NATIONAL ECONOMIC AND SOCIAL COUNCIL

An Investment in Quality: Services, Inclusion and Enterprise

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ABBREVIATIONS

ADM	Area Development Management
AER	Alternative Energy Requirement
ALMPs	Active Labour Market Policies
APSS	Approved Profit Sharing Schemes
ARFs	Approved Retirement Funds
AWU	Annual Work Unit
BERD	Business Expenditure on Research and Development
BGE	Bord Gáis Éireann/Irish Gas Board
BIG	Benchmarking and Indexation Group
BMW	Border Midlands and Western Region
CAP	Common Agricultural Policy
CAT	Capital Acquisitions Tax
CB	Child Benefit
CCI	Chambers of Commerce of Ireland
CDAs	Child Dependent Additions
CDB	City/County Development Board
CE	Community Employment scheme
CEPR	Centre for Economic Policy Research
CER	Commission for Energy Regulation
CGT	Capital Gains Tax
CHIU	Conference of Heads of Irish Universities
CHP	Combined Heat and Power
CIF	Construction Industry Federation
CLÁR	Ceantair Laga Árd-Riachtanais – National Targeted Investment Programme in Rural areas
CORI	Conference of Religious of Ireland
CPA	Combat Poverty Agency
CPI	Consumer Price Index
CSF	Community Support Framework
CSO	Central Statistics Office
CSW	Commission on Social Welfare

CWC	Community Workers' Co-operative
DART	Dublin Area Rapid Transit
DSL	Digital Subscriber Line
DTO	Dublin Transport Office
DWS	Developmental Welfare State
EC	European Community
ECHP	European Community Household Panel
ECJ	European Court of Justice
EEA	European Environment Agency
EGFSN	Expert Group on Future Skills Needs
EMS	European Monetary System
EMU	Economic and Monetary Union
EOCP	Equal Opportunities Childcare Programme
EPA	Environmental Protection Agency
ERM	Exchange Rate Mechanism
ESB	Electricity Supply Board
ESF	European Social Fund
ESIOP	Economic and Social Infrastructure Operational Programme
ESPAD	European School Survey Project on Alcohol and Drugs
ESRI	Economic and Social Research Institute
EU	European Union
FDI	Foreign Direct Investment
FDS	Flexible Development State
FIS	Family Income Supplement
FTE	Full-time Equivalents
GAIE	Gross Average Industrial Earnings
GDA	Greater Dublin Area
GDP	Gross Domestic Product
GGB	General Government-Balance
GNDI	Gross National Disposable Income
GNP	Gross National Product
HBS	Household Budget Surveys

HEA	Higher Education Authority
HICP	Harmonised Index of Consumer Prices
HR	Human Resource
HRM	Human Resource Management
IBEC	Irish Business and Employers Confederation
ICMSA	Irish Creamery Milk Suppliers Association
ICOS	Irish Co-operative Organisations Society
ICSTI	Irish Council for Science, Technology and Innovation
ICT	Information and Communications Technology
ICTU	Irish Congress of Trade Unions
IDA	Industrial Development Agency
IFA	Irish Farmers Association
ILO	International Labour Organisation
IMF	International Monetary Fund
INOU	Irish National Organisation of the Unemployed
IP	Intellectual Property
IPA	Institute of Public Administration
IPPR	Institute for Public Policy Research
IRN	Industrial Relations News
IT	Information Technology
JLC	Joint Labour Committee
LIIS	Living in Ireland Survey
MCA	Multi-Criteria Analysis
MIF	Management Information Framework
MNC	Multinational Corporation
MWs	Megawatts
NAPincl	National Action Plan for Social Inclusion
NAPS	National Anti-Poverty Strategy
NCPP	National Centre for Partnership and Performance
NDA	National Disability Authority
NDFA	National Development Finance Agency
NDP	National Development Plan
NEAP	National Employment Action Plan

NESC	National Economic and Social Council
NESDO	National Economic and Social Development Office
NESF	National Economic and Social Forum
NGO	Non-governmental Organisation
NICs	Newly Industrialising Countries
NMW	National Minimum Wage
NPM	New Public Management
NSS	National Spatial Strategy
NTR	National Toll Road
NWCI	National Women's Council of Ireland
NYCI	National Youth Council of Ireland
ODTR	Office of the Director for Telecommunications
OECD	Organisation for Economic Co-Operation and Development
OMC	Open Method of Co-ordination
PATs	Programmes in Advanced Technologies
PCP	Public Capital Programme
PCW	Programme for Competitiveness and Work
PESP	Programme for Economic and Social Progress
PMDS	Performance Management Development System
PPF	Programme for Prosperity and Fairness
PPP	Public Private Partnership
PRETA	Pre-Retirement Allowance
PRSI	Pay-related Social Insurance
PRTLI	Programme of Research in Third Level Institutions
PSO	Public Service Obligation
QAA	Qualified Adult Allowance
QAG	Quality Assurance Group
QNHS	Quarterly National Household Survey
R&D	Research and Development
RMI	Revenue Minimum d'Insertion
RTC	Regional Technical Colleges
RTDI	Research, Technological Development and Innovation

RTI	Rural Transport Initiative
SBAs	Strategic Business Areas
SEI	Sustainable Energy Ireland
SES	Socio-Economic Status
SFI	Science Foundation Ireland
SGI	Services of General Economic Interest
SGM	Standard Gross Margin
SGP	Stability and Growth Pact
SILC	Survey of Income and Living Standards
SIPTU	Services Industrial Professional Technical Union
SMEs	Small and Medium Enterprises
SMI	Strategic Management Initiative
SNS	Swedish Centre for Business and Policy Studies
SOE	Small Open Economy
SSIA	Special Saving Incentive Account
TEN	Trans European Network
TFR	Total Fertility Rate
TNC	Transnational Corporation
TSO	Transmission System Operator
UN	United Nations
UNCESCR	United Nations Committee on Economic, Social and Cultural Rights
UNDHR	United Nations Universal Declaration of Human Rights
UNICEF	United Nations International Children's Emergency Fund
VAT	Value Added Tax
VIPP	Virtual Independent Power Producer
VRT	Vehicle Registration Tax
WTO	World Trade Organisation

PREFACE

Since 1986, the National Economic and Social Council has produced five reviews of economic and social policy. These reports - *A Strategy for Development* (1986), *A Strategy for the Nineties* (1990), *A Strategy for Competitiveness, Growth and Employment* (1993), *Strategy into the 21st Century* (1996), and *Opportunities, Challenges and Capacities for Choice* (1999) have documented developments of the Irish economy and society, and provided a framework for the negotiation of the national social partnership agreements. The Council has now completed a sixth review of economic and social strategy. The 'Overview, Conclusions and Recommendations' of this review were published in November, 2002 as NESC Report No. 110. The Council is now publishing the main report from which those recommendations and conclusions were derived. This document is divided into three parts: review, vision and strategy.

Part I, a review of Ireland's long run economic and social development, shows that the recent development of the economy can be understood as the extensive growth a regional economy. It also show that the type of economic development achieved in recent decades has undoubted vulnerabilities. Ireland's long run social development—shaped by the legacy of the past and the economic context—also contains particular vulnerabilities. The Council sees these economic and social vulnerabilities as defining the enduring challenges that Ireland must address. A number of these vulnerabilities have materialized in recent years, and these define the immediate challenges for public policy and social partnership.

In Part II of the report, the Council outlines its vision, distinguishing vision as hope, as clear sight of realities, as perception of shared pressures and concerns and as sight of new possibilities. It emphasises that the achievements of the past 15 years have been based on (i) adaptation of the national policy and institutional framework; (ii) an expanded export sector and (iii) the development of the European Union. Ireland does not fit neatly into any existing model or category of socio-economic development. Many of the new economic and social possibilities were discovered by experimental problem-solving action involving government, the social partners and others.

Part III of the report outlines the Council's Strategy. The Council restates the importance of a consistent policy framework, encompassing macroeconomic, distributional and structural policies. Given the wide range of urgent structural/supply-side needs, the Council identifies the following common elements:

- the need to ensure scope for the necessary investment to take place;
- the need to ensure a high quality or standard of service and value-for-money; and
- the need to make the organisational and institutional changes necessary to achieve high-performance and co-ordination of a range of cross-cutting policies and organisations.

Within this context, the Council outlines its analysis, conclusions and recommendations in the following areas: inflation; the public finances; taxation and social protection; policies on poverty, unemployment and social exclusion; infrastructure; utilities and spatial development; and enterprise policy. The Council believes that, if appropriate choices are made across a range of policy areas, Ireland has the capacity to achieve an economically and socially inclusive society that has long term sustainability.

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The Council wishes to acknowledge the contribution of Forfás and the Department of Enterprise, Trade and Employment who provided material and assistance on enterprise policy for Chapter 10.

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The staff of several Government Departments, the Economic and Social Research Institute, the National Centre for Partnership and Performance, the Central Statistics Office, the Central Bank and the National Economic and Social Forum provided great assistance to the Secretariat throughout the preparation of this Strategy document.

Ann Marie O'Connor of the Department of Social and Family Affairs contributed to the drafting of this Report while a member of the NESC Secretariat. The administrative staff of the Council's Secretariat provided valuable support in the production and distribution of the various drafts of the report.

Part I

Review

CHAPTER 1

IRELAND'S LONG RUN ECONOMIC DEVELOPMENT AND VULNERABILITY

1.1 INTRODUCTION

This chapter describes Ireland's long-run economic development and identifies the main challenges that must now be addressed.

Section 1.2 provides a factual survey of the economy from 1960 to 2002. Focusing on the main economic indicators, it divides the period since 1960 into five phases: 1960-73, 1973-79, 1979-87, 1987-2000 and 2000-2002. Section 1.3 identifies and discusses five key factors that underpinned Ireland's remarkable economic performance in the 1990s: domestic policy and institutional change, competitiveness, EU membership and the European internal market, foreign direct investment and labour supply and education.

In Section 1.4, the Council outlines its understanding of how these factors worked together to produce unprecedented growth of output, exports, incomes and employment. It shows how this interpretation, built on analytical foundations advanced in earlier Council reports, can offer an understanding of both Ireland's poor long-run economic performance through much of the 20th century and the experience of boom in the 1990s. The Council explains how its interpretation differs from two others advanced recently: the first, that Ireland's economic development is fatally contradictory and, the second, that Ireland's progress is nothing remarkable, best seen as an inevitable convergence that happened to be delayed.

While the Council is not persuaded by each of these interpretations, it emphasises that the type of economic development achieved in recent decades contains undoubted vulnerabilities. The Council believes that acceptance of the core elements of Ireland's economic strategy demands recognition of these vulnerabilities. Accepting the country's position as a regional economy, which must retain high-value economic activity, means that we have to focus on what is necessary to make that economy sustainable (in both competitive and environmental terms), efficient and socially acceptable. These are the major challenges that must be met if Ireland is to secure its long-run economic and social development.

In Chapter 3 we apply this analysis to the economic experience of the past two years. The Council suggests that Ireland's current economic situation can be understood by noting that several of the vulnerabilities, noted earlier, have materialised together. These include a loss of competitiveness, the international down-turn, domestic policy mistakes, and the effects of several internal problems that have not been adequately resolved, particularly housing, settlement and infrastructure, the provision of public services, and productivity through continuous improvement. These are the major challenges that must be met if Ireland is to avoid a sharper economic setback in the coming years.

These immediate and medium-term policy problems are addressed in Part III of the report.

1.2 OVERVIEW OF THE ECONOMY 1960 TO 2002

1.2.1 Long Run Performance

Intensive and Extensive Growth

In examining the record of economic growth, it is useful to distinguish between intensive and extensive growth. Intensive growth refers to the rate of growth of income or output *per head*. Extensive growth refers to the growth of *total output* allowing for changes in total employment and population. As will be seen in Section 1.4 below, the distinction between intensive and extensive growth is particularly relevant in the interpretation of Ireland's recent growth and consideration of Ireland's current policy options.

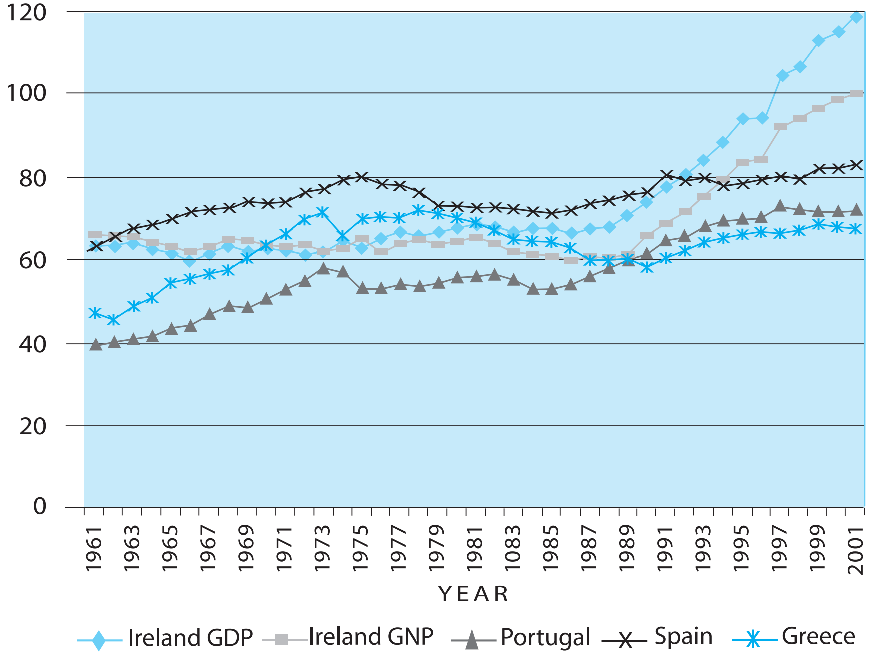
This section examines the trend in aggregate income using GNP and related measures. It is acknowledged that such measures are subject to a number of limitations. They do not take into account the value of unpaid work or the environmental costs of growth and do not represent a comprehensive measure of societal wellbeing. The Council has published a set of progress indicators that measure economic, social and environmental progress (NESC, 2002a). The direction of change of these indicators revealed that Ireland had made considerably more progress in terms of economic indicators compared to social indicators, while the headline environmental indicators chosen all moved in a negative direction. Nonetheless, economic growth, as measured by GNP and related measures, is relevant to the wellbeing of society as it affects the level of sustainable employment, the scope for higher incomes and the sustainable level of public expenditure and taxation. Broader dimensions of social progress are examined in Chapter 2.

Ireland's Long Run Growth Performance

To illustrate the historical significance of developments over the past 15 years it is worth briefly considering long-term economic performance. In the nineteenth century Ireland experienced de-industrialisation and a dramatic reduction in population through emigration. For much of the twentieth century, the growth of output per capita in Ireland was the lowest among 23 European countries, with the single exception of the UK (Kennedy, 2001). Irish output and living standards declined substantially relative to the European average. Since 1960, economic growth in Ireland has been sufficient, for the most part, to maintain Ireland's position relative to continental Europe and to converge with UK living standards. However, until the 1990s there was little progress towards convergence with average EU output or income per head. Then, during the 1990s Irish GNP per head (a better measure than GDP since the profits of multinationals are not included) leaped ahead and converged at a breathtaking pace with the EU average. By 2001, Irish GNP per capita was at 99.8 per cent of the EU average (EU average measured on a GDP basis)[1].

1. See the note to Figure 1.1 for details on the calculation of the relative GNP per capita figures.

FIGURE 1.1
GDP/GNP per Capita in Ireland, Portugal, Spain and Greece
EU15 = 100



Source: European Commission (2002), *European Economy*, No.6.

Notes: There is a discontinuity in this series in 1990. This adds between 1.3 percentage points (Greece) to 1.7 percentage points (Spain) for 1991, but does not alter the general pattern shown. The GNP series for Ireland was calculated by applying the ratio of GNP to GDP to the *European Economy* GDP series.

1.2.2 The Emergence of Growth: 1960 to 1973

The opening of the economy to free trade and the active policy of attracting foreign direct investment (FDI) in the 1960s were associated with a marked improvement in economic performance. GDP grew by an annual average of 4.4 per cent between 1961 and 1973. In this period there was little difference between GNP and GDP growth rates, and GNP grew by 4.3 per cent per annum (see Table 1.1). There was substantial growth in employment in industry and services. However, the decline in agricultural employment implied that there was little growth of total employment, which increased by just 0.2 per cent per annum. Productivity (as measured by GNP per worker) grew by 4 per cent and GNP per head grew by 3.5 per cent per year during this period.

TABLE 1.1
Annual Percentage Change in GNP, Employment and GNP per worker

	GNP	Employment	GNP per Worker	Population	GNP per Head
1961-73	4.3	0.2	4.1	0.7	3.5
1973-79	3.6	1.2	2.4	1.5	2.0
1979-87	0.8	-0.6	1.4	0.6	0.2
1987-93	3.6	0.9	2.6	0.1	3.4
1993-00	8.3	4.7	3.4	1.0	7.2

Source: Calculated from ESRI databank and CSO, *National Income and Expenditure 2000.*

1.2.3 International Crisis and EC Membership: 1973 to 1979

With the onset of the first oil crisis, there was a general slowdown in growth across the global economy. The slowdown in Ireland was less than elsewhere. Over the period 1973 to 1979, GDP in Ireland grew by 4 per cent per year, while GNP grew by 3.6 per cent per year. Irish growth rates of GDP, GNP and employment exceeded the EU average (GDP and employment growth of 2.5 and 0.2 per cent per annum respectively). However, the maintenance of economic growth was achieved at a cost of a marked deterioration in the public finances. The current budget deficit as a percentage of GDP increased from 0.4 per cent in 1973 to 6.8 per cent in 1975. A large deficit emerged in the current account balance of payments and there was a marked acceleration in inflation.

1.2.4 Recession, Disinflation and Fiscal Correction: 1979 to 1987

This period was one of generally poor performance for the Irish economy. GDP grew by an annual average rate of 1.7 per cent between 1979 and 1987. However, by this stage a major gap had emerged between GDP and GNP. Indeed, it became clear that there were a number of complexities in measuring the output and income of the Irish economy (see Box 1.1 for a summary explanation). From 1979 to 1987 the growth rate for GNP was just 0.8 per cent per year, with negative GNP growth in some years. Employment declined by an annual average rate of 0.6 per cent per annum. This reflected minimal growth of non-agricultural employment and the continuing decline in agricultural employment. Much of this period was one of recession in the international economy. However, Ireland's growth was exceptionally low and the decline in employment exceptionally high, as noted in NESC (1993a). On an International Labour Organisation (ILO) basis, unemployment increased from 5.5 per cent in 1979 to close to 17 per cent in 1987.

The tax/GNP ratio increased by 10 percentage points between 1979 and 1987, as the Government attempted to control the size of the public deficit. Despite this, the ratio of debt to GDP continued to spiral upwards, increasing from just over 70 per cent in 1979 to a peak of 124 per cent in 1987.

One positive aspect of this period was the success in getting inflation under control. The annual rate of inflation peaked at over 20 per cent in 1981 and declined from that point. It had fallen to 3.2 per cent by 1987.

TABLE 1.2

Output and Income Measure : Annual Percentage Change

	GDP	GNP	GNP adjusted for terms of Trade	GNDI	GNDI per head
1961-73	4.4	4.3	4.8	4.8	4.1
1973-79	4.0	3.6	2.9	3.2	1.7
1979-87	1.7	0.8	1.1	1.1	0.4
1987-93	3.9	3.6	3.2	3.2	3.1
1993-00	9.3	8.3	7.6	7.2	6.1

Source: Calculated from ESRI Databank and CSO, *National Income and Expenditure 2000.*

BOX 1.1

Alternative income measures

GDP is not a good indication of income in Ireland because GNP is significantly lower. The main factor behind the difference in the level of GNP and GDP is the profit outflows of multi-nationals[2]. The gap between GDP and GNP has been growing and is now around 15 per cent of GDP.

However, GNP is itself subject to a number of qualifications as a measure of real national income. The impact of real GNP growth on the real purchasing power of national income is affected by the trends in export prices relative to import prices, called the terms of trade. Changes in the terms of trade can be either positive or negative. Trends in GNP adjusted for changes in the terms of trade are shown in the third column of Table 1.2. It can be seen that during the 1960s that this measure of real income grew by more than either GNP or GDP. In the 1970s, changes in the terms of trade greatly reduced Ireland's real income, mainly because of increased oil prices. In later periods, this effect was more modest.

International Transfers

Real national income is also influenced by the level of current transfers received, such as EU supports. These transfers add to the real purchasing power of GNP. In relative terms they have fallen during the 1990s. Gross National Disposable Income (GNDI) incorporates the effects of the terms of trade adjustment as well as changes in these transfers, and is shown in fourth and fifth columns of Table 1.2. This is perhaps the best measure of growth of real national income.

2. As a result of a methodical change introduced from the 1995 national accounts, all profits (including retained earnings) of foreign direct investment (FDI) enterprises are excluded from GNP. Conversely, the retained earnings of Irish-owned multi-nationals abroad are included as part of GNP.

1.2.5 Stabilisation and Recovery: 1987 to 1993

The economy recovered strongly in the late 1980s. From 1987 to 1990, GNP grew by just over 5 per cent while employment increased by an annual average rate of 1.4 per cent. Unemployment (on an ILO basis) fell from close to 17 per cent in 1987 to just under 13 per cent in 1990. The correction of the public finances was a significant feature of economic performance in this period. Exchequer borrowing declined from close to 9 per cent of GNP in 1987 to around 3 per cent in 1988. The debt/GNP ratio began to fall, from 124 per cent in 1987 to 100 per cent in 1990. Real take-home pay began to increase with an annual average increase for a single worker of 2.6 per cent between 1987 and 1990 (based on Table 6.2 in NESC, 1999).

In the early 1990s, growth slowed across many OECD countries. However, the slowdown in Ireland was less than that experienced elsewhere. Between 1990 and 1993, GNP grew by an average of 2.6 per cent per year compared to the EU average (for GDP) of 0.7 per cent. Total employment grew modestly in Ireland, while it declined in several EU countries with a particularly high decline in the UK. The relatively strong growth of the Irish economy in this period was due to a strong export performance. The economy proved very competitive, as exports continued to grow despite recession in the EU. The growth of domestic demand was, however, subdued.

Recession in the UK and elsewhere in the early 1990s meant that net emigration from Ireland stopped. With only a modest increase in employment, the natural increase in the labour force was reflected in a sharp increase in unemployment. The level of unemployment increased from just below 13 per cent in 1990 to close to 16 per cent in 1993 (ILO basis).

1.2.6 Strong Economic Growth: 1993 to 2000

Here we summarise the main economic developments in this period of exceptional growth often referred to as the period of the Celtic Tiger. Further analysis and interpretation of this experience is provided in Sections 3 and 4 below.

Output and Incomes

From 1993 to 2000, the average growth of GDP was 9.3 per cent per year and the average growth of GNP was 8.3 per cent per year. GNDI has grown by an annual average rate of 7.2 per cent over the 'Celtic Tiger' period or approximately one percentage point less than the growth of GNP. Living standards, as measured by GNDI per head of population, have grown by an annual average of just over 6 per cent during this period. Significant transfers from the EU meant that the level of GNDI in 2000 was somewhat above the level of GNP. However, the pace of growth of living standards when measured by GNDI per head was around one percentage point less than when measured in terms of GNP per head.

Trends in take-home pay and social welfare transfers are presented in Chapter 2.

Employment

The most significant development in the period 1993 to 2000 was the increase of employment, which grew by an average of 4.7 per cent per year. The level of employment increased from 1.15 million in 1993 to 1.65 million in the first quarter of 2000, an increase of over half a million people (43 per cent) in employment. This was completely unprecedented in Irish economic history and was the fastest growth of employment in the OECD in this period.

The increased rate of growth and the dramatic increase in employment, meant that average Irish incomes converged rapidly with the EU average. The influence of employment in allowing this convergence is explained in Box 1.2.

There was a broadly based growth of employment across almost all sectors of the economy. As shown in Table 1.3, the fastest employment growth was in the building sector, where there was phenomenal growth averaging 12.3 per cent a year. The cumulative increase in employment in this sector was over 170 per cent. Employment in market services grew strongly, with annual average growth of 5.7 per cent, totalling more than 30,000 per year. There was also substantial growth of non-market services employment—

mainly in health and education—with average annual growth of 4.4 per cent.

BOX 1.2

International Convergence of Living Standards

There was rapid convergence with EU living standards in the 1990s. Living standards, as measured by GNP per capita, can be decomposed into two factors: the income generated per person at work and the share of the population in employment. A decade ago the primary reason behind Ireland's relatively low average GNP per person was the below average share of the population in employment. A key feature of the period from 1993 to 2000 was a growth in employment (4.7 per cent per annum) that greatly exceeded the growth of population (1.0 per cent per annum). This resulted in a very substantial growth in GNP per head of over 7 per cent per annum. This rise in the share of population in employment, or the decline in the economic dependency ratio, has been a key factor in the country's convergence to average EU incomes.

The employment-population ratio is a function of three ratios: the unemployment rate, the labour force participation rate (the share of the total labour force in the population) and the age dependency rate (the share of dependent age groups in the total population). The 'Celtic Tiger' period has been exceptional, as all three components of the employment-population ratio have moved in a favourable direction: the unemployment rate fell sharply, the labour force participation rate increased and the age dependency ratio fell (Kennedy, 2001).

The composition of employment by broad sector in 2000 is also shown in Table 1.3. The largest sector is market services comprising around 42 per cent of employment. Industry represented around 30 per cent of employment, of which manufacturing comprised 18 per cent and building just over 10 per cent, while there was just over 1 per cent employed in utilities and mining. Non-market or public services accounted for around 21 per cent of total employment while around 8 per cent of employment was in agriculture, forestry and fishing.

TABLE 1.3
Employment Growth by Sector : Annual Percentage Change

	1961-73	1973-79	1979-87	1987-93	1993-00	2000 % of Total
Agriculture	-3.3	-2.4	-3.7	-2.1	-2.3	7.7
Industry	2.3	1.4	-2.4	0.6	6.0	29.5
Manufacturing	2.0	1.2	-1.7	1.3	3.6	18.1
Building	3.4	2.3	-4.3	0.0	12.7	10.3
Utilities & Mining	1.6	0.7	-2.2	-4.4	1.4	1.1
Market Services	0.6	1.7	1.1	2.3	5.7	41.9
Wholesale and Retail	0.5	1.2	0.7	2.0	3.4	14.6
Insurance, Finance and Business	3.8	6.5	2.9	2.7	6.5	4.6
Transport & Communications	1.4	1.1	-0.5	0.7	5.4	6.3
Other Services	-0.4	1.8	2.1	3.5	8.0	16.3
Non-Market Services	2.8	4.5	2.0	0.9	4.4	20.9
Public Administration	2.6	4.1	0.0	-0.7	2.7	5.1
Health and Education	3.0	4.8	3.0	1.5	5.0	15.8
Total Employment	**0.2**	**1.2**	**-0.6**	**0.9**	**4.7**	**100**

Source: Calculated from ESRI Databank.

One of the most striking changes that has occurred in the Irish labour force has been the growth in female employment, particularly married women. In 1980, Ireland had one of the lowest participation rates for women in the paid labour force in Europe. However, a combination of cultural and legislative change, declining fertility, and an improving labour market has rapidly changed this situation. Most of this increase was due to the rise in the participation rates of married women, rising from 30.6 per cent in 1990 to 46.1 per cent in 2000. By the end of 2000, female labour force participation rates stood at 47.9 per cent, with the corresponding rate for men standing at 71.0 per cent.

Female employment has grown more rapidly than male employment: female employment grew by an annual average rate of 7.0 per cent between 1994 and 2000, compared to growth of 4.4 per cent for male employment. In terms of job numbers, the 'Celtic Tiger' period has been characterised by substantial growth of both male and female employment, with similar increases for both categories.

The growth of male employment consisted mainly of full-time employment; full-time male employment grew by an annual average of almost 32,000 between 1994 and 2000 while part-time male employment grew by an annual average of just 5,400. By contrast, among women, there was an approximately equal balance in the growth of full-time and part-time employment; the annual increase in female employment between 1994 and 2000 was 19,300 for full-time employment and 18,500 for part-time employment. Total full-time employment increased by over 51,000 per annum between 1994 and 2000, compared to an increase of close to 24,000 for part-time employment. Full-time employment represented 68 per cent of the increase in employment over the 1994 to 2000 period.

The *rate of growth* (in percentage terms) of part-time employment greatly exceeded the rate for full-time employment. Between 1994 and 2000, part-time employment grew by a rate of close to 12.6 per cent a year, compared to 4.2 per cent for full-time employment. The growth rate of part-time female employment was particularly high, with annual average growth of 13.4 per cent over this period.

TABLE 1.4
Annual Change in Full- and Part-Time Employment, by Gender 1994 to 2000

	Change 000s	% Change
Male		
Full-time	31.9	4.0
Part-time	5.4	10.5
Total	37.3	4.4
Female		
Full-time	19.3	4.8
Part-time	18.5	13.4
Total	37.8	7.0

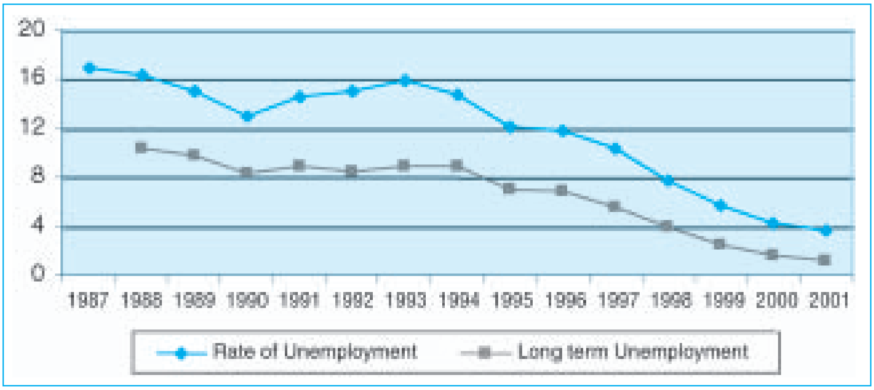
Source: Calculated from Labour Force Survey and Quarterly National Household Survey data (series provided by CSO).

Unemployment

The strong employment growth since the mid-1990s resulted in a large reduction in unemployment. In 1993 the rate of unemployment (ILO basis) was 15.9 per cent while by 2000 this had fallen to 4.3 per cent. The number of those unemployed fell from 222,500 in 1993 to 74,900 in 2000, a fall of 147,500. A striking feature of Irish unemployment had been the large number of those who were unemployed for long periods. In 1993, the number of long-term unemployed (defined as being out of work for one year or more) was 125,400 or 8.9 per cent of the labour force. Since then this has fallen significantly, paralleling the decline in the overall unemployment rate. In 2000, the number in long-term unemployment had fallen to 27,400 or 1.6 per cent of the labour force. The dramatic reduction in unemployment from the mid-1990s is the probably the single most significant social benefit from the period of strong economic growth.

FIGURE 1.2

Rate of unemployment and long-term unemployment



Source: ESRI databank.

Productivity

The growth of productivity during the 1993 to 2000 period was high by international standards, but not unprecedented compared to earlier Irish performance (see Table 1.1). Productivity trends are discussed in Chapter 6. The discussion in Chapter 6 includes an analysis of differences in productivity growth across different sectors of the economy.

Regional Pattern

A feature of the strong economic growth of the 1990s has been increased regional concentration. In 1993, just under 40 per cent of total employment was in the East (Dublin, Meath, Kildare and Wicklow) region while by 2000 this share had increased to 42.6 per cent of total employment. The share of both the Border (Cavan, Donegal, Leitrim, Louth, Monaghan, Sligo) and South West (Cork, Kerry) regions fell by over 1 and 0.8 percentage points respectively and the share for the South East fell by 0.7 percentage points. The shares for other regions (West, Midlands, Mid West) were broadly stable.

The increase in the regional concentration was particularly strong in relation to employment in IDA Ireland companies. In 1993, just under 35 per cent of permanent employment in IDA Ireland companies was in the East region, while by 2000 this share had risen to over 48 per cent. There are a number of factors responsible for the growing regional concentration of new employment. A key factor is the availability of skills. The demand for advanced skills by both overseas and domestic investors has been rising. Those with the required skills are attracted to urban regions that can provide a range of employers. The growing importance of high technology sectors also encourages regional concentration. As O'Malley (1994) noted, firms in modern high technology sectors seem to have a particular preference for location in more urbanised regions and it is these sectors that have shown the most rapid growth. Finally, the availability of infrastructure, sub-contractors and specialised services also tends to encourage investment in urban centres.

