suggests not only that *use* of new technologies is spatially uneven, but that their *generation* through the process of innovation is uneven also (see also CEC 1991).

These analyses can throw some light on certain issues which figure strongly in various studies of the factors shaping development in the years to 2010. In particular, they suggest that the concept of "globalisation" be used with care. A number of considerations suggest that it is incorrect to conceive of a one-way process of development from isolated and traditional economies to internationally engaged economies and, eventually,

globalisation. Likewise, it may be incorrect to use as a conceptual framework the idea of a one-way path from "traditional", local, clan-based, religious, societies to homogenised, international, society. This question of modernisation is examined in great detail in an important overview of social and economic research in Ireland, *The Development of Industrial Society in Ireland* (Goldthorpe and Whelan, 1992). The concepts of globalisation and modernisation have relevance to the perceived anomalies or paradoxes highlighted in the reports of the national institutes to the Forward Studies Unit. These concerned the coexistence of prosperous, homogenised, internationalised, social groups, with continuing poverty and deepening social duality (see Jacquemin and Wright, 1993, pp.31-32).

#### *Liberalisation of Agriculture*

An important global factor is the trend towards liberalisation of agricultural markets. A number of forces have combined to create pressure for extension of the GATT framework to agricultural products. The desire to secure a new GATT round – and the linking of liberalisation of trade in services to liberalisation of agriculture – suggest that there will be long-term pressure for further reform of the Common Agricultural Policy (CAP). While the Community would seem to remain committed to the main objectives of the CAP, a number of developments inside the Community have also undermined support for the traditional policy instruments used in pursuit of these objectives. Food security no longer requires heavy price supports. While price supports have gone some way to supporting agricultural incomes, they are now perceived as inequitable and do not necessarily preserve rural society. The increase in ecological awareness has also prompted scepticism of traditional policy. Finally, concern to facilitate reconstruction in Central and Eastern Europe has raised questions about the feasibility of some CAP instruments. The liberalisation of agriculture is discussed in more detail when we consider national factors, in Chapter 3.

#### *EC Enlargement*

The probable enlargement of the Community is a factor which will have economic as well as political consequences for both the Community as a whole and for Ireland. Analysis of this factor is at a relatively early stage in Ireland (see Brown, 1991).

#### *Capitalism in Central Europe*

The reintroduction of capitalist economic and social relations in central Europe is a development which will undoubtedly have economic consequences for the Community and Ireland. While little Irish research

has been undertaken on this subject to date, the increasing familiarity with the economics of international integration suggests that the skills to analyse this issue may be available.

## (ii) Cultural and Historical Factors

### *Inward Migration*

Changes in the Mediterranean confront member states, and ultimately, the Community, with great problems. The Southern member states face the prospect of substantial immigration from North Africa and the Middle East. This is already related to one of the most serious internal problems in Community countries – the revival of racism and ultra-right ideology. This revival, emphatically demonstrated in election results in France, Italy and Belgium and racial violence in many countries, dictates that the question of immigration will be dealt with one way or another. Furthermore, although it is *national* chauvinism which is on the rise, the question of immigration is inherently a Community issue – given the removal of frontier controls in the 1992 programme.

### *European Identity*

The economic and political uncertainties and threats listed above have a bearing on the cultural dimension of European integration. Is any discernible European identity emerging? Most of those who write on this question answer “no”, and stress the continuing prevalence of national identity. While it is, in some ways, hard to argue with this, it may not be a sufficient answer. Where a European identity is asserted – and it is clear that the European Commission and others wish to promote this – it tends to be defined in terms of democracy, liberalism and tolerance. This definition is patently insufficient. Many Americans would define American identity in the same terms. The aggressive history of Western European Christendom, in which the emergence of an identity developed in parallel with a hatred of Jews and Muslims, suggests that Europe is not essentially tolerant and tolerance cannot be seen as essentially European (Armstrong, 1988). It might be tempting to say that the question of European identity is irrelevant (except to those who are vainly bent on building a European nation-state). But this may not be correct. The question has concrete relevance for three reasons. First, it must be a consideration in devising practical approaches to immigration, enlargement and security. Second, despite the apparent persistence of national identity, economic and technological developments are now essentially international and are, in complex and uneven ways no doubt, creating an international economy and, perhaps, something of an

international society. Third, in addressing a range of concrete problems, and in acquiring the consent of the people that this be done at Community level, it will be necessary to draw on, and articulate, *values*, rather than rely solely on intergovernmental bargaining in secret.

If democracy and liberalism are not the basis of European identity, then what is? The report by the French team to the "shaping factors" project argues persuasively that the social market economy, and the existence of a powerful welfare state, is the real distinguishing feature of the European model. If this is so, then it raises serious questions about the chance of developing a European identity upon which economic, monetary and political union can be built. Two sets of challenges for the Community can be identified. Although all EC countries are mixed economies, differences between national systems of social rights and market regulation remain. The process of market integration disturbs these national patterns of allocational and distributional regulation and can thereby force changes in their "economic order" – towards either deregulation or reregulation at EC level (Pelkmans, 1982). So far, the Community has proven unable to deal with the implications of integration for the welfare state. Consequently, it is not developing a European identity around, what looks to be, the truly distinctive feature of its social, economic and political system.

A second set of challenges arise because, quite apart from differences in systems of social rights, there are threats to welfare states. One definite threat is political. As Jacquemin and Wright say in their synthesis:

....the global embracing of "neo-liberalism" appears to have weakened solidarity among the poor and the rich, among the unemployed and the overemployed, the dynamic regions at the expense of the depressed and the new sectors of the economy with only a blind eye turned towards Europe's depressed and declining industries and regions (Jacquemin and Wright, 1993, p.109)

But it should be recognised that, as well as this ideological or political force, there are economic and demographic factors which also threaten the European social market model. The collapse of the golden age of demand managed growth has dramatically increased the burden which unemployment puts on welfare systems. In many countries this has been exacerbated by ageing of the population. The slowing of growth, and the globalisation of finance and industry, have increased international competition and forced redistribution in favour of capital. As a result, the European social model is "now buffeted from all sides" (Jacquemin and Wright, 1993, p.111). This perspective suggests that, taking a long-term

strategic view, one of the major challenges for the European Community is to redesign the systems of social rights and welfare in ways which facilitate increased competitiveness and sustained growth of the European economy. But this is a long-term project which has some fairly immediate implications. As pointed out by the Italian and Spanish researchers, the people of Europe are unlikely to continue to give their consent to European integration if the project undermines national systems, but is itself focused on the "cold" agenda of the market. Although the accession of the EFTA countries will probably broaden and deepen the Community's consideration of the European social market model, effective action will require a dramatic improvement in the Community's decision making capacity and legitimacy (see Chapter 4).

### (iii) The Political Dimension

#### *Collapse of Communism*

The collapse of the Warsaw Pact will fundamentally alter the Community's external political environment. This will shape the political development of both the Community and some of its member states. The pressures are likely to arise in two areas. First, the collapse of the Soviet Union has altered the security of Western Europe and this may prompt a review of global security arrangements, including the role of NATO. Second, the demise of Soviet hegemony over Central Europe has unleashed national, ethnic and religious forces. These are likely to find themselves in conflict with one another – as in Yugoslavia – and this will inevitably raise political and security questions within the Community.

#### *EC Enlargement*

The enlargement of the Community will have political as well as economic consequences. Perhaps the most significant of these will concern the Community common foreign and security policy. The next enlargement is likely to bring a number of neutral states into the EC. At the very least this is likely to alter the character of the debate on a common defence policy. However, it would be rash to predict that this will mean a definite weakening of commitment to a common defence. The very meaning of alignment and neutrality are changing and a lot will depend on the concrete security situation which prevails around the time of the 1996 Inter Governmental Conference.

The question of enlargement will raise other profound political and institutional questions. The political issues concern the role of the European Union in the wider world. The institutional one's arise because

of the difficulty, probable impossibility, of deep union of 16 countries with the existing, heavily intergovernmental, decision-making system (see Chapter 4 below).

#### *German Unification*

The unification of Germany has already had profound effects on Germany and, given its hegemonic position, on the Community. Furthermore, it is probably a mistake to think that these problems and changes are short term ones resulting from the political opportunism displayed by the German government during and since unification. The development of the Eastern Lander is likely to take many years; they will not replicate the (protracted) German post-war miracle in four or five years. As a result, the whole German economy will probably function less well for the foreseeable future. The resulting continued westward migration (from both the Eastern Lander and other Central European countries) is likely to profoundly change German politics and society. An important result to emerge from this comparative project is that we should expect to see Germany as a country with problems and without its earlier ability to find solutions to them (see Chapter 9 of Jacquemin and Wright; 1993).

#### *North-South Relations*

The dramatic reversal of Third World development in the 1980s has undermined the notion of inevitable modernisation and means that disparities between the rich North and poor South will continue to present economic and political problems for many years to come.

## Chapter 3

### *FACTORS WHICH ARE SPECIFIC TO IRELAND*

From inside information extending over a series of years Mr Bloom was rather inclined to poohpooh the suggestion as egregious balderdash for, pending that consummation devoutly to be or not to be wished for, he was fully cognisant of the fact that their neighbours across the channel, unless they were much bigger fools than he took them for, rather concealed their strength than the opposite. It was quite on a par with the quixotic idea in certain quarters that in a hundred million years the coal seam of the sister island would be played out and if, as time went on, that turned out to be how the cat jumped all he could personally say on the matter was that as a host of contingencies, equally relevant to the issue, might occur ere then it was highly advisable in the interim to try to make the most of both countries, even though poles apart.

James Joyce, *Ulysses*.

There are few factors which are of relevance *only* in Ireland. This chapter defines a range of factors which are of particular relevance to Ireland. Mention is made of factors which may be relevant generally, but which are likely to take a *specific form* in Ireland. Among the economic and social factors discussed are the structure of the Irish economy (and its particular response to international developments), demographic patterns, the evolving social class structure and the burden of high long-term unemployment, public finance pressures, emigration, developments in agriculture and environmental issues. A range of inter-related cultural and historical factors which may shape Ireland's evolution can be identified, but it remains difficult to identify their causal significance. Three political factors are noted: Ireland's political culture and capacity for strategic policy-making, the question of local democracy and administration and the problems of Northern Ireland. The chapter continues with a discussion of the balance between national and international/EC factors. It is argued that the balance between these two will be different in each country,

reflecting their varied economic and political significance. In Ireland's case, interdependence tends towards the dependent end of the spectrum and this accentuates the significance of global economic factors and diminishes the significance of global political factors.

Finally, a distinction is made between those factors upon which there is agreement in Ireland and those which are the subject of controversy. Although there is agreement that certain dominant social and economic factors – such as the Irish economic structure, unemployment and international developments – will all be important, there is not agreement on *how* they will bear on future development. There is controversy on the relevance of a number of the cultural and political factors identified in this chapter and, in particular, on the interaction between these and economic development. Given the significance of this for the explanation of Ireland's long-run economic failure, and for approaches to improving the future performance, this chapter closes with an outline of the lively debate on Ireland's development. A range of historical, cultural, structural and political explanations have recently been synthesised in an important study commissioned by NESF. The argument of that study, by the Norwegian social scientist Lars Mjøset, is briefly explained and some of its possible implications for further research and for policy are noted.

### (i) Socio-Economic Factors

#### *Structure of the Irish Economy*

The evolution of economic activity in Ireland between now and 2010 will be shaped to a very large extent by the current structure of the Irish economy. This structure is one which is more than averagely externally oriented. Exports account for 56 per cent of GDP, while the average in the EC-12 is 22 per cent. While the external orientation of the economy clearly means that the overall pace of economic activity in Ireland will be strongly influenced by the international economic factors discussed in Chapter 2, this is not the aspect of economic structure which is under discussion here. What is of interest here is the *way in which* Ireland's economic structure will shape its response to international factors and the limits which its current economic structure places on its future ability to meet the employment, income and social needs of its population.

The relevant aspects of structure are the relative size of the agricultural, industrial and service sectors and the internal characteristics of the agricultural and industrial sectors. Agriculture accounts for a much higher proportion of employment and value added in Ireland than in the EC as a



whole (see the table of the basic statistics).<sup>1</sup> The share of industrial employment is lower than the Community average, but the share of industrial value added is a little higher. The first implication of these structural characteristics is that Ireland's economic and social development will be more than averagely shaped by developments in agriculture (see below).

The more significant aspects of Ireland's economic structure are those *within* the agricultural and industrial sectors. The former is discussed in more detail below. The manufacturing sector exhibits a significant element of dualism – between foreign-owned segments in, mostly, high-growth industries producing for international markets and indigenous firms in slower-growth segments. The indigenous manufacturing sector experiences considerable difficulty in achieving a firm foothold in international markets. The dualism is to be found in these differences in market orientation and market power, technology, management structure and plant and firm scale. Most important of all, the term dualism refers to the weak linkages between the foreign-owned branch plants and the Irish economy (Kennedy, 1991). It should be noted that there are two sides to dualism and part of the reason for Ireland's heavy reliance on an enclave of branch-plants is the remarkably poor performance of indigenous manufacturing over a long period.

It is this structure which will make the emerging international pattern of production and location (discussed in Chapter 2) such an important factor shaping Ireland's economic future. However, this structure does point to one of the major policy issues facing Ireland in the years to come: the task of developing competitive indigenous industries (see Chapter 5).

#### *Demographic Developments*

Three demographic trends will be of particular significance between now and 2010.

- inflows into the labour market, arising from natural increase, which exceed current and past rates of job creation. This pattern will continue until the early years of the next century
- a gradual ageing of the population relative to the age structure found in recent years. However, this ageing will remain less advanced than in other EC countries
- emigration will remain a significant factor in Ireland's development.

<sup>1</sup> Much more detailed accounts of Ireland's current and past position in the EC can be found in NESG (1989) and Kennedy (1992a; 1992b).

**IRELAND: BASIC STATISTICS**  
(with comparable EC 12 figures)

	<i>IRELAND</i>	<i>EC 12</i>
Population, 1991, m.	3.5	328.7
Population density, per sq. km.	51	145
Relative GDP per head of population, 1991, PPS	69	100
Relative GDP per worker, 1991	89	100
Unemployment rate 1991, %	16.8	8.6
% Employment by Sector, 1989		
Agriculture	15	7
Industry	28	32
Services	57	61
% Gross Value Added by Sector, 1988		
Agriculture	10	3
Industry	37	35
Services	53	62
Exports of goods as % GDP, 1991	56	22
Exports of goods - Intra-EC	43	14
Exports of goods - Extra-EC	13	8
% Population 14-24 in Education, 1989	50	43

*Social Class Structure and Unemployment*

A very important factor shaping Ireland's evolution is the social structure which has emerged in the period since 1960. While high rates of emigration have been endemic in Ireland since the early nineteenth century, the social structure within which emigration occurs has altered significantly (Breen, *et al.*, 1990; Sexton, *et al.*, 1991). After 1960 the occupational structure shifted dramatically - with a decline in the number of agricultural and unskilled opportunities and a sharp increase in the opportunities available to the middle class and skilled manual groups (Breen *et al.*, 1990). While these developments shifted the emphasis from family inheritance to education as a key determinant of occupational

position, it had some negative consequences which are of the utmost importance for development of the Irish economy and society. Chief among these is the emergence of a significant set of residual classes "stranded in the course of industrial development, especially farmers on marginal holdings and labourers without skills" (Breen, *et al.*, 1990, p. 59). It is these groups which account for much of the unemployed and especially, the long-term unemployed. It has been shown that "today's class structure contains a substantial number of positions that are viable only in so far as they are underwritten by State social welfare programmes and from which, especially given present economic circumstances, there appears to be no exit" (*ibid.*).

Long-term intergenerational consequences are likely to result from the interaction between the structure of, and high level of, unemployment. The fact that nearly half the unemployed are long-term unemployed, and that unemployment is predominantly concentrated among the less educated and less skilled, gives rise to the danger of fostering a deprived underclass which will transmit these handicaps to the next generation. Moreover, in these conditions, the persons involved become so detached from labour market processes that they exert no influence on collective bargaining, so that the fact of their remaining unemployed imposes no moderation on the level or structure of wage claims.

While casual observation, and even analysis, suggest that long-term unemployment has limited economic, political and social consequences for the system, as a system, it is not possible to ignore explosive potential of so serious a social problem on this scale. History, in both Ireland and other in western countries, suggests that serious social problems may be tolerated for long periods, but that the explosion when it happens is sudden, traumatic and unpredictable.

Overall there can be little doubt that the high level of total unemployment, and of long term unemployment, and the attendant poverty, constitute a major shaping factor for Ireland. The way in which this will bear on economic and social development is a central problem for social scientific analysis.

#### *Public Finance*

Ireland enters the 1990s with a high level of outstanding national debt and a taxation system which is widely agreed to be suboptimal. While this situation can, in large measure, be attributed to poor macroeconomic and public finance management in the late 1970s and early 1980s, it has been argued by the tripartite National Economic and Social Council (NESC) that the fiscal crisis has some longer-run determinants. NESC has pointed

out that the other side of the coin of structural problems in the economy, is low income per capita and high dependency rates, which tend to require higher baseline levels of social expenditure also. This line of argument leads to the recognition that "there is a public finance dimension to the developmental problems of the economy" (NESC, 1989, p. 200).