Saving and Consumption

Since 1987, the percentage of total income consumed has fallen from close to 85 per cent to around 72 per cent in 2000, with a corresponding increase in the total national savings share. The share of national income allocated to both personal and public consumption has fallen. This is largely explained by the increase in Government savings (see Box 1.3).

TABLE 1.5

Components of Gross Savings
Percentage of Gross National Disposable Income

	1961	1973	1979	1987	1993	1999	2000
Gross Savings	12.9	19.4	15.5	15.2	19.0	28.1	28.2
Depreciation	6.2	7.6	9.4	10.2	10.5	11.1	11.4
Net Savings	6.6	11.8	6.2	5.0	8.5	17.0	16.8
Personal	2.0	8.3	8.1	6.7	8.2	6.7	na
Corporate	5.5	6.7	7.3	5.8	3.6	4.7	na
Government	-0.8	-0.6	-6.5	-7.4	-2.5	6.5	7.4
Stock Appreciation	-0.4	-2.8	-2.7	-0.5	-0.8	-0.9	-1.0

Source: Calculated from ESRI Databank and CSO, *National Income and Expenditure 2000*.

BOX 1.3

Trends in Saving and Consumption

By definition, income is either consumed or saved. Consumption is divided into personal consumption and public consumption (i.e., expenditure by public authorities on goods and services, excluding transfer payments). The rise in the national saving share during the boom years may seem surprising. It is important to note that this is total national savings and comprises three elements: personal, company and government savings (See Table 1.5). It is the rise in government savings that is responsible for the increase in overall national savings up to the year 2000. Government savings is defined as the income of Government less current expenditure. It includes both Government surpluses and public capital expenditure. It has increased from –7.4 per cent in 1997 to +7.4 per cent in 2000. In contrast to Government savings, the personal savings share has fallen during the years of strong economic growth from 8.2 per cent in 1993 to 6.7 per cent in 1999. The personal savings share in 1999 was at the same level as in 1987. The corporate savings share increased modestly from 3.6 per cent in 1993 to 4.7 per cent in 2000 although this increase was less than the increase in corporate investment.

Investment

During the boom years following 1993, there has been a very substantial rise in domestic investment share from 16.2 per cent in 1993 to over 28 per cent in the year 2000. As noted above, there was also an increase in the national savings ratio over this period, although the increase in savings was less than the increase in investment. By 2000, the gap between savings and investment had been almost eliminated and there was a small level of net foreign investment/current account surplus of 0.6 per cent of GNP.

The main components of investment are investment in building and construction and machinery and equipment. There has been strong growth in both of these elements but it is building and construction investment that has been mainly responsible for the sharp increase in the investment share, with an increase from 9.3 per cent of GNDI in 1993 to 20.4 per cent in 2000. This includes both private and public investment. The machinery and equipment share has increased from 7.3 per cent in 1993 to 11.4 per cent in 2000. This is lower than the corresponding level in the 1970s. This probably reflects the influence of some high-tech sectors where output has grown without a proportionate increase in physical capital.

The rise in both national savings and domestic investment during the 1990s is a positive feature of the economy's development that can help to underpin its future growth. The share of investment in national income since 2000 has fallen. Sustaining a high level of investment is important to underpin future growth.

TABLE 1.6
Savings and Investment
Percentage of Gross National Disposable Income

	1961	1973	1979	1987	1993	2000
Gross Savings	12.9	19.4	15.5	15.2	19.0	28.2
Net Foreign Capital Transfers	0.0	0.0	0.0	-0.1	1.6	1.4
Statistical Discrepancy	2.4	2.8	2.4	1.5	1.1	-0.9
Total Available for National Investment	15.2	22.2	17.9	16.6	21.8	28.7
Domestic Investment	15.6	25.9	30.6	18.2	16.2	28.1
Net Foreign Investment	-0.4	-3.7	-12.7	-1.5	5.6	0.6
Gross National Investment	15.2	22.2	17.9	16.7	21.8	28.7

Source: Calculated from ESRI Databank and CSO, *National Income and Expenditure 2000.*

BOX 1.4

Investment and Saving in an Open Economy

In a closed economy, savings will be equal to investment by definition. This is not necessarily the case for a very open economy such as Ireland. Savings can be used either for domestic investment or the net acquisition of foreign assets. Domestic investment can exceed domestic savings, because of foreign borrowing or net inward foreign investment. By definition, the level of net foreign investment is equal to the current account surplus (positive net current investment) or the current account deficit (negative net current investment/foreign borrowing). Investment in an open economy can also be supplemented by capital transfers from abroad, such as EU Structural Funds.

The long-run allocation of resources from savings and capital transfers to investment is shown in Table 1.6. In 1961, national savings and domestic investment were at broadly similar levels. During the 1970s a significant gap emerged between domestic investment and national savings which was financed by substantial foreign borrowing. During the 1980s, the level of domestic investment was cut sharply, so that the share of income in domestic investment was brought closer in line with the level of national savings. By 1993, national savings substantially exceeded domestic investment and there was a current account surplus/net foreign investment of 5.6 per cent of GNDI. This reflected the weak growth of domestic investment in the early 1990s. During the boom years following 1993, there has been a very substantial rise in domestic investment share from 16.2 per cent in 1993 to over 28 per cent in the year 2000.

Public Finances

The period of strong economic growth since 1993 was associated with a fall in the share of public expenditure in GNP. Total public expenditure fell from 46.6 per cent of GNP in 1993 to 35.3 per cent in 2000. Notwithstanding the decline in the share of expenditure of GNP, there has been substantial growth in the level of expenditure. Growth of gross supply services expenditure (i.e., expenditure on current services) grew by an annual average of almost 8 per cent in nominal terms between 1993 and 2000. Capital expenditure has grown faster than current expenditure and indeed faster than GNP, with an increase in Exchequer capital expenditure from 3.8 per cent of GNP in 1993 to 5.5 per cent in 2000. In relation to tax revenue, there was a modest decline in the share of Exchequer tax revenue and social security contributions in GNP from 37.9 per cent of GNP in 1993 to 35.4 per cent in 2000. The significantly greater decline in expenditure share compared to the decline in the tax share resulted in a fall in the level of the deficit and a move into surplus on a general government basis by 1997. The level of the surplus peaked at 4.4 per cent of GDP in the year 2000.

1.2.7 Irish Inflation and International Slowdown: 2000 to 2002

Slower Output Growth

The year 2001 was characterised by a sharp slowdown in economic growth. GNP growth for 2001 was 4.6 per cent, less than half the remarkably high growth of over 10 per cent in the previous year. The growth of 4.6 per cent over the year 2001 as a whole is still substantial growth, but this was boosted by the strong growth in the early part of the year. GNP growth for the first quarter of 2001 was over 10 per cent while this had fallen to below 4 per cent in the final quarter.

The slowdown in growth in 2001 was due to a combination of external and domestic factors. There was a general weakening in growth in major economies and a particular weakening in the ICT sector. Towards the end of the year, confidence in the international economy was adversely affected by the attacks of September 11. Internally, growth in Ireland was adversely affected by the foot and mouth outbreak with particular effects for the agriculture and tourism sectors.

The year 2002 was another year of modest growth. There was quite strong growth of GDP in 2002, with forecasters estimating that GDP growth was between 3 and 4 per cent. However, 2002 was characterised by an unusually large gap between GDP and GNP growth. The growth of exports, which boosted GDP growth, was dominated by the chemicals sector. The growth of GNP, a better measure of economic activity, grew more modestly with most estimates for 2002 in the region of 2 per cent.

A recovery of the international economy is expected during the course of 2003, although the timing and pace of recovery is uncertain. Forecasters are also expecting the Irish economy to recover during 2003. The ESRI and the Central Bank are projecting growth rates of 3 per cent during 2003, with lower growth forecast by the Department of Finance and Davy Stockbrokers. Both the Central Bank and the Department of Finance emphasise that growth could be lower than their projections if there were a substantial loss of cost competitiveness arising from either wage inflation or a sharp appreciation of the euro.

TABLE 1.7

Estimates/Forecasts of GNP, GDP, Inflation, Unemployment

	GNP		GDP		Inflation	Unemployment
	2002	2003	2002	2003	2003	2003
ESRI	2.2	3.0	4.3	3.8	5.1	5.2
Department of Finance	1.8	2.2	4.5	3.5	4.8	5.3
Central Bank	2.5	3.0	4.5	3.5	4.5	5.0
Davy	0.7	1.1	3.8	2.6	3.7	6.0

Source: Department of Finance, *Budget 2003*; Davy Stockbrokers, *Sluggish Growth to Continue*, November 2002; ESRI, *Quarterly Economic Commentary*, Winter 2002; Central Bank, *Quarterly Bulletin*, Winter 2002.

Employment and Unemployment

The slowdown in economic growth is reflected in much reduced growth of employment. The Quarterly National Household Survey

(QNHS) showed that employment for the third quarter of 2002 had increased by just 0.5 per cent compared to the same period for 2001. There was a substantial decline in the industrial sector with an annual fall in employment of close to 17,000 or 5 per cent. Employment in agriculture, forestry and fishing fell by 3.6 per cent. There was a modest increase in employment in private services, with an increase of 5,700 or 0.7 per cent. Employment growth in construction continued to be robust up to the third quarter, with an annual increase of 3,600 or close to 2 per cent. The strongest employment growth was in the public service with an annual increase of over 20,000 or over 6 per cent. However, even here employment growth is now slowing and there was a fall of 3,500 between the second and third quarters.

The slowdown in employment growth has led to an increase in unemployment from 3.7 per cent in the first quarter of 2001 to 4.6 per cent in the third quarter of 2002. The rise in unemployment is less than might have been expected given the slowdown in economic growth. Factors that have moderated the rise in unemployment have been the increase in public service employment and a decline in labour force participation among younger people (15 to 34). It is also suggested by the Central Bank in its *Quarterly Bulletin* of Winter 2002 that some firms are holding onto workers in the expectation that conditions would improve in the near future. This interpretation is supported by the fact that hours worked have fallen.

Looking at 2003, all forecasters are expecting that unemployment will continue to increase. Forecasters are projecting average unemployment for 2003 to be in the region of 5 to 6 per cent. The rise in unemployment is a matter of concern for the Council.

Increase in Inflation

After several years of low inflation, inflation has re-emerged as a concern in recent years. There was a particularly large increase in the Consumer Price Index (CPI) in the year 2000, with an increase of 5.6 per cent. The rate of increase moderated somewhat in 2001 when inflation increased by a still substantial 4.9 per cent. The rate of inflation was approximately 4.7 per cent in 2002. Since 2001, inflationary pressures have been particularly strong in the services as against goods area. Central Bank data show that for 2001, it was above average services inflation that was responsible for Ireland having faster inflation than the euro area as a whole.

A range of factors contributed to the re-emergence of inflation in Ireland. The weakness of the euro contributed directly to higher inflation by increasing import prices and also by contributing to stronger demand in the economy. This factor is now being reversed with the strengthening of the euro. An expansionary fiscal policy also contributed to the strength of demand in the economy. The general strength of domestic demand along with associated wage inflation is a key influence on inflation. In addition, employers are facing higher non-wage costs, particularly higher insurance costs. The weakness of competitive forces in some parts of the economy in the context of strong demand growth is likely to have contributed to inflation. The euro changeover was also associated with cost increases for some goods and services.

Looking ahead, there are a number of factors that can be expected to exert downward pressure on inflation. The strengthening of the euro will reduce import prices while potentially lower wage inflation will also exert downward pressure. On the other hand, the indirect tax measures in the 2003 Budget added 0.85 percentage points to the increase in the CPI. Most of the increase arises from the higher excise duty on tobacco. The Department of Finance is projecting an increase in the CPI of 4.8 per cent for 2003. Given the nature of the tobacco product (there is widespread agreement that tobacco consumption should be discouraged given the proven evidence of its negative effects on health), it can be argued that the CPI excluding tobacco should receive as much attention as the headline rate of inflation. Excluding the increase in tobacco excise duty, the increase in the CPI would fall by ½ per cent to about 4.2 per cent. Most forecasters are projecting inflation in the region of 5 per cent for 2003.

A more detailed account of the factors that have caused inflation in Ireland in recent years can be found in Chapter 5.

Loss of Competitiveness

In recent years competitiveness has been under pressure from a number of sources. There has been a general rise in costs in the economy, including wage costs. The growth in wage costs is partly a reflection of increases in other costs in the economy. Housing costs in particular have risen dramatically in recent years and contributed to wage pressure, although high levels of owner occupation protect many from the negative effects of rising house prices. Bottlenecks arising from pressures on infrastructure are a key pressure on competitiveness, both directly by increasing costs and causing delays for business and indirectly by reducing the quality of life.

The trend in unit labour costs is a measure of wage competitiveness that incorporates the effects of differential productivity growth rates. This measure, as published in the OECD *Economic Outlook,* shows that since 1998, unit labour costs in the Irish economy have increased by more than the euro area average. In 2001, unit labour costs increased by 3.9 per cent in Ireland compared to an increase of 1.6 per cent for the euro area, while for 2002 there was an increase projected for Ireland of 3.8 per cent, compared to the euro area average of 1.8 per cent. This measure includes the full benefits of the very high productivity growth of particular MNC-dominated sectors. Unit labour costs in sectors with lower productivity growth would have increased by more than these average figures. Sectors particularly affected in this way would be tourism and indigenous manufacturing. Until recently, the effects of relatively higher growth of unit wage costs in Ireland have been partly offset by the weakening of the euro, but this effect is now being reversed.

The Council believes that a successful approach to addressing competitiveness can only be achieved through consistent policies across a range of areas. Competitiveness requires a sustainable fiscal policy and incomes policy as well as effective policies to promote enterprise and a pro-active competition policy. It also is dependent on progress in tackling quality of life issues, including improving the provision of public transport and other public services and making housing more affordable. The Council's positions across a range of policies relevant to competitiveness are presented in Part III of this report.

Deterioration in the Public Finances

The slowdown in growth has led to a sharp deterioration in the public finances. The General Government Balance (GGB) has fallen from a surplus of 4.4 per cent of GDP in 2000 to a marginal deficit for 2002. A decline in the surplus would be expected given the slowdown in the economy. However, the extent of the deterioration in public finances cannot be explained as a normal cyclical variation. The issue arises as to how there was such a rapid change in the public finance position over a short period. Essentially, public expenditure in the past two years has grown at a rate above GNP while there has been a sharp slowdown in revenue growth, reflecting both the slowdown in the economy as well as tax cuts.

1.3 IDENTIFYING THE KEY FACTORS THAT DRIVE GROWTH

Having surveyed Ireland's long-run economic development, we now identify and discuss the key factors that underpin growth, particularly the dramatic expansion of the past decade and a half. The factors identified are:

- Domestic policy and institutional change;
- Competitiveness;
- EU membership and the European internal market;
- Foreign direct investment (FDI); and
- Education and labour supply.

The way in which these have interacted with one another is discussed in Section 1.4.

1.3.1 Domestic Policy and Institutional Adaptation

A most important factor in Ireland's economic progress since the late 1980s was domestic policy and institutional adaptation. Three aspects of this are worthy of mention: the achievement of a consistent policy approach, social partnership and the approach taken to national developments. The role of each is discussed here.

A Consistent Policy Framework

The Council has argued in a number of strategy reports that a small open economy requires a consistent set of macroeconomic, distributional and structural policies. A consistent macroeconomic policy is required to ensure economic stability and low inflation. An approach to income distribution is required that allows for improvements in competitiveness and resolves distributional conflicts without disrupting the functioning of the economy. The third element of a consistent policy framework is structural reform that enhances the efficiency of the economy and international competitiveness and addresses social inequalities without significant adverse economic impact. Over the 1990s, Ireland made considerable progress in putting in place a consistent policy framework. Macroeconomic policy was based on preparation for and the eventual move to the euro. This approach took the exchange rate outside day-to-day party political competition and industrial relations conflict. Second, national agreements on pay, taxation, social welfare and social provision shaped distribution and generally ensured a low level of industrial relations conflict. Third, there was considerable progress towards putting in place appropriate structural policies, particularly in relation to economic development.

Social Partnership

The partnership approach would seem to have had a significant impact on the Irish economy, through three channels: wage bargaining, coherent and consistent macroeconomic policy and change in supply-side factors.

Consider first the impact of the partnership approach to wage bargaining. One of the most striking features of Irish economic performance in the period of partnership has been the enhanced profitability of business. Lane demonstrates that the rate of return on capital almost doubled, rising from 8.6 percent in 1987 to 15.4 per cent in 1996. The sharp rise in profitability coincides with "the formation of a new consensus among the social partners, as formalised in the negotiation of a sequence of national agreements", suggesting that "the incomes policy that lies at the heart of a new consensus is an important factor in explaining the income shift from labour to capital" (Lane, 1997/98: 228). The resulting environment of wage moderation and high profitability is almost certainly a key factor in Ireland's employment creation, attraction of inward investment and the unprecedented commercial success of indigenous companies (see also Honohan, 1999; McHale, 2000).

Fitz Gerald's econometric study of the Irish labour market leads him to suggest that the "impact of the partnership approach to wage formation has been less significant than many have assumed", since "the partnership approach served more to validate the results which market forces had made inevitable" (Fitz Gerald, 1999: 160 and 162). The main impact of partnership lay in improved industrial relations, which significantly enhanced economic performance, and the fact that "the partnership approach has also contributed to a more coherent approach to economic policy making" (Fitz Gerald, 2000a: 42).

This brings us to the second channel through which partnership influenced the economy: its contribution to the consistent policy framework described above. In macroeconomic terms, partnership was an important element in Ireland's transition from a high-inflation, volatile and conflictual economy to a low-inflation, stable, economy. In particular, consensus on the consistent policy framework summarised above, took the exchange rate, and therefore inflation, outside day-to-day party political competition and industrial relations conflict. It has also preserved a higher level of social solidarity, which seems an essential pre-requisite to sustaining redistributive policies and addressing issues of structural change and reform in a non-conflictual way.

The third channel of influence on the economy is a supply-side mechanism. This arose because there would seem to be a close connection between settling major macroeconomic and distributional issues, on the one hand, and constructive engagement with supply-side problems, on the other. Closing-off macro-economic alternatives freed management, trade union, voluntary sector and government energies for discussion of real issues that impact on competitiveness and social cohesion—corporate strategy, technical change, training, working practices, the commercialisation of state-owned enterprises, taxation, local re-generation and active labour market policy—and forced (almost) all to engage in realistic discussion of change.

However, we cannot accurately identify the role of partnership without considering the European dimension. By coincidence, the adoption of the partnership approach coincided with the programme to complete the European internal market (see below).

This tentative synthesis of the achievements and limits of partnership is one which emphasises that partnership cannot be divorced from the wide range of other changes taking place in the past decade and a half (see Chapter 3).

The Flexible Developmental State (FDS)

An important part of Irish public policy has been industrial and development policy. It is easy to underestimate the role of the state in Ireland's economic breakthrough, because it does not conform to the conventional idea of a "developmental state", of the type that drove the development of the Asian NICs (Woo-Cummings, 1999). Clearly, Ireland's economic breakthrough has not been driven by a developmental state which protects the local economy in order to incubate strong localised enterprises capable of competing in the international economy.

Research by Ó Riain helps us to clarify our thinking about the developmental state and to see more clearly what role the state has played, and can play, in the Irish state context. He distinguishes between the Asian "bureaucratic developmental state" and what he calls the "flexible developmental state" (Ó Riain, 2000). Both have what Evans describes as "embedded autonomy" (Evans, 1995).

The bureaucratic developmental states are embedded by close ties between state bureaucrats and domestic business. Although an educated labour force is critical, labour is typically excluded from the key institutions of the state. These developmental states retain their autonomy because they have a classical Weberian bureaucracy. While embeddedness allows the state to gather information and mobilise resources, autonomy guarantees that national development goals remain central to state action.

While the theory of the developmental state has shed a great deal of light on Asian development, it clearly cannot explain the role of the state in a small open democracy such as Ireland. Ó Riain suggests that the idea be extended along its three underlying dimensions—state intervention in the globalisation process, conditions of embedded autonomy, and threats to state intervention that emerge dynamically during the development process—to create a concept of a remade *flexible developmental state* (FDS) (Ó Riain, 2000):

> The FDS is defined precisely by its ability to create and animate post-Fordist networks of production and innovation and international networks of capital, and to link them together in ways that promote local and national development. The FDS can attempt to do this in two primary ways. It can connect to existing flows of capital by attracting FDI and then building local networks of production (typically sub-supply) and innovation (much more rarely) around this 'imported' industrial organisation. It can also attempt to foster indigenous networks of innovation and then encourage them to internationalise, but from a position of relative strength. In either case, the state development strategy is to connect the local and the global economy in such a way that local industrial transformation, accumulation, and development can take place. The FDS plays a key role in fostering 'better' connections to the global (Ó Riain, 2000: 165).

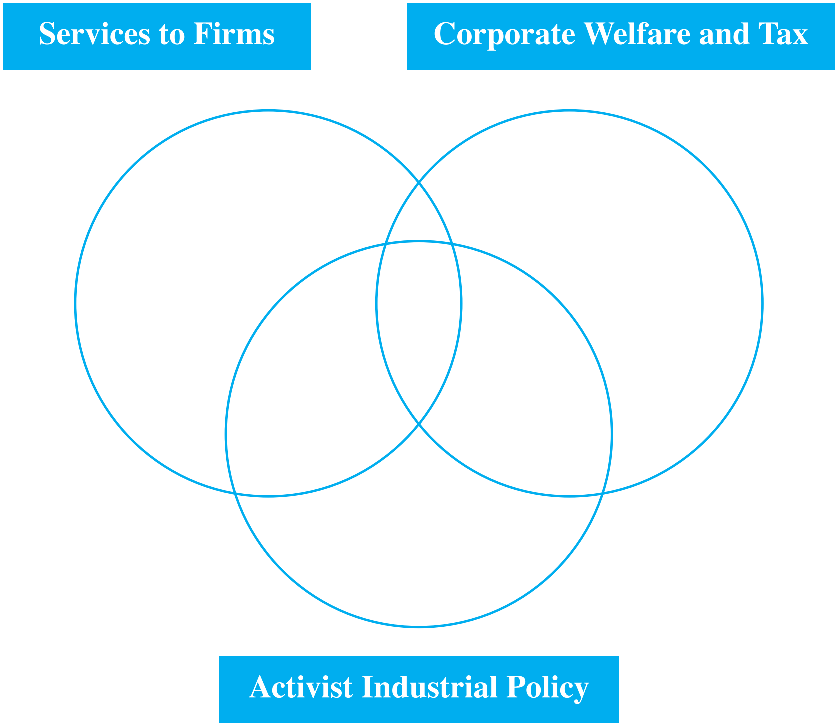
The software sector is perhaps the clearest example of what Ó Riain describes as the "two globalisations" that characterise the Irish economy of the past decade. The first of these derives from the attraction of FDI and, to a limited degree, embedding in the local economy ("The global goes local"). The second—and, as Ó Riain notes, most surprising in the context of Irish economic history—is the emergence of a local network of indigenous firms that have become integrated into international business and technology flows and have become successful in international markets ("The local goes global"). These are complemented by what Ó Riain sees as a third mode of integration into the global economy: the social partnership arrangements by which "the national level mediates local adjustment to the global" (Ó Riain, 2000: 184).

This perspective allows us to see that the Irish state—through a complex and flexible set of agencies and policies—has played a key role in the economic progress of the past decade and a half. Under a fairly invariant industrial 'policy', the agencies have flexibly reconfigured the package of services that they offer, in dialogue with their client firms. The agencies and the firms seem to be jointly exploring the latest organisational and technical possibilities and teasing out how they can be applied in Ireland. The development agencies are in a complex form of interdependence with government departments, universities and the social partners. This also constitutes a new form of external accountability.

In many respects, the conduct of development policy—and the flexible client-centred recasting of the services—is a model that allows us to see what a new form of public administration and agency can be.

In order to link this discussion of development policy to the analysis of social policy in Chapter 2, it may be useful to present the following picture of the three elements of development policy: corporate welfare and tax, services and activist policy initiatives by public agencies.

FIGURE 1.3
The Three Elements of Development Policy



While Irish policy initially relied heavily on corporate welfare and tax breaks and direct forms of activism (such as state-owned industrial firms), it has increasingly moved towards the provision of services and new forms of networked, or associational, activism. This theme will be taken up in subsequent chapters, when we discuss social policy, explore how the developmental and welfare aspects of public policy can be related to one another, and think about the organisational challenges that are now critical in so many areas of public policy.

The most significant success of Irish-owned companies in international business is in the software sector. Employment in Irish-owned software companies was 14,000 in 2000, almost 46.7 per cent of total employment in this sector (30,000). The bulk of exports, however, were by foreign-owned companies (90 per cent), although indigenous exports in 2000 had increased six-fold since 1993[2].

1.3.2 Competitiveness

International competitiveness has a key influence on the growth of a small open economy. One aspect of competitiveness is cost competitiveness. There are a range of ways of measuring cost competitiveness and these are examined in some detail in Chapter 6. Data on unit labour costs from the OECD *Economic Outlook* (June 2002) show that over the period 1990 to 1999, unit labour costs in Ireland increased by 0.5 per cent compared to a euro area average of 2.1 per cent. This exaggerates the improvement in relative unit labour costs for Ireland, as unit labour costs have been particularly reduced by the growth of a limited number of very high productivity sectors that are also subject to some distortion due to profit switching transfer pricing. Nonetheless, the position in relation to cost competitiveness was satisfactory over much of the 1990s and contributed to employment growth. As discussed above, this trend of an improvement in cost competitiveness has been reversed in recent years, but partly offset by currency movements.

Further insights into Ireland's competitiveness performance can be gained by considering export trends. Export demand can be analysed as the product of two factors, the growth of export markets and the performance of Irish exports in these markets. Kennedy (2001) has analysed the contribution of each of these factors. The growth of export markets depends on the growth rates of our trading partners. The key market for Irish exports is the EU. This market absorbs over 60 per cent of Irish exports. In the EU, there has generally been a fairly modest growth of GDP during the 1990s. However, despite the fairly modest growth, there has been strong import growth. Import demand in the EU grew by an annual average of 8.1 per cent between 1993 and 2000, close to the growth of 8.7 per cent during the years of much stronger GDP growth from 1960

3. Data supplied by the National Software Directorate, a division of Enterprise Ireland, the agency for supporting Irish-owned manufacturing and international services.

to 1973. This implies there was an increase in import elasticity. Kennedy suggests that this is a result of the single market.

Irish exports benefited from strong growth of export markets and Irish market share also increased substantially. Between 1993 and 2000, Irish exports grew at a phenomenal rate of over 16 per cent per annum. Export market growth increased by 8 per cent per annum over this period. The difference between export growth and market growth is a measure of performance in terms of increasing the market share of Irish exports.

TABLE 1.8

Irish Export Performance : Annual Percentage Growth

	Volume	Market	Performance
1963-80	7.7	3.2	4.4
1980-93	9.2	4.1	4.9
1993-2000	16.5	8.0	7.8

Source: Kennedy (2001) based on OECD Economic Outlook.

The growth of exports and export performance raises the question as to why Irish exports have grown so strongly. This is to a large extent the result of the success in attracting FDI, notwithstanding an improved export performance by indigenous manufacturing.

1.3.3 EU Membership and the European Internal Market

The deepening of European integration was a major factor in Ireland's economic transformation. That deepening had three main components:

- The programme to complete the European internal market;
- The doubling and reform of the Structural Funds; and
- The transition to monetary union.

These had direct effects on Ireland's economy and provided the context in which the factors discussed elsewhere in this Chapter were able to operate. Ireland's support for the deepening of

European integration has been vindicated by the economic success from 1987 to the present.

The European Internal Market Programme

The completion of the European internal market internal was a most important factor in the recovery and re-orientation of the Irish economy.

It was a major cause of the increase in US and Japanese investment in Europe in the late 1980s and early 1990s. This benefited Ireland in particular, as our commitment to the deepening of integration was a major attraction to the new wave of companies investing in Europe.

For Irish companies, the internal market provided both new market opportunities and a focus for their business strategy. Every sector and company was invited to analyse its readiness for intensified competition and wider market opportunities. Issues of peripherality and market access were widely discussed, and all sorts of solutions found. One of the striking changes in Irish business in the past decade is in logistics. To visualise these positive effects on business, consider, for example, how Irish food firms exporting to European markets benefited from the adoption of EU-wide labelling and content rules and the ending of delays at customs posts. Likewise, Irish service firms benefited from the right to establish offices and compete for public contracts in other member states.

The energising effect of the internal market was particularly important in services—such as banking, aviation and road haulage—which had operated in a relatively protected environment. Irish citizens and companies benefited from lower prices and better quality, and Irish companies responded to increased competition by adopting aggressive strategies at an international level.

Another important element of the internal market was free movement of capital. This benefited Irish individuals and companies, allowing them to access capital abroad, diversify their portfolios and maximise their return on capital.

A further critical aspect of the internal market programme was increased EC monitoring and control of state aids and public procurement. The internal market limited the ability of the larger and richer member states to protect their markets by state aid and strengthened the hand of Irish governments in promoting competition at home. But it did not undermine the Irish state's developmental role, as the EU has allowed more leeway for industrial policy in Objective 1 regions.

The internal market was a cause of significant change in public utilities—telecommunications, electricity, gas and postal services. But it did not dictate exactly how this re-regulation should be done, and Ireland retains discretion on how these sectors should be regulated. These developments are discussed in Chapter 9.

Indeed, Ireland's overall approach to market and social regulation has been significantly re-shaped by membership of the EU. This is evident in the creation of numerous independent regulatory agencies, such as the Employment Equality Agency, the Competition Authority, the Health and Safety Authority, the Environmental Protection Agency, the Food Safety Authority and the Office of the Director of Telecommunications Regulation. These new regulatory agencies have three important characteristics:

- They are independent of government and politics;
- They separate supply of a product from regulation of the sector; and
- They are a part of networks of European regulatory agencies.

It is up to Ireland to make these new regulatory agencies work effectively in the interest of citizens, customers and commercial success (see Chapter 9).

Indeed, the combination of social partnership and the European internal market programme is a particularly interesting aspect of the Irish story (O'Donnell, 2000). Social partnership has various advantages, as noted above. But one possible limit of consensus is the difficulty of undertaking radical action which disrupts entrenched interests in protected sectors. While social partnership stabilised the economy, European integration produced a steady pressure to make public services and utilities more efficient, consumer-oriented and independent of overt or covert state subsidy or protection. Thus, Ireland benefited from an unusual, but benign, combination of institutionalised co-ordination of the key economic actors and pressure for market conformity.

It was feared that completing the internal market might cause economic activity to concentrate in the rich centre of the EC. Irish and Spanish articulation of the possibility of greater regional inequality, and the Commission's desire to balance market deepening with greater economic cohesion, were important factors in the doubling and reform of the Structural Funds which accompanied the internal market programme.

From EMS to EMU

The development of European monetary integration was also a factor in the success of the Irish economy, although one on which there is less agreement.

The determination of exchange rates—and the impact of exchange rates on employment, exports and inflation—are the subject of much economic analysis on which there is considerable disagreement among economists. In addition, the EMS is the subject of much debate, complicated by the fact that the system worked in different ways at various times in its 20-year life. This is compounded in the Irish case, since sterling's non-participation in the System undoubtedly made the Irish experience more difficult. Indeed, an assessment of Ireland's participation in European monetary integration is complicated by the fact that British macroeconomic management, the instability of which influenced Ireland to join the EMS in 1979, has been much more stability-oriented since the mid-1990s.

Allowing for the variety of technical economic analyses, the following may be a balanced summary of Ireland's participation in the EMS and the transition to EMU (Honohan, 1993; Leddin and Walsh, 1998, O'Donnell, 2000):

- Although it took some time, the EMS encouraged greater discipline in both public finance and wage bargaining;
- Ireland used the realignments in the EMS to steer a pragmatic middle course between sterling and the German mark;
- The EMS regime was associated with high and volatile interest rates;
- The decision to join the single currency was based on a judgement of the relative significance of monetary and real factors in determining the long-term international competitiveness of a small European country;
- A policy approach consistent with low inflation, competitiveness and economic growth was achieved through a combination of EMS and the social partnership programmes, in place since 1987;
- The Maastricht criteria for entry to EMU provided agreed parameters for Irish fiscal policy through much of the 1990s;
- Given the flexibility of exchange rates in the 'wide EMS' after 1993, the move to the euro is a significant change and requires additional flexibility in other areas;
- The transition to monetary union has yielded low interest rates, which benefit companies and mortgage holders; and
- The conditions in which the transition to the monetary union occurred, and the weakness of the euro, have created inflationary pressure in Ireland.