The ratio of employment to population in Ireland at 31 per cent, is among the lowest in the EC. The cost of supporting this high level of dependency is one of the fundamental reasons why public expenditure and taxes are relatively high in Ireland for a country at its level of development. The low employment ratio also largely accounts, at least in an arithmetic sense, for the divergence in living standards between Ireland and the EC. In 1991, GDP per person employed in Ireland was little more than 10 per cent below the EC average but, because of the small proportion of the population in employment, GDP *per capita* was only 69 per cent of the EC average (see table). Although the employment/population ratio is influenced by demographic factors and participation rates, the major underlying explanation is the poor labour market conditions, as manifest particularly in the high unemployment rate, which is now the highest in the EC.

While a number of member states have public finance problems similar to Ireland's, there is a definite sense in which these are specific to each country. This arises, first and foremost, because taxation, expenditure and debt remain, for the time being, formally under the control of national politics. Both expenditure and taxation reflect social, economic and political structures and traditions (O'Connell and Rottman, 1992). In Ireland's case the slow progress of tax reform raises questions about the effectiveness of both the political and administrative systems (see below).

#### *Unemployment and Public Policy*

Sustained high unemployment will continue to profoundly shape the economic and social environment in which policy is formulated and business is conducted. It places severe constraints on the scope for reducing taxes or government expenditure. The continued pressure on government and state agencies for "job creation" can increase the difficulty of identifying and implementing policies which might secure employment and prosperity in the long run (e.g., development of indigenous manufacturing industry). This factor is intensified by the volatility of the Irish labour market, and its sensitivity to conditions abroad, especially in the UK, due to the long-standing ease of outward and return migration. Thus any given policy mix can be put under severe short-term strain by a worsening labour market in the UK, resulting in a sudden change in migration behaviour.

### *Migration*

Ireland's migration history is virtually unique in Europe (let alone among the EC-12) and this will undoubtedly remain a most important shaping factor. While some understanding of the social consequences of emigration has been achieved (Sexton, *et al.*, 1990), the economic effects have not been adequately explored. These are unlikely to be uncovered by the kind of macroeconomic comparisons undertaken in a recent study for NESC (Sexton, *et al.*, 1990). Mjøset's recent comparative study of Ireland's long-run development, also commissioned by NESC, strongly confirms the intuition of those social scientists who considered Ireland's emigration and population decline as not only symptoms, but also causes, of the country's poor economic performance. He sees emigration and population decline as one of the key forces in the Ireland's "basic vicious circle": Following the Great Famine:

....population decline emerged as a most persistent factor in Irish development, first through starvation and emigration, later through emigration only. This study confirms that this demographic pattern constitutes the most distinctive feature of Ireland's development. It is not only unique compared to our five contrast cases, there is simply no similar demographic experience anywhere in the modern world, so far (Mjøset, 1992, p.7).

The role of emigration as a factor shaping Ireland's future economic and social development is less easy to identify. One certain role is that it weakens the effect of various forces. It weakens the dynamic impact of a large young population on social and economic life. It quite radically breaks the connection between high levels of public investment in higher education and the stock of skilled labour in the Irish economy. To the extent that skills play a role in key mechanisms of economic development (a view of Adam Smith's which economists have recently reinvented) then Irish emigration weakens these mechanisms. In addition, it tends to weaken the Phillips curve effect, linking wage increases to unemployment. Overall, the long-standing international mobility of labour (when combined with recently increased mobility of capital) serves to undermine the meaning of the concepts "Irish economy" and "Irish society".

### *International Growth*

The development of the HERMES macroeconomic model has, in recent years, brought to light some of the complexities in the relationship between international growth and Irish economic performance. These

arise because of the significance and sensitivity of migration and foreign direct investment. (Barry, and Bradley 1991; Bradley and Fitz Gerald, 1991).

#### *International Patterns of Production and Location*

All Community countries will be enormously shaped by the evolving international patterns of production and location. Yet, as discussed in Chapter 2, it is most important not to confuse internationalisation, or even globalisation, with the emergence of uniformity or spatially even economic development. One of the most interesting aspects of recent geographical and regional studies is the analysis of the interaction between the global nature of enterprises and markets and the local/unique nature of each of the places where production and consumption take place. Thus, internationalisation seems to develop side by side with differentiation; the very international nature of the overall production system increases the economic significance of the differences between places. While some elements of economic and social life become homogenised, others become differentiated. It follows that these international patterns will have specific consequences in various Community regions, including Ireland.

#### *Developments in Agriculture*

Agriculture and food processing form an important part of the Irish economy. Consequently, there can be no doubt that Ireland's evolution in the post-1992 period will be shaped to a considerable degree by developments in agriculture. While it is common to analyse this by reference to reform of the CAP and possible changes in international food markets, this would be a partial approach. Nowhere is the interactive outlook which informs our approach more relevant than in the area of agriculture. Irish social scientists have, in recent years, begun to explore the relationship between the dominant, exporting, agricultural sector and the indigenous economic and social structures and policies (see Breen, *et al.*, 1990; Kennedy, *et al.*, 1988; NESc, 1989; Hannan and Commins, 1992). While these relationships are by no means adequately understood, sufficient progress has been made to allow the current CAP reform to be analysed in the correct context. Some of the relevant considerations are the following (NESc, 1992). First, while Ireland's national income is dependent to a considerable degree on the value of agricultural exports, the problem of rural development which Ireland faces is only partially an agricultural one. Second, the current phase of CAP reform constitutes a continuation of a reform process which has been in operation since 1977. Third, Ireland's long-run competitiveness in international food production

requires the removal of structural impediments. This depends more on domestic policy than Community policy. Fourth, the continuing problems of low and volatile incomes among a sizeable segment of Irish farmers, are due to structural characteristics which could only have been addressed by national policy (though a strong case can be made for some Community financial support). Fifth, while the CAP has provided considerable net transfers to Ireland, it hindered rather than helped the development of a strong food processing industry. Indeed, those features of the CAP which inhibit the development of a food industry producing high value-added, will not be fundamentally altered in the current reform. Sixth, the Irish food industry continues to face the challenge of diversification and development of high-value added products; this is akin to the problems which all indigenous industries face, rather than one to which the current CAP reform have particular relevance.

These observations have important implications for how the likely effects of CAP reform should be measured. They suggest that analysis should focus not only on changes in agricultural output and incomes, but also on the economy-wide effects, including the implications for the food processing industries. Furthermore, just as the effects of past CAP instruments can only be measured by reference to some alternative regime (see Matthews, 1988), so the likely effects of the current CAP reforms must ultimately be identified by comparison to some realistic alternative policy scenario.

A static analysis of the impact of CAP reform can be derived by assuming that everything stays constant except the policy instruments being changed in the current reform. The main immediate effect would be to reduce farm output – which is not surprising, since a key objective of the reform is to reduce agricultural production by means of a combination of price reductions and direct supply controls. The effect on real farm incomes will depend on the balance between output and price reductions, on the one hand, and direct compensation and reductions in input prices, on the other. Estimates vary from a small real income decrease to a fairly substantial fall (NESC, 1992).

It is of considerable significance that the effects of the reform will not be uniform throughout Irish agriculture. The negative effects will be greater in the beef sector than the dairy sector. Estimates of the static effects suggest that 44 per cent of farms would gain while 56 per cent would lose. However, most farms will be only marginally affected by the reforms. The direct compensation payments will tend to go to the smaller, more extensive, farms and the main losers will be larger, more intensive and efficient farmers (Leavy and Heavy, 1992).

A more dynamic analysis of the implications of CAP reform would take account of responses within the farm sector and the food processing industry. Since there has been very significant changes in the CAP in the past fifteen years, this experience provides a guide to the likely pattern of response in the coming years. Farmers' responses, including reduced fertiliser usage, will tend to reduce the impact of the reforms on both output and incomes. If the reform succeeds in reducing the supply/demand imbalance in the EC, then market prices will strengthen. Other possible responses include pursuit of off-farm employment, migration and, where these are not possible, reliance on social transfer payments. Analysis suggests that, given that similar income losses have been experienced in the past, the present reform may be "expected to underpin the continued, gradual, attrition of the farm labour force" (ibid).

Changes in agricultural policy are also likely to induce responses in the food processing industry. This industry accounts for almost 30 per cent of employment in Irish-owned manufacturing, and over 20 per cent of total manufacturing employment. For a variety of reasons the industry is primarily involved in the production of commodity products and relies on high-volume throughput and sales into intervention. The reduction in agricultural output will reinforce current pressures for cost cutting – suggesting the likelihood of further rationalisation and job losses. While an alternative response to supply constraints would be to move into higher value-added products, there are a number of factors which may prevent this. Irish food processing firms have a number of structural problems and face barriers to entry which are common throughout indigenous industry. However, it is now understood that the CAP reinforced these difficulties by providing non-commercial outlets (i.e., intervention) and by accentuating the already strong seasonality of raw materials supply in both the beef and dairy sectors. What is most significant is that the CAP reform will not fundamentally alter these characteristics of the system and may, indeed, reinforce seasonality.

The reform of the CAP will also have economy-wide macroeconomic effects. These have been estimated using the ESRI's HERMES macroeconomic model of the Irish economy. That analysis suggested that the loss in farm income (after compensation) would be roughly equal to the gain in consumer income. Given the fairly modest fall in agricultural output, the major macroeconomic effect may result from the effect of the reform on prices. The reduction in agricultural and food prices will reduce the overall price level in all member states. Indeed, the final real macroeconomic effects may depend on the relative size of these price reductions and the consequent gains and losses of competitiveness. If the



price fall was uniform throughout the Community, and if all prices were fairly flexible, then the long-run impact of the McSharry reform on the Irish economy may be to reduce long-run real GNP by perhaps 0.3 per cent to 0.5 per cent below what would otherwise prevail. If, on the other hand, European interest rates did not fall in line with prices, then Ireland's loss of GNP would be somewhat greater (Fitz Gerald and O'Connor, 1991)<sup>2</sup>.

Recent economic analysis suggests that the larger immediate fall in farm incomes may be less serious than the long-run implications. In particular, the mix of supply controls and price reductions might prevent Ireland from exploiting its competitive advantage in dairy and cereals. This is so largely because the supply control element of the reform package arises precisely in those sectors – dairy and cereals – in which Ireland could exploit comparative advantage.

#### *Environmental Developments*

While environmental developments and policy responses will have some influence on the development of all EC member countries, this factor may not be of particular importance to Ireland. This reflects Ireland's geographic position, low population density, lack of heavy industry, low average income (by EC standards) and relatively clean environment. This raises questions about the use of the new Cohesion Fund – which has been designated for transport and environmental programmes.

In assessing the relevance of the environmental factor it seems advisable to break the idea of "the environment" into its separate parts. The various types of air pollution, water pollution, pollution of food, congestion and decay of the natural and built environment, operate at different spatial scales and impact on various interest groups in different ways. While there is, among some Community citizens, an ideology which lumps these together to form a "green consciousness", it seems unlikely that this can adequately reflect the complexity of the issue or resolve the conflicts of interest which arise.

Probably the most important environmental issues for Ireland are those of water pollution, urban and rural planning and meat production. The problems in these areas go to the heart of the Irish political system. Only in recent years has the argument been made that low standards in these areas is actually harming Ireland's economic interest, by damaging

<sup>2</sup> These estimates of the likely effect of the reforms were based on the package as formulated in July 1991.

water resources used for tourism, limiting the kind of economic regeneration achieved in many cities in other countries and undermining the image of Irish food exports. While this is accurate it, in turn, reflects a dependent mentality that may be part of Ireland's economic problem. While it is important now to do whatever is necessary to protect Ireland's advantage in these areas, the literature on international competitive advantage suggests that, in general, the process works the other way round. That is, countries tend to develop an international competitive advantage in activities which they perform to a high standard *for themselves*. This is yet another example of the interaction between indigenous and global forces in the shaping of any country's role in the international division of labour.

### (ii) Cultural and Historical Factors

The cultural and historical factors which may shape Ireland's developments in the years to 2010 are, in many ways, the two sides of the one coin. The chief historical factor is the economic and social structures, created in the disastrous nineteenth century, and the political reaction to this of the Irish people – the push for, and achievement of, owner occupancy and political independence. In the course of these economic and political developments there emerged a particular cultural pattern which probably still has relevance to Ireland's future economic and social development.

Accounts of the modern Irish culture tend to note the following characteristics. The people seem unambiguously to share a common national, or ethnic, identity. Unlike other European nations this is not defined by a national language. Catholicism comes much nearer to being a defining national characteristic than either language or residence in Ireland. The family remains the centre of social organisation to a degree, and in ways, which differ from other Northern European societies. But it does not seem to play the role in economic organisation and social protection which is found in parts of the Mediterranean which share Catholicism and a family-centered social life. In addition, there is evidence, in Ireland, of a rapid convergence towards Northern European patterns of family formation, family size and sexual mores.

Irish culture contains a strong attachment to land ownership and occupancy. Indeed, it has been argued, more generally, that twentieth century Ireland has a "possessor ethic", rather than a "performer ethic", and Lee sees this as permeating Irish institutions, intellect, character and identity (Lee, 1989). Mass emigration has been a most important factor in Irish society for two centuries and this undoubtedly has cultural

dimensions. While it certainly makes the Irish one of the most internationalised peoples in the world (in the sense of residing in numerous places and having economic, political and cultural strategies of survival in numerous environments) it did not prevent considerable cultural closure in the period from independence to the 1960s. Since then, Ireland has become highly open to international cultural influences and an important, if not easily identified, feature of present and future cultural patterns is the way these are mediated and used by Irish society (O'Toole, 1990).

Sport and sporting organisations are important elements of the culture. Over 500,000 people (or 1 in 7 of the total population) were on the streets of Dublin to greet Ireland's football team after their quarter final defeat by Italy in the 1990 World Cup. A week later 50,000 greeted the victorious German side on their arrival in Stuttgart. Of course, this element of Irish culture may have more to do with the emergence of a new form of collective Irish identity than with soccer, *per se*. Indeed, one feature of the recent focus of identity around Ireland's football team, and Irish musicians, may be of general significance – the tendency for the identity to lose any definite connection with residence in Ireland. It seems possible that (Southern) Irish identity is ceasing to be *territorial* in any real sense and that the Irish may be ceasing to be a nation, in the classic sense, emerging more as an ethnic group. This possibility is yet another example of the fuzziness which has crept in to the units which we use to examine social and economic life in the Irish case.

Turning to political dimensions of culture we also find a combination of strong historical influences and recent change. The formation of Irish national identity, in the early nineteenth century, was virtually simultaneous with, and probably shaped by, the development of highly effective mass politics. Yet this political culture has been much less effective since independence – if national economic performance can be used as a criterion to assess political systems.

It is clear that each of these cultural characteristics have an economic dimension. However, it remains difficult to identify whether that economic dimension includes causation which runs *from culture to economic performance*. In recent years an important debate has developed concerning the relative significance of cultural, structural, historical and political factors in explaining the economic failure of independent Ireland. That debate has an important bearing on any attempt to identify the economic, cultural and political factors which will shape Ireland's development in the years to 2010. Some comments on these issues are made at the end of this chapter.

### (iii) The Political Dimension

The world geopolitical dimension is of minor significance to Ireland – largely by virtue of its size and location. By contrast, the domestic political dimension and the political development of the Community are of the utmost importance. Two aspects of domestic politics may be important if Ireland is to achieve its major economic and social goals: the development of a national political process capable of formulating and implementing strategic programmes and some rationalisation of the relationship between local and national politics and administration. A third political factor is the conflict in Northern Ireland.

#### *Political Culture and Strategic Policy-making*

A political culture which was highly sophisticated and successful in the struggle for owner occupancy and national independence has been much less effective in the expression and resolution of domestic conflicts and the formulation of strategic goals and policies. At its best, this political system failed, from independence onward, to maintain Ireland's relative economic position and failed to solve the problems of unemployment and mass emigration; at its worst it resorted to extreme pragmatism and resolved problems by reckless foreign borrowing – so driving the country to a severe fiscal crisis which has only been partially resolved.

Whatever the explanation for this political failure, many believe that an important attempt to move beyond it has been the willingness of the social partners and some political parties to develop a system of social and political concertation which allows the resolution of conflicts in the context of coherent strategic approaches. While the tripartite National Economic and Social Council has expressed the social partners' interest in this, and promoted its development, it has also become aware of how demanding a project it is (see NESc, 1990, Chapter 15). An important debate has developed on whether a system of consensus or social "concertation", along the lines found in several highly successful small European countries, is feasible and desirable in Ireland. This issue is discussed in some detail when we turn, in Chapter 5, to consider what Ireland can do to shape its own future.

#### *Local Democracy and Administration*

A second political issue which may shape Ireland's evolution is the question of sub-national politics and administration. Ireland has a highly centralised political and administrative system; the abolition of domestic rates in 1977 removed the vital link between local administration and

democracy (Barrington, 1991). In recent years the case has been made for the development of a more independent system of local government and democracy – though there is little evidence of popular pressure for this. The European Commission has also advocated substantial local involvement in the formulation, implementation and monitoring of Regional Development Programmes. So far, the Irish government has responded to these arguments for more local autonomy with extreme caution and has met the Commission's requirements in a perfunctory and formal sense only. The absence of popular pressure for decentralisation does not mean that the question is irrelevant to Ireland's future economic development. Various considerations tend to suggest that there is something in the argument for a more decentralised approach to both routine administration and to policies for economic development. One is the enormous emphasis, in the international literature on regional regeneration, on the role of local development agencies and policies in animating indigenous resources (see the discussion of cohesion in Chapter 4, below).