Conclusion

Given the importance of the internal market, the Structural Funds and the transition to the euro, it is clear that the deepening of European integration which begun in the mid-1980s, and continued through the 1990s, has been an important factor in Ireland's economic breakthrough since the late 1980s.

1.3.4 Strong Role of Inward Investment

To a significant extent, the improvement in Ireland's economic performance from the 1960s was driven by a newly established, export-oriented multinational base. During the 1960s and 1970s, foreign-owned, export-oriented firms accounted for virtually all of the net growth of employment in manufacturing. For the most part, indigenous industry did not perform well in the adjustment to free trade. The weak performance of indigenous industry has been a concern in several NESC reports. In his wide ranging comparative study for the Council, Mjøset (1992) identified Ireland's development problem as the weak development of indigenous industry.

US FDI flows into Ireland increased significantly in the 1990s; Ireland's share of all US FDI into the EU averaged well over 5 per cent over the 1990s (Duffy *et al*., 2001:15).

Contribution of Key FDI Sectors to Output Growth

In recent years the CSO has separately identified the contribution of key sectors that are dominated by foreign-owned multinationals (MNCs). These sectors are: reproduction of recorded media, chemicals, computers, instrument engineering, and electrical machinery and equipment. Software is partly included in 'reproduction of recorded media', but only to the extent that it is a manufacturing activity. These were by far the fastest growing parts of the economy, increasing output by an average rate of 21.5 per cent a year between 1995 and the 2000. Since the rest of the economy grew by an annual average rate of 6.7 per cent, it is clear that growth was not confined to the MNC sectors. But this growth rate of 6.7 per cent is more that 3 percentage points lower than the rate of growth of GDP (9.8 per cent) as a whole over this period and also lower than the rate of GNP growth (8.7 per cent).

Keating (2000) has presented a more detailed examination of the direct contribution of the top 34 MNC enterprises to both GDP and GNP. He estimated that in 1998 that these enterprises accounted for approximately €12.7 billion out of a 1998 GDP total of €77.5 billion and for about €3.8 billion of the GNP total of €67.3 billion. This represents a contribution to GNP of close to 6 per cent. These figures are exclusive of any induced multiplier effects and do not cover all MNCs.

Contribution of FDI to Exports

The expansion of exports has been particularly reliant on the contribution of FDI enterprises. Between 1993 and 1999, manufacturing exports expanded by approximately by €37.3 billion. Of this, €36.4 billion was due to foreign-owned companies while less than a billion euros came from Irish-owned companies. The contribution of foreign-owned companies to the growth of net export earnings would be substantially lower, given the high import propensity and profit repatriation of these companies. Exports by foreign-owned companies increased by 230 per cent, while exports by Irish-owned companies increased by 21 per cent over the 1993 to 1999 period. In 1999, the 10 FDI enterprises with the greatest value of exports accounted for exports to a total value of over one third of the total exports of goods and services. These 10 enterprises also accounted for imports of 27 per cent of the total (Keating, 2000).

The percentage increase in exports by Irish-owned industry was affected by the dominance of the food sector. This sector represents 60 per cent of the exports of Irish-owned companies and many of its products are subject to constraints on output. Excluding food, the increase in exports by Irish-owned manufacturing was over 50 per cent between 1993 and 1999[4].

Role of FDI in Employment Growth

The key FDI sectors also played a significant role in the increase in employment. Table 1.9 shows employment growth in manufacturing and internationally traded services, distinguishing between Irish-owned and foreign-owned enterprises. A striking feature is the very strong employment growth of internationally traded services—by an annual average of over 23 per cent between 1993 and 2000.

4. The data on manufacturing exports in this paragraph and the preceding paragraph have been calculated from the 1993 and 1999 CSO, *Census of Industrial Production*.

Manufacturing employment grew by close to 9,000 per year, while international services grew by an annual average of 7,500 over this period.

TABLE 1.9

Employment in Manufacturing and Internationally Traded Services

	1993 (000s)	2000 (000s)	Annual Change (per cent)	Annual Change (000s)
1. Manufacturing	219.4	281.0	3.6	8.8
2. Internationally Traded Services	15.8	68.3	23.3	7.5
3. Total 1 and 2	235.2	349.3	5.8	16.3
4. Irish-owned	128.0	169.1	4.1	5.9
5. Foreign-owned	107.2	180.3	7.7	10.4
6. Total Economy	1152	1588	4.7	62.3

Source: Calculated from Forfás, *Annual Employment Survey* 2000 and ESRI databank.

Notes: The employment figures include both permanent, full-time employment as well as part-time and contract employment. The figures for manufacturing include mining/quarrying, although this has only a marginal effect on the trends shown.

Employment in foreign-owned companies in these sectors increased by an annual average of 10,400 per year. Total employment grew by over 62,000. Therefore, the direct contribution of foreign-owned multinationals in the internationally trading sectors accounted for approximately 16 per cent of employment growth. It would also have induced additional employment elsewhere in the economy.

Over the period 1993 to 2000, Irish-owned companies contributed significantly to employment growth in the manufacturing and internationally traded service sectors. The expansion of employment of Irish-owned companies in these sectors represented over a third of employment growth in these sectors. To some extent, this is a reflection of the growth of domestic demand. The percentage of output of Irish-owned manufacturing that was exported declined from 35.3 per cent in 1993 to 31.3 per cent in 1999.

The employment impact of FDI became more significant as a result of the rise in the internationally traded services component of FDI. Internationally traded services employment (including both foreign- and Irish-owned firms) increased by around 7,000 per year between 1993 and 2000. The multiplier effect of FDI activity has also been increasing. Barry (1999) reports that Irish economy expenditure per job for FDI firms increased by over 50 per cent in real terms between 1983 and 1995. This implied a magnification of the sector's employment creation effects, applying to the existing base as well as to new employment.

Interpretation

The undoubted significance of inward investment by MNCs plays a central role in a number of interpretations of the Irish economy. It is clear that the improvement in export performance has been largely driven by MNCs. It is argued below that the Irish economy can usefully be thought of as a regional economy in which the growth of the export base has a major influence on the growth of the economy as a whole. From this perspective, MNCs have been a key influence on the very strong growth in the economy. At the same time, it is also clear from data above that growth has occurred across the economy and that the MNCs have accounted for a relatively small direct proportion (16 per cent) of the growth in total employment. As further analysis in Chapter 10 indicates, care has to be exercised in interpreting the meaning and significance of Ireland's reliance on inward investment.

1.3.5 Demographic Developments, Labour Supply and Education

Demographic conditions implied strong growth in potential labour supply during the 1990s, as a result of the baby boom of the 1960s and 1970s. Relatively low female labour force participation also meant that there was strong potential for labour supply growth. However, in itself, an increase in potential labour supply could have manifested itself in higher emigration and downward pressure on wages. High levels of emigration were evident in the late 1980s and continued into the early 1990s.

The 1990s saw not just an expansion in the quantity of labour, but an expansion in the level of education of those entering the labour force. This is widely, and correctly, regarded as a significant contributor to economic growth. In an open economy the overall level of education depends not only on the education system but is also affected by migration trends.

The increase in the educated workforce had a particular significance in the context of rising demand for skilled labour. The effects of improving human capital on the economy in this context have been examined using a formal model by Duffy *et al*. (2001). They estimated that the effect of holding human capital fixed at its 1990 level would be a reduction in GDP by 1998 of 6 per cent below its actual level and unemployment over 13 percentage points higher than its actual level. The improvement in human capital in Ireland had highly beneficial economic and social effects because it occurred at a time when the demand for skilled labour was increasing generally in developed countries and in Ireland in particular through FDI. In their analysis, Duffy *et al*. found that without the increase in human capital, the wages of skilled workers would have risen sharply resulting in a decline in competitiveness and a significant increase in wage dispersion. Without the improvement in human capital, the supply of unskilled labour would have increased very significantly. At the same time, the decline in competitiveness would have meant lower GDP and lower demand for unskilled labour. Hence, the very substantial increase estimated for unemployment.

1.4. UNDERSTANDING IRELAND'S ECONOMIC DEVELOPMENT

Section 1.3 has summarised five key factors which gave rise to Ireland's strong economic performance. The Council offers an interpretation that can incorporate these elements, without elevating any one of them inappropriately. It is also an interpretation than can make sense of current Irish developments and policy challenges.

1.4.1 An Interpretation of Ireland's Economy

In its reports since the mid-1980s, the Council has formulated its advice to government on the basis of a number of empirical observations and analytical principles. These included:

- The importance of competitiveness in a small open economy;
- The limited role of demand management in sustaining employment and output in Ireland;
- The role of European integration in facilitating the development of a small peripheral region;
- The importance of specialisation in high-value, high-growth, sectors in maximising the gains from trade and integration;
- That technological development can make it possible for certain countries or regions to rapidly improve their position in the international economic system;
- The validity of European regional policy and the importance of using Structural Funds to reduce the disadvantages of peripherality;
- Most of the policies that affect national prosperity are supply-side. These must produce flexibility. Successful supply-side policies, directed towards innovation and competitiveness, depend on a high level of social cohesion and co-operation;
- The validity of development policy in building first the capacity and then the capability of the export sector;
- The damaging long-run effect of emigration and the importance of increasing population and employment in Ireland;
- The inter-dependence between the traded and non-traded sectors, and the importance of an efficient non-traded sector;
- The interdependence between the economic and the political and the need for a consistent set of macroeconomic, distributional and structural policies based on a shared understanding; and
- The importance of regional networking in strengthening competitive advantage.

A similar perspective has been neatly encapsulated by Krugman, in his suggestion that the Irish economy can usefully be thought of as having some of the characteristics of a regional economy (Krugman, 1997). A regional economy is an open economy with the key characteristics of very high exposure to trade and a mobile labour force. In such an economy, the export base and its external competitiveness have a critical influence on the size of the economy. Investment in an open economy will be strongly influenced by the profitability of investment compared to other economies. The level of technology and know-how available in an open economy will be also strongly influenced by investment flows from abroad and the ability of the society to absorb technologies developed elsewhere. If, for whatever reason, the economy becomes more competitive in some rapidly growing export sector (industry or services), workers will be attracted to the region both to work in the export sector and to work in service industries whose expansion is induced by the growth in the export sector. If, by contrast, the export sector collapses in a regional economy, the economy may contract and workers emigrate. Consequently, competitiveness has a much more direct influence on a small regional economy than on a large national economy.

A regional economy is a type of a small open economy (SOE). An SOE can be divided into internationally traded and non-traded sectors. The internationally traded sector can further be divided into two sectors, *resource-based activity*, whose location is determined by the availability of some natural resource, and *mobile activity* whose location depends on competitiveness and profitability. While the non-traded sector is not directly exposed to international competition, it affects the competitiveness of the exposed sector and is also very much influenced by the level of activity in the traded sector.

This analysis has been implicit—and, in some aspects, explicit—in the Council's reports of the past decade and a half. Applying this set of ideas to the long-run development of the Irish economy, yields an analysis very similar to that developed by the Council in many reports.

1.4.2 Understanding Ireland's Long-Run Development

Before 1960 the Irish economy can be usefully thought of as a regional economy based on agriculture or a resource-based SOE (NESC, 1989; 1996a; Mjøset, 1992; Barry, 1999; Nolan and Nolan, 1991). Agriculture provided virtually all of the export earnings. There was a small industrial sector, that had been fostered through protectionism. This can be considered as expanding the size of the non-traded sector. This economy was able to achieve some productivity growth, mainly through growth of agricultural productivity. Labour supply contracted as emigration occurred. Agriculture could not provide a basis for employment growth. Productivity growth in agriculture did underpin some income growth in the economy. However, this was insufficient to provide much growth in the non-traded part of the economy (NESC, 1989). It was difficult to achieve either extensive or intensive growth.

There was a marked improvement in performance in the 1960s, as noted above. Freer trade provided a basis for improving efficiency and productivity. The decline in employment was halted and wages began to converge steadily with the UK (Fitz Gerald, 1999). The stabilisation of employment and growth in wages implies that the demand for labour was increasing. FDI was a critical factor in initiating this stronger growth in labour demand. There was rapid growth of manufacturing employment during the 1960s and as well as an expansion of non-traded services that had been declining.

The improvement in performance did not imply much convergence with average incomes in Europe. GDP per worker, or productivity, was converging from the 1970s. GNP per worker was converging since the mid-1980s (Duffy *et al.*, 2001).

Long Term Successes and Failures

In its 1996 Strategy report the Council summarised Ireland's successes and failures in the decades after 1960 (NESC, 1996a).

The outward looking strategy had four significant successes from 1960 to 1987. First, after a century and a half of virtual stagnation, Ireland achieved relatively strong economic and demographic growth. Second, there was a dramatic structural adjustment of the economy. In 1960, agriculture, forestry and fishing accounted for almost 37 percent of all employment. By 1987, this had fallen to 14 per cent. Third, these achievements were accompanied by a distinct modernisation. The period after 1960 saw a strong increase in living standards and expectations. Incomes, wages and welfare provisions converged with those in the UK and the quantity, quality and range of consumer goods increased strongly. Fourth, Ireland had great success in attracting inward investment and became accustomed, relatively early, to attracting and using inward investment.

Although the Irish economy achieved significant economic growth, adjustment, modernisation and inward investment since 1960, these successes are qualified in important ways. Growth was not handled well, giving rise to inconsistent claims on the Irish economy. Awareness of the international environment was incomplete. The adjustment of indigenous enterprises to international competition failed more often than it succeeded. Job creation was insufficient, old jobs were lost at a remarkable rate and unemployment increased. High levels of savings and corporate profits were not matched by investment in the Irish economy. Inevitable adversities were allowed to become divisive and produced delayed and insufficient responses. Overall, there was an insufficient appreciation of the interdependence in the economy—between the public and the private sectors, between the indigenous economy and the international economy, and between the economic and the political.

In 1996, the Council continued, "these problems arose as much in periods of strong economic growth, as in periods of international recession. An understanding of these weaknesses and the possibility of repeating them in a period of high growth, is critical in current circumstances" (NESC, 1996a: 21).

We can now elaborate this perspective somewhat, by saying that an important policy lesson from our long-term experience is:

- The need for early rather than slow reaction to new conjuncture;

- The need to maintain core long-term strategies and investments; and
- The need to modify these in the light of changing circumstances.

These lessons are relevant to the current situation, as is illustrated in Chapter 3 below.

1.4.3 Understanding Ireland's Experience of Economic Boom in the 1990s

Combining the factors listed in Section 1.3 above, with the analytical approach summarised in Section 1.4.1 we can also understand Ireland's remarkable economic boom in the 1990s.

It is, of course, a simplification to put the factors that caused growth in a given order, since in reality they operated simultaneously. Nevertheless, the Council sees the story of Ireland's boom in the 1990s as follows:

- The adoption of a consistent policy framework through partnership—especially fiscal correction—which increased confidence;
- Social partnership consolidated a trend towards wage moderation and significantly increased competitiveness;
- Organisational and technological developments prompted the American firms in IT and software that had led the revival of the US economy to seek outward investment;
- The Single European Market programme, initiated in the mid-1980s, played a major role because it:
    - Caused a large increase in both Japanese and American investment in Europe;
    - Increased the mobility of financial and other service firms;
    - Prompted Irish firms, in industry and services, to adopt new business strategies and organisational arrangements;
    - Prompted new approaches to the regulation of services and utilities;

  - Gave rise to a doubling of the Structural Funds (which were doubled again following agreement of the Maastricht Treaty);
- Ireland's competitiveness and large educated English–speaking workforce, made it an attractive location for US investment;
- Irish development policy assisted both inward investment and indigenous business revival because it:
  - Targeted emerging global leaders in high-growth sectors;
  - Produced an increased supply of computer science and other graduates;
  - Changed its focus from building capacity to developing capability;
  - Initiated innovative institutional arrangements in software and bio-technology;
- There was strong progress in indigenous business, because of cost competitiveness, increased organisational capability, improved industrial relations and greater entrepreneurship;
- As employment and profits increased a virtuous circle developed: buoyant tax revenue allowed tax reductions that supported continued wage moderation and further increased Ireland's competitiveness, which increased inward investment, yielding income that increased domestic demand, giving rise to non-traded business activity and further employment;
- The sense of an economic miracle was reinforced by two factors that are, in part, arithmetical:
  - Increasing employment and labour force participation, and falling dependency, meant rising income *per head of population* and rapid convergence to EU levels of income per head;
  - Increasing concentration in high-productivity sectors gave the impression of particularly strong productivity *growth*;
- The employment impact of FDI increased for two reasons:

  - An increase share of services, which are more labour intensive than manufacturing;
  - Increased linkages with the indigenous economy.

- Irish local development and active labour market policy played a role by aiding the transfer from welfare to work and re-vitalising localities;
- Low interest rates encouraged investment in both the corporate and personal sector;
- Low and predictable inflation yielded real income increases, underpinned wage moderation achieved through partnership and provided a stable business environment;
- Cost pressures arising from rapid growth were compensated, and probably camouflaged, by currency depreciation, both before and after the introduction of the euro; and
- Return migration and immigration allowed the boom to continue both directly, by facilitating extensive growth, and indirectly, by preventing an erosion of competitiveness.

To summarise, Ireland's dramatic economic performance in the 1990s was caused and sustained by three main factors:

- **The national policy and institutional framework**, which was consistent, highly focused on competitiveness and employment-creation, innovative and problem-solving;
- **An export sector** that was greatly expanded and increasingly concentrated in high-value, high-growth market segments; and
- **The European Union**, because it increased market access through creation of the single market and negotiation of WTO agreements, created a level playing field through re-regulation, provided a relatively stable monetary environment and supported Ireland's infrastructural and social development.

This interpretation differs from two others that have been recently advanced.

Irish Development Contains Fatal Contradictions

One alternative view is that Ireland's economic and social development is fatally flawed. O'Hearn argues that Ireland's development through participation in the international economy has done nothing to reduce its neo-colonial dependence and peripherality. He goes so far as to say, "In the main, the Irish tiger economy boils down to a few US corporations in IT and pharmaceuticals" (O'Hearn, 2001: 75). Indeed, he suggests that much of Ireland's growth is an illusion, reflecting the inflated output of key firms in a narrow band of sectors, such as computers, pharmaceuticals and software. Little real breakthrough has been achieved by indigenous enterprises.

It is undoubtedly true that foreign-owned multinationals have accounted for a very large proportion of Ireland's increased exports, output and employment in the tradeable sector. However, not all these foreign-owned multinationals can be seen as export platforms with little developmental impact on the Irish economy. More importantly, the predominance of foreign-owned multinationals' output and exports should not be allowed to occlude the very significant improvement in the capabilities and performance of indigenous firms in both manufacturing and services[5]. O'Malley's judgement on the performance of indigenous manufacturing is that the "the scale and durability of this improvement is without precedent in twentieth century Ireland" (1998: 35).

5. Employment in Irish-owned manufacturing enterprises increased by more than 10 per cent between 1987 and 1997 (O'Malley, 1998). This employment growth is not only greater than has been achieved in Ireland in the past, but significantly outpaces manufacturing employment growth in the EU, the UK, Japan, the US, Australia and Canada. Nor is it dependent on sub-supply to TNCs; exports of Irish firms increased faster than employment through the 1990s, despite slower growth in overseas markets than in the Irish economy. Indeed, the highest growth in employment in Irish manufacturing firms occurred in the more highly traded and internationally competitive sectors. Having been virtually stagnant between 1980 and 1987, the output of Irish-owned manufacturing increased by an average of 4.0 percent per year from 1987 to 1995—more than twice the OECD average. Ó Riain points out that industrial R&D spending in the whole economy increased in real terms by 15 percent among foreign firms and 16 per cent among Irish-owned firms.

Irish Development is Merely Delayed Convergence

O'Grada (2002) has recently proposed that the relatively strong Irish economic growth since the late 1980s can be interpreted as delayed convergence. He points to the long-run tendencies among OECD countries for convergence; those countries with below average incomes have tended to have above average growth per capita. He points out that looking at the long-run period since 1950, Ireland has been an exception in this regard. Despite having well-below average income in 1950, Ireland failed to achieve above-average growth in output per head until the late 1980s. As a result of the very strong growth in the period since the late 1980s, Ireland has recovered the lost ground since the 1950s. If growth is viewed over the period since 1950, Irish economic growth has been no higher than would be expected. A convergence perspective on economic growth also informs a recent analysis of Irish performance by Honohan and Walsh (2002).

From this perspective, what is puzzling about Irish economic performance is why it took so long for convergence to take place. The answer usually given is that convergence was delayed by various policy errors until the late 1980s.

Barry (2002) has identified two policy implications of the convergence approach. First, "the logic of the standard growth/convergence model certainly does not require non-orthodox policies such as Ireland's low rate of corporation tax" (Barry, 2002: 86). Indeed, O'Grada, in advancing the standard convergence view, explicitly describes Irish industrial policy as a "distortion". Second, "if the convergence view is correct, it suggests that we can now rest on our laurels; as long as we do not introduce inappropriate policies we are unlikely to fall behind average EU living standards" (Barry, 2002: 90). These policy issues are discussed further in Chapter 10.

1.4.4 The Vulnerabilities of Irish Economic Development

While the Council is not persuaded by either of the two perspectives discussed above, it is clear that each contains some accurate observations. When these points are combined with the Council's own interpretation it becomes clear that Ireland's small size, peripheral location and the type of economic development achieved in recent decades contains undoubted vulnerabilities. These vulnerabilities include the following:

- It is hard to measure and forecast the Irish economy and, therefore, hard to keep a clear view of facts, timing and trends (NESC, 1990; Keating, 2000; Blanchard, 2002). This makes it difficult to coordinate the actions of employers, unions and government[6];
- The reliance of the economy (not only its income, but also its very size) on international competitiveness means that public policy must achieve two things that can seem inconsistent:
  - Rapid and widespread adaptation of policy, laws, regulatory regimes and structures, in the traded, non-traded and public sectors;
  - A predictable long-term economic strategy and policy framework;
- The possibility of extensive growth can give rise to a range of problems:
  - Infrastructural and other bottlenecks;
  - Super-normal profits and rents;
  - Inflation;
  - The challenge of integrating people from abroad;
  - Patterns of spatial development that are undesirable;
  - Pressure on the environment;
- An export base containing rapid growth of very high productivity sectors can create pressures in both the economy and society;

6. Examples of these difficulties include (i) inflation prediction in the PPF (ii) debates over Irish wage levels and (iii) predictions of revenue.

- Financial openness can create problems, as well as advantages, for the corporate, personal and public sectors;
- The openness of the economy and society and its small size in world terms—and the associated importance of trade, international investment and labour mobility—means that the existence of international political and regulatory institutions is absolutely critical to both economic development and social cohesion. Ireland's size, location and model of economic development make it highly vulnerable if there were any loss of influence or status in the EU or, worse still, if there was a return to a less rule-based international system that did not constrain the naked use of diplomatic and economic power;
- The small size of the country, and its peripheral location, can make it difficult to devise the best regulatory regime in networked sectors, such as telecommunications, energy and parts of transport;
- Policy errors, such as pro-cyclical fiscal policy, will be punished severely, because of the importance of competitiveness;
- The need to build an export base containing high-tech, high-growth sectors, and the need to achieve a high level of employment in the market sector, can imply an unacceptable level of inequality (see Chapter 2 for further discussion of this);
- The possibility of extensive growth implies the possibility of extensive decline (through out-migration of both enterprises and people); and
- Wage trends can have very significant positive or negative effects. As Blanchard has noted, "in an economy such as Ireland, open in trade, capital, and most importantly labour markets, wage explosions can kill; on the other hand, wage moderation can do miracles" (Blanchard, 2002: 2).

The Council believes that acceptance of the core elements of Ireland's economic strategy demands a recognition of the vulnerabilities listed above. The policy implications of this are identified in Chapter 3 below.

CHAPTER 2

IRELAND'S LONG RUN SOCIAL DEVELOPMENT AND VULNERABILITY

2.1 INTRODUCTION

This Chapter offers an account of Ireland's social development in order to identify the major social challenges that must be addressed in national policy. Section 2.2 reviews the main social developments since 1987, the start of the current partnership period. It begins with evidence about trends in standards of living and the money incomes which support them, and continues with a review of other major indicators that reflect and affect people's quality of life and the overall well-being of society. Section 2.3 then adopts a long-term perspective and interprets the country's long-run social development, paying particular attention to the social effects of emigration and a weak national system of innovation, the evolution of the Irish welfare system, the effects of industrialisation on class transformation and social mobility, the different influences on income distribution, and, finally, the associated cultural processes of liberalisation, pluralisation, and secularisation. Given the many social problems that continue to be experienced in Ireland, some argue that our social system is fatally contradictory. Section 2.4 examines this view and concludes that it is more accurate to say that Irish society is open to a number of undoubted vulnerabilities which derive from the legacy of the past, the economic context, and the organisational challenge of public provision in an age of complexity and volatility. This analysis allows us to identify the challenges that must be met if Ireland is to secure its long-term social development. The Council's view on how they should be tackled is presented in Part III of the *Strategy* report.

2.2 SOCIAL DEVELOPMENTS SINCE 1987

It is not surprising that the dramatic economic growth of the 1990s further accelerated social changes. Many of these changes are linked to the major expansion of the labour force and employment and the associated large reduction in unemployment which have been reviewed in Chapter 1. Most of the direct social consequences of the employment expansion are hugely positive. These include higher living standards, an enhanced sense of well-being for many (caused, among other things, by the increased sense of autonomy that comes with earning), more gender balance, a reduced need for welfare and more resources available for supporting those who remain socially vulnerable. But other social consequences are challenging. These include a stronger contrast between multiple-earner households and households in which no-one is earning, a widening gap in hourly earnings, a step-increase in demand for childcare services, a greater squeeze on people's time, and the greater influence of work on physical and mental health.

The following sub-sections document some of the principal social developments that have characterised the current partnership period that began with the *Programme for National Recovery* in 1987.

2.2.1 Consumption and Living Standards

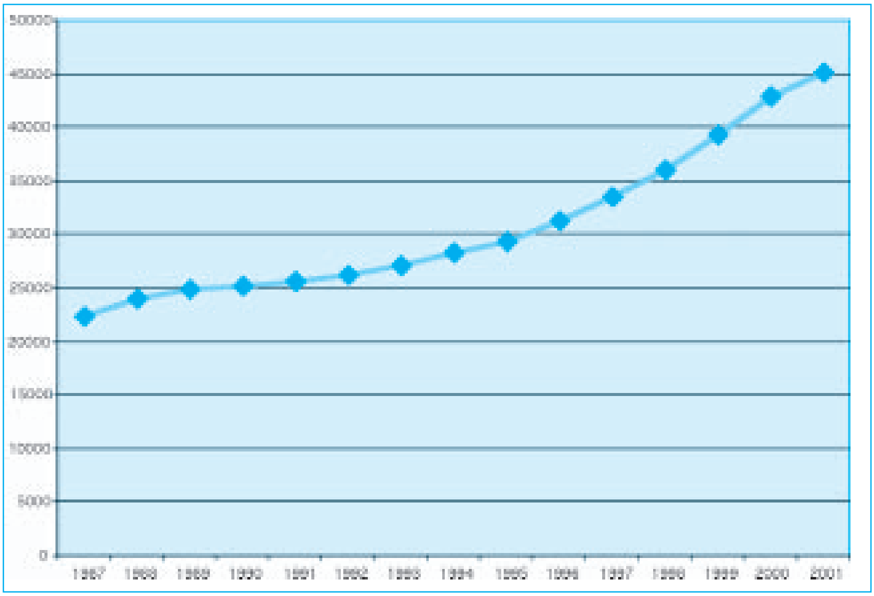
The element of GNP that is most directly related to current living standards is private consumption expenditure.[1] The total expenditure on goods and services by private consumers grew by approximately 100 per cent in real terms between 1987 and 2001. This has been driven partly by population growth but principally–as will be demonstrated below–by higher real incomes per capita. The net result is a huge increase in the volume of consumer spending taking place in the Irish economy, as Figure 2.1 demonstrates. These purchases are largely made out of disposable personal income (some of which is typically saved also), with credit and dissavings playing supporting roles. The average annual rate of growth in consumer expenditure in real terms was over 5 per cent during the 1990s, a significant figure for such a sustained period. Because of this, there has been a rapid convergence with the 'average spend' of

1. Current living standards are also raised when public services improve in quantity and quality.

consumers in the EU, as Figure 2.2 shows. In 1987, private consumption expenditure per capita in Ireland was only some 72 per cent of the EU average; by the year 2002, it is estimated that it was 95 per cent of the EU average (adjusted for differences in purchasing power).

FIGURE 2.1

Personal Expenditure on Goods and Services: € Million in Constant (1995) Market Prices

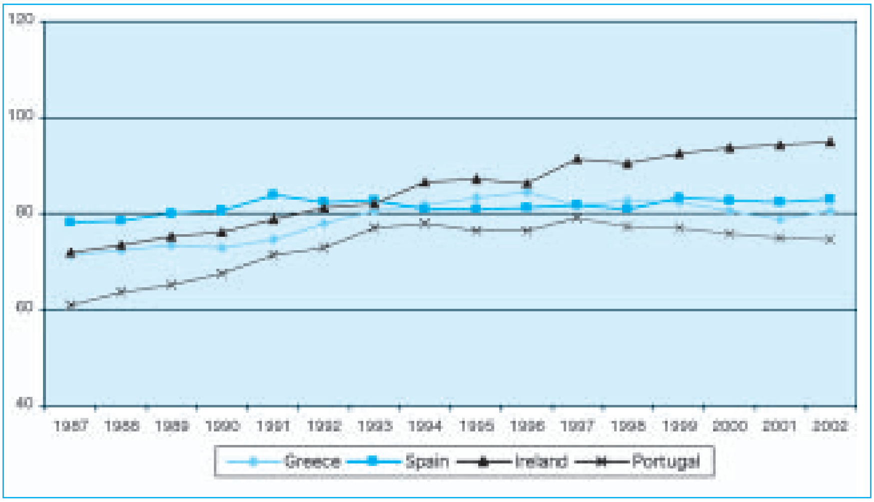


Source: CSO (1999, 2002), *National Income and Expenditure*.

A deeper insight into the change in living standards associated with this scale of increase in consumer purchasing power can be gleaned by comparing findings from the various Household Budget Surveys (HBS) carried out since 1987 (the most recent one in 1999-2000). It provides a window onto what Irish households are doing with their higher disposable incomes. Table 2.1 illustrates the changing composition of household expenditure over the 13-year period, 1987-2000. The most significant change is the falling expenditure share on food; it represented a quarter of average household expenditure in 1987 but had fallen to one-fifth in 1999/2000. The most significant increase was for services, whose share of expenditure increased from 22 per cent in 1987 to 25.7 per cent in 1999/2000. This item covers a wide range of services, including education, medical services, entertainment and holidays. Expenditure on transport also increased from 13.6 per cent in 1987 to 16.4 per cent in 1999/2000. Expenditure on housing increased from 8.8 per cent in 1987 to 9.6 per cent in 1999/2000, a modest increase that may seem surprising in view of the dramatic increase in housing costs in recent years. However, it reflects the fact that these figures represent expenditure averaged across all respondents to the HBS. In households that are paying full market rents, or that have recently taken on new mortgages, housing would represent a far higher share of expenditure.

FIGURE 2.2

Private Consumption Expenditure per head of population, EU (15) =100, 1987-2002



Source: *European Economy*, No 6, 2002.

TABLE 2.1
Composition of Average Weekly Household Expenditure (%)

Category	1987	1994-95	1999-2000
Food	25.2	22.7	20.3
Drink and tobaccn	8.0	7.7	7.6
Clothing and footwear	6.7	6.4	6.1
Fuel and light	6.3	4.9	3.8
Housing	8.8	9.8	9.6
Household non-durables	2.1	2.3	2.5
Household durables	3.9	3.6	4.6
Miscellaneous goods	3.5	3.8	3.4
Transport	13.6	14.4	16.4
Services and other expenditure	21.9	24.4	25.7
Total	**100.0**	**100.0**	**100.0**

Source: *Household Budget Surveys*, 1987, 1994-1995, 1999-2000.