#### *Northern Ireland*

Developments in Northern Ireland will inevitably shape Ireland's evolution in the years to 2010. The conflict of the past twenty years has had a number of effects. It has influenced Irish politics – but hardly in a way which enhances the ability of the political system to identify problems, mediate conflicting interests and execute strategic policies. The issue was frequently used in low level political competition, so distracting attention from more mundane economic and social matters; when it was occasionally treated seriously, it may have been politically damaging also, because it drew high-level political attention away from other critical issues. It has undoubtedly influenced economic development to some degree, by absorbing public resources, by severely damaging Ireland's tourist industry and, possibly, by influencing the rate of inward investment. It has clearly shaped Irish-UK diplomatic relations in ways which do not fully reflect the nature and density of social and economic relations between the two countries. Irish-British relations are noticeably different in the State and in civil society.

If any of these influences were to continue, then the problem in Northern Ireland would be a significant shaping factor. The Commission's Forward Studies Unit were interested in the potential for economic integration and co-operation between the Republic and Northern Ireland and work on the project included some examination of this question. While the findings of that research will be published separately the main directions can be summarised here.

The work reviews research on the European dimensions of the *Southern and Northern economies* and identifies the small extent to which this has focused on economic integration of the two regions. An initial assessment has been made of the potential for co-operation and whether the European dimension warrants increased co-operation. This is done by considering the basis for co-operation, the potential for economic interaction and the relevance of the European dimension. Various analytical approaches to market integration, developed in the European Community in recent years, provide a perspective from which to assess the potential for *market* integration. This suggests that the long-standing external orientation of the two economies may set limits to economic interaction between North and South. In addition, neither the 1992 programme, nor the supporting official and private sector measures, will remove a major barrier to increased interaction between North and South – political violence and the security response to it.

The potential for co-operation in European Community policy areas is also considered. This reveals benefits from co-operation in agriculture, border region initiatives, transport, energy and health care. An initial assessment has been made of the argument for an all-Ireland approach to Community policy – particularly structural policy. When account is taken of the relative significance of UK and EC policies to the North, and of the need to *give priority to the general governance of Northern Ireland*, there may be limited gains from a purely all-Ireland approach to the main lines of Community policy.

Attention is also paid to the political prerequisites of economic integration and co-operation. It is widely recognised, by students of the European Community, that integration of mixed economies is a political process. Consequently, just like the progress of European integration, the economic integration of North and South requires parallel policy and political developments. However, analysis of the potential for economic integration in Ireland reveals additional political requirements. At every step of consideration of economic integration, the security and political situation in Northern Ireland emerges as a major obstacle. This suggests that the political prerequisites for economic integration go well beyond the kind of harmonisation necessary in the rest of the Europe and, in fact, include some political resolution of the Northern Ireland problem. Finally, attention is focused on some long-standing claims concerning the possible effects of the European dimension on the problems in NI. It is argued that the political effects of European integration – in particular, its tendency to alter the terms of domestic political competition – may be particularly weak in the case of Northern Ireland.

#### **(iv) A Specific Balance Between National and Community Factors**

In designing the 12 country study the Commission's Forward Studies Unit requested that researchers should discuss both national and EC factors and policies. It is important to recognise that the balance between these two will be different in each country. In recent years there has been some advance in our understanding of the implications of EC membership for Ireland (NESC, 1989; Keatinge, 1991a; Keatinge, 1991b; O'Donnell, 1991b). One of the findings of that body of work is that the effects of membership, and the associated loss, or sharing, of sovereignty, must be evaluated by reference to an appropriate concept of sovereignty. The meaning of sovereignty differs from one member state to another, and over time. It follows that the extent and meaning of loss of sovereignty can be quite different in each member state. This implies that in analysing factors shaping development in the post-1992 period, the balance between Community (or international) factors and indigenous factors, will be seen to be different in each member state. This may be particularly so when considering factors which require political initiatives. Indeed, one implication of this is that correct application of the principle of subsidiarity may not imply the same allocation of policy functions to each member state.

In Ireland's case, the analysis of the balance between international and domestic factors reveals an interesting pattern. When considering socio-economic factors, the analysis strongly suggests that international factors and Community policies have particular relevance. Although we have cited many areas of domestic policy which are essential to success, it is also the case that there are definite limits to Ireland's economic policy autonomy, some of which arise from Community membership. However, when considering historical/cultural and political matters, we find relatively few global factors that will shape Ireland's development or, at least, it is not easy to identify what factors will do so. In part, this reflects Ireland's location and small size. In a more general sense, it reflects the fact that, except for superpowers, the significance of some political factor for a given country is dependent on that country's significance for the factor in question. This reflects the predominance of interdependence in the world. In Ireland's case, this interdependence tends towards the dependent end of the spectrum and this accentuates the significance of global economic factors and diminishes the significance of global cultural and political factors.

**(v) Consensus and Controversy in Ireland**

In assembling 12 studies of national shaping factors, the Commission was interested in the knowing the extent to which the main factors were agreed within each country and what factors were the subject of controversy. There is agreement that the following socio-economic factors will significantly shape Ireland's development.

- Structure of the economy
- Demographic trends
- Unemployment
- Public finance
- International economic growth
- Agricultural reform
- Environmental development
- EC enlargement

There would not, however, be complete agreement on *how* these factors will bear on future development. Analysis of these causal relationships and their implications for action is a major task facing Irish social science. Of course, social scientific research will not, in and of itself, remove controversy. The reasons for this should be noted. First, there are conflicts of interest inherent in economic and social life – indeed, that is one of the persistent findings of the social sciences. Second, the process of discovery of casual relationship in the economy and society can only proceed so far in the “laboratory” of social science research; key parts of economic and social reality can only become known through involvement in action to achieve economic and social goals and in the conflicts which such action inevitably engenders (O'Donnell, 1992).

There is likely to be controversy on the relevance of the following factors

- International production and location patterns
- All the cultural and historical factors discussed above
- The need for a system of consensus/concertation
- The need for more developed local government and democracy

Controversy over the relevance of these factors reflects both the innate difficulty of identifying their impact on economic development and the fact that there are conflicts of understanding and interest in these areas. The role of the technical and locational *pattern* of international economic



development, as opposed to the *rate* of international economic growth, has been discussed in Chapter 2(i). The debate over the need for further development of the system of social consensus, or political exchange, is considered in Chapter 5. Here, it may be useful to consider the relationship between structural, economic, cultural and political factors in the promotion or retardation of economic prosperity.

*The Interaction of Economic, Cultural and Political Factors*

If Ireland is to address its fundamental long-run problem – lack of internationally competitive indigenous economic activity – it must choose whether to focus its attention and action on structural characteristics (such as firm size or ownership of resources), economic factors (such as finance), cultural factors (such as entrepreneurship, education and training) or the political dimension (such as the electoral system, party structure or public administration). If all or several of these dimensions are considered important, then it is necessary to harness their interaction to create a virtuous rather than a vicious circle. There are two sources of information on these matters: Ireland's own past, and the past and current experience of other societies. Consequently, it can be argued that in considering the economic, political and cultural factors which will shape the future, and in devising ways to harness these forces, it is necessary to reach some understanding of the past.

A variety of explanations have been offered of Ireland's long-run economic failure, as indicated in mass emigration, high unemployment and a long-run failure to converge to the level of other European societies (for an overview see Kennedy, 1992b). The classical nationalist explanation cited the lack of legislative independence as the cause of Ireland's experience in the nineteenth century – though obviously some additional argument is necessary to explain the economic failure of independent Ireland. Another influential explanation, which can transcend both the union and independence, is that the South of Ireland lacked entrepreneurship (Lee, 1968). Indeed, this essentially cultural explanation has recently been enriched by Lee, who traces Ireland's twentieth century experience to the predominance of a "possessor ethnic", as opposed a "performer ethnic", in the country's institutions, intellect, character and identity (Lee, 1989). A more structural explanation has been developed by O'Malley (1989), who argues that Ireland, as a late-developing country, faced, and still faces, significant barriers-to-entry created by the scale, market power or technological lead of established firms in larger, more developed, economies. Political structures, in particular the nature of party politics and the failure of politics to present and mediate conflicting interests, are

emphasised by Girvin (1989). Although not intending to explain economic performance, others have analysed the relationship between national political mobilisation and the development of Irish Catholicism (Garvin, 1981; Inglis, 1987). But those political factors could have a direct influence on economic life, through their influence on state policy, and an indirect effect, through shaping cultural characteristics (such as the authoritarian family pattern) which might have been inimical to economic modernisation (Breen *et al*, 1990). Kennedy *et al* (1988) identify a set of proximate causes, which lie at the level of policy and public administration: failure to grasp the implications of the small size of the economy, absence of long-term perspective, and neglect of the human resource dimension. Finally, Crotty believes that the relevant comparison is with third world countries and develops an account in which capitalist colonialism plays a central role. In the nineteenth century the colonial power drew Ireland into a particular, and unpromising, role in the international division of labour. In the twentieth century, the social and political structures established under colonialism used the state in ways which favoured entrenched elites (Crotty, 1986). These structural, economic, cultural and political, explanations, though clearly not contradictory, tend to suggest different approaches to overcoming Ireland's problems.

#### *A Comparative Institutional Perspective*

If we reject the dominant tendency to vigorously separate the economic, the social and the political dimensions of life, then it seems likely that some synthesis of these different interpretations is possible (Kennedy, 1992b). The recent research commissioned by NESC, *The Irish Economy in a Comparative Institutional Perspective*, provides just such a synthesis. Its Norwegian author, Lars Mjøset, draws heavily on all the work cited above in order to present an interpretation of Ireland's experience which embodies the dynamic interaction of economic and social structures, global political factors, and cultural and attitudinal patterns. As such, it is a perfect example of the interactive outlook outlined in Chapter 1. Furthermore, like all history, it is oriented to the needs of the present. For the reasons outlined briefly below, it may force a major advance in the discussion of Ireland's historical development problem and, through that, may assist the choice of action to shape the future.

We noted above that Mjøset draws heavily on existing historical and social research. What then allows him to push forward the debate between structural, economic, cultural and political explanations? We can identify four elements, drawn from international developments in social science, which he brings to bear on the Irish case.

- (i) A definition of institutions which sees them as having two dimensions. First, institutions are the outcome of recurrent conflicts, where the parties have invested their "power resources" to reach compromises which secure favourable outcomes. Second, institutions are "sets of habits, routines, rules, norms and laws, which by reducing the amount of information necessary for individual and collective action, make reproduction and change of society possible (Mjøset, 1992, pp.32-33).
- (ii) A distinction, developed by Senghaas in a study of the European periphery, between two patterns of growth: (a) *Autocentric* – where growth occurs with socio-economic development and (b) *European peripheral* or *dependent* development – where growth occurs without socio-economic development. The relevance of this is that it provides a new category – peripheral development – into which Ireland might be put, which differs somewhat from the categories used in previous studies (such as "dependent", "post-colonial", "third-world", "late-developer", "Catholic", "resource-poor" etc.), and seems to improve on them.
- (iii) Use of the concept of a national system of innovation. A national system of innovation is defined as the institutions and economic structures which affect the rate and direction of innovative activities in the economy. In recent years, the focus has shifted from the innovative activity of the heroic entrepreneur to a number of institutional features inside and outside firms. These are believed to include the relation between banking and business, R&D activity, education, on-the-job training, higher education and the structure of the economy. Indeed, in the case from which this idea was largely developed (i.e., Denmark) the emphasis is more on routine commercial relationships between users and producers, and the way they promote interactive learning, than on R&D or scientific research.
- (iv) Adoption of a comparative method. In order to test the validity of the hypothesis discussed above, Mjøset compares Ireland with a set of, carefully chosen, countries: Denmark, Sweden, Finland, Switzerland and Austria.

At a most general level, Mjøset's conclusion is that Ireland's "basic vicious circle starts from two facts: the weak national system of innovation

and population decline via emigration. The mechanism whereby those two features reinforce each other must be sought in the social structure. These mechanisms are highlighted by studying contrasts which emerge from the comparison, with the other case countries" (Mjøset, 1992, pp.7-8). It is clear that these two facts are of a very different order: emigration and population decline are undisputed facts, while the existence of a weak national system of innovation is a complex hypothesis. This highlights the extent to which Mjøset's contribution to the Irish debate turns on the use of the four elements outlined above – particularly the concept of the national system of innovation.

Although considerable emphasis is given to cultural and institutional factors, the focus of his argument is on the *economic structure*. He draws on existing secondary material to provide fairly detailed accounts of the following episodes.:

- proto-industrialisation (eighteenth century)
- deindustrialisation (except around Belfast)
- pastoralisation
- protection of domestic industry (1932-1965)
- the period of export-led growth

The form of his argument is to assess the ability of existing theories (concerning lack of legislative independence, entrepreneurship and culture, colonialism and post-colonialism, late development, party politics etc.), to explain these developments *taking note of the various contrasts with Denmark, Sweden, Finland Switzerland and Austria*.

His conclusion is that each of these explanations, though valuable, are *insufficient* to explain Ireland's relative experience. He shares the basic diagnosis of several of these theories (especially O'Malley's), that Ireland moved from proto-industrialisation to deindustrialisation (in the nineteenth century) largely because it faced competition from the most advanced industrial empire in the world (p.11). What Mjøset adds to this diagnosis is the argument that this deindustrialisation was so strong, and the agricultural regime was incapable of supporting new industry, because Ireland had a weak national system of innovation. This, in turn, is explained by a combination of external and internal factors.

We have sketched an explanation which is more multi-causal (emphasising circles of cumulative causation) than those presented earlier. Certainly, we have only provided a rough sketch, and much research would be needed to spell it out in greater comparative detail.

Whatever the result of such a test would be, it seems that three perspectives must be combined: an emphasis on the demand side (especially on the dynamics of the domestic market), on the supply side (especially on linkages and national or local systems of innovation, along the lines of the Neo-Schumpeterian tradition), and finally, on the external forces of barriers to entry.

Our main conclusion is that in all the contrast cases – and even in Finland, the Nordic latecomer – a functioning national system of innovation came into being in the second half of the 19th century. In Ireland, a proper system of innovation developed only in Belfast. An effective system of innovation in other parts of the island could only have developed in close interaction with the transformation of agriculture. Ireland was, after all, an overwhelmingly agricultural economy. However, the trend towards pastoralisation, and the focus on live cattle as the major export item, did not encourage the nurturing of “micro-circuits” of the type which emerged during the Danish development towards a more intensive type of agriculture. The much more important role of the cooperative movement in Denmark, compared to Ireland, illustrates this main contrast (Mjøset, 1992, p.242).

This approach attempts to identify a number of factors – whether cultural, social or institutional – which tended to reinforce Ireland’s vicious circle in the nineteenth century and reproduce it in the twentieth. In the nineteenth century these included the paternalistic family structure and emigration, both closely related to increasing specialisation on the production and export of live cattle. These continued into the twentieth century and were reinforced by the interaction of national and Catholic mobilisation, and the influence which this had on both the state and civil society. This analysis can be seen as an effort to trace the structure, or skeleton, which lies beneath, and explains, the face of modern Ireland described so vividly by Lee (1989).

Turning to the present and the future it is possible to identify some positive and negative features which will probably shape the country’s evolution. The long view articulated by Mjøset allows us to see that Ireland still faces the fundamental problem of developing internationally competitive activities on a sufficient scale, and with sufficient roots in the Irish economy, to provide employment and prosperity. However, after the internal and external changes of the 1980s, the country now faces this problem with two new burdens on its back: historically high levels of long-

term unemployment and an overhang of national debt. Mjøset concludes that:

A major task for Ireland in the 1990s, therefore, must be to simulate an Irish system of innovation. Only this will solve some of the problems identified in the outward-oriented strategy... It should also be noted that such a system would be no cover for old-fashioned import substitution strategies. It does not involve state protection, but it implies the creation of factor advantages. It recognises that the world is open and that the goal is not substitution for imports, but rather an innovative approach to the question of export competitiveness.

The analysis of national innovation systems – even the way they worked during the Golden Age – indicates many elements from which Ireland may learn. But this learning must be combined with a clear understanding of the specific challenges of the present state of technological development. (Mjøset, 1992, p.18)

Putting aside, for a moment, the nature of this task, it is possible to mention three developments which may improve the chance of achieving this in the years to come. First, there is evidence that Ireland is developing the type of autonomous civil society which Mjøset identified in all his contrast cases.<sup>3</sup> Some of the limitations of the party political system – deriving from the catch-all nature of several parties and their traditional dominant concern for the agrarian interest – might possibly be overcome by the development of “political exchange” involving the social partners and government (See Chapter 5). Thus it is possible that some of the factors which, in the past, reinforced poor economic performance and thus created cumulative vicious circles, may not be so forceful in future. Third, it is possible that changes in technology and the international economy can reduce the significance of some of Ireland’s historical disadvantages and increase the economic relevance of some of Ireland’s strengths. This feature of technological change has been noted by Perez and Soete, who discuss the possibility of “windows of opportunity” for smaller and less advanced countries (Perez and Soete, 1988).

<sup>3</sup> He says that “the influence of secular forces was weaker than in any of the contrast cases. Thus Ireland’s civil society became a Catholic one, and Catholicism also represented a close tie to the state. State, Church and civil society were more strongly linked together than in any of the contrast cases”. (Mjøset, 1992, p.250).

Finally, despite the significant advance (in discussion of the interaction of economic, cultural and political factors) made possible by Mjøset's recent work for NESC, there remains considerable work to be done. In particular, though the idea of the national system of innovation has been shown to be a valuable organising concept, we do not yet have detailed knowledge of the particular system in Ireland in the 1990s. This alone identifies an important research task. A further, and even more difficult task, is identification and implementation of measures which will stimulate an Irish system of innovation.

## Chapter 4

### *CHALLENGES FOR THE EUROPEAN COMMUNITY*

[T]he universalist principles of democratic states need an anchoring in the political culture of each country. The principles laid down in the constitution can neither take shape in social practices nor become the driving force for the project of creating an association of free and equal persons, unless they are *situated* in the context of the history of a nation of citizens in such a way as to be connected with their motives and convictions.

However, examples of multicultural societies like Switzerland and the United States demonstrate that political culture in the seedbed of which constitutional principles are rooted by no means has to be based on all citizens sharing the same language or the same ethnic and culture origins...

That nation-states constitute a problem along the thorny path to a European Union is, however, less due to their insurmountable claims to sovereignty than to another fact: democratic processes have hitherto only functioned within national borders. So far, the political public sphere is fragmented into national units.

Jurgen Habermas, "Citizenship and National Identity: Some Reflections on the Future of Europe", 1991.

Despite the recent advances in European integration, and in our understanding of it, there remains considerable uncertainty about the future of the Community and Ireland's prospects within it. These too are economic, political and cultural. They arise, first, because there is an array of internal and external problems which threaten Europe and, second, because there are severe doubts about whether the Community, with its existing decision making system and institutional structure, can effectively deal with them. These problems and the Community's ability to deal with them are discussed in Sections (i) and (ii), respectively. The remainder of the chapter considers possible medium- and long-term approaches to cohesion.



### (i) The Internal and External Agendas

The Treaty of Maastricht extends the competence of the union to new policy areas such as the promotion of industrial competitiveness, establishment of trans-European networks, education, training, culture, consumer protection, civil protection, tourism, energy and development co-operation. More significantly, the Treaty contains a blueprint for full economic and monetary union before the end of the century. Quite apart from problems of managing a full economic and monetary union, the Community faces a set of immediate economic problems which, if not addressed, may disrupt or even destroy the transition to EMU. The EMS seems unable to play the role in the transition to EMU which is assigned to it in the Maastricht Treaty. This raises questions about the rules, norms and values which are embodied in that treaty. Economic growth remains low throughout the Community and unemployment, though it never fell much after the crises of the 1970s and early 1980s, is clearly emerging as an economic, social and political problem.

There also remains considerable doubt about whether the 1992 programme, on its own, will work, in the sense of restoring Europe's competitiveness relative to the US and Japan. Though there was, and remains, a strong case for the completion of the internal market, it is unlikely that deregulation and market liberalisation are sufficient to achieve the deeper structural and behavioural adjustments which provide the basis for a sustained period of innovation, growth and economic leadership.

It is also doubtful that the 1992 programme, and other Community policies, will succeed in significantly reducing spatial and social inequalities in the Community (NESC, 1989). If this is true generally, it is obviously of particular importance to Ireland.

If this combination of new policy areas and severe economic and social problems presents the Community with daunting tasks, the pressures seem remarkable altogether when the external environment is considered. As outlined in Chapter 2, the external environment will present the Community with a set of problems deriving from changes in Eastern Europe, the Mediterranean, global relations between the rich North and the poor South, international economic instability and environmental problems.

Overall then, the Community has a demanding internal agenda, containing the 1992 programme, EMU, cohesion, social Europe and the formulation of guiding values; it faces an uncertain, and in many ways threatening, external environment because of developments in Central

Europe, the Mediterranean, enlargement, North-South relations and environmental decay. This agenda and set of external issues would be likely to overload even the most authoritative and legitimate decision-making and administrative system. But the authority, effectiveness and legitimacy of the Community's system of governance are highly problematic.

### **(ii) The Authority, Effectiveness and Legitimacy of the Community**

Consider first the effectiveness of the system. The Community's policy process has long had three different decision-making systems for dealing with different sets of issues: the "Community method", pure intergovernmentalism and policy co-operation. Rather than move toward one decision-making model – as advocated at the 1991 Inter Governmental Conference by the Commission, The Netherlands and Belgium – the Treaty of Maastricht has codified this variety in the famous "Three Pillars" (Keatinge, 1992). But even the most effective of these models of policy making – the Community method – may lack sufficient effectiveness, authority and legitimacy to adequately address the problems which will confront the Community. In the period following the famous veto crisis this decision-making process was noted for its inertia and the fact that when it reached decisions these were often the lowest common denominator of the "national interests". Although the Single European Act (SEA) increased the efficiency and effectiveness of this process, it has been argued that disjointed incrementalism may not be sufficient to see the Community through the turbulent waters of the 1990s. "In the longer term the question of how to provide a system of government that has sufficient capacity, political authority and legitimacy at the Community level must be confronted in an overt fashion" (Laffan, 1991). Even now, the strong intergovernmental element, and fragmented Councils of Ministers, hamper the Community's decision-making system. What are represented as national interests are frequently no more than sectional or private interests and this leads to minimal and poor decisions. Although the SEA has greatly speeded up the processing of the 1992 programme, it should be noted that there existed a strong prior political consensus on the internal market. There is already evidence that the post-SEA system does not work so well on issues where more difficult conflicts require resolution. In addition, the Community method is under increased attack by opponents of European union operating under the guise of "subsidiarity".

This system would be even less satisfactory in the context of a move to EMU. As argued in Irish analysis undertaken before the currency crisis of late 1992, there is a definite reluctance to confront the political

consequences of EMU (Laffan, 1991). It was also argued that there are reasons to fear that the overall structure set out in the Maastricht Treaty will be somewhat unbalanced – with more coherent institutions and policy on the *monetary* side than on the economic. This results precisely from the fact that insufficient progress has been made on the political and institutional fronts to create a political body with the authority, capacity and legitimacy to determine a set of economic policies for the Community (O'Donnell, 1991c).

Enlargement will further expose the limits of the Community's institutional and decision-making system. There is some recognition that a much larger union could not be effective with intergovernmental bargaining at the centre of the system. This poses a most important question which requires not only political but conceptual innovation.

Turning to the other pillars, the prospects of addressing the internal and external agendas outlined above seem even smaller. Although the Treaty of Maastricht has nominally transformed the existing European Political Co-operation (EPC) into a Common Foreign and Security Policy (CFSP), the requirement of unanimity in this area, and the approach adopted by member states, greatly dilute the content of this policy – as demonstrated graphically in Yugoslavia.

While talk of the democratic deficit has long been viewed with great cynicism by some member states – and is, admittedly, often presented in abstract and idealist terms – it may be that the ineffectiveness of Community decision making (whether in law making or constitution writing) is, in part, a function of lack of legitimacy and authority. The rejection of the Maastricht Treaty in the first Danish referendum and the difficulties experienced in France have certainly brought the issue of legitimacy higher up the agenda. However, there is no guarantee that the question will be dealt with in a way which enhances the Community's capacity to address the internal and external problems listed above. Indeed, history may well be creating one of those conjunctures where rational, co-operative, solutions (though ultimately better for all parties) cannot be achieved, because of the short-term incentives to non-cooperative behaviour. Among the paradoxes of the current crisis is that it requires, above all, that the political leaders of Europe continue to co-ordinate their actions; yet one of the reasons for the crisis is that the political process of the Community has been conducted only at that elite level.

Overall, the institutional and decision-making system of the Community – in particular, the strong intergovernmental element – do not seem capable of dealing with the remarkable internal and external

agendas. It is this which suggests that the economic, political and cultural dimensions of the Community, and Ireland's place within it, are uncertain and, in many respects, threatened.

The internal and external agendas outlined above imply a definite overload of the Community's institutions and decision-making procedure. Although this is surely true, it may be mistaken to abandon or hive-off agenda items in the hope of getting a smaller agenda under control. The alternative is to look at the Community institutions and decision-making system. As with external pressures and crises, internal problems can, in some circumstances, galvanise a society and polity and, in others, loosen its internal ties. One reaction to the daunting agenda might be to halt deepening, and proceed to a shallow, but wider, Community in which most internal and external issues will be addressed by nation states. Another course may be available. Identifying such an alternative will be a difficult task. What can be said, however, is that, in the light of this remarkable agenda, the continuation of traditional haggling over the prerogatives of the nation state, which has occupied so much time and energy in recent years, is likely to be disastrous.

### (iii) Putting the Cohesion Issue in Perspective

The remaining sections of this chapter consider possible medium- and long-term approaches to cohesion in the EC. An attempt is made to put the cohesion issue in perspective. Three broad policy approaches to cohesion are identified and it is argued that the task facing the Community is to identify the potential and limits of each. Two dimensions of the cohesion issue are emphasised: the evolving interpretation of regional development and the relationship between regional and social inequality. Emphasis has shifted from the *external* determinants of regional growth, to *indigenous* factors in both leading and lagging regions. Recent reports to the Commission have emphasised the *social* as opposed to *spatial* nature of much inequality in the EC. These considerations allow some judgement on the potential and limits of each policy approach to cohesion. That judgement suggests that the Community should develop a combination of structural policies, differential application of other Community policies and budgetary mechanisms.

While Ireland's interest does undoubtedly focus on cohesion, an attempt has been made in recent years to put cohesion in the correct perspective. This is beginning to yield an improved understanding of the relation between domestic and Community policy, the place of the

cohesion question in the overall Community system and of the relationship between regional and social inequality.

The first of these insights – concerning the importance of domestic policy – derives both from analysis of regional problems and from recent research on Ireland's experience in the Community. The former has prompted rejection of deterministic theories of regional growth and decline and suggested that factors indigenous to a region have a significant bearing on its performance and even on the place which it occupies in the international division of labour. Among these indigenous factors are the economic and other policies pursued by national or regional authorities. This suggests that a necessary, though not sufficient, condition for cohesion, is domestic policies which promote the long-term strength of the Irish economy.

The detailed analysis of Ireland's experience in the Community confirmed this point. On the basis of such an analysis, NESc derived, and stated bluntly, a series of lessons. Of the twelve lessons of the period 1973 to 1987, half referred to *Irish policy* rather than international integration *per se*. These considerations led NESc to the view "that membership of the Community does not diminish the need for a national ability to identify solutions to national problems – even where these solutions require Community policies and action" (NESc, 1989, p. 218). A similar conclusion emerges from Kennedy's review of theoretical and empirical work on international and interregional convergence: "Whether or not Ireland converges with the rest of the EC will depend primarily on its own national efforts" (Kennedy, 1992a).

A perspective is also being attained on how the cohesion question relates to the wider set of Community goals and policies. In its report *Ireland in the European Community* NESc argued that Ireland must place the cohesion issue within a strategic approach to European integration:

To establish a given objective as an actual Community priority, it must be consistent with the resolution of the major problems facing the Community in general. There is clear evidence that concentration of any one member state on any one objective is liable to jeopardise the achievement of even that one objective, and certainly undermine the ability of the Community as a whole to address its problems (NESc, 1989).

More recently, an attempt has been made to interpret the place of cohesion in the Community system since the Treaty of Rome. This revealed that "the relationship between the regional objective and, say, the common

market objective, was tied up with, and a product of, the relationship between Community objectives, policies and institutions, on the one hand, and national objectives, policies and institutions, on the other" (O'Donnell, 1991d, p. 98). This analysis suggested that a significant change in the place of the cohesion issue in the Community, and significant enhancement of cohesion-promoting Community policies, requires a change in the relationship between the Community and the member states.

A third way in which the cohesion issue requires to be put in perspective, is to see the limits of the standard Community definition and conception of cohesion/non-cohesion, as inter-regional differences in average income per head. As will be seen below, this conception, and the indicators which are commonly employed, tends to conceal the fact that the problems of inequality, poverty and unemployment in the EC may be *social* rather than regional. This has implications for the definition and measurement of regional problems, the design and implementation of Community policy and Ireland's approach in the Community. In particular, it suggests that while Ireland has an enormous interest in cohesion (in the sense of narrowing intra-EC regional disparities in income per head) this objective cannot encompass the whole of Ireland's interests or needs.

The thread which connects all these discussions of Community policy is the central role of the political dimension. The implication of the work on the cohesion question cited above is that the place of economic and social cohesion in the Community system is linked to, and largely determined by, the degree of political cohesion or political union. This is now understood to a fair degree in Ireland. Furthermore, the development of other policies which have a major bearing on cohesion, such as macroeconomic policy and fiscal union, is also linked to political union.

#### **(iv) Defining the Cohesion Problem and Mapping Out an Approach**

It is possible to identify three broad policy approaches to cohesion:

- structural interventions
- differential application of other Community policies
- budgetary or public finance instruments.

The task facing the Community in the medium term, is to identify the potential and limits of each of these types of policy as a means of promoting convergence and maintaining cohesion. Since such an

evaluation shows that each approach has both potential and limits (see below), it seems necessary to devise a combination of all three approaches. The argument summarised below is that, in designing a combination of these three approaches, account be taken of two particular factors: first, the social, rather than purely spatial, nature of much of the inequality in the Community and, second, the current limits on our ability to devise and implement policies which are consistently capable of reversing regional fortunes.

#### *Both a Short- and Long-Run Focus*

A central element of the argument and proposals outlined below is that, whatever the limits of current resources and political possibilities, the Community should adopt a set of policies which are consistent with a long-term programme for cohesion. Consequently, it is appropriate to consider measures and approaches which may not be feasible on a large scale at present but which, because of their effectiveness and analytical justification, could be established in embryonic form in the short run. In other words, reviews of cohesion policies should avoid the temptation of a quick-fix, or the delusion that the problem will be solved in the coming years, and establish policies and mechanism which make sense, on either a larger or smaller scale, in the long run. Likewise, it is important to design a set of approaches to cohesion which are consistent with the evolving Community system of overall economic and social management – if it can be called a system – and with the evolving relationship between the Community and the member states.

#### *A Three-Pronged Approach to Cohesion*

It is argued below that Community policy for cohesion might have three main elements in the long term:

- development of the Structural Funds
- serious consideration of the cohesion dimension of competition policy, agriculture policy, overall European macroeconomic policy and tax harmonisation/competition.
- Community support for minimum levels of public good provision in weaker regions and member states.

In designing instruments under each of these headings, the social element of the cohesion problem could be taken into account in various ways.

### (v) Two Dimensions of the Cohesion Issue

There are numerous dimensions to the issue of social and regional inequality, including the regional impact of the internal market programme, the relationship between cohesion and macroeconomic policy and performance, and the cohesion implications of EMU. While these have been much discussed in recent years, two other dimensions seem less frequently cited, certainly in Ireland. These are, first, the evolving interpretation of regional development and, second, the relationship between regional and social inequality. The task in the medium term is to derive the implications of these for policy. These implications concern the potential and limits of the three policy approaches to cohesion.

#### *The Evolving Interpretation of Regional Development*

A study of research on regional issues and regional policy shows that the subject is experiencing a period of considerable turbulence. The "principle of cumulative causation" was an important element in the analysis of regional problems. That principle stated that if there are "economies of scale in production" or "economies of agglomeration" then a region which gets an initial advantage will find that advantage reinforced as its level of production increases. On this view, economic disparities, far from being self-adjusting, or self-correcting, as in orthodox economic analysis, tend to be self-reinforcing.

This idea played a significant role in post-war regional policy, which was designed to increase demand for the region's exports. This was done by attracting growth industries to the region (by measures such as capital grants, etc.) and improving the productivity and export propensity of existing industry (via capital grants, labour subsidies and infrastructural investment). While this form of regional policy had some success, it has not served to fundamentally reverse regional decline or reshape the pattern of regional development. The focus of the theory and policy on demand as the ultimate determinant of regional prosperity seems to have led policy-makers to ignore non-cost factors operating on the supply side.

Disappointment with the results of post-war regional policy, and observation of new pattern of regional development, has led to interesting developments in the theory of regional development. A common feature of recent approaches is a rejection of the more deterministic theories of regional growth and decline. There is evidence that the hierarchy of regions is not as stable as certain versions of the theory of cumulative growth and decline would imply; strong regions can go into decline and weaker regions can surpass them. This is sometimes linked to regional



effects of technical and organisational change and the regional pattern of innovation (see Chapter 2(i)). Regional theorists have also reassessed the significance of transport infrastructure in regional development, since the regional problem is no longer seen purely in terms of *accessibility* to richer regions. Emphasis has shifted from the *external* determinants of regional growth, to *indigenous* factors in both leading and lagging regions. Factors such as innovation, entrepreneurship, the level and quality of public good provision, labour market and social structures, economic and other policies, institutional arrangements between industry, finance and the state, and the size and nature of the indigenous market, have all been identified as significant.

From a policy perspective these developments in the interpretation of regional problems, and especially the recognition of the role of indigenous factors, have both optimistic and pessimistic implications. They are *optimistic* in that they undermine the idea that external structural factors in the wider international economy condemn any region to inevitable backwardness. But these developments are *pessimistic* in that, while they point to the need for, and the potential of, local initiative, they also suggest that regional disadvantage is, in part, the result of multiple indigenous factors. This undermines the view that there are one or two policy instruments which, if applied on a large enough scale, would solve the regional problem. It is argued below that the multiplicity of possible factors, and the proliferation of policy instruments, constitutes one of the main problems facing regional policy now.