A further indication of changing living standards is provided by considering the share of households with various household appliances and facilities. A selection from the items for which the HBS provides data is given in Table 2.2, chosen because of the extent of the change in each case and their suggestiveness about altering lifestyles in Irish households. For example, while a television was already a common household feature in 1987, there was a substantial increase in the percentage of households with more than one television from 14 per cent in 1987 to almost 50 per cent in 1999/2000. The proportion having two or more cars has also increased substantially from 10.4 per cent in 1987 to almost 24 per cent in 1999/2000. The growing presence of new electronic products in Irish households is captured by the increase from 6 per cent to nearly 30 per cent of those with a home computer between 1987 and 2000 and the inclusion for the first time in the 1999-2000 survey of mobile phones and internet access as household facilities to be monitored.

TABLE 2.2

Percentage of Households with Household Facilities

Item	1987	1994-1995	1999-2000
Clothes Dryer	21.8	26.3	42.0
Dishwasher	7.6	18.7	32.0
Double glazing	13.0	33.0	53.9
Burglar alarm	3.6	11.7	23.9
Two or more TV sets	14.0	28.4	49.0
Motor Car – one only	51.8	51.1	50.1
Motor Car – 2 or more	10.4	14.0	24.2
Home computer	6.1	16.0	29.3
Mobile phone	–	–	44.3
Internet access	–	–	14.2

Source: CSO, *Household Budget Survey* 1999/2000, preliminary results.

Studying how consumer spending over the last two decades has responded to higher incomes and altered demographics, Duffy *et al.* (2001) have calculated the sensitivities of consumer demand for different items to changes in consumers' incomes and a change in the item's price respectively. The elasticities they have calculated in Table 2.3 represent the percentage change in expenditure on a category of goods or services that is likely to result from a one percentage point change in income or price in 1999. The income elasticities are particularly revealing as they point to the 'downstream' consequences of changing consumer behaviour—for example, how increases in real incomes will translate, through higher demand for particular products and services, into sources of new employment and pressures on the environment arising from the increased supply. The figures suggest, for example, that a doubling of income in 1999 would see a rise of 131 per cent in expenditure on services and of 119 per cent on durables, but only a 42 per cent rise in expenditure on food.

TABLE 2.3
Income and Price Elasticities of Demand

Category	Income (at 1999)	Price (at 1999)
Food	0.4280	-0.3410
Alcohol	0.9364	-0.7304
Tobacco	0.1246	-0.1597
Clothing	1.1214	-0.8283
Fuel	0.4717	-0.3009
Durables	1.1970	-0.8858
Transport equipment (inc. cars)	1.0321	-0.8398
Other goods	0.9162	-0.7269
Services	1.3130	-1.0165

Source: Duffy *et al*. (2001): 62.
Note: Elasticities are calculated over the period, 1979-1999 (Per Head).

2.2.2 Income Levels

Driving these developments in consumption and living standards have been trends in earnings and other incomes. Gross Average Industrial Earnings (GIAE) grew by 25 per cent in real terms over the fifteen-year period, 1987-2001, (Table 2.4), but the growth in real take-home pay was significantly greater still as personal taxation was reduced. Between 1987 and 2001, the cumulative increase in real take-home pay for a single person on average manufacturing earnings was about 60 per cent and for a married person 54 per cent. These increases are in marked contrast to the first half of the 1980s when real take-home pay decreased by over 7 per cent because of the impact of inflation and tax. The trend in earnings is discussed in more detail in Chapter 6 where international comparisons are made and the implications for competitiveness explored.

For a significant section of the population, a critical influence on their living standards is the purchasing power of social welfare payments. From 1987 up to 2001, social welfare payments increased substantially in real terms, by 30 per cent for a person receiving a contributory old-age pension and by 53 per cent for a person in receipt of long-term unemployment assistance (Table 2.4). These rises in social welfare payments in real terms exceeded the growth in GAIE but the increase in the contributory old age pension lagged considerably behind developments in net pay. The relative position of a significant group of pensioners, accordingly, deteriorated significantly. This development highlights the significance of viewing tax and welfare changes together in framing public policy.

TABLE 2.4

Indices of growth in Gross Average Industrial Earnings, Take-Home Pay, and Selected Social Welfare Payments, in Real Terms, 1987– 2001 (1987 = 100)

Year	Gross Average Industrial Earnings (GIAE)	Real Take-Home Pay (after tax) Single Person[1]	Real Take-Home Pay (after tax) Married Person[1]	Rate of Old Age Contributory Pension, Single Person	Rate of Long- Term Unemployment Assistance, Single Person
1987	100.0	100.0	100.0	100.0	100.0
1988	103.0	104.1	102.4	101.0	108.8
1989	102.9	106.2	103.8	100.0	117.1
1990	103.5	108.0	105.0	101.7	125.3
1991	104.8	109.4	106.5	102.5	128.4
1992	105.6	112.9	108.5	103.6	129.7
1993	109.9	114.4	110.8	105.6	132.2
1994	110.3	118.0	113.4	106.2	133.0
1995	109.6	120.3	114.7	106.3	133.0
1996	111.4	122.6	116.6	107.8	135.1
1997	113.2	128.4	121.4	110.4	139.3
1998	115.3	133.4	126.1	114.7	142.1
1999	119.9	140.1	136.0	121.1	145.8
2000	121.0	149.3	145.6	123.7	145.5
2001	124.5	160.4	153.8	130.2	153.1

Source: Department of Finance; Department of Social and Family Affairs.
Note: 1 = average manufacturing earnings.

2.2.3 Income Distribution

An important aspect of social development is the degree of equality or inequality in incomes, opportunities and outcomes. This section examines the distribution of income in Ireland during the 1990s, inquiring respectively into the distribution of earnings across individuals, of market income across households, and of disposable income (income after taxes and transfers) across households and per capita. The factors that caused these trends in income distribution are identified and discussed later in the chapter.

Individual Earnings

Earnings from employment—including wages, bonuses, benefits-in-kind and other benefits—represent by far the largest share of household income. The distribution of earnings is a key influence on overall income distribution. The trend in the distribution of earnings in Ireland since 1987 has been documented by Barrett *et al.* (2000), using data from the Living in Ireland surveys. The distribution of gross hourly and weekly earnings in Ireland, in 1987, 1994 and 1997 is shown in Table 2.5.

TABLE 2.5

Distribution of Earnings, Ireland 1987, 1994 and 1997

As Percentage of Median	1987	1994	1997
All employees, gross hourly earnings:			
Bottom decile	47	47	48
Bottom quartile	73	68	69
Top quartile	137	150	153
Top decile	196	224	233
Full-time employees, gross weekly earnings:			
Bottom decile	49	48	51
Bottom quartile	75	72	71
Top quartile	135	143	142
Top decile	182	197	202

Source: Barrett, Fitz Gerald, & Nolan (2000), Tables 7.1 and 7.2.

It is clear from these data that there was a substantial widening in the earnings dispersion between 1987 and 1994, and this continued at a more modest pace between 1994 and 1997. In 1987, those in the top decile had hourly earnings of 196 per cent of median earnings; this had increased to 224 per cent by 1994 and to 233 per cent by 1997. The hourly earnings of those in the lowest decile were virtually unchanged as a percentage of the median from 1987 to 1997, although the relative hourly earnings of those in the lowest quartile (i.e. the lowest 25 per cent of income earners) fell from 73 per cent of median earnings in 1987 to 68 per cent of median earnings in 1994 and had recorded no real improvement by 1997.

TABLE 2.6

Summary Measures of Earnings Dispersion in OECD countries, 1994

	Top Decile/Median	Median/Bottom Decile	Top/Bottom Decile
Sweden	1.59*	1.34*	2.13
Belgium*	1.57	1.43	2.24
Germany*	1.61	1.44	2.32
Finland	1.70	1.40	2.38
Netherlands	1.66	1.56	2.59
Switzerland	1.68	1.58	2.65
Italy*	1.60	1.75	2.80
Australia	1.75	1.64	2.87
Japan	1.85	1.63	3.02
New Zealand	1.76	1.73	3.05
France	1.99	1.65	3.28
UK	1.86	1.78	3.31
Austria	1.82	2.01	3.66
Canada	1.84	2.28	4.20
US	2.07	2.10	4.35
Ireland	**1.97**	**2.06**	**4.06**

Source: Nolan, B., B. Maitre, D. O'Neill, O. Sweetman (2000a).
* = 1993.

Compared to other OECD countries, the level of wage dispersion in Ireland in 1994 was high. As Table 2.6 shows, in 1994, the ratio of average earnings in the bottom-to-top deciles was 4.06 in Ireland; only Canada and the US had higher ratios. The ratio ranged from 2.13 in Sweden to 3.66 in Austria.

Market Income of Households

Households receive market income from sources other than earnings, namely, pensions, rent, interest, and dividends, and they will often contain more than one income recipient. The distribution of overall market income across households ranked by income is shown in Table 2.7 for 1994, 1997 and 1998. It is noteworthy that over the period, 1994 to 1998, the distribution of market income became somewhat more equal. There were significant increases in the shares of total market income accruing to the third, fourth and fifth deciles, with a cumulative increase of 3.6 percentage points between 1994 and 1998. The share of the top two deciles fell by 3.7 percentage points and the Gini coefficient also fell[2]. This improvement in the distribution of market income across households, despite the widening in the earnings dispersion already noted, reflects the improved employment opportunities from which members of households in the middle of the income distribution appear to have benefited in particular.

2. This is a summary measure of dispersion. A value of zero on this measure indicates complete equality, while the closer the measure is to one the greater the level of inequality. It is discussed in more detail in Chapter 8.

TABLE 2.7

Decile Shares in total Market Income, Households ranked by income, 1994, 1997 and 1998

Decile	1994	1997	1998
1st Decile	0.0	0.0	0.0
2nd Decile	0.0	0.0	0.0
3rd Decile	0.3	1.1	1.5
4th Decile	2.8	3.8	4.2
5th Decile	6.0	6.6	7.0
6th Decile	9.0	9.5	9.5
7th Decile	12.1	12.0	12.0
8th Decile	15.4	15.1	15.2
9th Decile	20.4	19.2	19.3
10th Decile	34.0	32.8	31.4
All	100.0	100.0	100.0
Inequality Measure			
Gini	0.565	0.536	0.520
Theil	0.587	0.529	0.495

Source: Nolan, B., Maitre, B., O'Neill, D., Sweetman, O. (2000a).

Disposable Income

Arguably, what most determines people's standard of living is not their market income but their income after payment of income tax and PRSI contributions and the receipt of money transfers (including social welfare), i.e., their disposable income. Data from the Household Budget Surveys confirm both the substantial rises in disposable income per household and per person that have occurred in Ireland in recent years and that the gap between high-income and low-income households is widening.

TABLE 2.8

Average Weekly Disposable Household Income by Gross Household Income Decile, 1987, 1994-95 and 1999-2000

Gross Income Decile	1987 €	1994-1995 €	1999-2000 €	Change 1994/1995-1999/2000 %	Change 1987 to 1999/2000
1st Decile	58.25	79.68	106.23	+33.3	+82.4
2nd Decile	95.44	124.75	174.42	+39.8	+82.8
3rd Decile	130.44	169.94	249.42	+46.8	+91.2
4th Decile	163.51	220.58	331.80	+50.4	+102.9
5th Decile	196.71	273.20	423.01	+54.8	+115.0
6th Decile	235.82	335.26	515.93	+53.8	+118.8
7th Decile	284.72	408.35	617.76	+51.2	+117.0
8th Decile	341.62	488.10	743.45	+52.3	+117.6
9th Decile	420.63	596.68	925.52	+55.1	+120.0
10th Decile	624.76	882.86	1428.71	+61.8	+128.7
State	255.17	357.96	551.69	+54.1	+116.2

Source: Household Budget Surveys, 1987, 1994-1995, and 1999-2000.

As Table 2.8 shows, average weekly disposable household income increased by 54 per cent between 1994 and 2000, and by 116 per cent between 1987 and 2000 (38 per cent and 58 per cent in real terms respectively)[3]. Households in the lowest decile experienced a rise of 33 per cent over the shorter period and of 82 per cent over the longer period. However, the rises were larger further up the income distribution with the result that the income gap between households at the top and bottom of the distribution widened appreciably. The ratio of average incomes in the top decile of households to average income in the lowest decile rose from 10.7 in 1987 to 11 in

3. The cumulative rise in the Consumer Price Index was just under 12 percentage points from mid-1995 to mid-2000, and about 37 percentage points from the start of 1988 to mid-2000 (the periods corresponding to the HBS data collection points).

1994-1995, and to 13.4 by 1999-2000 (note that the deciles are formed by ranking households by their gross weekly income).

Because average household size has been falling in Ireland, the increases in household incomes recorded in Table 2.8 understate the increases in the disposable incomes of household members. The standard way to take account of the size and composition of households in the analysis of the distribution of disposable income is through the use of equivalence scales. An equivalence scale is a device which acknowledges that adults can share some expenses when they live in the same household and that children need less money than adults; it adjusts household income accordingly to estimate the money income available to support each member of the household (assuming a fair intra-household distribution). When household incomes are adjusted in this way in Table 2.9, we see that the rise in per capita income was greater than the increase in household incomes otherwise suggests; average weekly disposable income per capita rose by 61 per cent between 1994-95 and 1999-2000 (44.5 per cent in real terms) and by 138 per cent since 1987 (74.5 per cent in real terms). The weekly disposable incomes per capita of the lowest decile of households in 1999/200 were some 38 per cent higher than the poorest decile in 1994-1995 and 106 per cent than in 1987. On the other hand, the richest 10 per cent of households in 1999-2000 had weekly disposable incomes per capita that were 63 per cent higher than the equivalent households 5 years earlier and 152 per cent than 14 years previously. As a consequence of the increases being greater for the top two deciles than for the lowest, the per capita income gap widened; the ratio of average per capita income in the top decile to that in the lowest decile rose from 3.85 in 1987 to 3.98 in 1994-1995, and to 4.7 by 1999-2000.

TABLE 2.9

Average Weekly Disposable Income Per Capita by Gross Household Income Decile, 1987, 1994-95 and 1999-2000

Gross Income Decile	1987 €	1994-1995 €	1999-2000 €	Change 1994/1995-1999/2000 %	Change 1987 to 1999/2000
1st Decile	47.75	71.14	98.36	+38.3	+106.0
2nd Decile	56.47	82.07	109.01	+32.8	+93.0
3rd Decile	59.56	83.72	128.57	+53.6	+159.0
4th Decile	62.89	89.30	150.82	+68.9	+139.8
5th Decile	73.67	103.48	176.99	+71.0	+140.2
6th Decile	83.33	123.71	200.75	+62.3	+140.9
7th Decile	97.51	141.79	232.24	+63.8	+138.2
8th Decile	116.20	170.66	263.63	+54.5	+126.9
9th Decile	136.12	201.58	322.48	+60.0	+136.9
10th Decile	183.75	282.97	462.37	+63.4	+151.6
State	99.67	147.31	237.76	+61.4	+138.5

Source: Table 2.7. Number of Equivalent Adults supplied by CSO.
Note: Equivalence scale (1/0.7/0.5).

Nolan *et al*. (2000a) use data on household incomes obtained through the successive Living in Ireland Surveys and provide a complementary perspective on trends in the distribution of income across Irish households (note they use a slightly different equivalence scale to the CSO, viz., 1/0.66/0.33[4]). In Table 2.10 they rank households by their equivalent disposable incomes in 1987, 1994, and 1998 and then identify the share of total equivalised disposable household income being received by each decile.

4. For a detailed discussion of the issues involved in selecting equivalence scales, see Callan, Nolan *et al* (1989, Chapter 5).

TABLE 2.10

Decile Shares in Total Equivalised Disposable Household Income, 1987, 1994, and 1998

Households	Share in Total Equivalised Disposable Income		
Decile	**1987**	**1994**	**1998**
1st Decile	3.2	3.9	3.4
2nd Decile	4.8	4.8	4.3
3rd Decile	5.8	5.4	5.0
4th Decile	6.5	6.1	6.2
5th Decile	7.4	7.1	7.6
6th Decile	8.7	8.7	9.1
7th Decile	10.2	10.5	10.6
8th Decile	12.3	12.7	12.8
9th Decile	15.2	15.9	15.8
10th Decile	25.9	25.0	25.2
Total	100	100	100
Gini	0.330	0.326	0.338

Source: Nolan *et al*. (2000a).

The distribution of equivalised disposable income became slightly more equally distributed between 1987 and 1994. The share of the top decile fell by approximately 1 percentage point to 25 per cent, that of the lowest decile rose by 0.7 percentage points to 3.9, and the Gini coefficient dropped from 0.330 to 0.326. This effectively presents a pattern of broad stability in the distribution of income over the period. In the 1994 to 1998 period, however, the share of the top decile moved marginally upwards, the share of the bottom three deciles fell by 1.4 percentage points between them and the Gini coefficient increased to 0.338 which was above its 1987 level.

2.2.4 Trends in Poverty

New data on income poverty in Ireland became available in mid-2002. Developments over the period since 1987 can be summarised in two observations: (i) the number of people falling below fixed income thresholds, or semi-fixed as in the case of the 'consistent poverty' measure, has declined dramatically; (ii) the number of people falling below purely relative income poverty lines remains high, and the extent by which a significant proportion of them are falling below them has become greater. These patterns are illustrated in the following Tables.

TABLE 2.11

Percentage of Persons below Real Income Standards, 1987, 1994, 1997 and 2000.*

Real Income Standard	1987	1994	1997	2000
40% mean income, 1987	6.8	1.8	1.3	0.6
50% mean income, 1987	18.9	7.2	2.9	1.0
60% mean income, 1987	29.8	18.4	8.0	3.0
40% mean income, 1994	n.a.	5.2	2.3	1.1
50% mean income, 1994	n.a.	17.4	7.8	3.0
60% mean income, 1994	n.a.	30.4	17.3	8.6

Source: Callan *et al.* (1996), Table 4.12; Nolan *et al.* (2002a), Tables 3.7; supplementary data sourced from ESRI.

Note: *Income averaged across individuals. Equivalence scale 1/0.66/0.33.

Table 2.11 presents the positive evidence using two sets of fixed real income lines, namely, percentages of mean income in 1987 and 1994 that are uprated for inflation. It shows, for example, that the percentage of people falling below 50 per cent of mean income in 1987 and indexed to prices thereafter (rather than average income) fell from 19 per cent to just 1 per cent over the fourteen years. In the base year (1987), unemployment was high and agricultural incomes depressed so 50 per cent of mean income in that year is a low standard. However, using 50 per cent of mean income in 1994 and indexing it to prices records an improvement that is almost as dramatic: about 17 per cent of the population were below this line in 1994 but only 3 per cent were still below the same line in real terms seven years later. Using measures of consistent poverty confirms the same trend, as shown in panel [a] of Table 2.12. For example, the percentage of people below 70 per cent of median income and experiencing basic deprivation fell by 62 per cent between 1994 and 2000. For these reasons, the period known as the 'Celtic Tiger' has been termed "remarkable" and "dramatic" for its effects in raising money incomes (Nolan *et al.*, 2002a: 22, 23).

TABLE 2.12

Percentage of Persons in Consistent Poverty and Below Relative Income Poverty Lines, 1994, 1997 and 2000 (Income Averaged Across Individuals).

	Percentage of Persons Below Standard			
Measure	**1987**	**1994**	**1997**	**2000**
[a] Consistent Poverty				
50% median income and experiencing basic deprivation	5.5	3.5	5.2	3.1
60% median income and experiencing basic deprivation	12.7	8.3	7.8	4.4
70% median income and experiencing basic deprivation	17.8	14.5	10.7	5.5
[b] Relative Income Lines				
50% median income line	9.1	6.0	8.6	13.8
60% median income line	19.7	15.6	18.2	22.1
70% median income line	28.8	26.7	29.0	28.2

Source: ESRI. Equivalence scale 1/0.66/0.33.

When a purely relative measure of income poverty is used, the developments in incomes associated with the economic boom appear in a less positive light. The numbers falling below 50 and 60 per cent of median income declined slightly between 1987 and 1994 but rose markedly between 1994 and 2000 (panel [b], Table 2.12). The rise was greatest for the numbers under the 50 per cent line; about 6 per cent of the population were below this line in 1994 but 14 per cent by the year 2000. There was relatively little change in the proportion of the population falling below the 70 per cent line;

however, nearly 50 per cent of those below it in 2000 were also below the 50 per cent line as against 22 per cent in 1994. This suggests that the extent by which people are falling below the different relative income poverty lines has been increasing, a trend which is confirmed by further data (not shown, see Nolan *et al*., 2002a) showing that the per person income gap (average shortfall below the income poverty line of those people who are below it, expressed as a percentage of the line) and internal distribution of income among the population below the poverty line have each deteriorated (*op. cit*. 2002a: Tables 3.5 and 3.6). It is clear that the measure of consistent poverty records a significantly different trend over time, as well as a different level at each point in time, in the proportion of the population in poverty to that recorded by measures based on relative income alone, even though both measures are based on the same percentages of median income. This means that the non-monetary 'indicators of deprivation', which are used in addition to income in the consistent poverty measure, have, in effect, dictated the fall over time in the proportion of people in consistent poverty. The usefulness of this measure for continuing to monitor trends is discussed in Chapter 8.

This deterioration in relative income poverty has a simple explanation. Average incomes rose sharply during the economic boom, fuelled by increases in income from work and property, and median incomes were pulled up by the growing proportion of people in employment; this raised the income thresholds below which people are deemed to be in relative income poverty. For example, the money value of 50 per cent of mean weekly household equivalent income increased by 75 per cent between 1994 and the year 2000 [from £64.69 to £113.22], and by 21 per cent between 1998 and 2000 alone. Once increases in social welfare were not of the same magnitude, some increase in relative income poverty was largely inevitable.

The changing composition of the populations falling below the different poverty lines is analysed in Chapter 7, which also contains the Council's recommendations for social welfare. Issues concerning the measurement of poverty are discussed in Chapter 8.

2.2.5 Learning and Life Chances

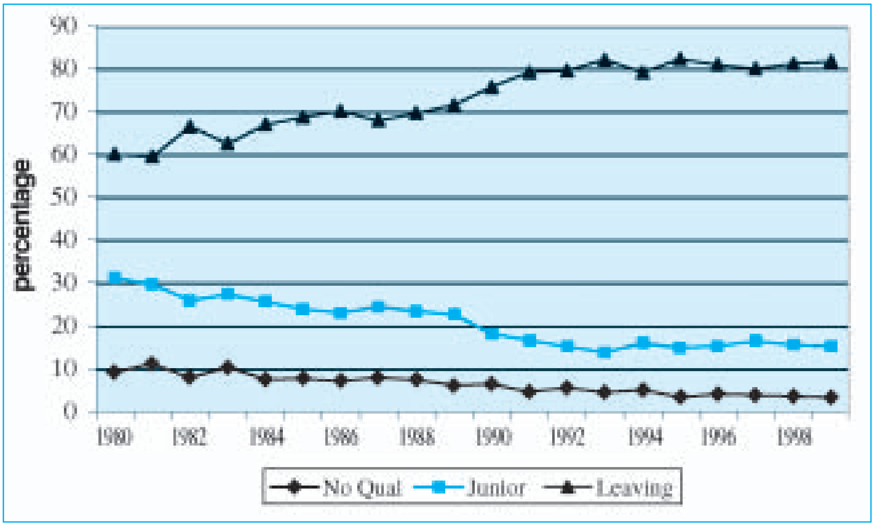
The Council has long identified education as one of the key determinants of success for the individual as well as for society generally. Changes in education were crucial in facilitating the economic transformation which occurred during the 1990s. In its 1996 *Strategy* report, the Council described the growth in educational participation since the late 1960s as impressive but observed that “the low starting point …and the long time it takes for subsequent improvements in educational attainment to feed through to the adult population” (1996a: 38) meant that human capital growth had yet to exert its full effect.

Second and Third Level Expansion

The period since 1987 has seen a levelling off of improvement in the proportion of young people completing secondary education and a rapid expansion in educational participation at third level.

Figure 2.3 below highlights the increasing retention rates in second level education since 1980. The proportion of second level school leavers with a Leaving Certificate qualification has risen from 60 per cent in 1980 to almost 82 per cent in 1999. There has been a corresponding decline in the numbers leaving prior to the Leaving Certificate. In 1980, 31 per cent of students left the education system at Junior Certificate level. By 1999, this had reduced to 15 per cent, with a further 3 per cent leaving without having sat for any official examination (McCoy and Williams, 2000). In addition to those who leave the education system during second level, it is estimated that approximately 1,000 young people every year do not transfer from primary to second level education (NESF, 1997a). Since 1995, there has been a distinct levelling off in the percentage of secondary level students completing their Leaving Certificate and it is clear that further progress will require further diversification of what is on offer at second level as well as fresh attention to the resources and motivation of young people from socially disadvantaged backgrounds (NESF, 2002a).

FIGURE 2.3
Qualification Level of School Leavers



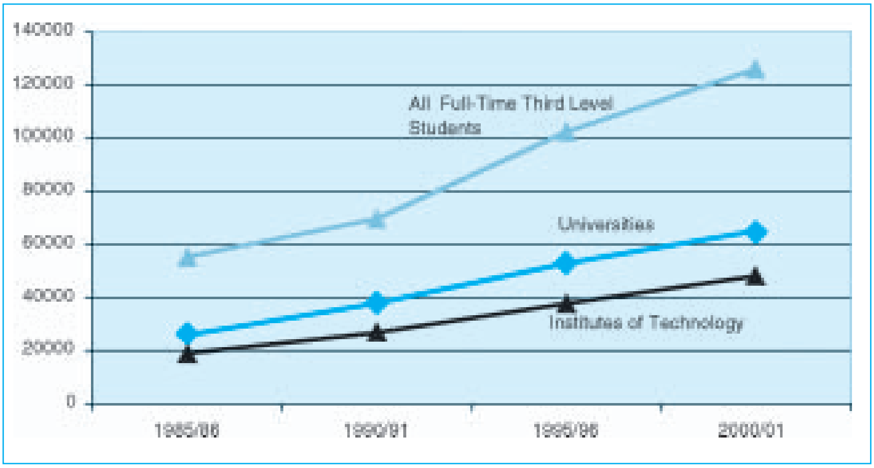
Source: McCoy, S. and Williams, J. (2001) *1999 Annual School Leavers Survey*, Draft.

In addition to the growth in participation and retention at second level there has been a rapid growth in the numbers of people entering third level education. The number of full-time third level students increased by 27 per cent between 1985 and 1990, by 47 per cent between 1990 and 1995, and by 23 per cent between 1995 and 2000 (Figure 2.4). By 1999, the total annual intake of full-time students into third level was equivalent to 56 per cent of the population aged 17, up from 28 per cent in 1985. During the six years of exceptionally rapid economic growth, 1995 to 2000, a steady 5 per cent per annum growth rate was maintained in the aggregate number of third level students (full-time and part-time), with the proportion studying part-time rising from 18 to 20 per cent. This expansion in enrolment was facilitated by the diversification of higher education institutions which had begun in the 1970s and featured the expansion of the existing technical colleges in Dublin and Limerick, the development of a network of Regional Technical Colleges (RTCs) (subsequently, all were redesignated as Institutes of Technology) and the establishment of two National Institutes of

Higher Education, which subsequently became the University of Limerick and Dublin City University. The Institutes of Technology had become an important feature of the third level sector by the mid-1990s. Over the period, 1995-2000, they typically accounted for 37-38 per cent of full-time third level students—the proportion had been as low as 6 per cent in the late 1960s—and for about one half of all full-time new entrants in each year (their courses are shorter on average than University courses). The overall scale of expansion of higher education in Ireland has been broadly similar to that experienced in other European countries (Clancy, 2001). The proportion of the population participating in third level education, however, continues to be well behind the standard set by the best-achieving countries, with the proportion of first-time entrants to higher education who are aged over 20 being particularly low (OECD, 2002a, Table C2.1).

FIGURE 2.4

Number of Persons Receiving Full-Time Third Level Education by Type of Institution Attended, 1985/86, 1990-91, 1995/96 and 2000/01



Source: HEA

Social and Gender Differences in Educational Participation

It has been argued that educational expansion and economic growth can result in a reduction in inequalities in education on the basis of social background. All social classes/socio-economic groups have participated in the expansion in education that has taken place since 1980. However, change has not been even. Despite the substantial rises in retention rates and entry to third level education, socio-economic inequalities in educational participation and attainment have been persistent. They continue with regard to second level retention rates, levels of attainment at Leaving Certificate and participation at third level. These inequalities in education result in further disparities in the labour market, with research indicating the significant consequences of levels of educational attainment for access to employment and pay levels.

Gender differences in educational participation and attainment became more apparent during the 1990s. For example, boys are more likely to leave school without a qualification, less likely to sit their Leaving Certificate, likely to take fewer honours papers and to score less across a wider range, and—since 1992—less likely to transfer into third level education when they have a Leaving Certificate. Young women tend to achieve higher results in formal examinations after controlling for their initial ability/performance levels and social background. The corollary of these observations, of course, is that Irish girls are doing better not just relatively to boys but immeasurably so by the standards of an earlier Ireland and face steadily wider economic and social opportunities as a result. By 1998, 53 per cent of higher education admissions were women, the first time that female higher education entrants fully reflected their proportionate representation among Leaving Certificate students.

Gender differences persist in the types of courses taken by young men and women at both second and third level education. These educational differences translate to some extent into female advantage on early entry to the labour market, with higher employment rates and higher occupational statuses. However, this advantage is 'ambiguous' as pay levels among young women have not improved as much as the higher status of the jobs they enter would suggest and also young women are less likely than men to achieve mobility out of lower paid jobs over their early years in the labour market. Smyth and Hannan state that the persistence of these gender differences must be placed in the context of continuing gender differentiation in the type of education received and the existence of occupational and industrial segregation by gender in the labour market (2000: 126).

Lifelong Learning

While participation levels in second and third level education have increased for young people, earlier failures in the system have left a large minority of older age groups who are poorly equipped to take advantage of the new employment opportunities in the economy. This failure is particularly apparent in relation to adult literacy in Ireland. When the literacy skills of adults (ages 16-64) in a range of countries in 1995 were profiled by the OECD, Ireland's performance was found to be poor in absolute and comparative terms (OECD, 1997). The aim of the OECD's Adult Literacy Survey was not to assess attainment as such but to identify levels of literacy that were sufficient to cover demands at work, in the home and the community. The survey found that between 23 and 25 per cent of the Irish population scored at the lowest level (Level 1), meaning that they could at best perform tasks which required the reader to locate a simple piece of information in a text. This percentage was the highest in any of the countries surveyed, except for Poland. By contrast, only 6 per cent and 10 per cent scored at Level 1 in Sweden and the Netherlands respectively. About 33% of the Swedish respondents scored at the highest levels (Levels 4 and 5) while the corresponding figure in Ireland was about 12% (DES, 1998:31).

The plight of many Irish adults is of major significance, not only in terms of social inclusion but also in terms of competitiveness. Literacy problems pose severe problems for both the individuals concerned and the economy; performance at Level 3 is considered desirable in order to avoid difficulties in coping with social and economic life in contemporary society. Lifelong learning or continued learning is central in both addressing issues of inequality and social justice and in developing personal and cultural development and an active citizenry.

Analysis and recommendations on how to improve educational opportunities for young people and adults are developed in Chapters 8 (social inclusion) and 10 (continuous improvement and learning) of this report.

2.2.6 Social Diversity

During the 1990s, Ireland continued to become a more diverse society. Changes proceeded apace with regard to family formation and structure, while an increase in immigration has brought a notably greater cultural diversity to Irish cities and towns. This section describes these changes. The policy issues arising are dealt with later (Chapter 8).

Changes in household formation and family type have important consequences for the economy, the labour market, and the welfare system (NESC, 1999). Overall, the shift is towards a greater diversity of family forms, with individuals through their life span possibly moving through a variety of family forms.

Between the Census of 1986 and that of 1996, one-person households increased from 18 per cent of all private households to 21 per cent, and households comprised of childless couples increased from 11 per cent to 13.6 per cent. The two fastest growing categories of households, thus, were households without children. There was an increase of one percentage point in the proportion of lone-parent households; they constituted 11 per cent of all households in 1996, an absolute increase of 27,500. As a proportion of all families with children under 15 years, families headed by a lone parent made up 13.8 per cent of households in 1996 as compared to 7.2 per cent in 1986. Data from Labour Force Surveys supplement that from the 1996 Census. The former estimate that lone parents increased by over 18 per cent in the period 1992 to 1997, with an increase of over 30 per cent in the numbers with dependent children aged under 15 years.[5] The increase in numbers is reflected in the number of lone parents/separated spouses in receipt of social

5. Both the Census and the Labour Force Survey can underestimate the number of lone parent families, as they exclude some families who do not head their own households e.g. those living with their parents.

welfare payments over the same period. Data from the Department of Social Community and Family Affairs (2000) show that that the numbers in receipt of the One-Parent Family Payment (formerly Lone Parents Allowance) increased from 25,231 in 1990 to 70,387 in 1999[6].

The 1996 Census was the first in which information was explicitly sought on cohabiting couples; it revealed that under 3 per cent of private households were cohabiting couples with or without children (31,229 households). Cohabiting couples without children accounted for almost 11 per cent of all childless couples in 1996, while those with children represented 2.5 per cent of all couples with children. Furthermore, 43 per cent of women and 55 per cent of men in cohabiting relationships were aged 30 years or over, thus indicating that cohabitation may not just be a precursor to marriage but a more permanent form of union in many cases (Commission on the Family, 1998: 188).

By 1995, the marriage rate had dropped to 4.3 per 1,000, its lowest level in 100 years. Between 1995 and 1998, the marriage rate fluctuated between 4.3 and 4.5 per 1,000. However, figures for the last two years of the decade showed that this decline was reversed, with increases in both the number of marriages and the rate per 1,000 population in 1999 and 2000. This change resulted in the marriage rate rising from 4.3 per 1,000 in 1997 to 5.1 in 2000, bringing it back to its 1990 level.

While there are no comprehensive data on marriage breakdown in Ireland, figures on numbers of divorced and separated individuals in both the Census and the Labour Force Survey show a steady increase since 1986. The number of formerly married persons rose from 37,250 in 1986 to 87,800 in 1996. Divorce legislation was introduced in 1996 following a referendum in 1995. Latest figures available are those to the end of July 2000. In that period, 3,346 divorce applications were received by the courts of which 2,623

6. This is not a measure of the number of lone parents, but a measure of those who are entitled to a social welfare payment, regardless of their living arrangements. They exclude those not entitled to welfare payments due to their income from earnings or maintenance payments.

were granted. In the same period 1,035 judicial separations and 56 annulments were granted.

By 1990, the Irish Total Fertility Rate[7] (TFR) had fallen to one-half of the level of 1970 and come within the low range common among western countries. Between 1994 and 1998, however, the total fertility rate recovered somewhat to reach 1.9, placing it at the top range of EU member states, but still below the replacement level of 2.1[8] (the rate first fell below the replacement level in 1989)[9]. The CSO, in its projections, conclude that this slight recovery in fertility is unlikely to be maintained and that the long-term decline can be expected to resume, but at a more moderate rate (1999: 11).

The birth rate (number of births per 1,000 population) can pursue a distinct course to the TFR, i.e., it can rise even while fertility rates are falling simply because the proportion of women of childbearing age in the population is increasing. The number of births in Ireland reached a low point of 48,000 in 1994 but, after that, it increased each year to reach over 54,200 in 2000, an increase of 13 per cent on 1994 (although still 27 per cent lower than a 1980 peak). The birth rate per thousand of population for the first two quarters of 2001 stood at approximately 15.1, compared to a rate of 14.3 for 2000.

One of the most striking trends in relation to births has been the growing proportion of births taking place outside of marriage. CSO figures show that in 1986 non-marital births accounted for one out of every ten births in Ireland; by 1995, the incidence had increased

7. The technical definition of the TFR given by the CSO is that it "represents the theoretical average number of children who would be born alive to a woman during her lifetime if she were to pass through her childbearing years (ages 15-49) conforming to the age specific fertility rates of a given year".

8. The estimated replacement rate in order for the population to reproduce itself is 2.1 (CSO, 1999).

9. The CSO in its *Population and Labour Force Projections* 2000-2031 (1999:10) give an indication of the impact of decreases in fertility rates between the mid-1960s and mid-1990s by calculating the theoretical number of births which would have occurred in 1996 if the age specific fertility rates of 1965 still applied. Using the 1965 rate, the number of births in 1996 would have been double what it actually was, 107,000 as opposed to the actual figure in 1996 of 50,000 births.

to one out of five and, by 1999, 31 per cent of births were outside marriage. It is important to note that births outside marriage do not necessarily equal lone parenthood, as some of the mothers are in cohabiting relationships or they may move into marital relationships at some point in the child's life.

One of the more visible changes brought about by the rapid economic growth of the 1990s and the tightening labour market is net immigration. Since 1996, Ireland has been experiencing net inward migration, a factor which has enabled the labour force to grow rapidly. The estimated number of immigrants in the year to April 2000 was 42,300, outnumbering emigrants (22,300) by almost two to one. Returning Irish nationals were the largest immigrant group in the period 1995 to 2000, 43 per cent in the year to April 2000, with a further 34 per cent being EU nationals, 5 per cent from the US and 18 percent came from outside the EU or USA. Over the latter part of the 1990s, the proportion of Irish and UK immigrants decreased, while the percentage of immigrants from the rest of the EU and the rest of the world increased. Chapter 8 will reflect in more depth on these developments.

2.2.7 Housing, Population Concentration, Settlement, Transport

Some of the strongest concerns that economic growth may have outstripped social progress during the 1990s have had to do with the cost of housing, the perception of urban sprawl and traffic congestion.

Housing

Data for the five-year period 1995 to 2000 show that the overall stock of housing units increased. An important difference developed in the trends relating to local authority and private housing. There was a consistent increase in private housing completions from some 26,500 in 1995 to over 46,500 in the year 2000 or from 7.4 per 1,000 population to 12.3 per 1,000 population. In contrast, local authority completions and acquisitions were lower in 2000 (2,204) than in 1995 (2,960). The difference in the two trends is reflected in the decrease in the ratio of local authority to private houses from 1:10.6 in 1995 to 1:12.0 in 2000. The decrease in the ratio of local authority to private housing is more marked in housing completions from 1:6.9 in 1995 to 1:14.6 in 2000.[10]

Other housing indicators adopted by NESC in order to measure progress are local authority waiting lists and housing affordability. The meaning of 'affordability', or how it is measured, is an unresolved issue. Affordability is generally taken to measure some given standard of housing or accommodation that can be secured without placing an undue financial burden on the household's income. The NESC recognises that "an accurate affordability index covering all tenures, incorporating maintenance as well as purchase price and rents is probably the most desirable of all housing indicators. Such an affordability index is not available at present and hence the proxy indicator used gives an indication of the purchase affordability" (2002b: 256). Using the ratio of average house price to the average industrial wage as an indicator of housing affordability, data shows that the ratio of the average price of new houses to average industrial earnings increased from 4.33 in 1990 to 5.29 in 1997 and to 7.40 in 2000. The corresponding figures for the Dublin area are 5.34, 6.32 and 9.70, with figures for second hand houses showing an even more dramatic fall in affordability (NESC, 2002b: 47). This figure is mainly indicative of house prices. It does not take into account the decrease in interest rates and reductions in income tax which have taken place and which have affected mortgage repayment levels.

Settlement: Housing Patterns

While the housing stock (increasingly private) expanded rapidly, there was a significant divergence between the spatial pattern of the expansion of the housing stock and the growth of employment. This

10. Voluntary housing completions totalled 951 in 2000 (0.25 per 1,000 population, the figure in 1995 was 1,011, or 0.28 per thousand population (NESC, 2002a:78). Preliminary data for 2001 indicate that the total number of voluntary housing completions was 1,200 in 2001.

is most evident in the Dublin area, but also arises in other regions. Williams and Shiels (2000) point out that the East region (Dublin, Meath Kildare and Wicklow) accounted for 49 per cent of the employment growth but only 36.5 per cent of new dwellings over the period 1994 to 1999. This imbalance between employment and housing growth has meant a spreading out of development beyond the East region to the counties of outer Leinster. An aspect of this development has been large-scale development in small villages with inadequate infrastructure.

The pattern of development in the eastern part of the country has been characterised by Williams and Shiels as one of uncoordinated peripheral expansion. They argue that this is the least sustainable option but it is the likely result of the present policy mix. This pattern essentially involves meeting urban housing needs in a dispersed manner without adequate infrastructure and services. Addressing the infrastructure deficits of dispersed development requires greater investment in suburban road, water supply, drainage and other utilities compared to the alternative of a more compact form of urban development. This pattern relies on long distance commuting often by car and contributes to increased congestion. Of particular concern is that it does not facilitate co-ordination of land use and public transport. Without such co-ordination the current level of investment in public transport will not be used in the most efficient manner.

The phenomenon of sprawl is not confined to the East region. There has, for example, been a rapid growth in the number of one-off homes constructed in the countryside, prompting some sharply opposed views on the significance of the trend. On the one hand, such one-off houses can offer a solution to the problem of housing affordability for some people; on the other hand, they can be damaging to landscapes in scenic areas.

Population Concentration

Accompanying the general increase in population that has taken place in Ireland since 1960 has been a concentration of population. From the mid-1960s onwards, Ireland has become a predominantly urban society. This urbanisation accompanied the decline in dependence on agriculture both as a source of national output and employment. The growing urbanisation is particularly striking in Dublin city and the greater Dublin area. In 1961, Dublin accounted for just over a quarter of the population while the share of the Mid-East region[10a] was 6.7 per cent. By April 2002, approximately 28.6 per cent of the population was living in the Dublin area (reflecting a slight decline from the 1996 figure of 29.2 per cent) and 10.5 per cent in the Mid-East region (a corresponding rise of 0.9 per cent on 1996).

The impact of net inward migration on population increases in recent years is particularly noteworthy. Table 2.13 on page 86 highlights this trend.

For the first time ever, net inward migration accounted for more than one half of the total increase. Most strikingly, every county experienced net in-migration. In absolute terms, the largest net in-flows were to counties Cork (excluding Cork city), Meath and Kildare, followed by Galway and Dublin. The relatively small net in-migration of just over 13,250 to Dublin (consisting of the four new local authority areas) is particularly noteworthy as it is equivalent to a rate of only 2.0 persons per 1000 of average population, the third lowest among all counties.[11]

The role of inward migration is especially significant in some of the most rural counties. For example, it accounts for 92% of the total increase in Mayo, 75.6% in Kerry and almost 70% in Westmeath. In Leitrim and Roscommon, the excess of deaths over births would have resulted in population decline in the absence of net inward migration.

The geography of population change since 1996 demonstrates a very considerable expansion of the area under the influence of Dublin and also a significant turn-around in the population of many rural areas. A little over one fifth (21.4%) of the total increase took

10a. Mid-East Region – Kildare, Meath and Wicklow.

11. The role of net migration in contributing to population growth may however, result in greater sensitivity to economic shocks, which could impact on future demographic patterns.

TABLE 2.13

Components of population change for each Regional Authority, 1996-200

Regional Authority	Population		Population increase	Natural increase	Estimated net migration	Average annual rates per 1,000 of average population		
	1996	2002				Population increase	Natural increase	Estimated net migration
State	3,626,087	3,917,336	291,249	138,182	153,067	12.9	6.1	6.8
Border	407,295	432,366	25,071	10,373	14,698	10	4.1	5.8
Dublin	1,058,264	1,122,600	64,336	51,079	13,257	9.8	7.8	2
Mid-East	347,407	412,650	65,243	22,781	42,462	28.6	10	18.6
Midland	205,542	225,588	20,046	7,317	12,729	15.5	5.7	9.8
Mid-West	317,069	339,930	22,861	10,935	11,926	11.6	5.5	6.1
South-East	391,517	423,540	32,023	13,720	18,303	13.1	5.6	7.5
South-West	546,640	580,605	33,965	15,530	18,435	10	4.6	5.5
West	352,353	380,057	27,704	6,447	21,257	12.6	2.9	9.7

Source: Central Statistics Office (2002), *2002 Census Preliminary Report*, Dublin: CSO: Table 3 place in Dublin (old county area) and another 22.4% occurred in the Mid East region. Just over two-thirds of the total increase took place in urban areas compared with 92% over the 1991-96 period. Excluding peri-urban zones (rural areas close to the main urban centres) approximately 18% of the increase occurred in the open countryside, in villages or in small towns with fewer that 1500 persons.

Some declines were recorded in 1211 districts (35% of the total). The most extensive areas of rural population decline were in northwest Mayo, northwest Cork/east Kerry, north Roscommon, south Leitrim, west Cavan and southwest Donegal. While the total decline in rural areas is widely dispersed, it accounts for a little less than 30% of the decline recorded for all districts. Conversely, some of the largest relative and absolute declines were in some urban wards or census districts.

CSO projections (based on the 1996 Census figures) estimate an increase in the population of the Dublin region by over a half million persons in the period to 2031, increasing its population share to 36.2 per cent (CSO, 1999). Apart from the Midlands, which is projected to lose 10 per cent of its population, each Regional Authority area is expected to experience population growth over the thirty-five year period 1996 to 2031, although in the case of the South-East the projected increase is less than 1 per cent. Dublin is projected to be the fastest growing area followed by the Mid-East. These areas will grow due to natural increase, international migration and through internal migration from the remaining six regions. The heaviest losses due to internal migration are identified in the Midland and Border areas.

Population growth and concentration in Ireland differs in many respects from the internal migratory patterns at EU level. In the past, the economic transition from agriculture to manufacturing resulted in people moving from the countryside to the cities. The trend towards "urbanisation" is still apparent in EU applicant countries and rural areas within the EU, including Ireland. However, this type of movement is not currently the most significant in the EU member states as a whole. With the transition to a service and information economy, rural to urban flows have been replaced by flows from big city centres towards their metropolitan areas ("suburbanisation") or towards more distant small and medium sized cities and rural areas with medium density. This pattern has a number of consequences: large cities have lost a part of their population, while mid-sized settlements are growing. This suburbanisation is dependent on age; at the EU level the move is made mainly by adults 30-44 years old with children looking for a better environment or a more affordable dwelling. In contrast, Dublin city saw its population increasing by 2.7 per cent between 1996 to 2002 with increases also recorded in Galway (14.9 per cent), Limerick (3.9 per cent) and Waterford (4.8 per cent). Cork city reflected EU trends with a 3 per cent decrease.

Ireland also differs in relation to remote and low-density rural zones, which continue to lose their population in most EU states. The figures contained in Census 2002 point to a majority of these regions experiencing population growth in Ireland.

Transport

An effective transport system is critical to quality of life, a competitive economy and environmental sustainability. Over the past decade the transport system has become less effective in meeting people's needs as a result of a significant deterioration in traffic congestion. While by no means limited to the Dublin region, some statistics for this region illustrate the seriousness of the problem. Between 1991 and 1998, peak-time journey times in the Dublin region increased by 64 per cent and the share of journeys accounted for by public transport actually fell by 8 per cent. Car ownership is growing rapidly; it rose from 11.6 cars per 100 adults in 1961 to 40.1 in 1991 and to 51.2 in 1998, reflecting the close correlation of car ownership with economic growth (Goodbody, 2000; Table 4.1). This still leaves it well below the average of richer European countries and there is acknowledged potential for further growth in car numbers (Tax Strategy Group, 2000). However, the more important issue is the pattern of car use; in European countries with higher levels of car ownership, the car can still account for a lower modal share of passenger travel. In Ireland, the car's modal share of passenger kilometres is estimated to have risen from 83.4 per cent in 1987 to 86.6 per cent in 1996; by contrast, the modal shares of buses and rail were 9.9 per cent and 3.4 per cent respectively in 1987 and 9.4 per cent and 2.3 per cent in 1996 (Goodbody, 2000: Table 3.1).

To some extent, the problems of traffic congestion are an inevitable result of the economic boom. More people in employment and higher disposable incomes mean that more people are able to purchase a car and use their cars more often. Vehicle numbers and GDP are very closely correlated. However, transport problems are not purely the result of economic growth. The dispersed pattern of housing development in Ireland requires high car dependence. In particular the sprawling nature of housing around (and often at a great distance from) the Dublin area has contributed to car dependence and traffic congestion. At present, there is a high level of public investment under way in public transport. However, significant challenges remain in this area. Investment in public transport needs to be complemented with land use planning that facilitates the use of public transport.

2.2.8 The Environment and Sustainable Development

Environmental sustainability is a key dimension of the Council's vision for a successful society. It is widely accepted that a citizen's quality of life is directly affected by the environment in which he or she resides—both in positive and negative terms. Equally, the quality of the environment and economic progress are inter-linked and interdependent. The Council's 1999 Strategy stressed the need to maintain the quality of the natural environment in line with economic progress, stating that rapid growth that degraded the environment or left a significant portion of the population in poverty would not represent sound policy or a sustainable outcome.

However, a number of factors, including those outlined in Sections 2.2.1 and 2.2.7 above, have combined to increase demands and pressures on the environment in recent years. Statistics from the

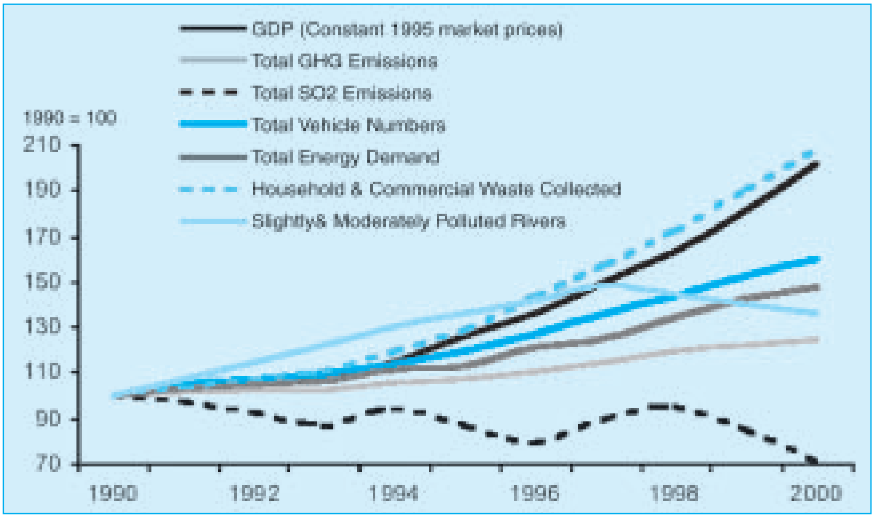
EPA (2002) point to a number of negative trends in relation to the environment. Some of these are:

- In 2000, almost 2.3 million tonnes of household and commercial waste were generated in Ireland—an increase of over 60 per cent in five years;
- The emission of greenhouse gases in Ireland in 2000 had increased by 24 per cent above 1990 levels (a figure which exceeded the level committed to under international obligations by 11 per cent);
- The total number of vehicles increased by 60 per cent in the period 1990 to 2000—creating more infrastructural bottlenecks around the country and adding to local air pollution; and
- Industrial production doubled during the period 1995-2001—leading to greater energy consumption, emissions to air and waste generation.

The overall trend therefore, as outlined by the EPA (2002), is one of environmental pressures becoming more acute in line with increasing economic growth. In particular, the volume of household and commercial waste has become a major issue. Figure 2.5 below illustrates the significant relationship between household and commercial waste and economic growth—highlighting the significant challenge in decoupling waste generation from economic growth. In the case of most of the other indicators the rate of increase of the environmental pressure has been slower than the rate of increase of GDP—this is termed relative de-coupling. Only in the case of sulphur dioxide, where there has been an actual decrease in the amount of emissions, has there been an absolute decoupling from GDP.

FIGURE 2.5

Eco-Efficiency in Ireland 1990 - 2000



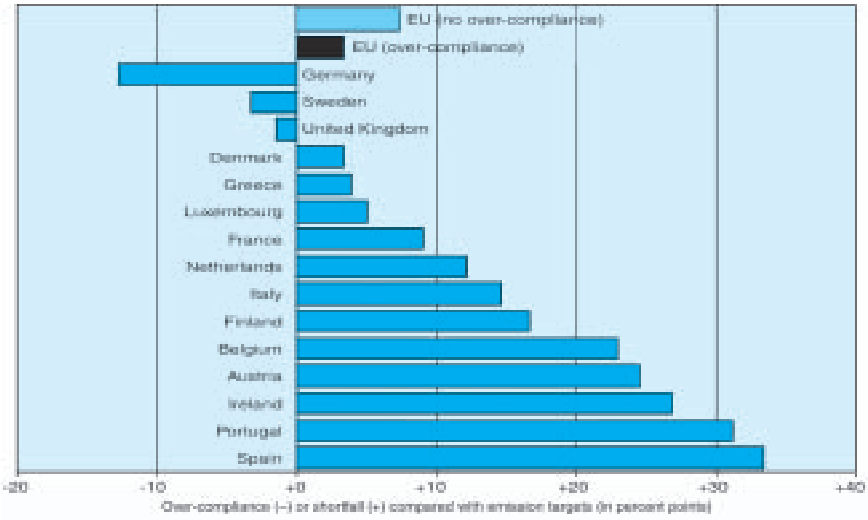
Source: EPA; *Environment in Focus 2002: Key Environmental Indicators for Ireland*; EPA 2002

In comparative terms, Ireland would appear to be considerably behind other EU member states when considering key environmental indicators. The Kyoto Protocol of 1997 set a target for an aggregate 8 per cent reduction in greenhouse gas emissions in the EU over 1990 levels which was to be achieved by 2008 - 2012. Under the system of burden-sharing agreed by EU member states, Ireland was set a target of 13 per cent. The *National Climate Change Strategy* of 2000 sets out a range of measures to achieve reductions in greenhouse gas emissions in all sectors to meet Ireland's Kyoto target. Key cross-sectoral measures include taxation, negotiated agreements, and the flexible Kyoto mechanisms of emissions trading, Joint Implementation and Clean Development.

However, as indicated above, this target had already been breached with a figure of 23.7 per cent in 2000, due to the rapid economic growth of the previous decade. This is projected to rise to 37 per cent by 2010 in the absence of corrective measures. Figure 2.6 below shows that of the 15 member states surveyed, Ireland had the third highest shortfall between emissions targets and projected emissions based on existing measures alone, highlighting the need to implement the *National Climate Change Strategy* as a key priority.

FIGURE 2.6

Gap (over-compliance or shortfall) between emissions targets for 2010 and projected emissions based on existing measures alone



Source: European Environment Agency, 2002

The reduction of landfill in waste management is another area in which Ireland is one of the EU member states with the most progress to make. The European Environment Agency identifies three categories in relation to landfill use in the EU:

1. Those that are currently landfilling less than 35 per cent of Biodegradable Municipal Waste (BMW) produced (Denmark, Austria, The Netherlands and the Flemish region of Belgium);
2. Those that are currently landfilling between 35 per cent and 75 per cent of BMW produced (France, Finland, Norway, Germany and Italy);

3. Those that are currently landfilling more than 75 per cent of BMW produced (Spain, the United Kingdom, Ireland, Greece and Portugal).

An EU Directive on the landfill of waste sets, as a policy target, the phased reduction of BMW going to landfill. By 2006, Member States are restricted to landfilling a maximum of 75 per cent of the total amount by weight of BMW produced in 1995. This target increases to 50 per cent in 2009 and 35 per cent in 2016. Countries that landfilled more than 80 per cent of BMW produced in 1995 may postpone the attainment of these targets for a maximum of four years.

The EEA sees the continuing growth in the production of municipal waste as a key potential barrier to meeting the targets set by the Directive.[12] It states that countries need to plan for this and ensure that adequate recovery capacity (e.g. composting, anaerobic digestion, material recycling, energy recovery etc.) is available for the increasing quantities of waste that will require diversion away from landfill. This indicates a particular challenge for Ireland, given its high dependency on landfill.

The Council also notes other significant challenges for Ireland in achieving sustainable development, both in terms of minimising the negative impact of economic growth and in meeting international obligations. Failure to comply with European directives has resulted in a number of legal actions taken by the EU Commission, with daily fines imposed for certain lapses. Recent cases include:

- A decision by the European Commission to refer Ireland to the European Court of Justice for the second time, in order to enforce a previous judgement of the Court handed down in September 1999 with regard to peat extraction;
- A European Court judgement in November 2002 requiring the Government to implement new legislation creating legal liability for the supply of water to group water schemes, or otherwise face daily fines; and

12. European Environment Agency (2001); *Indicator Fact Sheet Signals 2001–Chapter Waste*; http://themes.eea.eu.int/

- The initiation of legal action by the Commission for failing to comply with EU rules on water quality.

It is noted, however, that improvements in relation to certain environmental indicators have been made, due to such factors as the introduction of licensing in the industrial sector, changes in fuels used, increased efficiency in energy generation and the growth of environmentally friendly initiatives such as recycling. These include[13]:

- A decrease of 29 per cent between 1999 and 2000 in emissions of sulphur dioxide;
- The recovery of over 50 per cent of waste generated in the manufacturing sector; and
- While over 30 per cent of river channel is still considered to be polluted to some extent, the most recent assessment of river water quality in Ireland shows an improvement in water quality for the first time since surveys began.

Sustainable development links the economic, social and environmental objectives of society in a balanced way. International experience charts the path from compliance to sustainable development through a number of developmental points. In the early days of sustainability, the emphasis was on compliance through regulatory standards. Approaches have successively become more proactive, moving to environmental management systems, integrated management systems and design for sustainability (whereby environmental protections are part of the design of production facilities).

Given Ireland's comparatively late development in this area, a range of policy instruments will be required—ranging from regulatory instruments, environmental management systems to sustainable design of production processes to ensure eco-efficient outputs. Changes in inputs, including transfers to more efficient forms of energy, should also be supported. However, while Ireland has significant ground to make up to improve its league position, it is

13. EPA, 2002

not starting from scratch. Ireland has developed leading edge systems in areas such as food safety (overseen by the Food Safety Authority of Ireland) and integrated pollution control (a key function of the EPA). Individual companies have also begun to implement environmental management systems and cleaner production technologies.

The Council notes that since the development of a programme for action under Agenda 21—the international community's action plan for sustainable development—in 1992, and other relevant international and EU developments, considerable progress has been made in Ireland at a structural, policy and legislative level. This includes the Government's 1997 strategy, *Sustainable Development: A Strategy for Ireland*, and supporting and complementary policy documents in areas such as climate change, recycling and waste management.

An important aspect of future progress will be operation within international and national policy frameworks for environmental protection and sustainable development. The Department of the Environment and Local Government (2002a) identifies a number of national policy priorities such as climate change, nature and biodiversity, environment and health, and waste management, which corresponds closely to the current EU policy framework. Supporting legislative, regulatory and institutional reforms have been identified to address these priorities (ibid). A number of cross-sectoral policy developments, such as the *National Spatial Strategy*, also provide opportunities to advance sustainable development.

The Department of the Environment and Local Government also notes the following significant developments, which will undoubtedly contribute to future improvements:

- The strengthening of institutions for environmental protection and sustainable development, including:
    - The Environmental Protection Agency; the Irish Energy Centre, and the environmental information service, ENFO;
    - The establishment of Comhar to advance the national agenda for sustainable development;

- A modern legislative framework for the protection of all the environmental media has been put in place;
- An integrated pollution control licensing system has been put in place in advance of EU requirements;
- Government policy (including the National Development Plan and associated Operational Programmes) are increasingly reflecting environmental priorities;
- A number of Government Departments have adopted strategic sectoral policy documents; and
- In excess of 1 million hectares have been formally established as networks of protected areas for biodiversity.

Comhar, the National Sustainable Development Partnership established in 1999 – which is made up of 25 members drawn from a wide range of nominating bodies within the environmental, community, statutory, professional and economic sectors – has set out a framework for policy makers and stakeholders to benchmark progress in the area. This is based on 12 principles for sustainable development.

PRINCIPLES FOR SUSTAINABLE DEVELOPMENT

1. The use of non-renewable resources should be minimized
2. Use of hazardous / polluting substances and wastes created should be minimised; waste management should be environmentally sound
3. Renewable resources should be used within the capacity for regeneration
4. The quality of soils and water resources should be maintained and improved
5. The diversity of wildlife, habitats and species should be maintained and improved
6. Air and atmosphere should be protected and human-induced effects on climate minimised

7. The development of resource potential in one region should not compromise the ability of other regions to achieve their own potential
8. Social inclusion should be promoted to ensure an improved quality of life for all
9. Sustainable development depends on co-operation and agreement between states
10. The quality of landscapes, the heritage of the man-made environment and historic and cultural resources should be maintained and improved
11. Decision-making should be devolved to the appropriate level
12. Stakeholder participation should be promoted at all levels of decision-making

Source: *Comhar*, 2002

Sustainable development is dependent on collaboration and partnership across government, but also with NGOs and the individual citizen. The challenge in breaking the negative relationship between economic growth and environmental protection is a significant one. Meeting these challenges is exacerbated by a number of factors:

- The highly politicised and often emotive debates around waste management, water charges, etc.;
- Public attitudes towards paying for environmental protection – a Department of the Environment and Local Government survey in 2001 showed that, while Irish people are quite concerned about environmental quality and issues, less than 20 per cent were willing to pay higher taxes or prices, or make cuts in their standard of living, to this end.

The Council welcomes the recent developments as outlined above, which each contribute to ensuring that environmental protection is a key dimension of economic and social development, in terms of both policy development and implementation. In particular, it supports the policy objective of increased eco-efficiency, which aims at breaking the link between economic growth and environmental degradation and use of natural resources, and acts as a key indicator of sustainable development. A full range of instruments should be developed to achieve this aim, ranging from controls and sanctions for non-compliance with standards, to proactive and integrated approaches between Government, business and individual citizens.

The trend of increasing environmental pressures as a result of economic growth must continue to be tackled, albeit at a greater rate, by public sector policy and legislative and regulatory reform to ensure a mutually reinforcing relationship between environmental sustainability and social and economic progress.

2.2.9 Legal and Institutional Developments Affecting Social and Equality Policies

The 1990s witnessed some particularly important legal and institutional changes in the social area that will be explored in more detail in Chapter 8 but, nevertheless, belong in this inventory of key social developments during the 1990s. The Employment Equality Act, 1998, came into force in October, 2000, and prohibits discrimination in the area of employment on nine grounds – gender, marital status, family status, sexual orientation, religion, age, disability, race, and membership of the Traveller community. The Equal Status Act, 2000, signed into law in 2001, provides protection against discrimination outside the field of employment on the same nine grounds as the 1998 Act but applies to any goods and services which are available to the public, whether paid or unpaid, provided by the public or private sector. An Equality Infrastructure underpins this legislation and both the Equality Authority and the Office of the Director of Equality Investigations, with respectively pro-active and reactive roles, began operations in October, 1999. The National Disability Authority (NDA) Act, 1999, mandated the NDA to be proactive in nature and require all Government departments and State agencies to participate in initiatives to advance and underpin the inclusion of people with disabilities.

In addition, strategic policy frameworks have been developed in recent years designed to bring greater coherence and effectiveness to diverse activities influencing social objectives, principally the *National Anti Poverty Strategy*, the *National Health Strategy*, the *National Childrens' Strategy*, the *National Drugs Strategy*, the *Employment Action Pla*n and the first three-year plan of the NDA.[14]

The Council believes that these legislative and institutional developments mark a major milestone on Ireland's road from nominal to real acceptance of the dignity of the human person and the fundamental equality of all people within its territory. Committing resources to protect and promote individual rights and to enable Irish society to celebrate diversity is integral to eliminating poverty and social exclusion.

There have been parallel developments in the articulation of rights and obligations in other spheres. Through the Education Welfare Act (2000), the State has accepted the right of every child in the State to attend a recognised school or otherwise receive an appropriate minimum education. Though without giving it the force of law, Ireland and the other EU Member States adopted the Charter of Fundamental Rights at the Nice European Council (2000) as a contemporary summary and articulation of the respect for rights that should characterise European societies. Ireland has incorporated the European Convention on Human Rights into law and a Human Rights Commission was established in July, 2001, honouring a commitment under the Good Friday Agreement. This Commission is responsible for the promotion, protection, and development of human rights in the State and for creating and fostering a human rights culture in Irish society.[15]

14. The NDA's first strategic plan, *A Matter of Rights* (2001), identifies four priority action areas for 2001- 2003. These are: developing policies that promote the equal status of people with disabilities; guiding and monitoring the implementation within five years of the accessible public services programme; influencing attitudes in Irish society; and assuring best practices in services for people with disabilities.

15. Some of the Commission's its functions which impact particularly on social policy are: to keep under review the adequacy and effectiveness of law and practice in the State relating to the protection of human rights; to make

These policy and legal developments are, clearly, of major significance for social policy and, in Chapter 8, the Council takes the opportunity to contribute to the discussion as to how a rights-based approach can guide and shape the formation of social policies.

Having documented these long term and recent social changes, the Council offers its interpretation of them in the following section.