#### *The Relationship Between Regional and Social Inequality*

In striking a balance between the three broad approaches to cohesion, the Community might take greater note of the relationship between regional and social inequality. In the EC it is common to define and measure the cohesion problem by reference to average regional per capita incomes. There is a fundamental problem in defining and measuring the problem in this way: measures of inter-regional inequality depend on the regional boundaries which are selected. This is one of a series of statistical problems which arise as a result of what is known as the "modifiable area unit problem" (Arbia, 1989). The problem bedevils not only the measurement of regional problems, but also any attempt to use statistical analysis to "explain" them. However, it is most important to realise that these are not only statistical problems and, in fact, reflect a real property of the economy and society. Ultimately, they are a reflection of the limits of the concept of a region in either economic or social terms.

This can be seen when we consider the implications for policy. The idea that regional economic disparities should be reduced for the sake of equity only makes sense if there is a relationship between spatial equity and social equity. The pursuit of inter-regional equity as a policy goal has been characterised as substituting "place prosperity" for the more fundamental goal of "people prosperity". It can be argued that in the absence of analysis of the relationship between spatial equity and social equity, the pursuit of inter-regional equity becomes a meaningless goal (Gore, 1984). The implication of this seems to be that regional policies can constitute an unsatisfactory approach to the cohesion question, precisely because they reduce the *cohesion* question to a purely *regional* question. These approaches can lead policy-makers and others to assume that problems *in* peripheral regions are problems *of* peripheral regions, that problems *in* rural regions are essentially problems *of* rural regions. Geographers and certain regional theorists have, in recent years, seen the limitations of this viewpoint and named it as "spatial separatism", where, by separatism they have in mind, not a political position, but the analytical "notion that it is possible to identify, separate and evaluate the spatial as an independent phenomenon or a property of events examined through rough spatial analysis" (Sack, 1974). It should be stressed that criticism of this viewpoint does not imply that regional patterns do not matter but, as Gore says, "that the questions have been formulated in the wrong way. They have been formulated in a way which tries to separate a spatial pattern from the social processes which are occurring within a country, and then evaluate its effects" (Gore, 1984).

Approaches which have been informed by these insights have been adopted in two recent reports on Community cohesion policy. In a report to the European Parliament, *A New Strategy for Economic and Social Cohesion*, by the National Institute for Economic and Social Research (NIESR) in London, in collaboration with other institutes, there is considerable emphasis on two related aspects: the social nature of much of the cohesion problem and the need for a wider range of indicators if the objectives of cohesion policy is to include pursuit of social goals: it is argued that the data on a wide range of economic and social phenomena should be considered and, in particular, that "it is necessary to look at the distribution of incomes and not just the average level" (Begg and Mayes, 1991, p. 77). They also noted the artificiality of boundaries and the existence of situations in which cohesion appears to be lacking – such as those of ethnic minorities or urban problems – but which are not picked up by existing indicators (*ibid.*, p. 84). Likewise, a report to Directorate General XXII of the European Commission, entitled *Methods for Achieving*

*Greater Economic and Social Cohesion in the EC*, by the Trans European Policy Studies Association (TEPSA), put considerable emphasis on the problems of measurement and analysis and on the tension between "place prosperity" and "people prosperity" (TEPSA, 1991). In both cases these factors were considered to have significant implications for Community policy.

While this aspect of the cohesion problem requires further study in each specific situation, it is possible, even in the medium term, to adopt an approach which takes account of the most obvious policy implications of the existing research in this area. These are three. First, the significance of social disadvantage suggests that we consider a wide range of national and Community policies, and not just those concerned with regional cohesion. Second, there are likely to be limits to the degree to which it is possible to achieve cohesion objectives by means of purely regional policies, i.e., policies which manipulate the location of economic activity. Third, the main policy instruments which are known to be capable of enhancing equity (long in use in the member states) will have to become a part of Community policy if cohesion is to be attained. These policies include the budgetary mechanisms which support inter-regional and, most significantly, interpersonal equity – through social insurance, income redistribution or the provision of public goods. This reinforces the importance of developing the budgetary or fiscal element of Community cohesion policies.

#### **(vi) The Potential and Limits of Structural Interventions**

A central element of any new approach to cohesion must be a realistic assessment of the degree to which structural policies are capable of overcoming problems of regional and social inequality. There would seem to be an emerging consensus about the potential and limits of structural policies. There are three elements to this consensus. The first is a recognition that traditional approaches to regional problems are no longer adequate. Second, it is agreed that structural regional policy should focus primarily on indigenous resources and innovation potential. Third, development and implementation of policy along these lines poses a number of difficult challenges and these suggest that there are, as yet, definite limits to what can be achieved by this approach on its own.

#### *The Limited Potential of Traditional Policy*

Despite the problems of evaluation there is a very widespread agreement that traditional regional policy has limited future potential.

Two kinds of problems can be distinguished. First, even where traditional regional policy succeeded in attracting mobile projects to designated regions, and where extensive infrastructure was constructed, the effects on these regions were generally less than was expected. Second, since the crisis of the 1970s, regions are subject to new kinds of pressures and require new kinds of restructuring which may not be much assisted by conventional regional policy. This is a major theme of recent work on regional policy (see Wadley, 1986; Albrechts *et al.*, 1989; Chisholm 1990) and industrial geography (see Gertler, 1988; Schoenberger, 1989; Gertler, 1989). Put very briefly, the types of economic activity and structures which prevailed after the recessions of the 1970s and 1980s implied a somewhat different geographical pattern of production.

In a recent overview of new perspectives for regional policy in the 1990s, Albrechts *et al.* (1989) note that:

Unequal regional development is the result of an historic process which has, through a series of consecutive phases, continually produced new socio-economic and political inequalities within and between regions ... Spatial development policies can thus only be successful if the historically developed structural conditions which determine uneven development are identified and addressed.

While we are a long way short of a comprehensive theory to explain uneven development, recent work has focused on innovation and indigenous agglomeration forces as significant elements in the process of regional development, on the grounds that these are an important component of the economic advantages of leading regions. In what are sometimes referred to as "new" structural policies, support for firms tends to focus on research, marketing or skills rather than grants for acquisition of fixed assets (Stohr, 1989).

#### *The Strengths of New Structural Policies*

The strengths of this approach are evident from this brief account alone. The policy seeks to enhance those factors which are now believed to be among the important sources of regional competitive advantage (Chisholm, 1990). It takes the supply side of the regional economy seriously in a way which earlier policy did not (*ibid.*). It accords a much more significant role to local initiative – a factor which has received too little attention in the literature on regional economics. The new approaches recognise the potential role of regional uniqueness and seems, therefore, to be consistent with the current pattern of regional

restructuring and the strategies of firms. The Community might make an ongoing assessment of the strengths and weaknesses of these types of structural policy.

The emphasis in the new policy is on development of infrastructure in its widest sense. This involves an emphasis on amenity, communications infrastructure, education and training and the development of an information and contact-rich environment. In many cases, R&D is supported, especially in small firms. The development of business services is given a priority (Albrechts and Swyngedouw, 1989). Modern regional development theory suggests that "it is the mutual dialectics between top-down structural development and bottom-up local uniqueness which actually determines the regional development process" (Albrechts, *et al.*, 1989). The new forms of structural regional policy are frequently designed as a combination of top-down, supranational (and national) planning and co-ordination, and bottom-up animation of indigenous actors.

All of these strengths suggest that policies for indigenous development and innovation-oriented regional policy have considerable potential to improve the structure of the Community's weaker regions. This constitutes a strong case for continued pursuit and development of Community policies of this sort.

#### *The Limits of New Structural Policies*

Perhaps the most general and significant drawback of the view that regional development depends crucially on indigenous resources and innovation, is that this insight does not tell us what precise policies to pursue. In his recent review, *Regions in Recession and Resurgence*, Chisholm says that "the real problem is one of converting these general points into practical programmes on the ground" (Chisholm, 1980, p. 174). This is a point which is repeated throughout the literature on the subject (see, for example, Moulaert, 1991; Albrechts and Swyngedouw, 1989). The difficulty can be further illustrated by considering some of the implications of the focus on amenity, communications, education and an information-rich environment. It has been argued that policy must be specialised, decentralised, co-ordinated and flexible. But this calls for an institutional framework which may be lacking in many regions. Where they work, such institutional arrangements tend to be a natural extension of the existing political and administrative system. Such an institutional framework is not easily created where it does not exist – especially where the severity of regional and social disadvantage have created economic and social fragmentation and apathy.

*The Limits of Indigenous Development*

While the new focus on a "bottom-up" approach to regional development is, undoubtedly, an important correction to the traditional "top-down" approach, it is of the utmost importance that the limits of this approach be recognised.

The first of these concerns the "locality trap". As Moulaert says "some interpretations and applications of the industrial district concept over-stress the endogenous development potential at the expense of the global economic structure to which the local economies belong" (Moulaert, 1991, p. 16). Second, there also exists a "smallness trap". This trap consists of an excessive emphasis on small enterprises as the engine of local economic development and naïve belief that policy which fosters them can reverse regional decline. Third, there is a tendency to try to replicate strategies which are fitted for strongly coherent socio-economic structures. Many of the Community's regions are not suited to becoming industrial districts or high-tech centres and policies based on these ideas will probably fail (Moulaert, 1991). Fourth, despite the new emphasis on indigenous development, few regions can afford to totally ignore inward investment. Research on the location needs of modern firms suggests that no region is debarred from attracting firms because of natural characteristics, but also implies that some regions will have very limited ability. Poor quality of amenity and skills are both an *effect*, as well as a *cause*, of regional disadvantage (Chisholm, 1990).

Fifth, experience suggests that innovation is an inherently imbalanced activity. It tends to occur in clusters, in both time and space – an observation which dates back to Schumpeter, and beyond (Dosi, 1988). This sets definite limits to what can be expected from innovation-oriented regional policy. Modern research suggests that innovation is based on a wide range of interlocking advantages. It follows that it is difficult to influence it by means of public policy (Armstrong and Taylor, 1987).

Finally, one of the dangers facing modern structural policy is the possibility of a proliferation of schemes and policy interventions. One result of the emergence of a plethora of regional policy interventions is that it reinforces the importance of policy monitoring and evaluation (Chisholm, 1990). Others have argued that almost anything can now qualify as a regional policy measure – an observation some might feel is confirmed in Ireland (Higgins and Savoie, 1989). The whole thrust of recent analysis undermines the view that there are one or two policy instruments which, if applied on a large enough scale, will solve the regional problem. It is precisely the multiplicity of possible factors, and the proliferation of policy instruments, which constitutes the main problem of regional policy now.

*Conclusions On the Potential and Limits of Structural Policy*

These considerations form the basis for an assessment of the Structural Funds and their role in an overall set of Community policies in the medium and long term. The evidence strongly suggests that the Community's Structural Funds, which embody a combination of traditional and new forms of structural policy, will not be sufficient to achieve a large reduction in spatial and social disparities in the coming decades. Three reasons can be identified. First, the total resources allocated to Community cohesion policies are small relative to the size of the problem, relative to the effects of other Community policies and relative to the size of national regional and sectoral aids in operation in richer regions of the Community. Second, and of even greater importance, our knowledge of the forces determining regional growth and decline has not reached a stage where development programmes which are consistently capable of reversing regional fortunes can be implemented – though striking regional regeneration has been achieved in some countries. Third, the Community's structural policies do not take sufficient account of the element of inequality which is social rather than spatial in its causes and consequences.

**(vii) Differential Application of Other Community Policies**

Article 130b provides that the cohesion objective should be taken into account in the formulation and implementation of Community and national policies. There is a definite, but *finite*, number of Community policies which can be applied in a differential manner in order to promote cohesion. The limits arise from the need to have a single internal market, on the one hand, and the need to pursue certain Community-wide objectives (such as R&D, the environment, etc.), on the other.

There are two areas of Community policy, agricultural policy and competition policy, in which it is particularly feasible and important to act in ways which contribute to cohesion. The recent reform of the CAP does, indeed, take this into account. In addition to these acknowledged areas, it is possible to identify two other policy areas which will have a major impact on cohesion. These are:

- policies which enhance overall economic growth
- tax harmonisation.

Only the Community as a whole and its larger, richer, member states can directly influence the overall rate of economic growth. Yet growth is

necessary for cohesion. Tax policies are important because tax competition may pose a threat to the poorer member states. Research shows that tax competition can erode tax revenues and the provision of public goods. If tax harmonisation is insufficient, or if national tax policies are uncoordinated, then "fiscal dumping" will arise and will be harmful to cohesion (Van der Ploeg, 1991; TEPSA, 1991). These considerations define limits to the potential of Article 130b as an overall approach to cohesion. This suggests that this approach must be pursued alongside structural policies and budgetary approaches.

### (viii) Budgetary Policies For Cohesion

#### *An Eclectic Approach*

In order to choose what extension beyond the current Structural Funds is appropriate it is necessary to assess the arguments for different kinds of budgetary mechanisms in a federal or pre-federal system. In recent years the discussion of this has been undermined by early introduction of possible political difficulties and exclusive focus on narrowly interpreted efficiency criteria. Those attitudes, which reduce discussion to cynical *realpolitik* or an academic game, have never served the Community well, and contrast with the rigour and depth of the approach to the internal market programme. The role of budgetary mechanisms in the Community can be considered from a *microeconomic*, a *macroeconomic* and a *developmental* perspective; it is possible to apply either *efficiency* or *equity* criteria. Exclusive focus on one perspective and one set of criteria serves little or no practical purpose. Any sensible proposal for achieving greater cohesion will inevitably combine both equity and efficiency arguments and must take account of microeconomic, macroeconomic and developmental considerations. It seems sensible to adopt an eclectic approach which takes account of each of the following aspects of the issue and allows for the fact that these are not totally separable from one another.

- the possible routes to economic and social cohesion
- the efficiency and equity argument for minimum levels of public good provision in all regions of the Community
- the principles of public finance and policy assignment in a system of multi-level government
- the need for risk-sharing in EMU
- the new economics of integration which highlights the degree to which genuine integration undermines national policy.



Although these issues cannot be discussed here, it can be argued that whichever of these approaches is adopted a similar conclusion emerges: there is a case for development of the Community's budgetary mechanisms in ways which will increase its contribution to economic and social cohesion (TEPSA, 1991). While pure efficiency arguments can be advanced in support of this proposition, a wiser and more realistic approach is one which combines efficiency and equity arguments.

#### *Social Security or Public Good Provision*

The recent NIESR report to the European Parliament advocated the development of a new instrument, operating through the social security system, to target aid to the most disadvantaged households in the Community (Begg and Mayes, 1991). While this has much to commend it, an alternative which might be considered is Community support for a minimum level of public good provision throughout the EC. The case for this has been made in the report from Trans European Policy Studies Association to DGXXII. There it is argued that budgetary mechanisms for this purpose would be far more than a support of living standards. They could contribute to regional development, could enhance the internal market, could be consistent with the principles of public finance and would prevent the harmful effects of tax competition. Guaranteed provision of minimum levels of education, health, social security and public economic services will enhance the indigenous development potential of many weaker regions and member states (Van Rompuy, *et al.*, 1991).

Although there are arguments for more advanced forms of fiscal union than this, the support of minimum levels of public good provision, or the introduction of a new social security instrument, constitutes an interesting first step and a feasible development in the next stage of the integration process. It represents a distinct compromise between the various budgetary options available, rather than using any one approach in a grand design for a developed fiscal union. Furthermore, it is an approach to cohesion which can be introduced at a low level, in recognition of the current political realities, and enhanced as the political cohesion of the Community develops.

#### *Conclusion*

Two themes have dominated this discussion of the EC's medium- and long-term approach to cohesion. The first is the need to take greater account of the social nature of much of the cohesion problem. This can be done both in the definition of eligibility and in the targeting of policy. It

might be argued that the acute disadvantage of certain individuals, families and groups is purely a matter to be dealt with by national policy. However, the same logic would undermine the Community's right to define how member states use the existing structural funds. Such rules dictate that member states create infrastructure (and training) which they would otherwise be unable or unwilling to do. The persistence of acute social disadvantage shows that member states are either unable or unwilling to undertake certain measures. There would be no essential difference between the two. Indeed, there is a clear logic to Community involvement when it is recognised that, while the costs of economic integration are partly regional, they almost invariably fall on particular age, occupational, class and ethnic groups. Furthermore, from the evidence of the 1980s, market integration seems to constrain the ability of nation-states to ameliorate these costs.

A second theme was the need for structural policies to focus on the real barriers to regional economic development. This can only happen "if the historically developed structural conditions which determine uneven development are identified and addressed" (Albrechts, *et al.*, 1989). It is our best judgement on these constraints to development which should guide the allocation of Structural Funds. This developmental perspective is a necessary prelude to capital budgeting based on narrow, and ultimately unreliable, cost-benefit arithmetic. The latter approach tends to go hand in hand with arguments for wider eligibility and weaker additionality requirements. Changes of that sort are also advocated as a solution to problems (of administration and of finding matching funds) which are experienced with the existing Structural Funds. While these problems are genuine ones, the widening of eligibility and the relaxation of additionality may not be the correct solutions. While the widening of eligibility seems to be in line with the insight that regional disadvantage is the result of multiple indigenous factors, it may, in fact, have a damaging effect on structural policy. The reason is that the widening of eligibility, on its own, could exacerbate the central weakness of new forms of regional policy – the proliferation of instruments and the inclusion of too wide a range of expenditures. It could allow regional, national and Community authorities to walk away from the, undoubtedly difficult, problems of identifying the conditions which determine uneven development and devising structural interventions which can genuinely improve the supply-side of weaker regions. Under wider eligibility, Community Structural Funds could, more and more, come to be spent in ways which have little or no impact on the social and economic structures which really inhibit development – while still perhaps failing to focus on the individuals, families and social groups

suffering the greatest disadvantage. Eventually, the Structural Funds, and the idea of Community regional and social policy, could become discredited.