2.3 UNDERSTANDING IRELAND'S SOCIAL DEVELOPMENT

In outlining the Council's interpretation of Irish social development, this section deals respectively with:

- The constraints placed on long-run social development by emigration and a weak national system of innovation;
- The evolution of the Irish welfare system;
- The effects of industrialisation on class transformation and social mobility;
- The influences on income distribution; and
- The cultural processes of liberalisation, pluralisation, and secularisation.

2.3.1 Understanding Long Run Social Development: Emigration and Weak National System of Innovation

Much of the Council's work over recent decades sought to identify the causes of Ireland's disappointing long-run development and to find agreement on more effective strategies. The work undertaken for the Council by Mjøset described the country's long-run experience as a 'vicious circle'. He argued that '"the basic vicious

recommendations to Government (either of its own volition or on being requested) on measures to strengthen, protect and uphold human rights in the State; to promote understanding and awareness of the importance of human rights (and, for those purposes, to undertake or sponsor research and educational activities).

circle starts from two facts: the weak national system of innovation, and population decline via emigration" (Mjøset, 1992: 7). He showed that the mechanisms by which these facts reinforced each other could be found in the social structure. He demonstrated this by comparing Ireland's social structure with that of a selected group of small European democracies. This revealed that the more successful small countries "all developed autonomous civil societies" (Mjøset, 1992: 250). In Mjøset's view, "Ireland's problem may be described as follows: the Irish social structure had emigration as its precondition and most potential entrepreneurs would choose Hirschman's exit option" (p. 17).

This research also revealed structural elements among the causes of Ireland's difficulty. While Austria was a free rider on Germany's economic success in the post-war period, Ireland was a free rider on Britain's economic decline.

This combination has led the Council, over the past two decades, to propose that Irish strategy must work simultaneously on two related fronts. Domestic policy reform must improve the country's economic and social capacity, capability and cohesion. International policy must continue to secure Ireland's position in the EU—since this provides a much better international context for a small peripheral state than any past or present alternative—and make Ireland an attractive location for the production of high-value goods and services. The Council's analysis of long-run social experience fits closely with its interpretation of Irish economic development, summarised in Chapter 1 above.

It would require a detailed study to establish whether or not a national system of innovation is now in place, or imminent, which can perform the tasks identified by Mjøset. It is easier to underline the comprehensive population recovery and development that has been steadily consolidating itself over the last four decades and which, if Mjøset's analysis is correct, should make Irish society and the Irish economy more open to innovation. The overall population level reached an all-time low point of 2.8 million in 1961 but every census since then has recorded an increase. This was largely because net emigration declined substantially and no longer ran at high levels that were wholly cancelling out the significant natural increase in the population caused by high fertility rates. Indeed, in the 1970s, net immigration took place for the first time and was associated with a surge in the number of births to boost the population recovery further. Substantial net emigration emerged briefly in the late 1980s but did not take root and the 1996 population at 3.63 million was the highest on record in the 20th century. Between 1996 and 2002, net immigration reoccurred on a more substantial level than in the 1970s and helped to bring the population to 3.92 million in 2002. However, by this time Ireland's high fertility rates had declined substantially. The total fertility rate first dipped below the replacement level of 2.1 (the level at which a population reproduces itself) in 1989 and settled below it in 1991; CSO projections for well into the 21st century do not foresee it returning above it (*Population and Labour Force Projections, 2001-203*1. CSO, July 1999).

A second feature of population recovery has been a change in the age-dependency ratios. In the 1960s, because of the legacy of the heavy emigration of the 1950s, age-dependency rose to levels that were exceptionally high by previous Irish standards and by comparison with contemporary patterns in other developed countries. These levels began to decline slowly in the 1970s, and more substantially after 1986 when the child population began to decline, the older population had not yet begun to increase, and the active age group continued to enjoy growth. The Council noted (1996a) that this favourable demographic position was projected to continue until 2006, after which the age-dependency ratio will be driven upwards due to the growth in numbers of older people. Developments in the economic-dependency ratio (the number of dependants per 100 people at work) were slower to record improvement because of the high level of unemployment in the early 1980s but, with the fall in unemployment after 1987 and associated increase in participation rates, this indictor too has been showing steady improvement.

The Mjøset analysis pointed to multiple, interacting influences between population decline and economic underperformance, which had become ingrained in Ireland's economy, society and political culture. Positive links between population growth and demographic change, on the one hand, and a strong economic performance, on the other, are already evident but their full unfolding is not automatic and will require institutional and policy changes on many different fronts.

2.3.2 The Evolution of the Irish Welfare System

Historical Outlines

Ó Riain and O'Connell (2000) describe the evolution of the welfare state in Ireland as an example of delayed development. They summarise the position at the foundation of the state as follows: "The legacy at the time of political independence in 1922 combined an underdeveloped economy and a minimalist state. The inheritance included an attenuated version of British welfare institutions, including the poor relief system, an embryonic social insurance system providing unemployment and sickness compensation to manual employees, limited health and housing services and subsidised education" (324).

There were few welfare innovations in the first decade after independence. However, the 1930s ushered in an era of reform. Benefit payments were increased, new income maintenance schemes were introduced and a public housing programme was implemented. In 1947, a unified Department of Social Welfare was established. The Social Welfare Act of 1952 made universal various schemes of income maintenance. Cousins (1995) argues that the Irish system emerging in the 1950s remained "fragmented with little commitment to inter-class solidarity, unlike the relative universalism of the systems in the UK or Scandinavian countries". In the health area, attempts at reform, which would entail greater state involvement, were discouraged by the Catholic Church and private medical practitioners. The educational system remained predominantly private, with most of the population only able to attend primary level, which was state subsidised.

It was in the 1960's and 70s that the quality of social citizenship started to expand, with services improved and coverage of income maintenance payments expanded – contributory pensions were introduced in 1961, occupational injuries benefits in 1967. In that year also, free second level education was introduced. In the area of health, reforms included a reorganisation of general practitioner services in 1970 and the extension of eligibility for free hospital services for the entire population. By the end of the 1970s, the basic structure of the present welfare system was in place (Ó Riain and O'Connell, 2000: 326). This expansion has continued over the past two decades, with the role of the state now extending far beyond redistribution of income to involvement in direct employment, in subsidising voluntary and private market activity, and in providing and financing education, health care and housing services.

The Impact of EU Membership

Membership of the European Community played an important role in the expansion of the Irish welfare state, particularly in regard to the rights of women and workers[16]. It is accepted that, without membership of the European Community, legislation on equal pay and equal treatment for women would not have reached the statute books when it did. The Community was responsible for major advances for women such as the removal of the marriage bar in public employment, the introduction of maternity leave and greater equality in the social welfare system. Health and safety for workers in Ireland has also been considerably enhanced by membership of the European Community. This is not surprising given the fact that health and safety has been the main bulwark of European social policy mainly under the influence of member states from northern Europe. Irish workers have also benefited from the influence of the European Community in the areas of redundancy, work-time organisation and industrial democracy. Even if one believes that some of these positive developments for women and workers would have occurred anyway, membership of the European Community has undeniably accelerated progress in these areas and contributed significantly to the development of the Irish welfare state.

16. This and the next paragraph draw heavily on Kennelly and O'Shea (2002).

The European Social Fund also funded both training and employment programmes for workers during periods of high unemployment in Ireland. There may also have been more intangible demonstration effect from the European social model on the development of Irish social policy, which both protected and enhanced social protection and provision in this country. This effect may have been particularly important during the 1980s when both the UK and the USA embarked upon an attempt to either reduce public spending or dismantle the welfare state.

Understanding the Irish Welfare State

Research on welfare states has tended to identify welfare typologies, aiming to distinguish and group countries with similar regimes. The principles underlying different welfare regimes result in qualitatively different arrangements amongst state, market and family. They are reflected in whether programmes are targeted or universal, the conditions of eligibility, the quality of benefits and services, and the extent to which employment and working life are encompassed in the state's extension of citizen rights (O'Connor, 1996: 2). The basis for classifying welfare regimes varies according to the typology used. Some are based on levels of social spending, others on degrees of de-commodification[17] and social stratification, and others on the relationship between paid and unpaid work.

There is considerable debate regarding where Ireland fits. Indeed, the Irish case has proven hard to place in many of the typologies developed in the study of comparative social policy. Ireland is sometimes classified in the liberal group of Anglo-Saxon countries with the UK, USA, Australia, Canada and New Zealand. At other times it is grouped with corporatist, conservative countries such as Austria and Italy. Most analyses of the Irish welfare state point to its late development (1960 onwards) and its role as a mechanism of stratification in relation to class (Breen *et al*., 1990; O'Connell and Rottman, 1992; Ó Riain and O'Connell, 2000) and/or in relation to gender (McLaughlin, 1993). Some of the features of the Irish welfare state that make it difficult to classify include:

17. The degree to which people can uphold a socially acceptable standard of living independently of market participation (O'Shea and Kennelly)

- Catholicism and the role of the Catholic Church;
- Ireland's colonial and post-colonial status (Cousins);
- The underdevelopment of class based politics;
- The traditional importance of agriculture; and
- The role of the state.

Ó Riain and O'Connell (2000) contrast the Irish welfare state expansion to the Scandinavian pattern, with its emphasis on universalistic entitlements creating solidarity between social classes and a commitment to reducing inequalities. The Irish pattern has been to achieve solidarity through expansion of the social insurance system and the provision of basic levels of services, with only a slight commitment to reducing inequalities. In this system, a basic level of services is provided to all, ensuring that those classes disadvantaged in the market are taken care of at a basic level of provision, while at the same time ensuring that middle and higher income groups can supplement that basic level of provision by relying on their own resources and drawing on tax expenditures (Callan and Nolan, 2000: 181). This 'pay-related' two-tiered and in some instances three-tiered system is particularly evident in pensions, health and education. The pension system, for example, is comprised of a non-contributory means-tested tier, a contributory public tier and a third tier combining contributory state pensions with occupational pensions and other private pensions. Pension and health insurance contributions are both subsidised through tax expenditures.

Combining these facts with the emphasis on means-testing and targeting of benefits and the limited services facilitating the participation of women in employment (i.e. limited childcare and family friendly policies) illustrates well the liberal character of the Irish welfare state (Ó Riain and O'Connell, 2000). However, they point out, labour market policy points to a different orientation, as does the management of schools and hospitals (see below).

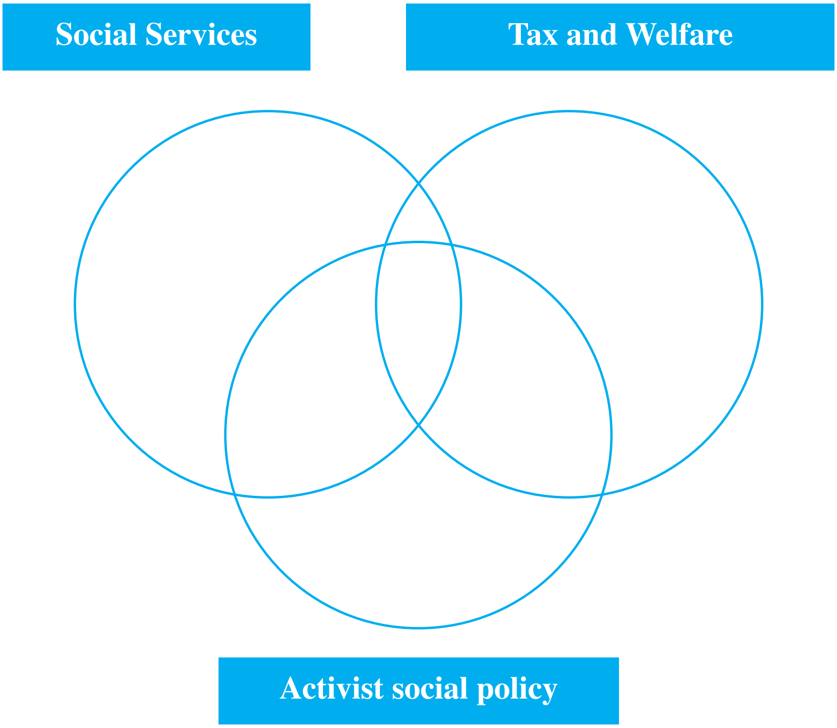
McLaughlin (1993) identifies Ireland as a Catholic corporatist type welfare regime. The principle of subsidiarity and especially the primacy of the family in the provision of services is central to such regimes; state intervention is acceptable once the principles of subsidiarity and societal consensus are adhered to. While there is limited commitment to redistribution, extreme inequalities are unacceptable. "Thus, Catholic corporatist welfare regimes can embody both liberal and social-democratic welfare principles" (207). This Catholic corporatism is strongly reflected historically in the treatment of women and is still reflected in the significant involvement of religious orders in the management of schools and hospitals although these are almost entirely publicly funded.

The significant deviation from Ireland's characterisation as a liberal welfare state arises when one takes a broader view of the welfare state, that is of state intervention for social purposes (Kleinman and Piachaud, 1993). Such interventions include industrial and labour market policy. It is in these areas that the Irish state has been highly interventionist. This has been evident in industrial policy for several decades. It has become highly interventionist in labour market policy over the past decade.

Three Dimensions of the Welfare System: Tax and Welfare, Services and Activism

In parallel with the account of industrial development policy presented above, the welfare system can been seen as containing three over-lapping elements: tax and social welfare, the provision of social services, and activist social and welfare policy. The tax and welfare element represents the traditional income protection instruments. It contains a combination of three approaches: universalist, insurance and residual. In the past decade or so, this element of the welfare system overlaps with the activist element, where income maintenance systems have been turned into, or combined with, active labour market policies. The activist side of social policy can itself be seen to contain three elements: active labour market policies (ALMPS), local and community development initiatives and social economy programmes.

FIGURE 2.7
The Three Dimensions of the Welfare System



This way of thinking about the overall welfare system is helpful in both studying the evolution of the system and in thinking about future options.

As regards the evolution of the system, it brings out both the achievements of the Irish approach and some of its limitations. After decades of modest social protection, there was a major, if gradual, extension of income protection. In the face of a severe crisis of unemployment, Irish policy became highly activist, in initiating both ALMPs and new approaches to local and community development. As regard services, the acceptance of housing as a fundamental bedrock of individual and social well-being, the recognition of market failure in both land and housing, and the consequent development of an extensive social housing policy were critical in creating the cohesion of Irish society in the second half of the 20th. century (Fahey, 1999). The huge extension of education, and the increasing recognition of its role in facilitating Ireland's economic development, is also, undoubtedly, a major achievement of Irish social policy.

This broad view also highlights some of the past limitations, and present challenges, of the system. The tax and welfare system, like those in many countries, was based on a male-breadwinner model and offered limited protection against some of the risks that many citizens faced. The social and care services were delegated to bodies that did not always respect the dignity and interests of citizens and were unequally available to different social classes. The activist dimension was underdeveloped.

This broad view has the advantage of not focusing excessively on tax and income maintenance. As Esping-Andersen says, "a major problem with the design of postwar welfare states was that they pursued 'equal opportunity' more through income maintenance than through labour supply management" (Esping-Andersen, 1996:. 260). In some respects this broad view yields a more positive assessment of the evolution of the Irish system. The social investments, such as the expansion of housing and education, are taken into account. This is important, because income maintenance alone cannot be expected to achieve equality and, where it does, it creates disincentives to work and education (Esping-Andersen, 1996: 264).

But when we bring services and activism into the picture, we still find that the system has left more inequality than is socially fair or economically desirable. More telling still, judged against a goal that has become increasingly central to Irish economic and social well-being—equality of opportunity—the system has not achieved what the Council believes to be necessary.

2.3.3 Industrialisation, Class Transformation and Social Mobility

One of the most profound long-term changes in Irish society was industrialisation and the associated changes in class structure.

Social mobility can be measured in a number of ways. Absolute social mobility refers to changes in the occupational structure and the overall amount of mobility associated with it. For example, a period which witnesses a large decline in the role of agriculture as an employer and growth in the role of services is likely to record extensive social mobility overall. Relative social mobility refers to the relative occupational success of people from different class origins. For example, the likelihood of entering a white-collar occupation may be very different for a person from a farming background and a person from an unskilled manual background. Trends in each kind of mobility can be understood as the outcome of economic development and public policy (see Layte and Whelan, 2000).

After the foundation of the state and prior to 1960 there was little in the way of industrial development in the country. Even in 1961, two-thirds of exports were agriculture related and 44 per cent of males worked in agriculture. Agriculture itself was based on small, family-run enterprises and social mobility was very much linked to inheritance of the family farm (Layte and Whelan, 2000: 94). Between 1961 and 1996, however, profound changes took place in both the economic and social spheres. The proportion of males in agriculture fell from 36 per cent to 13 per cent of the workforce, while the proportion of managers, professionals and administrators rose from 8 per cent to over 20 per cent. The skilled manual workforce grew from 12 to 18 per cent of the workforce between 1961 and 1996.

In terms of the effects such changes had on the class system, the proportion of those from farming backgrounds fell dramatically as did those entering the farming class. Unskilled manual workers formed a smaller proportion of all employees in 1994 than they did in 1973, while skilled manual destinations, after an initial increase up to 1987, remained stable after this point. Layte and Whelan (2000) point out that the restructuring which took place in Irish industry in the 1980s, as it was exposed to international competition, encouraged this process, with Ireland moving from being an agricultural society to a post-industrial one. Professional and managerial occupations increased from 13 per cent of destinations in 1973 to 19 percent in 1994, and routine non-manual work almost doubled over the period (2000: 95). Thus, industrialisation brought with it a decrease in recruitment into agricultural positions and an increase in service and routine non-manual positions. Also, the structure of these classes became more heterogeneous as those from other classes were recruited into these classes.

Examining the extent of absolute social mobility, upwards or downwards, the research found "a clear trend over time towards increased upward and long-range upward mobility" (p. 96). In 1973 just less than 10 per cent had been mobile into the professional and managerial class. By 1987 this had increased to 12 per cent and by 1994 to 14 per cent' (p. 97). They point out that a similar trend was experienced in relation to long-range upward mobility. In 1973, less than 4 per cent had risen from the working class to the professional and managerial. By 1987, this was just less than 6 per cent and by 1994 it was close to 7 per cent. At the same time there was no corresponding increase in downward mobility. "The profound changes in the class respondents' experienced significantly increased long-range upward mobility opportunities" (p. 97). Their data show that between 1987 and 1994 growth was observed predominantly in the professional and managerial class with a corresponding decline in the manual sector: "As a consequence it is among the latter that we observe a striking increase in upward mobility and a proportionate decline in downward mobility. The nature of the long-term transformation of the class structure in Ireland was such that extreme social closure at the top was not a possibility" (p. 105). This very significant change in the occupational structure and the large amount of absolute social mobility it afforded, is an important feature of the evolution of Irish society in recent decades.

It also puts into sharp focus the contrasting evolution of relative social mobility. In this regard, the research by Whelan and Layte points to the fact that after the 1960s the importance of inheritance as a means of gaining social position had declined. Free second level education had been introduced and educational qualifications had become increasingly important. Thus it could be expected that the enhanced absolute social mobility opportunities and the expansion of educational opportunities would lead to a more meritocratic society.

The Council reflected, in 1996, on the significant influence of class origin on educational attainment and noted the different ways in which social groups had responded to, and been affected by, the educational expansion that began in the late 1960s. Farm families were particularly successful in accessing education, including at third level, and thus entering the white-collar occupations coming on stream through the restructuring of the economy. Indeed, the scale of their success had contributed to some rural areas being drained of young people and human capital. The unskilled and semi-skilled working class, by contrast, did not prove as able to adapt to the new economic realities. While their jobs were in decline similarly to farmers, their children did not increase their participation in education to the same extent and were particularly unlikely to be in third level. As a result, relatively few of them found their way into the new white-collar occupations associated with the country's stronger economic performance. The Council concluded:

> The differential response to educational opportunity between the classes most affected by economic change has yielded the principal social structural defect in modern Irish society – the creation of large segments of the working class which have lost their traditional occupational base, been unable to find new occupational outlets, had their children poorly integrated into the full range of the education system, and been progressively marginalised as a result (1996a: 42).

The research carried out by Layte and Whelan presents an index of inequality of outcome between the professional and managerial class and the non-skilled manual class. Examining the extent of these inequalities over time, the research finds that, rather than a decrease in the scale of class advantage over the period 1973 to 1994, there was in fact an increase. Finally, examining trends over time in the relationship between class origin and destination, the research indicates a clear correlation between the two and, rather than observing a reduction in the association, the evidence suggests a pattern of little change over time.

2.3.4 Understanding the Influences on Income Distribution

Trends in income distribution were reported on in 2.2.3; they are an important input to the Council's *Strategy*. In order to understand these trends it is necessary to identify the different components of income and the factors that shape the distribution of these across individuals, occupational groups and households. Consequently, this section identifies the following 'layers' that together give rise to the trends in poverty and income distribution reported in Section 2.2.3:

- Changes in market income, distinguishing between:
  - Changes in wage and profit shares;
  - The increasing dispersion of earnings between *individuals* and *occupational groups*;
  - The distribution of market income across households;
- Changes in distribution of *disposable* income, distinguishing between the impact of:
  - Changes in social welfare transfers;
  - Trends in the progressivity of income tax and employees PRSI contributions.

The Section closes by documenting the distributional impact of budgets from 1987 to 2001.

Changes in Market Income: Wage and Profit Shares

Changes in the wage and profit shares of the economy are analysed below in Chapter 6 (Section 6.4.5). Since 1987, the share of total profits in domestic output has increased and there has been a corresponding reduction in the wage share. The impact of these changes in wage and profit shares on the distribution of household income, however, has been limited for two reasons: first, the profits of multinationals which dominate trends in the overall profit share are not part of Irish households' income; second, among Irish-owned companies, profits only affect households when distributed to shareholders.

Thus, despite the rising profit share in national output and declining wage share, the distribution of market income has been fairly stable in recent years and became somewhat more equally distributed between 1994 and 1998, as noted in 2.2.3 above.

TABLE 2.14

Trends in Earnings Dispersion, Ireland and Other OECD Countries, 1987-1994

Country	Top Decile/Bottom Decile		
	1987	1994	Change
Canada**	4.45	4.18	-0.27
Germany*	2.83	2.80	-0.03
Belgium*	2.45	2.24	-0.19
Finland	2.51	2.35	-0.16
Japan	3.15	3.01	-0.14
Sweden	2.10	2.18	0.08
Australia	2.81	2.86	0.05
Netherlands	2.53	2.58	0.05
France	3.18	3.08	-0.10
UK	3.31	3.39	0.08
New Zealand**	2.83	3.03	0.20
Austria	3.47	3.65	0.18
Italy*	2.30	2.33	0.03
USA	4.24	4.52	0.29
Ireland	**3.67**	**4.06**	**0.39**

Source: Barrett *et al*. (2000), Table 7.3
* = 1993 not 1994; ** = 1988 not 1987.

Changes in Market Income: International Perspectives

It is important to note two aspects of the context in which recent trends arise. First, Ireland has for some time had relatively high levels of wage dispersion, compared to other OECD countries. Second, across the world there has been a rise in earnings inequality in the 1980s and 1990s, although this has been greater in the Anglo-Saxon world than in continental Europe. These aspects are confirmed by Table 2.14.

Explanations of Increased Earnings Inequality

The rise in earnings inequality in OECD countries can be decomposed into three elements:

(i) an increase in educational wage differentials, that is, in wage inequality across those with different education levels;

(ii) an increase in age-related wage differentials, that is, the return to experience;

(iii) an increase in within-group wage inequality, that is, inequality not accounted for by (i) or (ii).

In the US and the UK, there have been large and simultaneous increases in earnings inequality across all these dimensions. In addition, many other OECD countries experienced some rise in at least one of these components. There was a sharp increase in returns to experience in Australia, Canada, France, Israel and the Netherlands, while returns to education increased in Israel and Sweden. Overall, "what we observe is a diversity of experience but with almost all countries experiencing some increase in inequality" (Gottschalk and Smeeding, 1997: 652).

It is widely agreed that there has been increasing demand for the labour of those with greater skills and education levels. Various theories have been advanced to explain this, and the associated increase in the gap between skilled and unskilled wages. The principal explanations are:

- The growth of trade with less developed countries, where the price of unskilled labour is far lower (Wood, 1995; Esping-Andersen, 1996);
- Changes in technology that are biased in favour of skilled labour; and
- The move from manufacturing to services which creates a greater trade-off between employment and equality (Esping-Andersen, 1996; Iversen and Wren, 1998).

Yet the rise in inequality has been higher in the Anglo-Saxon countries than in continental Europe. Explanations for this difference include:

- Stronger labour market institutions in Europe—wage bargaining, unionisation, minimum wage laws and social welfare systems—have limited the rise in earnings inequality associated with technological change (Krugman, 1994; OECD, 1994);
- Stronger labour market institutions in Europe, by compressing the dispersion of wages, create an incentive to adopt technology that enhances the productivity of unskilled as well as skilled workers (Acemoglu, 2002); and
- Countries now find it harder to simultaneously achieve high employment, earnings equality and budgetary restraint. Scandinavian countries tend to achieve high employment and earnings equality, but risk tax revolts. Continental Christian democracies achieve budgetary restraint and earnings equality, but are tending to high levels of unemployment. Countries with a more liberal welfare state achieve high levels of employment and budgetary restraint, but tend towards inequality (Iversen and Wren, 1998).

The relative merits of these different theories remains the subject of on-going discussion and research. But it is clear that they share the observation that the level of inequality has increased and new thinking is required to achieve the goal of fairness and cohesion (Esping-Andersen, 1996).

The Irish Experience of Increased Earnings Dispersion

Turning to Ireland, it seems that there was an unusually large increase in earnings inequality between 1987 and 1994 and that the distribution of earnings in Ireland is significantly more dispersed than other European countries with the exception of the UK (Table 2.14). This rise in earnings dispersion occurred at a time when there was a very substantial increase in the supply of skilled labour in Ireland. It is clear that there has been an even larger increase in the demand for skilled labour, and this is consistent with the shift in the demand towards skilled labour discussed above.

The rates of return for different levels of education (as indicated by wage premia) have been measured by Barrett, Callan and Nolan (1999). The general picture shown by their research was one of increased returns to university degrees and to junior cycle qualifications, approximate stability in returns to the Leaving Certificate and some evidence of a slight decline in returns to non-university third level qualifications. Overall, it was found that the high returns to education, taken together with the change in the age-education profile of employees, account for most of the observed increase in earnings dispersion between 1987 and 1994.

A significant factor driving the demand for skilled labour in Ireland has been the rapid influx of FDI in high technology sectors. However, wage dispersion has increased in all industries, so that FDI is likely to be only part of the story (O'Reardon, 2001).

In view of the significant differences in labour market indicators between Ireland and the UK, it is surprising that the increase in the dispersion of earnings in Ireland was greater than in the UK in the 1987 to 1994 period. Since 1987, Ireland has had a series of social partnership agreements including centralised agreement on wage increases. The share of employees in trade unions has declined in Ireland, but remains relatively high compared to the UK and the US. While wages councils were abolished in the UK, the Irish wage levels set by the Joint Labour Committees (JLCs) continued to rise and there was an substantial expansion in the numbers covered by JLCs. Furthermore, Irish social welfare support for the unemployed became significantly more generous than in the UK (Nolan *et al*., 2000a). In view of these differences, it is difficult to understand why there was a larger increase in earnings dispersion in Ireland than the UK over the 1987 to 1994 period.

The most recent earnings data referred to here are for 1997. More recent years have seen the emergence of labour shortages for all types of labour, including unskilled labour so that this period has seen stronger growth in wages among lower income employees. This period also saw the introduction of a minimum wage. The overall direction in the distribution of earnings in the most recent years is not known.

Changes in Household Income

The widening earnings distribution analysed above would, in itself, have contributed to a more unequal distribution of market earnings *across individuals* and skill groups. However, as discussed above, the distribution of market income *across households* has been fairly stable in recent years, and, in fact, became somewhat more equal. The primary factor contributing to the more equal distribution of market income *across households* has been the very strong growth of employment since the mid-1990s. This contributed to a significant increase in the income shares of the third, fourth and fifth deciles.

An important feature of recent social development has been the increase in female labour force participation. The effect of changes in female labour supply and wages on household income distribution has been examined by O'Neill and Sweetman (2000). They found that the rise in employment rates of married women was concentrated among women married to men with below average earnings, although women married to unemployed men were an exception to this. The rise in employment rates among spouses of men with below average earnings would tend to have an equalising affect on the distribution of household income. On the other hand, the distribution of female wages tends to be significantly more dispersed than that of male earnings. As female earnings become more important in their share of household income, this would tend to increase the dispersion of household earnings. Furthermore, wage growth among women has been most pronounced for women married to high earnings husbands. The contribution of these different effects to household income distribution was decomposed to O'Neill and Sweetman and, overall, they concluded that changes in the earnings of married women appear to have had an equalising effect on household incomes over the 1987 to 1994 period.

Changes in Disposable Income

The distribution of disposable income is a product of changes arising from the market and changes due to the impact of tax and social welfare policy. How have tax and welfare policy altered the trends in the distribution of market earnings outlined above?

Changes in Disposable Income: The Role of Social Welfare Transfers

The evolution of social welfare rates have a crucial role to play in affecting equality in the distribution of disposable income across households. Even if welfare payments are improving in real terms, unless they keep pace with other incomes, the relative position of those who are dependent on welfare will deteriorate, negatively affecting relative income poverty rates and increasing inequality in the distribution of disposable income (Table 2.4 above). Alongside the overall impact of rates of payment is the effect that differing rates of increase among groups of welfare recipients can have on the composition of those classified as experiencing relative income poverty.

Over the period 1980 to 2000, the focus of welfare policy has been on various groups within the welfare system with rate increases targeted accordingly. In the 1980 to 1987 period, the rate of increase to old age pensions was considerably higher than for other groups. From 1987 to 1994, priority was given to raising the lowest rates of social welfare payments, e.g., Unemployment Assistance. At the same time, rates for other groups (the elderly and widows) rose by less, although still ahead of inflation. This was influenced by the recommendations of the Commission on Social Welfare (1986), which highlighted the inadequacy of the lowest rates of payment. By 1994, there was a good deal of convergence in the rates paid across the different schemes, although differences remained. Between 1997 and 2000, the focus returned to the elderly with pensions for the elderly rising by 15-18 per cent in real terms, whereas the insurance and assistance payments for the unemployed or sick rose by 7 per cent. By 2000, the lowest rate of weekly payment was 79 per cent of the highest rate of payment, though the gap was less than it had been in 1980. The extent of the changes within this period was sufficiently pronounced to produce marked changes in the position of one group of social welfare recipient versus another over time (Callan and Nolan, 2000:184).

In examining the overall level of welfare payments and their relationship to increases in other incomes, various measures can be used: gross average industrial earnings (GAIE) as used by the CSO, net average earnings and average household disposable income from the Household Budget Surveys. Over the period 1987 to 1994, the rates of some social welfare payments rose more rapidly than mean incomes, while for other payments rates increased at a slower pace, although still more than inflation. This resulted in relative poverty rates remaining moderately stable over the period. However, from 1994 to 2000, the percentage of persons and households below relative poverty lines rose (Table 2.11). This reflected the fact that the incomes of those relying on social welfare payments fell behind the rapid growth in after-tax earnings (Table 2.4).

In summary, social welfare payments, while increasing in real terms, have grown more slowly than disposable (after-tax) income, notwithstanding the fact that some social welfare payments have exceeded the growth of gross manufacturing earnings. This has resulted in relative income poverty in 2000 being higher than it had been in 1987, while consistent poverty has fallen substantially since 1987.

Changes in Disposable Income: Tax Progressivity

There have been significant changes in the tax structure over the period since 1987. In 1987, there were three rates of income tax. By

1994, this had been reduced to two, with the abolition of the 58 per cent rate. The lower rate was cut from 35 per cent to 27 per cent, to 24 per cent, and in 2001 it was reduced to 20 per cent. The top rate was also cut, reaching 46 per cent by 1998 and 42 per cent by 2001. The size of the band covered by the bottom rate was also expanded considerably. Major structural changes were introduced: in 1999, standard-rating of personal and PAYE allowances was introduced, with an offsetting increase in the standard rate band, as part of the shift towards a system of tax credits (this was completed in 2000); in 2000, a shift towards greater individualisation in the tax treatment of married couples commenced.