## Chapter 5

### *POLICY RESPONSES AT THE NATIONAL LEVEL*

[Prosperity] must in every nation be regulated by two different circumstances; first, by the skill, dexterity, and judgement with which its labour is generally applied; and, secondly, by the proportion between the number of those who are employed in useful labour, and that of those who are not so employed. Whatever be the soil, climate, or extent of territory of any particular nation, the abundance or scantiness of its annual supply must, in that particular situation, depend upon those two circumstances.

Adam Smith, *Wealth of Nations*, 1776.

Ireland faces two central policy problems. The first is the need to overcome its long-run failure to develop indigenous activity on a scale sufficient to provide for its employment, income and social needs. The second is the fact that, unlike previous generations, Ireland now faces this old challenge with an enormous economic and social problem of unemployment and an overhang of public debt. Only in the very long run are these two problems one and the same. Even if effective policies for the development of competitive indigenous activity were in place, these would not significantly reduce unemployment, especially long-term unemployment, in the medium term. Nor would they address the social problems which derive from unemployment. Although these must be the central goals of policy, it is likely that they require change in a wide range of other policies areas.

This chapter opens with a characterisation of the overall economic policy problem which Ireland will have to solve in the period to 2010. A small economy in Ireland's position requires a macroeconomic framework, a suitable system of income distribution and policies for structural adjustment. While some progress has been made towards meeting these three requirements, there remains a need for the formulation and implementation of policy in many areas. Section (ii) considers what set of procedures and institutions will best encourage the setting of strategic

policy priorities. While some consider recent experiments in tripartite "concertation" or "political exchange" to be an important attempt to overcome the weaknesses of Ireland's political system, others see "national consensus" as positively harmful. Given the importance of this issue, it is relevant to assess the current state of this debate. Although this paper does not contain detailed discussion of specific policies, Section (iii) comments briefly on the two central policy problems, indigenous development and unemployment.

### (i) The Policy Problem at the National Level

The perspective which informs this paper is one which stresses the significance of domestic policy – regardless of the enormous influence of international economic forces. While all countries require effective policies across a wide range, it is possible, in Ireland's present position, to structure this idea in a way which simplifies the problem and highlights the most important issue. That issue is the need for policies which achieve structural adjustment and promote development.

This way of presenting the main policy requirements was recently formulated by the tripartite National Economic and Social Council (NESC). In its report *A Strategy for the Nineties* NESC drew on its study of a number of European countries to identify the requirements for a consistent policy framework in a small, open, European democracy. It is possible to identify three elements of such a consistent policy framework. First, the economy must have an appropriate macroeconomic policy approach. The second strand must be an evolution of incomes which ensures continued improvement in competitiveness, and an income determination system which handles distributional conflicts in a way which does not disrupt the functioning of the economy. Third, especially in open economies, there must be a set of complementary policies which facilitate and, where necessary, promote structural adjustment in order to improve competitiveness.

In recent years Ireland has made progress towards achieving two of these three elements, in the view of NESC. The EMS provides the core of a macroeconomic approach, which seemed to have settled down once domestic monetary and fiscal policy and the evolution of incomes became consistent with the exchange rate policy. Since 1987 income growth has been consistent with improving competitiveness – arguably because the tripartite agreements negotiated in 1987 and 1991 encompassed not only pay but the evolution of the public finances, tax reform, social welfare and, indeed, adherence to the EMS.

However, NESC argued that it is now urgent that Ireland develop the third element of a consistent policy approach – policies for development and adjustment. Consequently NESC made the case for structural reform in the following areas:

- tax reform
- social welfare
- housing
- health
- education
- the management of public enterprises
- industrial policy
- structural policy in agriculture
- special measures to reduce long-term unemployment.

NESC drew on its own work, and that of public commissions and other social scientists, to formulate policies in each of these areas. While there are clear and convincing policy proposals in some areas, such as tax reform, housing and health, there remain considerable uncertainties in other areas – for example, industrial policy, education policy and measures to reduce long-term unemployment. The purpose here is not to discuss each of these areas in detail but to characterise the policy problems which face Ireland in the post-1992 period. To do this we can distinguish between three sets of structural policy areas.

- (a) Those where a clear policy approach exists and is in the process of implementation.
- (b) Those where analytically clear policy proposals have been formulated but which have not been implemented because of political or administrative failure.
- (c) Those where there remains considerable uncertainty and disagreement about what would constitute an effective policy.

The policy problem facing Ireland is formidable because there are a considerable number of policy areas in categories (b) and (c). This fact raises the question of what is the best set of procedures and institutions which can set strategic policy priorities and achieve their implementation (see NESC, 1990).

## (ii) Social Consensus and Strategic Policy Making

### *The Developing Case for Corporatist "Political Exchange"*

In listing the main economic and political factors which will shape Ireland's future, we placed emphasis on the attempt by the social partners and some political parties to develop a system of social and political concertation which allows the resolution of conflicts in the context of coherent strategic approaches. Indeed, consensus among the social partners was seen as an essential element of past success, and a crucial competitive factor in the future, in the national reports prepared by the research institutes in the Netherlands, Belgium, Denmark, Germany and Luxembourg (Jacquemin and Wright, 1993, p.30). However, in Ireland's case the long-run possibility and benefits of this development cannot be taken for granted. Industrial sociologists have raised questions about Ireland's ability to sustain such arrangements and some economists believe that they are positively harmful. In addition, questions are sometimes raised about the democratic nature of national tripartite arrangements. Given the importance of this issue it may be useful to briefly assess the current state of this debate.

The tripartite National Economic and Social Council (NESC) has been the protagonist in articulating the case that Ireland's economic and social performance could be enhanced by the development of a more sophisticated and wide-ranging system of social consensus. The production, within the context of NESC, of a common analysis of Ireland's economic crisis in 1986, and the agreement on a programme to avert further disaster, is widely acknowledged to have been instrumental in facilitating the formulation and implementation of government policies to tackle the public finance crisis (Hardiman, 1993). In addition, those policies were then implemented as part of a formal three-year agreement between the social partners and government, the Programme for National Recovery (PNR). The success of this programme seems to have heightened NESC's interest in a possible link between three elements: the formulation of an agreed analytical understanding of economic and social problems, the implementation of a consensual approach to distributional issues and the ability of government to adopt a strategic as opposed to a short-run, perspective (NESC, 1990). Simultaneously, a number of Irish social scientists had reached the conclusion that "it has taken an inordinantly long time for Irish awareness of European experience to develop and that even yet there are few enough systematic attempts to draw on that experience" (Kennedy *et al.*, 1988).

NESC's interest in social consensus was reinforced by its work on Ireland's membership of the European Community. In reviewing the very poor economic performance through most of the 1980s, it was necessary to consider the role of Ireland's EMS membership. While NESC accepted that, in the years after 1979, macroeconomic policy was too expansionary, it argued, in contrast to the conventional view, that this cannot be a complete explanation of Ireland's experience in the EMS. Focusing on the inertia of pay determination, NESC drew attention to the fact that part of the wage pressure in the early 1980s represented the attempt of workers to recoup tax increases:

This episode illustrates that satisfactory implementation of the decision to join the EMS required not only recognition and acceptance of the macroeconomic policy conditions, nor only acceptance of the implications for wage increases in the private sector, but also consensus on the management of the public finances, especially taxation (NESC, 1989).

This political economy interpretation suggested that, allowing for international developments it was no coincidence that Ireland's membership of the EMS finally began to take hold, and the Irish economy began to recover, precisely when the social partners and government agreed the wide-ranging, three year, PNR.

More generally, NESC's long view of Ireland's experience in the international economy created an interest in the ideas emerging in international political economy. Analysis of the performance of small, European, industrial democracies, such as Austria, Switzerland, Norway and Denmark led Katzenstein to attribute their success to "corporatist" arrangements. These systems of economic and social concertation were said to avoid distributional conflict and enhance the flexibility which is necessary for a small country in a changing international environment (Katzenstein, 1985). It was this developing focus on the role of social consensus which led NESC to commission the recently published study, *The Irish Economy in a Comparative Institutional Perspective* (see NESC, 1990, Chapter 15).

#### *The Nature of and Conditions for Successful Political Exchange*

Industrial sociologists have raised important questions about the potential for corporatist governance in Ireland. Hardiman compared the Irish centralised pay bargains in the 1970s with the patterns of neo-corporatist "political exchange" in Austria, Sweden and Norway (Hardiman, 1988). Important conditions which facilitated concertation in those countries were not met in Ireland. Contrary to what was sometimes



believed in Ireland, the absence of class politics reduced the likelihood of comprehensive agreements. Because of the structure of the economy, Irish employers did not have the cohesiveness which was present in other countries. Most important of all, corporatist agreements require high union density, a unified trade union movement and a high degree of authoritative centralisation on the part of the union federation. Thus, Hardiman's study explained the limited success of national agreements from 1970 to 1981 and raised doubt about the potential for future development. Her identification of the legacy of British patterns of decentralised organisation and collective bargaining, as a constraint on the capacity of the Irish Congress of Trade Unions (ICTU) and, through that, on the likelihood of genuine and productive "political exchange" or concertation, was shared by other students of industrial relations (Breen *et al*, 1990).

There can be no doubt that the structures and procedures which sustain national tripartite arrangements were weak in Ireland *when compared with the classical corporatist models*. But this may not warrant the conclusion that effective further development of such arrangements is unlikely. A number of factors suggest that "the choice between politicised industrial relations and the autonomous industrial relations envisaged by liberal theory remains open to trade unions, employers and the State" (Roche, 1992).

First, although Irish industrial relations have not traditionally conformed closely to the classical corporatist model, they have certainly not moved in the direction predicted by "liberal theory", a direction which might foreclose the possibility of corporatist "political exchange". Roche's study of the development of Irish trade unionism reveals "the degree to which the Irish case deviates from the liberal pluralist prediction of an increasingly sectionalist trade unionism fragmented by occupational interests and progressively less capable of conceiving of itself as a 'movement' transcending the immediate priorities of its many component groups" (Roche, 1992, p. 309).

In addition, a number of recent developments, in both Ireland and elsewhere, might be considered to weaken earlier scepticism. Amalgamations of Irish trade unions have continued apace in recent years. In 1987 and 1991 the trade union movement entered three year agreements with employers and government. Both the PNR and the Programme for Economic and Social Progress (PESP) further advanced the earlier trend to politicisation of industrial relations. Most important of all, the political exchange covered a wide agenda – including pay, taxation, social policies, public finance management and adherence to the EMS

parity – some of which are collective goods of a distinctly class-related character. (NESCS, 1989; Roche, 1992). Indeed, ICTU consciously articulated a long-term strategy which drew on the models of “political exchange” developed in other European countries (Roche, 1992; Hardiman, 1992). The establishment of the Central Review Committee would seem to have improved the effectiveness of tripartite concertation, and may go some way to overcoming the ineffectiveness which tends to arise from the short-term orientation of some Irish political parties and the general localism and particularism of Irish politics (Hardiman, 1992; Mjøset, 1992). Hardiman notes these and other features of the PNR and PESP, which “mark them off from the agreements of the 1970s” (Hardiman, 1992).

The difficult international economic circumstances of the 1980s drove many countries – such as Australia, Spain, Portugal and Greece – to experiment with the introduction of centralised agreements. In her recent review, Hardiman makes the point that “an analysis which is less focused on Northern Europe and Scandinavia reveals that Ireland was far from unique in seeking a centralised solution to economic difficulties during the 1980s” (Hardiman, 1992). At the same time, the emergence of new types of economic problems in the advanced Northern European countries put long-standing systems of industrial and economic governance under extreme pressure. These two sets of developments would seem to have a number of consequences for the assessment of the prospects of social concertation in Ireland. They suggest some revision of our ideas on both the *conditions for* and the *nature of* corporatism. Indeed, many now reject a general or uniform notion of corporatism (Mjøset, 1992).

The emergence of neo-corporatist arrangements in countries other than the paradigmatic Northern European cases, suggests a review of the conditions which facilitate such arrangements. The requirement for an inclusive or “encompassing” trade union movement seems to remain. But the political conditions may be less restrictive than was previously believed. In her recent review, Hardiman notes that the “political character of the party or parties in power may be important *in either of two ways*”. First, government by a Social Democratic or Labour Party tends to encourage secure arrangements – as in the classical corporatist model. However, Fritz Scharpf has argued that where that does not apply, another political situation can be conducive to neo-corporatism: a narrow ideological distance between political parties, especially on how to manage the economy. This tends to encourage stable and long-run agreements between economic interests, because it reduces the likelihood that a change of government will cause a sharp reversal of economic policy – as, for example, it tends to do in Britain (*ibid*).

The developments noted above also suggest some revision of earlier notions on the *nature* of corporatism. Reviewing the experiments in Southern Europe and Australia, Hardiman notes that "the terms of the agreements in each of these countries differed in a number of ways from the stable neo-corporatist practices established elsewhere in an earlier and economically more buoyant period – and this was true of the Irish experience in the late 1980s as well" (Hardiman, 1992). Likewise, in discussing Australia, Sweden and Germany, Mjøset, drawing on Scharpf, says that "if we prefer to use the term corporatism, we must be aware that the term has entirely different implications in the 1970s than in the 1980s" (Mjøset, 1992). The essential difference is that, in the 1980s, national demand management was greatly constrained and wage restraint, instead of protecting full employment, facilitated redistribution in favour of capital. Thus corporatist arrangements are much more defensive, from a union point of view, than they were in the earlier period.

This fragmentation of the meanings of corporatism, and widening of the conditions which can facilitate it, strongly suggest that we cannot dismiss the possibility of significant further development of the "political exchange" begun in the PNR and the PESP – a view which now seems to be shared by students of industrial relations (Roche, 1992, p.326; Hardiman, 1992, p.357). The nature of possible further developments is considered presently.

#### *The Case Against National Consensual Arrangements*

If these developments confirm at least the *possibility* of more developed tripartite arrangements, what of its *desirability*? In our characterisation of the overall policy problem at the national level we have reported elements of NESC's case for such a development and we have noted the positive evaluation of the PNR by industrial sociologists. By contrast, some economists are hostile to these developments. This case has been outlined by Durkan (1992). He states his premise explicitly:

....income policies should move wages closer to the market clearing wage if there is unemployment... The objective of income policies is to ensure that incomes rise less rapidly than they would in the absence of incomes policies (Durkan, 1992, pp. 347-8)

This premise is the basis on which Durkan's evaluation rests.

If they are to be fully successful then one would expect sustainable full employment, though this could result from a well functioning labour market...The Irish economy has consistently exhibited high

unemployment... This fact, in itself, suggests that incomes policies were not successful in Ireland, though it is always possible to argue that particular circumstances prevailed (Durkan, 1992, p.349).

Both the premise and conclusion of this argument require careful consideration.

The premise seems only partially correct: even in Ireland, centralised pay agreements frequently have the objective of *increasing* the incomes of certain, weaker, groups, above what the market would produce. In other countries, incomes policies have had many objectives other than income restraint – as the literature on corporatism makes clear (see Hardiman, 1988; Mjøset, 1992). To infer the failure of income policies from the continuing existence of high unemployment in Ireland is not compelling. The fundamental and long-standing development problems of the Irish economy, which account for much of the unemployment, can hardly be seen as “particular circumstances”.

To advance a case against the PNR it would be necessary to show that the regime of decentralised bargaining from 1982 to 1987 was preferable to the regime of consensus since then. Durkan points out that the breakdown of centralised bargaining did not result in an outbreak of industrial disputes. However, when faced with the dismal economic performance which this period of freedom from centralised and politicised bargaining produced, it is necessary to appeal to a very “particular circumstance”: “the widening of the tax wedge ... still led to wage increases being excessive relative to output prices” (Durkan, 1992, p.358). But, as NESC identified, in an economy and society such as Ireland, this interaction between the public and private sector spheres is inevitable: it is precisely the inclusion of taxation, social welfare, social provision and the exchange rate – i.e., the social as well as the market wage – in the ambit of consensus, that constitute the strongest argument in favour of the PNR and the PESP.

In Durkan’s interpretation, the politicisation of industrial relations and pay bargaining is unambiguously harmful, since it “adds to the bargaining power of trade unionism on an ongoing basis” (Durkan, 1992, p.357). This contrasts sharply with the view of industrial sociologists and with the international literature on comparative political economy. While it cannot be argued that politicisation is *inevitably* or *inherently* beneficial, circumstances can be identified – in the economy, in the structure and consciousness of the trade union movement and in the party political system – in which politicisation is conducive to agreements which resolve distributional conflicts in ways which enhance equity, employment and competitiveness. While no generalised case for politicisation of industrial

relations and distributional issues can be made, the generalised case *against* such politicisation tends to overlook the fact that politics – with its tendencies to clientalism, opportunism and lack of strategic vision – will still exist if pay bargaining becomes decentralised.

Furthermore, without national agreements, income determination will remain a non-competitive, highly collectivised, process, with tendencies to monopoly power on both sides of industry. In his recent study, Mjøset notes that medium sized, decentralised unions may push up wages, whereas, with a strong central organisation, responsible action and concern for solidarity is more likely (Mjøset, 1992, p.331). Indeed, Scharpf argues that even in the 1980s and 1990s, when corporatism has become defensive (in the sense of trading wage moderation for much less than full employment) centralised bargaining can have the important role of ensuring that the costs of retrenchment (cuts in public expenditure, falling real incomes and increasing profit share) are distributed in a “fair” way (*ibid*). The contrast between the social and economic developments in the UK, with decentralised and highly sectional bargaining, and countries such as Sweden and Austria, provides strong evidence for this. The PNR can be seen as having confirmed that Irish unions’ decision to move away from the “British model” was a viable strategy (Mjøset, 1992, p.399). Critics of the very idea of concertation should be prepared to openly embrace that model – since it may be the only realistic alternative to recent experiments with a new system<sup>4</sup>.

What of the argument that recent experiments with concertation are undemocratic and stifle the policy debate? Here again, British models and modes of thought may play a role. The idea that the procedures and institutions of neo-corporatism are undemocratic, would seem to derive from the notion that the Westminster model is the *definition* of democracy. Most continental Europeans have experience of quite different, but no less democratic, models of governance. It is probably too early to evaluate the argument that social consensus stifles policy debate. However, the evidence seems unlikely to support that view. The key factor is the nature of the Irish party political system and its ability, on its own, to articulate and resolve conflicts of value and interest in Irish society. The record is not a good one. It can be argued that both articulation and resolution of conflict has been somewhat improved since 1987.

<sup>4</sup> To be fair, it should be said that trade unionists who oppose all centralised bargaining *are* prepared to openly embrace the British model. Hardiman notes that “the core of organised challenge to ICTU’s strategy continued to reside in the minority of trade unions, largely composed of British-based unions and some Irish-based craft unions, which opposed any departure from ‘free collective bargaining’ as a matter of principle” (Hardiman, 1993, p.153).

*Specific Criticisms and Limitations of Recent Irish Agreements*

While a convincing *general* case against recent Irish experiments with national political exchange remains to be formulated, *specific* criticisms of the content of the PNR and PESP may, of course, be justified. Two issues in particular, cause concern. One is the increasing problem of unemployment and the other is the influence of the public sector pay bill on the public finances. It is argued that the negotiation and administration of Irish national bargains might give higher priority to the problem of unemployment. Failure to do this is sometimes attributed to the fact that *the unemployed do not have direct representation in centralised negotiation*. The PNR and PESP did, of course, encompass key factors which affect the unemployed, such as social welfare and some social provision. One test of the hypothesis that the partners to these national agreements have *no concern whatsoever* for the unemployed, might be to assess what decisions were made in these areas.<sup>5</sup> In general, there is a case for social concertation to encompass as many factors and groups as possible. It is not so frequently mentioned that the PNR and PESP did not encompass the self-employed, the professions, and others – even though the growth of their incomes (and prices) are of material relevance to employers, trade unions, the state and the unemployed, because of the extensive tax expenditures which they receive and the opportunities for tax evasion and avoidance which are available (Hardiman, 1992; O’Connell and Rottman, 1992). If the absence of the direct voice of the unemployed may have allowed those at the national negotiations not to “see” the unemployed, they could scarcely avoid seeing the standards attained by others who are also outside the consensus (while not, of course, being outside the benefits of what O’Connell and Rottman have described as, the “pay-related welfare state”). It seems likely that both absences make it less easy to achieve consensus on wage settlements which would maximise employment.

It should be noted that the apparent inability of the social partners and the state to give absolute priority to unemployment does not make a case against the PNR and the PESP, as such, unless it can be shown that some, realistic, alternative procedure would give higher priority this problem. So far, nothing approaching such a demonstration has been forthcoming from the critics of social consensus. Indeed, criticisms based on the

<sup>5</sup> It might also be informative to compare those decisions with the proposals, on areas of policy which directly affect the unemployed, of some of those most hostile to centralised political exchange.

"absence" of certain groups or individuals from the negotiation of national consensus, tend to alternate randomly between extreme cynicism and extreme idealism. The cynicism arises from thorough-going application of the notion that self-interest predominates in all spheres – including politics. However, self-interest can be shown to be an inadequate explanation of political behaviour -and this inadequacy shows in some discussions of the PNR and the PESP. As Lewin says "on the contrary, it seems as if people are led to act in their political roles on certain 'convictions' about what is best for society as a whole, by certain ideologies" (Lewin, 1991). Although the prevailing view is cynical, occasional recourse to idealism is necessary if critics of "political exchange" are to imagine how, in a world of decentralised, sectional and non-political bargaining, agents who act only in their own-self interest, will take *greater* account of the problems of the unemployed and other marginalised groups. Of course, in truth neither cynicism nor idealism is philosophically or *empirically*, warranted:

Rousseau's belief in the unbounded goodness of human beings is a hypothesis as unnecessary in explaining modern politics as Hobbes self-interest hypothesis is a distortion...An understandable ambition to eradicate the reputation of being naive idealists must not seduce political scientists into denying the findings of their own political research. For the most part men try to further the public interest in politics. But they do so because in the long run such policies are also in their own interest (Lewin, 1991, p.112).

It is not possible to analyse systems of neo-corporatist governance without drawing on the findings of research in industrial sociology and political science.

The second specific criticism of the PNR and PESP concerns public sector pay. It can be argued that, in some years, the rate of increase in the total public sector pay bill is slowing the downward path of the debt/GNP ratio, which all sides agree is necessary, and maintaining the tax burden on the traded sectors. While this argument has some force, it is not sufficient to simply *call for* lower public sector pay across the board, nor is it constructive to see this as a sufficient case for abandonment of the experiment in social concertation. A serious criticism of the public sector pay provisions of the PNR and the PESP, one upon which action could be taken, would require a detailed examination of the structures and practices of the Irish public sector. Attention would have to be given to management, motivation and rewards. Within that analysis, appropriate

weight would have to be given to the justifiable demands and expectations of the wider society – in terms of both finance and service.

The existing achievements and limits of the recent Irish experiments in political exchange are well put by Mjøset in his comparative institutional analysis of the Irish economy.

Based on the positive experience, major collective actors in Ireland began to discuss a long term strategy in which macroeconomic policies aiming at low inflation, low interest rates and control of the national debt would be hopefully combined with fundamental structural reforms, radical tax-reform, and a major offensive to fight long-term unemployment and improve social services. The “social market economy” of Germany was mentioned as one model. While the PNR mainly implied short term coordination, a longer term strategy would need to address the problems of unemployment, emigration, and lack of indigenous industrial development. (Mjøset, 1992. p.384 )

The ability to address these problems will be the ultimate test of recent developments in political exchange. Mjøset’s answer to one of the questions put to him by NESC, concerning consensus, was as follows:

In sum, carrying through this project has convinced us that the general notion of consensus should not be at the centre of the debate about policy learning. If a general formula is needed concerning relations between institutions and growth, it should focus on the inter-relationship between the broader institutional arrangements and the “national system of innovation” surrounding the “development blocks” – the clusters of important firms – of a particular economy (Mjøset, 1992, p.16).

The question then is whether centralised bargaining and political exchange increases or decreased the chance of addressing the problems of unemployment, emigration and lack of indigenous industrial development. The record of the Irish political and administrative system, acting on its own, is very poor indeed. Thus, although Mjøset is surely correct in his advice that we should not put the idea of consensus, *per se*, at the centre of debate, it can be argued that, in Ireland’s case, a suitably developed system of political exchange can assist the formulation and implementation of strategic policies. This is, no doubt, a highly demanding task and implies both a need to learn from the experience of other societies and a need for institutional and political innovation to address the unique combination of Irish problems and structures.



### (iii) Development Policy and Unemployment

The policy areas over which there remains uncertainty are also the two most important issues facing the society: economic development and unemployment. Together, these constitute and define the cohesion problem in Ireland. The purpose of this short section is to highlight this fact and bring out some of the uncertainties which still exist in analysis and policy.

#### *Development Policy*

The recent report of the Industrial Policy Review Group, entitled *A Time for Change: Industrial Policy for the 1990s*, known as the *Cullinton Report*, advocated a range of policy measures to encourage the development of industry in Ireland. The proposals include radical reform of the taxation system (to increase the relative rewards to productive activity and remove fiscal barriers to financial intermediation), a strong shift from state grants to equity, more limited and discretionary support from the state agencies, the development of clusters around sources of national competitive advantage, and the reduction of bureaucratic interference with the operations of commercial state enterprises. What is most striking about these proposals is their similarity to those produced in a number of previous reports, particularly those by NESC in the early 1980s. Indeed, this similarity is noted by the new policy review group. In this context, probably the most significant feature of the *Cullinton Report* itself, and the widespread support for it, is that it signifies eventual acceptance that Ireland has no alternative but to develop a larger and more competitive indigenous industrial sector.

The question then arises: is the development policy problem in Ireland simply one of political and administrative inertia or stalemate? While there are definite political and administrative problems, in this as in other areas, it would be a mistake to assume that this adequately characterises the situation. Indeed, the fact that "the policy shift has not been as decisive in practice as it has on paper" (IPRG, 1992, p. 62) would seem to reflect both administrative *and analytical* uncertainty about the alternatives to grant aid and the attraction of foreign direct investment (FDI). While the focus of both NESC and the *Cullinton Report* on access to seed and venture capital, marketing, technology and management, seem well founded (and certainly worth a try) there remains a sense that we do not understand in sufficient detail the origin and cause of Ireland's development problem. To a considerable extent, the historical focus of policy and resources on foreign-owned branch plants has been a reflection of the practical

difficulties of promoting indigenous firms, rather than a conscious policy decision (though some constitutional optimist can always be found to support FDI as *the* route to economic development).

Indeed, within a relatively stable overall policy approach, the emphasis of policy can be seen to have shifted from a focus on capital-shortage, to marketing, technology and management – partly in response to changes in the international business literature. In recent years, under the influence of increased Structural Funds, official emphasis has shifted to peripherality. But this tends to be conceived in a purely spatial way, leading to a strong emphasis on transport costs and transport infrastructure with little consideration of their role in *development*. An important requirement now, is research which will assist a structuring of the multiple factors which undoubtedly influence the competitiveness of Ireland's indigenous sectors. The development agencies – the Industrial Development authority, EOLAS, the Irish Trade Board and SFADCO – have recently initiated a new collaborative venture with each other and the ESRI. The establishment of an Industrial Development Research Centre, funded by these agencies, at the ESRI, is an attempt to create a programme of research with a focus on industrial policy. Work is being undertaken on the linkages between manufacturing and services and on Ireland's competitive advantage. However, the total resources available for this work, and hence the total research effort, remains limited, given the importance of the issue to Ireland's long-run development. Some comments on the issues which this throws up are made in the concluding chapter.

### *Unemployment*

The second major task facing Ireland in the 1990s and the new century is the problem of unemployment. This must be seen as an independent social and economic problem, because even a dramatic improvement towards the development of competitive indigenous activity will not, of itself, solve the existing crisis of unemployment. The structural and other policies designed to assist competitiveness – such as reform of taxation, social welfare, housing and the management of public enterprises – will have beneficial, but limited, immediate effects on employment and unemployment. The process of developing indigenous competitive advantage itself, is a long term one and cannot be expected to reduce unemployment in the medium term – a point emphasised by Kennedy (1992a). In the very long run, of course, a vibrant productive sector, combined with appropriate manpower and other policies, can ensure low unemployment. It is not possible in this paper, to present a detailed discussion of policies to reduce unemployment. The points outlined below

are intended merely to argue that Irish social scientists and policy makers should continue to actively consider policies which might substantially reduce unemployment.

The combination of very high levels of unemployment since the mid-1980s, and a series of theoretical and empirical studies, have resulted in considerable fatalism about unemployment – both in the society and among social scientists and policy makers. In order for action to be taken to significantly reduce long-term unemployment, it is necessary that this fatalism be overcome. But this is difficult to do; it seems to have become accepted that there is no intellectually respectable argument that unemployment can be significantly reduced. One effect is that economists and policy makers can cease to look for ways of reducing unemployment.

It is argued here that although experience and research do teach us many negative lessons about policy, a somewhat different slant can be put on much of this work. That slant is one which suggests careful interpretation of the negative evaluation of past and existing policies and which tries to use these negative evaluations to point us to policies which can work.

Two areas of policy are of particular relevance in this respect: training and special employment measures. In the case of training it seems necessary to distinguish between its three possible roles: long-run enhancement of productivity and competitiveness, *maintenance* of low levels of unemployment as a part of an active labour market policy and rapid *reduction* of high levels of long-term unemployment. In the case of special employment measure there is a need to clarify whether targeted labour subsidies and direct employment creation can be greatly extended.

During the 1980s, Ireland, like most EC member states, relied increasingly on training as the main policy response to unemployment. This change of policy emphasis would seem to have more to do with abandonment of demand management, income policies, employment subsidies and public works, than with any convincing case in favour of training. Training will only reduce unemployment when unemployment is due to a mismatch between the skills of the unemployment and existing vacancies. Since only a fraction of unemployment in Ireland, or Europe, would seem to be of this type, it follows that training will only reduce unemployment if it is accompanied by some policy measures which increase the demand for the labour of those undergoing training. This is not a case against training the long-term and young unemployed; but it should be accepted that this, on its own, is not a policy to reduce unemployment – except in one sense which is mentioned below.

This reliance on training may also have been reinforced by the perception that other approaches – particularly special employment

measures – do not succeed in reducing unemployment. Three types of special employment measures should be distinguished: employment subsidies, direct job schemes and enterprise or self-employment schemes. International and Irish research has raised doubts about the ability of these measures to reduce unemployment. Evaluation studies have shown that most recruitment subsidies carry heavy *deadweight* costs, i.e., many subsidised jobs would have been created anyway (Breen and Halpin, 1989). Job creation schemes do not create deadweight effects, nor do they displace existing employment; the problems identified with these schemes are that they are *temporary* and *cost* more than unemployment assistance (Breen, 1990). Schemes which provide financial support to unemployed persons in order that they can establish their own enterprises, have also been evaluated negatively. Research suggests a heavy *displacement* effect, such that a large proportion of the new business is taken from other Irish enterprises (Breen and Halpin, 1988).

If a conceptual approach to reducing unemployment is to be found, it may lie in careful re-interpretation of these research findings and combining them with the findings from other research. Let us begin by stating a number of key proportion which seem to have been verified in both the British and Irish cases:

- (i) The long-term unemployed play no role in restraining wage pressure. High long-term unemployment does not create the downward pressure on wages which might help to eliminate it.
- (ii) For a variety of reasons there is a strong element of *hysteresis* in unemployment, i.e., if unemployment becomes high it will tend to stay high and if it becomes low it will tend to stay low (Barry and Bradley 1990).

To these can be added an important element from research on the HERMES macroeconomic model.

- (iii) The Irish economy displays strong migration and labour supply mechanisms, such that an increase in general demand for labour will be met largely by return migrants and new entrants to the labour market (Bradley and Fitz Gerald, 1991).

These three propositions all suggest the need for, and significant benefits from, increased demand for labour which is *targeted on the long-term unemployed*. On the basis of propositions (i) and (ii) Layard and others –

who have developed the most widely accepted explanation of British unemployment – developed the case for a massive extension of special employment measures in the UK, including labour subsidies targeted on the long-term unemployed (Layard *et al*, 1986; Layard, 1986). This argument suggests that against the deadweight effects of labour subsidies must be weighed the hysteresis effects – effects which might not be picked up in existing evaluation studies, because of the small scale of most of the schemes in existence. To look no further than the deadweight effects is to assume that a person who spent a year on a programme has no better job prospects than if he or she were still unemployed. Similar interpretation may apply to negative research findings on job creation schemes. These unavoidably ignore the hysteresis effects and cannot test the possibility that direct hiring, *in combination with a range of interventions* in the economic and social environment, could produce a permanent effect from temporary schemes. Likewise, training of the long-term unemployed which merely *redistributes* job chances, might be worthwhile. In all these cases, recognition of the tendency to *redistribute* job chances can be seen, not as a case against special employment measures, but as reinforcement of the need to *target* the schemes on particularly disadvantaged groups.

This discussion is not intended to suggest that labour subsidies and direct hiring should be massively extended; detailed costing and other work is necessary. What it says is that it may be mistaken to see existing evaluation studies as a reason to stop analytical and practical exploration of ways of reducing long-term unemployment. A similar view was presented by NESF in *A Strategy for the Nineties*. This orientation is also found in a forthcoming American book on poverty. Reviewing three decades of poverty research, Haverman and Sawhill ask “why does the policy analysis community seem so disheartened, so inclined to ply their disciplinary trade rather than to identify, to think through, to hone down bold new policy designs for both scholars and policy makers to assess and debate?” (Haveman and Sawhill, 1993). They suggest a number of explanations which open the way to a different orientation to the same research results. First they suggest that policy retrenchment and political rhetoric may have undermined belief in the potential of public intervention. Second, most evaluation studies assess the effects of *marginal* interventions (such as labour subsidy or job schemes) on *one* variable (such as employment or unemployment):

But what if the production function is “synergistic” or additive? What if a jolt of job training by itself – or a jolt of day care by itself, or housing, or job creation, or police protection, or health care, or income support

by themselves – yield little if any impact on poverty, as many evaluations have found? But, conversely, what is a major dose of a *constellation* of these measures taken together, could yield major increases in esteem, productivity, responsibility and income among the poor? ... Yet if such synergies and potentials for taste and motivation changes do exist, our methods would fail to discover them. And, as a corollary the policy suggestions which follow from our studies would fail to reflect them (Haveman and Sawhill, 1993, pp.11-12).