TABLE 2.15

Redistributive Effect of Income Tax in Ireland 1987, 1994 and 1998 using LII data

	Gini before tax	Gini after tax	Redistributive Effect	Average tax rate	Progressivity index	Differential treatment
1987	0.3870	0.3418	0.0452	0.1540	0.2685	108.2%
1994	0.3837	0.3374	0.0463	0.1452	0.2887	105.4%
1998	0.3837	0.3468	0.0369	0.1397	0.2453	107.9%

Note: The household is the unit of analysis

The Council commissioned the ESRI to analyse the effect of these changes in tax and employees social insurance. Table 2.15 above shows that the level of inequality in the pre-tax distribution was little different in 1994 and 1998 to 1987. Turning to the summary inequality measure for post-tax income, this was again similar in 1994 to 1987, but somewhat higher by 1998. Thus, the overall measure of redistributive effect was very much the same in 1994 as it had been in 1987, but by 1998 it had fallen. The average tax rate and progressivity measures show how this came about. Comparing 1994 with 1987, we see that the average tax rate was down, though not sharply, but the degree of progressivity had risen and this compensated in terms of overall redistributive effect. By 1998, by contrast, the average tax rate was down once more, again not dramatically, but the degree of progressivity was lower, producing a fall in the overall redistributive effect.

Turning to employee PRSI contributions and associated levies, there were significant changes in these deductions over the period since 1987. A comparison of 1994 and 1998 shows that the overall redistributive impact of employee PRSI contributions (including levies) was lower in 1998 than 1994. This was because both the average rate and the progressivity of these deductions had fallen over the period (see Chapter 7).

The Distributional Impact of Budgets from 1987 to 2001

It is also useful to analyse the distributive impact of tax and welfare policy as a whole over the past 15 years18. This is done by looking at the impact of changes in tax and welfare on different parts of the income distribution. The focus of the analysis is on tax units, rather than households, since the tax and welfare systems do not, for the most part, operate on a household basis.

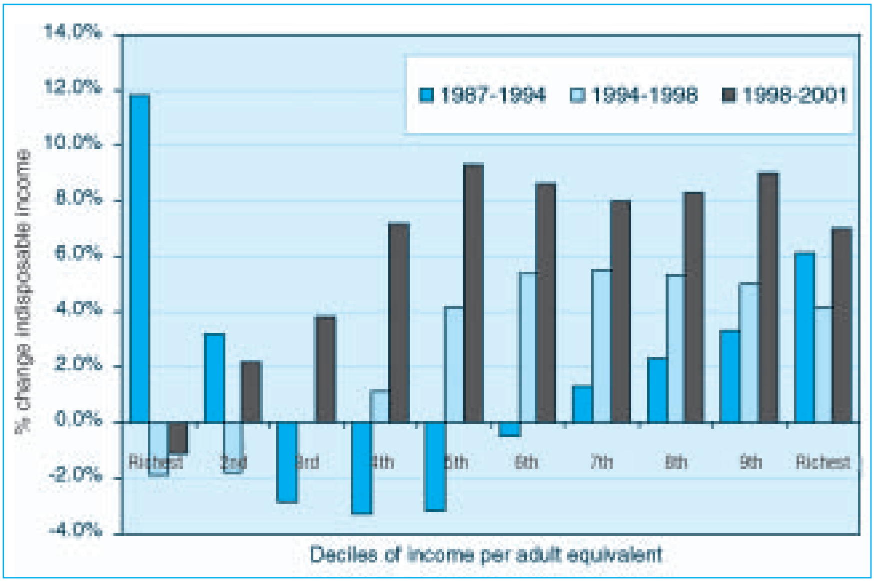
In carrying out their analysis, the benchmark used by the ESRI is to index tax and welfare parameters to the growth in average earnings (broadly defined). Using this benchmark, they look at three sub-periods: 1987-94, 1994-98 and 1999-2001. Figure 2.8 examines the gains, relative to the "distributionally neutral" benchmark, for each income decile during each sub-period. The 1987 to 1994 period was one in which income tax rates were cut and social welfare payment rates were streamlined, with special increases for those on the lowest rates, as recommended by the Commission on Social Welfare. This is the main factor behind the high percentage increase in income in the lowest income decile. Low-to-middle income groups fared less well than under a wage-indexed policy; indexation of tax allowances would have been of greater value to this group than the tax rate cuts actually implemented. The size and structure of the tax cutting packages gave gains to upper middle and high-income groups, with the proportionate gain rising with income.

18. The following section draws on NESC analyses of the distributive impact using the SWITCH tax-benefit model (Callan and Nolan (1999), Callan *et al*. (1999), and Callan and Nolan. (2000))

In the period 1994 to 1998, the standard and top tax rates were cut, along with a widening of the standard rate band, increases in personal allowances and a restructuring of the PRSI system. Social welfare rates generally rose by more than prices, but not as fast as the economy-wide earnings measure used by the ESRI. Some welfare payments did rise faster than other measures of earnings, such as the Gross Average Industrial Wage, used by the CSO. Overall, low income families fared less well under actual budgets than under a distributionally neutral earnings indexed benchmark, while those in the upper half of the income distribution gained 4 to 5 per cent more. The richest 10 per cent of families gained about 4 per cent from Budget changes, over and above what they would have gained from the simple indexation rule. But the poorest fifth of the population gained 2 per cent less from Budget changes introduced than from indexation.

FIGURE 2.8

Distributive Impact of Budgetary Changes, 1987-2001



The 1998 to 2001 period saw the greatest average gains, but again the distribution of the gains was uneven. Those in the bottom decile would have fared better under earnings indexation. Others in the bottom 30 per cent of the income distribution saw gains of 2 to 4 per cent, but higher gains of 7 to 9 per cent were recorded by the lower-middle, middle and upper reaches of the income distribution.

Focusing on the Budgets of 1999, 2000 and 2001, it was Budget 1999 that moved tax policy towards tax credits, via a standard-rated personal allowance, and the Budget in which resources were concentrated on increasing the standard-rated personal allowance. It is this latter feature which helped to focus gains on the middle of the distribution, rather than its upper reaches. In Budget 2000, the average gain in disposable income across all families was just under 3 per cent, measured against the wage indexation benchmark. The poorest one-fifth of family units did not share in this gain, with losses (relative to wage indexation) for the poorest one-tenth. Middle and upper income family units gained approximately this average, or slightly above. The relatively low gains for the poorest income groups reflect the balance that was struck between increased welfare expenditure and tax cuts. The upper reaches of the income distribution gained more from tax rate cuts and the widening of bands.

On the other hand, post-budget adjustments—such as the PRSI exemption limits and the Home Carer's Allowance—were of greatest proportionate benefit to the lower and middle reaches of the earnings distribution. Budget 2001 gave rise to an average gain of close to 3 per cent above the indexation benchmark. Low income groups fared 1 or 2 per cent better than wage indexation on average, but middle and higher income groups saw still greater gains. Most other income groups saw a gain of close to 3 per cent, with gains close to 4 per cent in the fifth and ninth deciles. These estimates take account of the main changes in income tax rates, tax credits and the standard rate band (including the further individualisation of the band). They also include the main changes in social welfare payment rates. Among the items not included is the distributive impact of the Special Savings and Investment Scheme.

Summary of the Influences on Income Distribution

In Ireland, over the period since 1987, a period in which average real disposable incomes rose by some 80 per cent, the distribution of disposable income across households was relatively stable, becoming somewhat less equal between 1994 and 1998. These trends are the net outcome of a range of influences:

- Changes in the wage share of national output had only a limited affect on the distribution of *household* income (See Chapter 6 for analysis of the wage share);
- The dispersion of earnings from employment *across individuals* and occupational groups continued to rise;
- Despite this, the distribution of market income *across households* became somewhat more equally distributed, reflecting the growth of employment and fall in unemployment; and
- The distribution of overall *disposable income* across households became somewhat more unequal, because social welfare payments increased by less than post-tax earnings.

The net effect of these changes was that, while the proportion of the population in consistent poverty fell from 17.8 per cent to 5.5 per cent, the proportion of the population at risk of relative income poverty did not fall (approximately one third were below 60 percent of average income in both 1994 and 2000) and an increased number were well below that line.

In analysing these developments, and framing future strategy, the Council acknowledges, first, that there has been a substantial increase in the level of social welfare payments and major progress in transforming the tax system since 1987:

- There has been a substantial increase in the level of social welfare payments. Increases in some social welfare payments substantially ahead of earnings contributed to stabilising the income distribution over the 1987 to 1994 period. In the post 1994 period, social welfare payments grew at rates similar to, and in some cases faster than, most of the sectoral gross earnings measures published by the CSO, including earnings in industry, the public sector and financial services. It is clear that policy decisions have included the desire to increase living standards of the poorest and those dependent on state transfers; and

- There has been substantial progress in transforming the tax system since 1987, by substantially increasing in the income level at which people enter the tax system, increasing the threshold for payment of the higher rate for single taxpayers and reducing marginal tax rates.

The Council also recognises that tax reductions have been an important part of the strategy to promote the growth of employment and reduce unemployment:

- Tax reductions contributed to wage moderation and facilitated an increase in labour supply, thereby stimulating employment growth and reducing unemployment;
- Nobody knows the exact magnitude of these effects on employment and unemployment and the degree to which they would differ if a more egalitarian tax and welfare reform strategy had been adopted; and
- The resulting expansion of employment and reduction in unemployment contributed to a somewhat more equal distribution of market income *across households*. Thus, while the direct quantifiable effect of tax reductions was to widen the distribution of disposable income, they probably also had an indirect equalising effect on the distribution of household income.

The Council identifies the risk of poverty and inequality as one of the vulnerabilities to which the Irish economy and society is prone, and in Chapters 4, 7 and 8, it outlines ways in which these vulnerabilities should be addressed.

2.3.5 Liberalisation, Pluralisation and Individualisation

The final element in an understanding of Ireland's social development is a set of changes that might be described as liberalisation, pluralisation and individualisation. Among the significant social changes in recent decades are:

- A weakening in traditional forms of authority;
- A revival of Irish culture and increased confidence in Irishness;
- The emergence of a culture of revelation and investigation, which can be a step on the road to a stronger culture of compliance and accountability;
- The spread of information technology through a large segment of society;
- Social and cultural effects arising from return migration and immigration. As Fitz Gerald says, "the multicultural nature of the economy, if not of the wider society, has been part of the current Irish success story" (2002. 80);
- The discovery of the Irish diaspora: during the late 1980s and 1990s, Ireland has partly *become* internationalised, and partly *re-discovered* that it has been internationalised for a very long time (O'Donnell, 2000);
- Recognition of the effects of discrimination and inequality on life opportunities and participation in society;
- Increased rates of drug abuse;
- Increased levels of violence in incidents of public disorder;
- Pluralisation of lifestyles, values and ethnic composition;
- Increased numbers of refugees and asylum seekers, vulnerable in several ways;
- Increased evidence and awareness of racism;
- Harmful consumption of alcohol, cigarettes and drugs, as well as a more sedentary lifestyle and overwork are negatively affecting the nation's health, including that of the young, and have already notably increased the incidence of obesity in Irish society;
- Decreased participation in elections and, on initial evidence, in voluntary activity; and
- Greater emphasis on involvement of the people affected by poverty, social exclusion and inequality in policy development and delivery.

It is clear that the processes of liberalisation, secularisation, pluralisation and individualisation contain a complex mixture of positive and negative elements. Indeed, these processes are related to the underlying economic trends described earlier.

While all these changes are related, it is probably incorrect to view them in a deterministic way. Thus, while a more liberal and plural society can be a more violent and materialistic one, this is not necessarily so. The Council believes that, working with what we have been given by nature and history, the quality of collective and individual life remains open to the influence of reason, engagement and solidarity.

In a like manner, the Council does not see the trends to liberalisation, secularisation and individualisation as 'modernisation' of a linear, deterministic or predictable type. Most of the cultural and social elements of earlier decades—spirituality, family, music, sport and local loyalty—are still present. But they are adopted and used in varying combinations to form a range of identities.

In its 1996 *Strategy* report, the Council focused on three clusters of relationships—those centred on family, gender and community—and concluded that, despite some growing pressures on them, the balance of evidence did not support the view that Irish life was becoming more individualistic and less attractive.

For example, a negative image of trends in family life could be suggested by the rise in births outside of marriage, the introduction of divorce and the acknowledgement of violence and abuse within families after 1960. However, the Council pointed to the many counter-balancing positive trends—such as the higher levels of material and emotional investment in children on the part of parents, the rapid growth in children's educational attainment, and greater concern for the personal rights and needs of children. It concluded that the reality was actually a net improvement in the social resources and capacities represented by family life in recent decades. At the same time, the 1996 Strategy report recognised that some families continue to have a poor quality of life and that their circumstances worsen as the circumstances of the majority improve, simply by virtue of changing relativities. The view expressed by the Council was that the 'crisis of the family', in so far as it exists, is a crisis of the uneven distribution of resources rather than in the overall quality of family life. Some of these resources have a material base and so are subject to redistributive action by the state and, thus, can be addressed and eased by policy; others, however, are less easy to address.

The Council further identified change in the social, cultural, legal and economic position of women as the single greatest change in Irish society since 1960. It saw this reflected in the greater participation of women in public life, the transformation of the 'traditional' roles of women as housewife and mother, and the decline in marriage fertility. The central questions highlighted by the Council in 1996 were how to overcome a plateau effect and make further progress in advancing towards greater gender equality overall, and how to respond more effectively to the uneven distribution of benefits across groups of women as their social class, region, family circumstance and age could give them a very different experience of the progress that had been made.

The Council also noted significant developments in the community as a social resource since the 1980s. This was shown by communities' responses to economic and social dislocation and the state's involvement of community groups in a range of new area-based initiatives. The discovery of community groups as potential partners with state agencies was originally prompted mainly by the EU, but now attracts increasing domestic funding. Advocates of the approach see it as drawing out the unused potential of an area and distributing the benefits in an equitable way (NESC, 1994). Critics point to the structural weaknesses in the approach and to the inadequacy of the area-based perspective, i.e. that poverty is actually found in social groups rather than localities. In spite of these reservations, the Council concluded that community initiatives have a role to play and that the development of community life is a resource in Irish society.

The Council reiterates its 1996 conclusion that there has been a substantial advance in many basic social resources and capacities in recent decades. It believes that, on balance, Ireland's social and economic development has been enhanced by the emergence of a more autonomous, varied and open civil society. However, this presents in a new form the underlying challenges of achieving a society that enables the full flourishing of all its people. For example, the developmental impact of the advances made has been reduced by their uneven distribution across social groups and geographic areas, damaging the life-chances of those involved and amounting to the main structural weakness in Irish society.

2.4 THE SOCIAL VULNERABILITIES OF IRISH DEVELOPMENT

2.4.1 Contrast with Alternative Interpretations

The account of Ireland's social development outlined above combines the social side of the earlier pattern of indigenous development and the social side of a dynamic regional economy in an age of information technology. This is by no means a complete account. Nor is it a complete account of how public policy has shaped both earlier indigenous development and more recent economic and social trends. In introducing the recent ESRI study *From Bust to Boom?*, Nolan *et al*. (2000b) emphasise the fact that the state plays a central role in the shaping of developmental and distribution outcomes. The authors add: "However, we treat each of these state roles as largely referring to the relatively distinct and identifiable institutional realms of industrial and economic development and welfare state policy" (p.3). The future development of the economy and society, and perhaps the analysis of past developments, requires that the developmental and welfare dimensions of public policy be more closely linked.

While the Council's interpretation of Irish society remains incomplete, it can be contrasted with a number of alternatives, each of which claims to have a comprehensive explanation.

These alternatives see Irish social policy and organisation as fatally contradictory. One version suggests that Ireland's economic and social development can be explained by its continued position as a dependent peripheral country in a neo-colonial relation with the dominant capitalist powers (O'Hearn, 2001). Thus, O'Hearn denies that Ireland has made any real economic breakthrough, and says "In the main, the Irish tiger economy boils down to a few US corporations in IT and pharmaceuticals" (O'Hearn, 1996). A related view acknowledges that significant economic growth has occurred, but sees it as "economic success and social failure" (Kirby, 2002). This "correlation of economic success with social failure…is no accident. It derives from the central feature or Ireland's industrialisation, namely its high level of dependence on inward investment" (Kirby, 2002: 141). In both cases, Ireland's experience is explained is by the state's adoption of a neo-liberal economic and social strategy. In both cases, social partnership is seen as a mechanism by which social groups are co-opted to neo-liberalism (Kirby, 2002: 163).

A central aspect of these interpretations is the dual claim, first, that Ireland's recent economic growth is characterised by an expansion of low-skilled, low-paid, jobs and, second, that this is an unavoidable feature of the path of economic development that Ireland has adopted. Addressing the first of these claims, O'Connell (2000) notes that:

> It is generally assumed that recent growth has been accompanied by a corresponding increase in inequality and the emergence of qualitatively different form of marginalisation, exclusion and polarisation. Such arguments have generally not been accompanied by detailed empirical analysis and the reality, we will argue, is somewhat more complicated. (p. 3)

Having analysed the long-run trends in the labour market and the class structure and occupational structure of Irish society, O'Connell concludes that "the more recent trends represent a continuation of well-established trends over the past three or four decades" (p. 76). What are these trends? "Overall the long run trends in the class structure have entailed an up-grading of the quality of positions in the labour market and there is little in this long-run transformation of the class structure to suggest a deterioration in the quality of jobs" (O'Connell, 2000: 76).

The view that Ireland's social development is fatally contradictory does not seem to provide an accurate or persuasive account of the role of public policy in Irish society. Consider the claim that Ireland has followed a neo-liberal path in the areas of welfare and social services. Ó Riain and O'Connell (2000) point out that, in its response to unemployment, the Irish welfare state has departed in two important respects from the standard 'residual' or liberal welfare regime.

First, there has been a solidaristic commitment to maintaining and even increasing the real value of unemployment benefit and assistance payments since 1987. This is driven by the terms of the social partnership accord, and "differs markedly from the regimes, such as Britain" (Ó Riain and O'Connell, 2000: 333). In Ireland, the distribution of household income was relatively stable during the 1980s and into the 1990s, "with no suggestion of the marked increase in inequality seen in the USA and the UK" (Nolan *et al*., 2000b: 346).

A second departure from liberalism can be found in employment policy. Liberal and conservative social policies tend to favour passive approaches, and to eschew intervention to promote labour market re-entry of the unemployed. In contrast, Ireland "has been particularly innovative over the past decade or so in bringing about a shift in the balance from passive income support to active labour market policies with temporary employment and training programmes, and in reducing unemployment/poverty traps" (Ó Riain and O'Connell, 2000: 333-4).

Likewise, the Council is not persuaded by the argument that the trends in income distribution and inequality in Ireland are adequately explained by our high-level of participation in the international economic system. As Nolan *et al*. say, "The Irish experience and its distributional consequences is not simply a story of globalisation, forced withdrawal of the state and the promotion of neo-liberalism" (Nolan *et al*,. 2000b; 1). In fact, the Irish state has been "flexible, reactive and developmental" (p. 2). While this makes it the study of public policy complex, and the effects of state action varied, it means that it cannot be neatly explained by any single theory or doctrine.

2.4.2 The Vulnerabilities of Irish Social Development

While the Council does not accept the alternative perspectives discussed above, it is clear that they contain accurate observations. When these are combined with the Council's own interpretation, it becomes clear that Ireland's small size, historical experience, institutional structures and type of economic development contain undoubted social vulnerablities. These vulnerabilities include the following:

- The legacy of limited indigenous development created significant inequalities in opportunity and unfair outcomes and yielded limited resources for social protection and social services;
- Economic openness creates the possibility of extensive decline, which can create unemployment, poverty and emigration;
- Economic openness creates the possibility of extensive growth which, in certain circumstances, can have a number of negative, as well as many positive, social effects:
  - increased earnings disparity;
  - rapid population increase, with attendant problems in provision of public services, transport, health-care, education and housing;
  - a rapid switch from emigration to immigration;
- The over-riding need to achieve non-agricultural development implies policies oriented to the attraction of inward investment in high-tech, high-growth sectors and to achieving competitiveness which can, in certain circumstances, yield relatively high levels of income inequality;
- The over-riding need to create employment implied approaches to economic and social policy that maximised job creation and

minimised the risk of work disincentives, which can risk poverty and unacceptable levels of inequality;

- The consensus-orientation of both the society and the policy system, though it has many advantages when well co-ordinated, makes socially beneficial policies and institutions vulnerable to blockage by narrow interests;
- Centralised and/or bureaucratic systems for providing social services run the risk of rigidity, inefficiency, high-cost and limited response to citizens' diverse and changing needs; and
- The institutional legacy created a mixed economy of welfare which, though it can be highly targeted on the least well off, is vulnerable in a number of ways:
  - it can become a 'two-tier' system;
  - it can delegate social services to organisations that adopt hierarchical and inflexible modes of delivery;
  - it may not respond flexibly to new social needs and changing circumstances;
  - structural problems in service delivery may provide a disincentive to greater welfare effort and encourage disengagement from the public system;
  - welfare benefits may progress unevenly or fall behind wider income trends;
  - it can provide inadequately for those not attached to the formal labour market.

In summary, these social vulnerabilities arise from three general sources:

- **The legacy of the past**, that yields a society containing greater inequalities of opportunity and outcome than is desirable;
- **The economic context**, which requires competitiveness, high levels of employment and which can give rise to extensive growth (or decline); and
- **The organisational challenge** of providing quality public services in an age when citizens' needs are varied, complex and

changing and in which the limits of bureaucratic delivery are acutely felt.

It is clear, therefore, that there is no comprehensive doctrine—of the market, the state, society or globalisation—that uniquely explains Ireland's current social situation and unambiguously guides action.

The vulnerabilities identified above are discussed further in Chapter 3, where their implications for current national strategy are explored.

Part II

Vision

CHAPTER 3

EXPERIENCE, UNDERSTANDING AND NEW POSSIBILITIES

3.1 FROM REVIEW TO STRATEGY

This section identifies how the review in Part I of the report provides the basis for the Council's proposed economic and social strategy in Part III. The faculty that takes us from the past to the future is vision—vision as hope, as clear sight of realities, as perception of shared pressures and concerns and sight of new possibilities. Hence, vision is the central theme of the chapter.

3.2 VISION AS HOPE: A SUCCESSFUL SOCIETY

In its 1999 *Strategy* report, the Council proposed a new vision for Ireland. It argued that the foundations of a successful society are:

- A dynamic economy;
- A participatory society;
- Incorporating a commitment to social justice;
- Based on consistent economic development that is socially and environmentally sustainable; and
- Responds especially to the constantly evolving requirements of international competitiveness, understood as the necessary condition of continuing economic and social success.

This vision had several dimensions, the most important of which were:

- Economic inclusion based on full employment;
- Social inclusion, reflecting full participation in those activities which constitute the norm in society;
- Successful and continuing adaptation to change;

- Commitment to the utilisation and development of the potential of the Information Society and the promotion of research and development;
- Commitment to lifelong learning;
- Environmentally sustainable and balanced development between regions and between urban and rural areas;
- Commitment to the further development of the European Union and international solidarity; and
- An entrepreneurial culture.

The Council also pointed out that the realisation of its vision would have a number of practical beneficial consequences for individuals and for society. These would include:

- Every child would leave primary school literate and numerate;
- Every student would complete a second cycle programme appropriate to the individual's capacity and interests;
- Every person seeking employment would be equipped with the personal skills and supports to find satisfying employment at reasonable rates of pay;
- Every person would have access to lifelong learning, a sense of personal security in a changing work environment, an opportunity to balance work and family commitments and a capacity to share the gains made by successful competitive firms and high performance public bodies;
- Every family would have access to healthcare, affordable housing appropriate to their needs, good quality childcare and a well functioning public transport system;
- Every firm would have the capacity to compete effectively in the global market place, through enhanced partnership with their employees and a supportive business environment backed up by an appropriate macroeconomic policy;
- Every region would have an efficient physical infrastructure to support sustainable economic activity, and promote social cohesion, based on a balance between urban and rural needs;

- Disadvantaged communities would have received the benefits of an investment programme and more responsive public services to overcome the accumulated burden of unemployment and marginalisation; and
- Average living standards (GNP per capita) would have exceeded the EU average, those dependent on transfer payments would share in the increased affluence and a reduced rate of poverty would ensure a more widespread participation in the lifestyle of a mature developed economy.

The Council reiterates the vision of a successful society outlined in 1999. It remains of the view that a successful society is one in which individuals, families, associations and communities, whether geographical or interests based, can flourish and in which the public system enables them to achieve their changing goals. It should be clear from this account of a successful society that equality is one of the central concerns of the Council: equality of educational service and opportunity, of access to training and employment opportunities, of chances to balance work and family life, of access to the key services that assist well-being, of local and regional infrastructure, in short, equality of status in access to the services of the public system. The major challenge is to identify what would be necessary to achieve the outcomes listed above and to build a consensus to meet these requirements.

3.3 VISION AS SIGHT

In order to motivate and guide action the successful society must be visible, at least in outline, from where we are. This means that it must be based, to a significant degree, on economic, social and policy experience—vision as sight. This section outlines how the Council sees Ireland's past economic and social experience.

3.3.1 Understanding Ireland's Experience

A key aspect of vision is clear sight of past experience. Ireland's economic and social experience has been documented and interpreted in Chapters 1 and 2. Overall, Ireland's dramatic economic performance in the 1990s was caused and sustained by three main factors:

- **The national policy and institutional framework**, which was consistent, highly focused on competitiveness and employment-creation, innovative and problem-solving;
- **An export sector** that was greatly expanded and increasingly concentrated in high-value, high-growth market segments; and
- **The European Union**, because it increased market access through creation of the single market and negotiation of WTO agreements, created a level playing field through re-regulation, provided a relatively stable monetary environment and supported Ireland's infrastructural and social development.

As discussed in Chapter 2 above, Ireland's social evolution in the past decade was shaped by economic expansion and also in significant ways by the legacy of the past and by public policy.

3.3.2 Trusting Ourselves: Revising Means and Goals

A critical aspect of vision is clear sight of how public policy, the social partners and others have influenced the economy and society, and how they can influence it in future. Over recent decades the Council and others developed a particular view of what a successful economy would look like, what role public policy has in promoting economic and social development, the nature and role of social partnership, the desirable and likely pattern of enterprise-level partnership, the contribution that EU membership can make and the social patterns and social policies that would be evident in a prosperous economy. Our view on these issues was, in large measure, derived from study of the patterns of economic and social life, and public policy, found in the richer states that we aspired to catch up with, and was often described as a superior 'model'.

Now that a significant degree of economic and social catch up has been achieved, a more successful economy, society and public system looks significantly different from the model that was envisaged. This new view is by no means complete, but some of its key features are identified here. More important than the substance of the new view, is the way in which actual developments differ from our best strategies, and how this forces us to alter how we think about strategies, models and plans—and, most of all, about experimental action.

While the state is as important as was envisaged, its role in promoting economic development is somewhat different. The state remains critical in providing a vision and coherent strategy, in shaping economic and social development, and in achieving economic and social balance. Economic and social balance are now seen to depend not only on redistributive taxation and welfare, but on a complex range of services. Its developmental role can be distinguished somewhat from its regulatory role, and each seen in new ways. Its developmental role is no longer seen as protecting the national economy in order to build strong localised enterprises. Rather it depends on its ability to create and animate networks of production and innovation and international networks of capital, and to link them together in ways that promote local and national development. In Chapter 1, the idea of the Flexible Developmental State was used to characterise these roles of public policy (Ó Riain, 2000). The state's regulatory role lies in correcting a range of market failures, in order to meet the goals of long-run investment, efficiency, universal service and social cohesion. Depending on circumstances, that role can be played by regulation or state ownership, or a combination of both. Overall, a successful state requires a new combination of policy-making implementation and monitoring (NESF, 1997b).

The patterns of business development involve less indigenous clustering of large firms and more internationalisation and networking than was envisaged in earlier decades. Indeed, the Irish experience raises questions about some influential theories of indigenous agglomeration and clustering, on the one hand, and FDI and globalisation, on the other. Successful sectors show limited clustering, of the sort advocated by Porter, and Irish-owned firms do not seem to have a 'home base' in Porter's sense (Clancy *et al.*, 1998; O'Donnell, 1998). Although Porter's 'diamond' remains relevant wherever competitive advantage exists—since demand condition, factor condition, firm strategy and inter-industry synergies are necessary—the diamond is rarely contained within Ireland. Instead, the firms that succeed are often those that integrate themselves, with the help of Irish government agencies, into international networks. This can, of course, include close networking and sectoral strength within Ireland. Ó Riain's analysis suggests that two broad modes of integration into the global economy can co-exist, each 'combining local and global networks in different ways' (Ó Riain, 2000:160). It highlights the multiple roles which a flexible developmental state can play in fostering more advantageous connections to the global economy.

The Council and others concerned with Irish public policy were at one time interested in the high quality of public governance and economic performance achieved in the most successful Northern European neo-corporatist countries in the post-war period. It is clearly tempting to see the emergence and significant success of social partnership in Ireland as an adoption of 'neo-corporatism'. But the Irish case, and perhaps also the Dutch case, suggests that what has emerged in Ireland is different in several important respects. Firstly, Ireland displays few of the structural characteristics traditionally seen as necessary for successful neo-corporatist 'political exchange' (Hardiman, 1988). Secondly, the substance of Irish policy under partnership differs from post-war European neo-corporatism (Teague, 1995; Taylor, 1996). Thirdly, the social partners and government have developed a perspective which goes well beyond the categories used to understand and characterise post-war European neo-corporatism. Irish social partnership may best be seen as a form of post-corporatist concertation, involving a wider range of social groups, in the context of a rapidly changing and more internationalised economy and society.

There was also a particular view about how enterprise-level relationships might evolve. Differences between the technological and managerial profile of foreign-owned and indigenous companies were a cause of much research and concern in the 1960s and 1970s.

Nevertheless, in those decades there was considerable uniformity in industrial relations. A model based on collective bargaining and arms-length dealings between unions and management, diffused throughout much of industry and services. This naturally shaped understandings of what form greater enterprise-level partnership would take and of what national institutional framework would support greater partnership.

However, research by Roche shows that in the 1980s and 1990s there has been a distinct fragmentation and divergence in industrial relations practices. Four types of industrial relations have emerged: an approach characterised by explicit union-management partnership structures and processes, a non-union human resource (HR) model, an approach of managerial unilateralism and de-regulation and, in some sectors of the economy, continued adversarialism with only piecemeal innovation (Roche, 1998). In this context, the Council, in its 1996 *Strategy* report, emphasised the importance of enterprise-level partnership, outlined the principles for a supportive national framework, and recommended action to implement enterprise-level partnership.

Within this framework, the innovative experiments of recent years show that, while differences remain on how partnership should be ideally defined, working within the terms of the national partnership agreement, employers and unions can reach a consensus on procedures for assessing the current conditions in an organisation and initiating partnership activity. This process of extending shared understanding through joint actions between employers, employees and unions is central to the development of enterprise partnership, organisational capability and performance. Just as Ireland's strong economic growth and system of social partnership are not easily understood in terms of the models that we had in mind, so developments in workplace relations stretch conventional categories.

While the EU was seen as an important source of agricultural supports and structural funds, its impact on Ireland is now recognised to be much wider, encompassing extensive regulatory change and providing an institutional framework to govern deep internationalisation of markets, technology and, to a lesser extent, society.

The society that has emerged also differs in significant ways from what was expected. Demographic and economic trends yielded greater population growth. The quantitative recovery of the Irish population was elevated into a considerable qualitative development by the sustained increase in education. The severe crisis of the late 1970s and the 1980s created a set of social problems and inequalities that became quite entrenched. At the same time, all western societies faced a greater challenge in combining budgetary restraint, high employment and equality (Iversen and Wren, 1998). This combination of domestic crisis and international change posed a major challenge both to Ireland's traditional social policy and to alternatives based on the experience of societies that did not confront Ireland's combination of developmental challenge and unemployment crisis.

At the same time, there was, as the Council argued in its 1996 *Strategy*, considerable enhancement in social resources and capabilities. The changing legal, cultural, economic and social status of women was undoubtedly a most significant development. There was evidence of a net improvement in the social resources and capacities represented by family life, particularly in the overall advance in the condition of children. Ireland displayed considerable vitality in the continuation, formation and vibrancy of associations, and the crises of the 1980s prompted both the revival of local community activity and a new engagement, on the part of the State, with communities as partners in promoting development and combating social exclusion. The greater than expected increase in employment and living standards has produced a further set of social changes that are noted in Chapter 2. Among these would seem to be greater diversity in modes of life, experience, outlook and ethnicity, a weakening in traditional forms of authority, increased level of drug and alcohol abuse and increased pressure on the family and other social resources through longer commuting times and inadequate services. In the context of a more complex, diverse and volatile society, effective social policy is recognised as more diverse, fragmented and decentralised than the post-war models of welfare which it was hoped to build. Hence effective social policy requires a different kind of public administration from the post-war administrative state.