This overview of American research on poverty expresses well the orientation to Irish unemployment which is tentatively suggested above. Rather than claim that particular policies can achieve a significant reduction in unemployment, it is claimed merely that, properly interpreted, existing evaluation studies do not *dictate* a drift to fatalism and that there are intellectually rigorous reasons to continue active debate and experimentation on how to significantly reduce unemployment. One concrete implication, of course, is that (as history shows) large scale reduction in unemployment requires more than marginal schemes. Large scale measures cost large amounts of money. This further pushes the issue beyond the realm of existing evaluation schemes, back to the political sphere where it properly belongs. Fatalism about unemployment, whether it is generated by analysis or politics, or both, has one convenient effect for those in employment – it prevents anyone asking whether we are willing to bear the cost of the large scale and many-sided measures which might achieve a large reduction in unemployment.

## Chapter 6

### CONCLUSIONS

Many of the arguments resemble the question of the precedence of the chicken or the egg. The establishment of a successful monetary union may well require support from a strong, centralised, or at least inter-regionally co-ordinated, fiscal (and regional) policy to ease the complications of regional adjustment. Yet it is difficult to establish a centralised fiscal authority unless there is monetary union, a single currency...It seems unlikely then that a fixed exchange-rate system can be maintained until political harmony and social agreement allow the division of burdens within the area and the direction of policy in each major part of the system to be decided by an accepted central *political* authority.

Charles Goodhart, *Money, Information and Uncertainty*, 1989.

Confusion arises from the attempt to balance a global and a local perspective. We are constantly reminded of our global inter connectedness, but we live our lives at the local scale. The cultural anthropologist Paul Rabinow has referred to the awareness of this dualism as "critical cosmopolitanism:" We share ... a specificity of historical experience and place,... and a worldwide macro-interdependency. Although we are all cosmopolitans, *homo sapiens* has done rather poorly in interpreting this condition. We seem to have trouble with the balancing act, preferring to reify local identities or construct universal ones. We live in-between.

Nicholas Entrikin, *The Betweenness of Place*, 1991.

#### (i) Factors Shaping the Future of Ireland and the European Community

This paper is part of a 12 county study of the economic, cultural and political factors which will shape the development of the European Community in the years to 2010. In identifying these factors the guiding conception has been the idea that despite small size and great openness of

the Irish economy and society, the effects of international forces will be mediated by indigenous social, economic and political factors. Likewise, despite the large size of the European Community, and some of its member states, its development will be significantly shaped by external factors. Movements towards an interactive outlook of this sort can be identified in a range of social sciences in recent years.

The evolution of both the European Community and Ireland will continue to be influenced by a range of international factors. These will include economic, cultural and political forces. The international economic environment is likely to be one of continuing crisis and change. The important factors include technological change, the globalisation of manufacturing industry, profound changes in the structure of finance, changes in the geographical patterns of production and uncertainty about the principles of macroeconomic management. These are a set of inter-related phenomena, reflecting the breakdown of the post-war "golden age" and the failure of a stable new pattern to emerge. An important feature common to technological change, financial developments and macroeconomic volatility and uncertainty is the increase in international interdependence. Other international economic factors which will shape development in both the EC and Ireland include the liberalisation of agriculture, EC enlargement and the re-establishment of capitalism in Eastern Europe.

Two international cultural factors may be significant for the Community and Ireland's prospects within it. The first of these, inward migration into the EC, heightens the significance of the second, European identity. The important international political factors include the collapse of the Soviet Union, German Unification, EC enlargement and North-South relations.

Factors which are likely to be of specific relevance to Ireland are discussed in Chapter 3. The most important of these is the structure of Ireland's agricultural and industrial sectors: these structures will shape Ireland's response to international developments. Ireland's evolution will be shaped as much by the geographical and organisational *pattern* of the international economy as by its overall rate of *growth*. Other important socio-economic factors include demographic developments, the emerging social class structure with its high rate of unemployment, the pressure of public finance, migration and developments in agricultural regulation. It is possible to identify a range of cultural factors which will combine to shape the lives of Irish people. While these have an economic dimension, it remains difficult to identify whether that economic dimension includes causation which runs *from culture to economic performance*. Two aspects of domestic politics may be important if Ireland is to achieve its major



economic and social goals: the development of a national political process capable of formulation and implementing strategic policies and development of a more independent system of local government and democracy. A third political factor is the conflict in Northern Ireland. Research on this project included some examination of the potential for economic integration and co-operation between the Republic and Northern Ireland. The findings of that work are to be published separately. Chapter 3 ends with a short account of an important and evolving debate on the interaction between economic, cultural and political factors in Ireland's long-run economic failure. Attention is drawn to the recent work of Mjøset (1992) which attempts to synthesise a range of detailed existing studies on each of these factors. The idea of a "national system of innovation" emerges as a useful organising concept, but it is clear that we have very limited detailed knowledge of the particular system in Ireland in the 1990s.

#### (ii) Challenges for the European Community

Consideration of the international and national factors reveals that the European Community faces a demanding internal agenda, containing the internal market programme, EMU, cohesion, social Europe and the formulation of guiding values. It faces an uncertain and, in many ways, threatening external environment because of developments in central Europe, the Mediterranean, enlargement, North-South relations and environmental decay.

This internal and external agenda implies a definite overload of the Community's institutions and decision making procedure. An important question, then, is whether the EC should abandon certain problems and goals in the hope of getting a smaller agenda under control. In fact, this seems unlikely to work. The Community cannot abandon the central internal and external problems of its economic strength. To say that economic strength has to be a central priority is not to suggest that it is an *alternative* to political union, but to see it as a *condition* for such union. At the same time, an unqualified emphasis on the economic strength of the Community is likely to be self-defeating, since it will be unable to earn the consent of European citizens to the policies pursued, or even to the idea of formulating policy at Community level. Although this argument implies that the internal and external, and the economic and the political, are inextricably intertwined, it is possible to identify four concrete challenges for the Community: change in the EC's decision making system,

development of the European social market model, competitiveness and macroeconomic management.

The well known problems with the authority, effectiveness and legitimacy of the Community's system of governance are noted in Chapter 2. Improvements on all these dimensions are an absolute precondition for facing the challenges of the European social market model, competitiveness, and macroeconomic management. In the face of these challenges, it is striking that the Community remains so constrained by its decision making, and, ultimately, its political system. Intergovernmentalism transforms what should be issues of *politics* into issues of *diplomacy*. The method of dealing with each differs, traditionally, in a number of ways. One of these is the centrality of *values* in ordinary political discourse and competition, and centrality of "national interests" in diplomacy. The conduct of Community politics through the latter method has two drawbacks. First, the "national interests" represented by member states can less and less encompass the real interests in European society, and hence their debate does not bring the real forces and issues to light. Second, the Community, its agenda and its debates, cannot engage the allegiance of the citizens, and the absence of values from its discourse leaves the field to ethnic and other ideologies. The fact that a common response to these problems is the call for *less* decision making at Community level, illustrates the depth of the crisis into which the Community has moved. It should also remind us of the possibility, well-known both historically and analytically, that systems of intergovernmental relations are quite capable of producing sub-optimal, and even disastrous, outcomes for all parties.

The second priority listed above – the development of the European social market model – derives from the discussion of European identity, in Chapter 3, as well as from consideration of the economic and social factors which will shape Europe's future. Despite certain rhetorical claims, it seems difficult to define a European identity in terms of democracy, liberalism and tolerance. The report by the French team to the "shaping factors" project argues persuasively that the social market economy, and the existence of a powerful welfare state, is the real distinguishing feature of the European model. If this is so, it raises serious questions about the chance of developing a European identity upon which economic, monetary and political union can be built. To date, the Community has proven largely unable to deal with the implications of European integration for the welfare state. In addition, quite apart from differences in systems of social rights within the EC, there are threats to welfare states generally. These threats are political, but also economic and demographic. This perspective suggests that, taking a long-term strategic view, one of the

major challenges for the European Community is to redesign systems of social rights and welfare in ways which facilitate increased competitiveness and sustained growth of the European economy. This challenge also combines economic and political dimensions.

The third challenge is the competitiveness and economic strength of the Community. This can be seen as a necessary condition for both political union and the continuation of the European social market model. A key question is whether their completion of the internal market is sufficient to re-establish the competitiveness of Europe *vis a vis* the US and Japan and to unleash long-term forces of innovation and economic growth. Although opinions differ on this question, many believe that neither history nor theory suggest that negative integration is sufficient. If further Community policies are necessary – in areas such as technology, infrastructure, manpower or the governance of industry generally – then the identification, agreement and implementation of such policies is a significant long-run challenge. Once again both the economic and political dimensions interact.

The fourth long-run challenge also combines economic and political problems. The economy of the European Community requires macro-economic management; the interdependencies between the national economies mean that this cannot be done effectively at national level, and that the attempt to do this will increase volatility and, ultimately, produce a sub-optimal outcome for all. Some believed that the Maastricht Treaty obtained a blue print capable of providing a system of macroeconomic management for Europe, including a stable transition to EMU. It is now clear that this was not so. Not surprisingly, there are different interpretations of what is wrong with the treaty (including EMS). In few cases will those interpretations differ from positions taken before the crisis which broke in September 1992.

The current position would seem to fit perfectly Goodhart's description of a chicken and egg situation (quoted at the head of this chapter). Although economic integration is generally a gradual process, monetary and macroeconomic integration may not be amenable to this gradual advance (Honohan, 1991). Both because of the nature of monetary reforms, and because of the close link to political power, it may be necessary to proceed in a different way. But the combination of rapid movement to EMU and prior agreement on the creation of a central political authority, have proved too much for the Community in the early 1990s. The Maastricht Treaty provided for neither. While some will consider that it provided for too much, this perspective suggests that it provided for too little. The establishment of a system of macroeconomics

management capable of sustaining growth will remain a major challenge for the Community, in both its internal and external affairs, in the years to 2010.

### (iii) Challenges For Ireland

There can be no doubt that the two greatest challenges facing Ireland are the reduction of unemployment and the development of competitive indigenous economic activity on a scale sufficient to meet its social, economic and employment needs. However, as in the case of the European Community, these cannot be seen as purely economic challenges to which technocratic solutions can be found. They are, above all, political challenges; they also have definite social and cultural dimensions. Their solution will require action on many fronts and change in a wide range of existing arrangements. Consequently, although unemployment and indigenous development are the two ultimate challenges, contemplation of solutions to them requires that some intermediate challenges and issues be considered first.

The requirements for a consistent economic policy framework in a small, open, European democracy can be seen as having three interdependent elements. First, the economy must have an appropriate macroeconomic policy framework. The second strand must be an evolution of incomes which ensures continued improvement in competitiveness, and an income determination system which handles distributional conflicts in a way which does not disrupt the functioning of the economy. Third, especially in open economies, there must be a set of policies which facilitate and promote structural adjustment in order to maintain competitiveness in a changing international environment. In 1990, NESc argued that Ireland had made progress towards achieving two of these three elements. The EMS provided the sheet-anchor of the macroeconomic approach and a national agreement on pay, taxation, social welfare and social provision, determined distribution. There was, NESc argued, an urgent need to develop policies for development and adjustment. To this end, NESc drew on its own work and that of many others, to suggest structural reform in taxation, social welfare, housing, health, education, the management of public enterprises, industrial policy, structural policy in agriculture and special measures to reduce long-term unemployment.

The dominant challenges of unemployment and indigenous development suggest that two of the three elements of the policy framework require considerable further development. The systems which

determine income distribution, in the widest sense, need to be further attuned to meeting these central challenges. Policies for structural change and indigenous development remain very incomplete. Little progress has been made in reducing long-term unemployment.

In addition, recent developments raise some doubts about the first, macroeconomic element of the policy framework. The issue is not whether Ireland should leave the EMS, but whether that system, in combination with the prevailing conduct of fiscal policy in Europe, can provide a stable but buoyant environment during the 1990s and whether it can progress to EMU by the beginning of the next century. Furthermore, since the three elements of the domestic policy framework are interdependent, any loss of the EMS sheet-anchor could disrupt both income distribution and structural policies.

Assuming that the macroeconomic framework stays in place, the need for further development in income distribution, structural policies for indigenous development and measures to reduce long-term unemployment, raises another intermediate challenge. What approach to policy formation will maximise Ireland's ability to identify and implement strategic policies in these and other areas? Does the system of centralised bargaining and "political exchange", developed in the PNR and PESP, help or hinder progress on the central challenges of unemployment and indigenous development? While NESC has developed the case for social consensus, industrial sociologists have raised questions about Ireland's ability to sustain an effective system of neo-corporatist political exchange, and some economists have argued that they are positively harmful. In addition, questions are sometimes raised about the democratic nature these arrangements. The current state of this debate is reviewed in Chapter 5.

Support for centralised bargaining and tripartite policy formation in Ireland is based on a set related arguments. These include belief in the benefits of an agreed analytical understanding of economic and social problems, recognition of the role of taxation and social provision – the social wage – in bargaining between employers and unions and, perhaps most important, doubts about the ability of the Irish party political system, on its own, to formulate and implement strategic policy approaches. While some industrial sociologists doubted that the economic, trade union, and party political structures in Ireland could support an effective system of neo-corporatist political exchange, recent developments would seem to have modified this view. The general case against recent centralised programmes on pay and policy is based on their failure to produce full employment and opposition to any politicisation of industrial relations.

The critics have, however, failed to explain how, freed from centralised and politicised bargaining, partly politics will produce better economic management and decentralised, sectional, pay bargaining will give higher priority to the unemployed and other marginalised groups.

While a convincing *general* case against recent Irish experiments with national "political exchange" remains to be formulated, the real question is whether this system can enhance Ireland's ability to meet the two outstanding challenges, unemployment and indigenous development. The tripartite system may well be more effective than the Irish party political and administrative system, acting on its own. However, this does not mean that the tripartite system can mount a real challenge to unemployment and lack of indigenous development. This depends on the willingness and ability of the participants to analyse these problems, negotiate serious policy changes and deliver on these. This is a highly demanding task. It implies both a need to learn from the experience of other societies and for institutional and political innovation to address the unique combination of Irish problems and structures.

On unemployment, the argument of this paper is that, to an extent, this should be seen as a separate problem from the task of indigenous development. This is so, because the development of competitive indigenous activity is a long-term task which will not reduce unemployment in the years to come. A significant reduction of unemployment during the 1990s will only occur if additional policies are put in place. The policies which might be considered capable of reducing unemployment are training and special employment measures, such as labour subsidies, direct job creation schemes and enterprise or self-employment schemes. Although some schemes of each of these types are in existence, there is clearly considerable fatalism – among policy makers, social scientists and in the society – about the possibility of significantly reducing unemployment.

This fatalism may, in part, reflect increased reliance on training and loss of faith in special employment measures. One way of breaking out of this situation may be, first, to distinguish between the different roles which training can play, second, to review and re-interpret the negative evaluations of special employment measures and, third, combine these findings with other important insights into the nature of the Irish economy. This would show that although training has a central role in developing competitiveness in the long run, and can greatly assist in *maintaining* a low level of unemployment, it has, on its own, very limited power to *reduce* high levels of unemployment. This requires that there be an increase in the *demand* for the labour of those being trained. Such an increase can be generated by labour subsidies or direct job schemes. But

evaluation studies suggest that labour subsidies have a large *deadweight* effect and direct hiring is both *temporary* and *costly*, and this seems to have undermined faith in the ability of these, and any other public policy, to significantly reduce Ireland's unemployment.

It is possible, however, that this loss of faith is excessive and that active debate of policies to reduce unemployment should be continued. The results of the evaluation studies can be interpreted as highlighting the need for measures which are *targeted* on the long-term unemployed. The evaluation studies cannot capture the *hysteresis* effects which Irish and international research suggests are present. More generally, it may not be correct to use marginal studies of marginal schemes to draw negative conclusions about the possible effects of large scale and multi-dimensional schemes. While this paper does not make the case for any particular approach (detailed costing and planning would be necessary) it does seem that the debate on the use of training, labour subsidies and direct job schemes to significantly reduce unemployment, may have been closed prematurely.

There is now widespread agreement that Ireland must develop competitive indigenous activity on a significantly larger scale if it is to meet its long-term income, social and employment aspirations. There is also agreement on a number of the principles which should guide action and the policies which should be implemented: reform of the tax system, improvements in infrastructure, a switch from grants to equity and greater focus on industrial clusters. There is less agreement on the reforms of education and training proposed in the *Culliton Report*. This suggests three distinct challenges: implementation of the measures which are widely agreed, further exploration of the role of education and training in the Irish economy and analysis of how, in Culliton's words, to use policy "selectivity to establish industrial clusters around sources of national competitive advantage".

The emphasis on clusters in the *Culliton Report* is a significant step forward. The Industrial Policy Review Group drew heavily on Porter's observation that "nations succeed not in isolated industries but in *clusters* of industries connected through vertical and horizontal relationships" (Porter, 1991). The significance lies less in adoption of Porter's particular idea of clusters, or in use of his formula for identifying national competitive advantage, than in opening Irish policy and discussion to some general trends which have been identified in numerous countries and analysed in various ways. All of these would seem to have in common the following general propositions.

- (i) All firms and industries are not of equal significance to a country's long-term competitiveness.
- (ii) The economy should not be seen as just a random collection of firms and industries. Certain *aggregations* of firms and industries are significant in creating competitiveness.

These propositions suggest the following questions:

- (i) On what basis do we judge some industries more significant than others, and what industries emerge as *key sectors* for Ireland?
- (ii) What existing, or potential, aggregates of firms and industries are relevant to Ireland's competitiveness?

Finding answers to these questions, and acting on the basis of those answers, is the challenge which faces Ireland if it is to develop competitive indigenous activity.



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