Taken together, the slight deviation from the expected model or goal on many fronts—the role of the state, business development, social partnership, industrial relations, the EU and social policy and patterns—amounts to a significant deviation when all are taken together. What is clear from Ireland's experience is that:

- Ireland does not fit neatly into any existing model or category of socio-economic development;
- Much greater economic and social progress occurred than was deemed possible within the models that informed earlier analysis;
- Ireland has succeeded with an eclectic approach, that seeks to adopt the best features of different socio-economic models;
- Many of the new economic and social possibilities were discovered by experimental problem-solving action involving government, the social partners and others; and
- Changes in many parts of the economy, society and the state can amount to significant change in the whole.

Because of this, the Council rejects any one-dimensional view, that the changes in the past decade are due to a single factor, whether it be fiscal correction, tax reduction, inward investment, educational attainment, market liberalisation, high technology, European integration, labour supply, changes in social policy or indeed, social partnership itself. In contrast, the Council believes that the changes since the late 1980s—in the economy, business, public policy, enterprises, the EU and society—have been the product of widespread policy and institutional adaptation and experimentation. Although not derived from a preconceived plan or model, each change has been deliberate.

It is the willingness and ability to change policies, arrangements and institutions that ultimately underlies Ireland's success. This is confirmed by the fact that Ireland continues to achieve less in precisely those areas where we have not adapted institutions, policies and arrangements.

As in its previous *Strategy* reports, the Council identifies in this report what it sees as the key strategic goals of public policy in the coming years and the policy priorities that it views as necessary to achieve those goals. But, based on the experience summarised above, it recognises that an effective public system is one which learns from experience and experimentation to continuously improve policy and implementation. Indeed, it emphasises that the goals of policy must themselves be revised in the light of experience. Rather than see public policy as guided by timeless high-level goals, it understands it as a problem-solving process which is guided by action-oriented co-ordination and information. This reflects that fact the life of the society—like that of individuals, the public system and the economy—is realised in history.

3.4 SEEING IRELAND'S ENDURING VULNERABILITIES AND CHALLENGES

3.4.1 The Vulnerabilities of Irish Economic Development and Ireland's Enduring Economic Challenge

The Council's analysis and interpretation of our long-run economic development lead it to conclude that Ireland's small size, peripheral location and the type of economic development achieved in recent years contains undoubted vulnerabilities. The Council believes that acceptance of the core elements of Ireland's economic strategy demands a recognition of the vulnerabilities listed in Section 1.3 above. Accepting the country's position as a regional economy, which must retain high-value economic activity, means that we have to focus on what is necessary to make that economy:

i. Competitive in a changing world;

ii. Environmentally sustainable;

iii. Efficient, through finding and implementing appropriate market and regulatory regimes in different areas; and

iv. Socially acceptable (see below).

These are major challenges that must be met if Ireland is to secure its long-run economic and social development.

3.4.2 The Vulnerabilities of Irish Social Development and Ireland's Long Run Social Challenge

In terms of Ireland's long-run social development, the Council's analysis and interpretation leads it to conclude that Ireland's small size, historical experience, institutional structures and type of economic development contain undoubted social vulnerabilities. These social vulnerabilities, listed in Section 2.4 above, arise from three general sources:

- **The legacy of the past and public policy**, that yields a society containing greater inequalities of opportunity and outcome than is desirable;
- **The economic context**, which requires competitiveness, high levels of employment and which can give rise to extensive growth (or decline);
- **The organisational challenge** of providing quality public services in an age when citizens' needs are varied, complex, and changing and in which the limits of bureaucratic delivery are acutely felt.

It is clear, therefore, that there is no comprehensive doctrine—of the market, the state, society or globalisation—that uniquely explains Ireland's current social situation and unambiguously guides action.

The understanding of Ireland's economy and society outlined above, and the identification of the social problems to which Ireland is vulnerable, helps us to identify the policy challenges that must be addressed if Ireland is to secure its long-term social and economic development:

- Recognising the legacy of the past, we must not only reduce inequalities of outcome, but systematically re-balance opportunity in favour of the least advantaged;

- Accepting our adoption of an internationalised economy and a social model based on high levels of employment, we must recognise that this combination can, in certain circumstances, tend to inequality and poverty, and we must have a major policy focus on addressing these problems;

- Accepting our adoption of an internationalised economy and a social model based on high levels of employment, we must recognise that this combination can tend to put pressure on the family and other social relationships. We have to identify the things we value and find ways to protect them;

- Accepting our adoption of an internationalised economy and a social model based on high levels of employment, we must recognise that this approach is only socially acceptable and economically sustainable if a few key aspects of personal and social well-being—housing, education, health services, transport, enough income to live with dignity and, nowadays, training and life-long learning—are secured for everybody;

- Recognising the limits of centralised or bureaucratic provision of complex services, we must examine the content, delivery, monitoring and evaluation of public policy and services. This recasting of public policy must include reconsideration of the roles of central departments, agencies, professionals, branch offices and citizens in setting goals, delivering services and monitoring performance. This is one reason why the Council sees organisational change as central to Ireland's current challenge and gives it considerable prominence in its proposed Strategy (see Sections 3.6.1 and 3.7.2, as well as Chapters 8, 9 and 10 below).

These are major social challenges that must be met if Ireland is to secure its long-run social and economic well-being.

3.5 SEEING IRELAND'S CURRENT SITUATION

A third aspect of vision is seeing Ireland's current situation clearly. This section applies the analysis of Ireland's vulnerabilities to the economic and social experience in the past two years and to its current context

3.5.1 Economic Vulnerabilities Materialised

The Council suggests that Ireland's current economic situation can be understood by noting that several of the vulnerabilities, listed above, have arrived together:

- A loss of competitiveness through:
  - Sharply increased non-wage costs;
  - Upward pressure on living costs and wage costs, in the context of slower productivity growth;
- The high-tech downturn in the US;
  - Exchange rate developments that no longer cushion any loss of cost-competitiveness;
  - Unresolved internal issues: particularly concerning land, housing, settlement;
- A sharp deterioration of the public finances, reflecting:
  - The economic slow-down; and
  - Pro-cyclical policy;
- Insufficient delivery in many public services;
  - Slow progress on other changes: such as Science/ Technology and life-long learning;
  - Expensive and slow progress on some key infrastructural developments;
- Growing pressure on the environment from several sources.

These problems define the immediate context in which the Council's *Strategy* is framed.

3.5.2 Social Vulnerabilities Materialised

The Council believes that our immediate social situation can be understood by noting that several of Ireland's vulnerabilities, discussed above, have materialised together over recent decades and in recent years:

- The major industrial shake-out in the 1980s created problems, the legacy of which are still present;
- Extensive growth of the national economy has had many positive social effects, but has also contributed to several social problems:
    - Increased land and house prices, that are influencing wage bargaining, increasing inequality, raising business costs, and increasing the cost of public infrastructure;
    - Pressure on the health services, which most adversely affect those reliant on the public system;
    - Pressure on the family through long commuting times and shortages of childcare;
    - Increased immigration, which has benefited the economy significantly, can nevertheless give rise to certain problems and pressures;
    - Social resources and capabilities, including those within the family, are now stretched in some areas;
    - Environmental problems, as evidenced in difficulties in waste management;
    - Rapid physical development which may lower the aesthetic quality of the built environment;
    - Centralised and rigid systems of social policy and social services which have proved unable to meet the needs of citizens, and this is felt most acutely by those most reliant on the public system;
- Public policies to combat exclusion and inequality have progressed significantly—through the formulation of strategies and allocation of resources—but now confront real challenges of implementation (see Chapter 8 below);

- Ireland has experienced a relatively large increase in earnings dispersion in a context in which the dispersion of earnings was already high by international standards;
- While Ireland continues to have a tax and welfare system that significantly reduces the degree of inequality in market incomes at any given time, and changes in the welfare system have contributed to a number of positive social developments, the overall balance of tax and welfare changes have been more favourable to those on higher incomes.

The materialisation of these vulnerabilities provides the agenda that must be addressed if Ireland is to achieve fair and sustainable social progress.

3.6 SEEING SHARED PRESSURES AND CONCERNS: COMPETITIVENESS, QUALITY OF LIFE AND FAIRNESS

In developing its new *Strategy* report, the Council identifies the principal influences and pressures on three main dimensions of economic and social life: competitiveness and organisational performance, quality of life and the fairness of opportunities and outcomes.

3.6.1 Influences and Pressures on Competitiveness and Organisational Performance

We now know that competitiveness and organisational performance are influenced by a wide range of indigenous, international and policy factors. In addition to the normal influences, a number of new pressures are now being experienced. These include: domestic economic management; transport access, commuting time, quality and costs; problems of labour supply (including the issues of childcare and immigration); wages and salaries; and staff capability and flexibility. Public policy and the action of the social partners must address the main pressures on competitiveness and organisational performance.

3.6.2 Influences and Pressures on the Quality of Life, Including Life at Work

Despite the economic and social advance of recent years, there are a number of influences and pressures on the quality of family and work life. These include: earned and other income sources; childcare, care of older people and people with disabilities; transport access, commuting time, quality and costs; housing access and costs; enterprise-level partnership; health services access and costs; the quality and price of services; the benefits and difficulties of immigration; environmental problems; and time constraints that make it difficult to balance work, family and community life.

These pressures, which affect different people in different ways, must be addressed if people are to feel that the economic breakthrough is worthwhile, and are to be willing to make the changes necessary to secure the foundations of long-term prosperity and a more equal and socially inclusive society.

3.6.3 Influences and Pressures on the Fairness of Opportunities and Outcomes

In addition to these pressures on competitiveness and the quality of life, there is a widespread sense that opportunities and outcomes are still not fairly available to all. Some of the influences and pressures on the fairness of opportunities and outcomes are as follows: earned and other income sources; health service inequalities; housing access, costs and location; education and learning inequalities; quality of work life; transport access, commuting time, quality and costs; the availability and price of services; childcare, care of older people and people with disabilities; the availability of recreational and cultural amenities; and the benefits and difficulties of immigration.

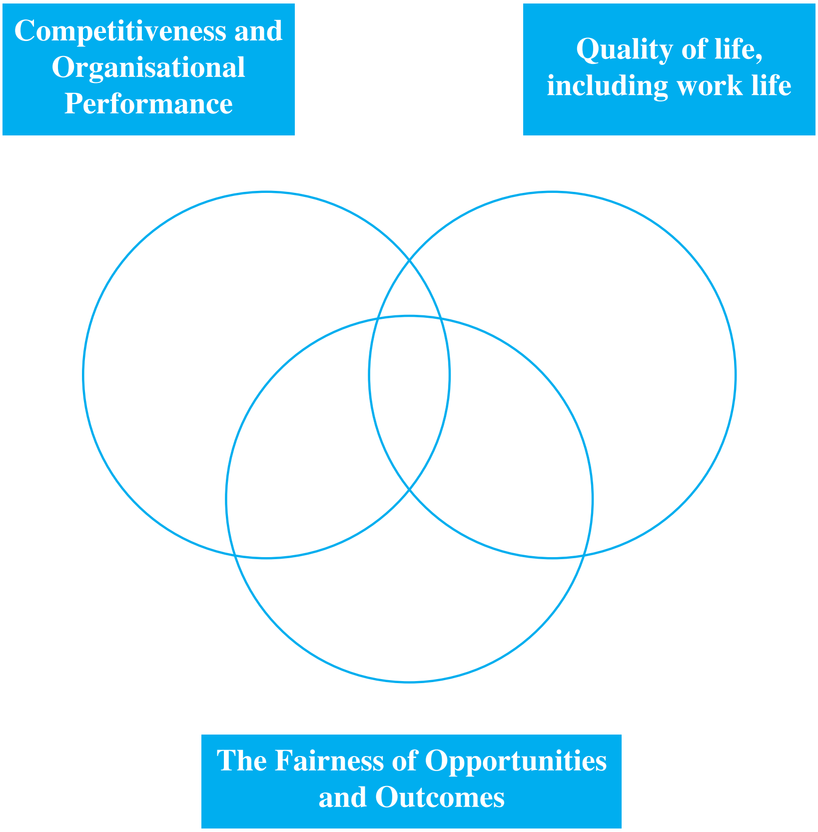
The Council's *Strategy* report reflects its belief that unfair opportunities and outcomes are damaging to social cohesion, competitiveness and the quality of life. The fairness of opportunities and outcomes should be one of the primary goals of public policy, the social partners and Irish society, and not a secondary objective.

3.6.4 Shared Influences and Pressures

Representing these influences and pressures graphically, it is clear that there is a significant overlap. Many of the pressures on competitiveness and organisational performance, quality of life and fairness are similar.

FIGURE 3.1

Influences and Pressures on Three Main Dimensions of Economic and Social Life



A partial view of any of these influences or issues can be damaging and even self-defeating. The Council believes that viewing the competitiveness, quality of life and fairness dimensions *together* allows us to enlarge our thinking and enhance the effectiveness of policy and behaviour, on the part of government and social partners alike.

3.7 DISCLOSING NEW POSSIBILITIES

The final aspect of vision is seeing new possibilities. These are more often disclosed through action and experimentation, than through analysis or ideological debate. The Council believes that new possibilities in four areas are particularly relevant:

- The emerging new centre in public administration;
- The emerging patterns in the workplace and organisation;
- The emerging Developmental Welfare State;
- A new kind of social partnership, that will be appropriate to a new kind of public administration, a new kind of workplace and new approaches to welfare and social service provision.

Each of these is briefly described below. The Council emphasises that it is here sketching future possibilities rather than recommending precise lines of policy.

3.7.1 The New Centre in Public Administration

Many of the macroeconomic, distributional and structural supply-side problems, identified throughout this report, pose major organisational challenges to government, public agencies, business, trade unions and the community and voluntary sector. In addressing these problems, we must take account of changes in the capabilities of government and the social partners, and new patterns of public management across the world.

In Ireland and elsewhere, the traditional administrative state delegated authority to civil servants and to interests in civil society, such as trade unions, employers' associations, and others. While this remains an important aspect of democratic governance, it was increasingly recognised that these forms of delegation were not always sufficiently accountable or co-ordinated. The complexity, volatility and diversity of economic and social problems, and of social groups, was seen to undermine the capacity of traditional post-war legislative and administrative systems.

In response, some countries adopted an approach known as New Public Management (NPM). Determination of policy was to be separated from its execution. The scope of departments, programmes and agencies was reduced, so that they could aim for defined outcomes, assessed against global performance measures. Despite some successes, this approach has not achieved the ‘straight line accountability’ it sought. Firstly, it has proved impossible to separate strategy from implementation, or more generally, conception from execution. Secondly, narrowing programmes in the interest of accountability had the unintended consequence of the making it more difficult to co-ordinate the narrower entities. This is evident in what are often called ‘cross-cutting’ or ‘wicked problems’, such as the improvement of education or the provision of treatment to drug abusers. In these and other problems, policy must draw on the local knowledge of service providers and service users *and* requires co-ordination of service provision across a wide range of agencies. Across the democratic world attention has now turned to finding better ways to address these problems.

For a variety of reasons, Ireland has not adopted the New Public Management approach. This puts a greater onus on us to show that our alternative approach—based on partnership and the Strategic Management Initiative (SMI)—can do better in addressing cross-cutting problems. The Council believes that in working out how Ireland is to achieve a complex set of productivity improvements, infrastructures and public services, consideration should be given to the best organisational arrangements that are now emerging in public administration in many countries.

Among the most promising new arrangements, are those in which local actors are given freedom to set goals for improvement and are given the means to achieve them. In return, they must propose measures for assessing their progress and provide rich information on their own performance. The centre pools the information and ranks performance by reference to periodically revised measures. This approach increases local innovation, and makes the local transparent. The centre retains the right to sanction those who continually fail. But it does so to complement, not undermine, local autonomy. There are a number of instances of this new approach in Ireland in recent years.

Some consideration of these possibilities is necessary if Ireland is to achieve the services that are urgently necessary for competitiveness, well-being and social inclusion. On international and Irish experience, it seems impossible for a centralised government system, on its own, to achieve a complex set of supply-side infrastructures and services. But, equally, an adequate shared understanding and policy approach to these problems cannot be achieved by high-level analysis and negotiation among the social partners.

The Council believes that an important dilemma facing public policy and partnership derives from the fact that neither government, of the traditional kind, nor social partnership, as it currently exists, are capable of meeting the key challenges. Many of these policies can only be agreed, analysed and changed in the context of doing them. Indeed, where successful experimental approaches have emerged (in Ireland and elsewhere) it is the local units that do the problem solving. Consequently, the achievement of continuous improvement, in supply-side infrastructures and services poses major organisational challenges to government, public agencies, business, trade unions and the community and voluntary sector.

3.7.2 Emerging Possibilities in the Workplace and Organisation

A second new possibility that can be discerned is the workplace of the future. A growing consensus exists in relation to the Irish competitive and social vision. This consensus centres on ambitious aspirations to build up and develop a highly skilled, adaptable and flexible labour force capable of sustaining international competitiveness and public sector modernisation.

According to Forfás, our future success will be fundamentally dependant on our ability to achieve an environment where research and knowledge, high level skills and expertise, high quality infrastructure and business services are combined in a flexible and creative way.

Equally, the provision of modern public services capable of responding effectively and efficiently with integrated solutions to people's changing needs requires a commitment to organisational change and co-operative working relationships.

Achievement of these ambitious aspirations requires a recognition that people's working lives are also undergoing major change, as are their preferences with respect to when, how and even where, they wish to seek employment and undertake work. Work-life balance as a concern has been driven by cultural change, by the rising female participation rate and its effects on gender relations in the home, by care responsibilities, by increasing travel times to work, and by changes in patterns of production and service delivery that involve the dissolution of conventional boundaries between leisure and work periods. Also, surveys have revealed a growing interest among employees in greater participation, involvement and partnership in the workplace.

There is evidence in both the private and public sector, that, in response to the pressures for change in patterns of employment and work systems driven by these trends, organisations are willing to radically re-think critical aspects of organisation, control and management, with significant beneficial consequences for both the organisations and the individuals involved.

Improving the knowledge-creating capacity of the workplace, the effective handling of problems and the achievement of continuous improvement are now at the heart of work organisation in many areas. To capture the benefits of co-operation, flexibility and learning, organisations are moving away from hierarchical structures and are focusing partnership on issues relating to higher organisational performance, sustaining competitive advantage, modernising public services and promoting co-operative working relationships and arrangements that are flexible and responsive to employees' changing needs.

The implications of these changes for the labour market, organisational adaptiveness, human resources and industrial relations in short, for the workplace are understood to be demanding and some of these have been sketched out in very broad and general terms by institutions such as the National Centre for Partnership and Performance, Forfás and the Labour Relations Commission, as well as in programmes such as the Strategic Management Initiative.

However, as pointed out by Roche in his review of the workplace of the future for the NCPP, there has been relatively little systematic focus on preconditions in the workplace for the type of competitive advantage and forms of public service delivery Ireland seeks to pursue, and no systematic attention has been devoted in business, trade unions or the policy community to the changes in practices, polices and institutions required to align the labour market and world of work to the competitive and social vision to which Ireland stands committed (NCPP, 2001).

Our capacity to understand trends driven by new competitive pressures and new employment preferences has been limited by the quality of information, data and analysis hitherto available. There is growing recognition that an effective policy response to the changing workplace will be predicated on a qualitative change in the nature of deliberation and analysis in this area. The Council notes and welcomes, the commitment in the Programme for Government to "request the National Centre for Partnership and Performance to establish a Forum on the Workplace of the Future to help establish a comprehensive agenda on this issue". A critical issue for the Forum will be how best to align workplace and organisational development with Ireland's competitive and social vision, as well as with the preference and needs of employees.

The Council believes that the establishment of a Forum on the Workplace of the Future offers the opportunity to generate and disseminate knowledge of workplace change and modernisation, to foster in-depth discussion in this area and to undertake, in the field of employment, work and organisational change, the kind of fundamental review already undertaken by the Council and other bodies in areas of industrial policy, education, European integration, taxation and social policy.

3.7.3 From a Differentiated to a Developmental Welfare State

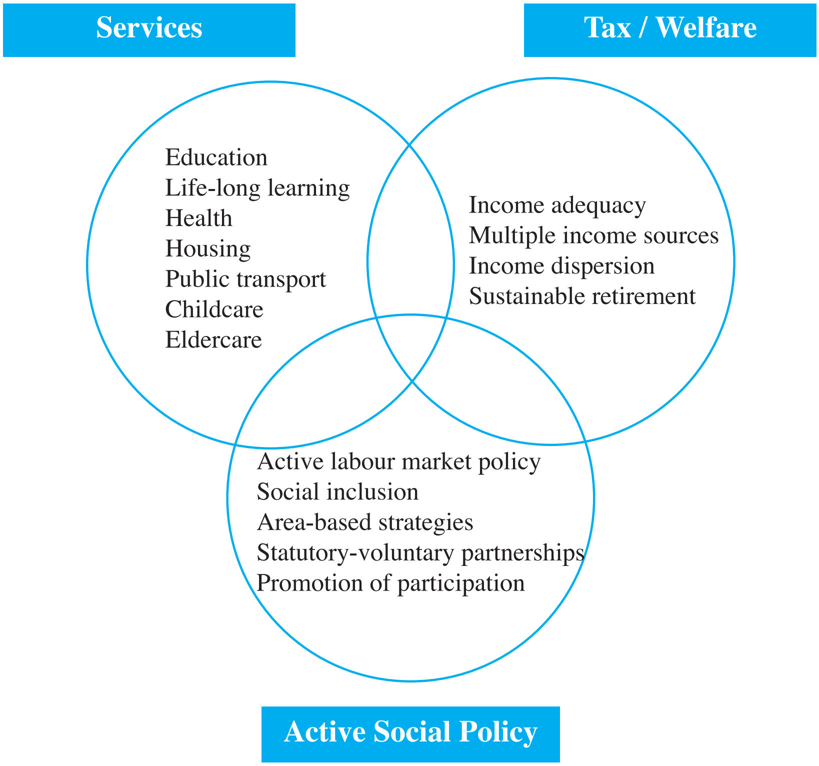
A third emerging possibility is a new kind of welfare state, more suited to the economic, social and technological realities of the 21st century. A key challenge for Ireland is to devise a welfare system that not only addresses social risks and needs more adequately, but also connects more fully with the Flexible Developmental State (FDS) described in Chapter 1, hence the term Developmental Welfare State. To sketch the possible shape of a Developmental Welfare State, we outline some key characteristics of the existing system and ways in which they might be modified

The evolution of the Irish welfare state is discussed in Chapter 2 above. As noted there, Ireland's system of income protection contains a mix of universal, insurance-based and residual payments. Consequently, it can be termed 'differentiated' (Mishra, 1990). Because it evolved in response to the claims of different 'constituencies', it can also be termed the 'Clientelist Welfare State' (Peillon, 2001). Some aspects of the development of the Differentiated Welfare State in Ireland help us to anticipate the main outlines of its possible successor:

- Means-tested social assistance of long duration for people of working age coped with the fact that the economy did not employ a significant proportion of the population;
- With a chronic shortage of employment, membership of the labour force (and associated entitlements) were narrowly defined;
- A dualism developed between those with a relatively firm attachment to the paid workforce (supported by insurance-based payments and tax expenditures) and those with a tenuous link (supported by means-tested payments and services);
- The social welfare sphere took over where the economic sphere left off; it dealt with the failures of the economic model, the damage it had wrought, or simply with where it had been unable to reach.

- There was high support for the welfare state partly because a high proportion of the population were beneficiaries, albeit in quite distinct ways.
- The assumption of a principal breadwinner underpinned the structure of payments;
- The state was central in administering social policy programmes and there was limited involvement of local authorities.
- While the voluntary and community sector was relied on, the contractual arrangements with it were unsatisfactory in numerous ways (Peillon, 2001).

FIGURE 3.2
The Developmental Welfare State



The conceptualisation of the welfare state outlined here and in Chapter 2 can be used to sketch what a Developmental Welfare

State might look like (see Figure 3.2). A first circle groups services that would become available to all members of society. The state would be involved in ensuring that services were provided by Government or others. A second circle encompasses the redistributive activity of taxation (including tax expenditures) and *all* social transfers. Cross-cutting challenges that require an *integrated* response would be here; for example, an effective floor to incomes, 'making work pay', more freedom to interrupt employment for caring or educational purposes, restraining income inequalities, and meeting the income challenge of population ageing. The third circle represents active social policy: active labour market policies, social inclusion policy, strategies for urban regeneration and rural development, and more formal involvement of voluntary and community organisations in shaping policies, delivering services and monitoring outcomes.

The Developmental Welfare State (DWS) would regard itself as neither contesting nor compensating for the functioning of a competitive, knowledge-based regional economy, but as an integral part of it. It would adapt to changes in family patterns, demography and social values. It might also be termed the 'Integrated Welfare State' because of its characteristic emphasis on achieving integration across programmes and between the economic and the social spheres (Mishra, 1990; Peillon, 2001). It would differ in the following ways from the traditional welfare state:

- Social protection would have *direct economic functions*, promoting growth, countering inflation, enhancing productivity, strengthening social cohesion;
- With no significant reserves of untapped workers, the DWS would target *high employment rates* and *life long learning*;
- It would facilitate movement in and out of the workforce;
- The assumption of a 'family breadwinner' would give way to a recognition of new family structures and participation patterns;
- Deliberation and improvement would take place at different levels, with central agencies retaining a key monitoring role;

- There would be greater involvement of local government in ensuring the delivery of quality services (e.g., childcare, social inclusion);
- There would be greater diversity of service provider—public, semi-public, private, non-profit, trade union and community and voluntary sector—and a more integrated system of planning and monitoring;
- Statutory-voluntary relations would be more formal and integrated, with state agencies having a greater say in the standard of the services to be provided, and in monitoring outcomes; and
- There would be an evolved system of governance that balances the interdependence and autonomy of the various stakeholders.

The Developmental Welfare State in advanced countries is likely to address a similar set of tasks concerning:

- The *quality of childhood*, to raise the productivity of the future labour force and stem the intergenerational perpetuation of social disadvantage;
- A *female-inspired transformation of employment* as work-life is recast to enable women and men balance home responsibilities and employment;
- The *quality of employment* would replace the reduction of unemployment as a target for improving individual and social well-being;
- The maintenance of *'one nation'* in retirement.

The Council sees such a Development Welfare State as an interesting new possibility that might evolve from the changes already taking place in Ireland's system. The changes outlined above provide a sketch of a new possibility, rather than a list of recommendations that the Council has agreed. Whatever model of welfare emerges, the Council believes that the strengthening of services (the first circle in Figure 3.2) is crucial at this stage in Ireland's development:(a) to provide greater security to the increasing proportion of the population in employment and enable them to enjoy a higher level of well-being for any given level of disposable income, and (b) to lessen the dualism between the population relying on insurance-based/ tax-subvented supports and those relying on means-tested ones.

3.7.4 A New Approach to Social Partnership

The Council believes that social partnership has made a significant contribution to Ireland's economic and social development. It has done this by identifying and addressing important tasks facing Irish society.

In previous *Strategy* reports the Council has offered the following characterisation of partnership, as it has developed since 1987:

(i) The partnership process involves a combination of *consultation, negotiation and bargaining*;

(ii) The partnership process is heavily dependent on a *shared understanding* of the key mechanisms and relationships in any given policy area;

(iii) The *Government* has a unique role in the partnership process. It provides the arena within which the process operates. It shares some of its authority with social partners. In some parts of the wider policy process, it actively supports formation of interest organisations;

(iv) The process reflects *inter-dependence* between the partners. The partnership is necessary because no party can achieve its goals without a significant degree of support from others;

(v) Partnership is characterised by a *problem-solving* approach designed to produce consensus, in which various interest groups address joint problems;

(vi) Partnership involves *trade-offs* both between and within interest groups;

(vii) The partnership process involves *different participants* on various agenda items, ranging from national macroeconomic policy to local development (NESC 1996a: 266).

This list can be seen as both a *description* of the partnership process as it is, and a set of *conditions* for effective participation in the process.

A distinction can be made between two different conceptions, or dimensions, of partnership:

- Functional interdependence, bargaining and deal making; and
- Solidarity, inclusiveness and participation.

Effective partnership involves both of these, but cannot be based entirely on either. While these two dimensions are both present, even together they are not adequate.

There is a third dimension of partnership, which transcends the two discussed above. Partnership involves the players in a process of deliberation that has the potential to shape and reshape their understanding, identity and preferences. This idea, that identity can be shaped in interaction, is important. It is implicit in the description of the process as "dependent on a shared understanding", and "characterised by a problem-solving approach designed to produce consensus" (NESC, 1996b: 266). This third dimension has to be added to the hard-headed notion of bargaining, (and to the idea of solidarity), to adequately capture the process.

Partnership can only retain its relevance if it continues to identify and tackle the substantive problems confronting the economy and society. Partnership can work only if its structures and methods are in tune with underlying trends in technology, society and organisation.

The Council believes that the vision and analysis set out in this report provides guidance on how partnership might be re-vitalised and recast:

i. Given the shared analysis of Ireland's development and vulnerabilities, partnership must be structured to address the most pressing vulnerabilities and problems while attending to long-term development;

ii. Given the analysis of how past progress was achieved—

without rigid models and revising both means and goals—partnership must remain flexible; and

iii. Given past experience that successful new approaches are more often discovered by experimental action than by analysis or ideological debate, partnership must focus on concrete projects, joint action and deliberation based on experience.

The analysis of the existing and possible emerging institutional elements of Ireland's economy and society also has implications for partnership. The important existing elements and new possibilities sketched above are:

i. The flexible developmental state;

ii. New approaches to public administration, services and accountability;

iii. The developmental welfare state;

iv. The emerging workplace of the future.

Partnership must facilitate the emergence of new possibilities, such as those listed above. Whatever form the new arrangements take, a critical task for Ireland, if the economic and social policy are to be more complementary, is to connect economic development, public sector modernisation and welfare more closely with one another. Partnership can assist or hinder this.

These are the contexts in which the partnership procedures must be reviewed. In many respects, the 'Frameworks' in the Programme for Prosperity and Fairness (PPF) embodied the kind of flexibility that is suggested by the analysis reported above. Yet they have not been entirely satisfactory. In developing partnership, clarity should be sought on:

- Issues that can be decentralised and do not need to be on the agenda of national partnership;
- Issues that are national, but could be addressed more effectively if there were more focus on implementation;

- Issues that require to be in the social partnership process at national level, which might be either:
  - national-level policies, such as taxation;
  - local or sectoral issues, but where the national-level social partners can contribute collectively and individually;

The Council is not in a position to identify what problems fall into each of these categories.

In exploring these possibilities for the future of partnership, it is clear that the partnership agenda now overlaps with three other agendas:

- The Strategic Management Initiative and modernisation programme in the public service;
- The need for further reform of local government, further devolution and clarification of the relation between local government and local partnership; and
- The NESF's programme of work on social capital, the commitment in the Programme for Government to 'promote social capital in all parts of Irish life through research' and the identification of social capital, particularly for disadvantaged communities, as a 'key objective' of the NAPS (2002:8).

The Council believes that these possibilities for partnership, and synergies with other programmes, must be actively explored.

Part III

Strategy

CHAPTER 4

RECASTING IRELAND'S CONSISTENT POLICY FRAMEWORK FOR THE COMING YEARS

In this Chapter, the Council outlines the consistent policy framework that has informed its *Strategy* reports since 1990, and recasts that framework for the years ahead. This involves agreement on the parameters of macroeconomic policy, distributional arrangements and structural or supply-side measures. This Chapter outlines how the Council now approaches the task of putting policies in the three 'boxes' of a consistent policy framework: macroeconomic, distributional and structural.

4.1 THE COUNCIL'S CONSISTENT POLICY FRAMEWORK 1987 TO 2002

In its previous *Strategy* reports (1986, 1990, 1993, 1996a and 1999), the Council set out a framework that informed its contribution to social partnership and policy. It argued that there are three requirements for a consistent policy framework in a small, open, European democracy:

(i) Macroeconomic: the economy must have a macroeconomic policy approach that underpins low inflation and steady growth of aggregate output;

(ii) Distributional: there must be an evolution of incomes which ensures continued improvement in competitiveness, which handles distributional conflict in a way which does not disrupt the functioning of the economy and which is fair; and

(iii) Structural: there must be a set of complementary policies which facilitate and promote structural change in order to maintain competitiveness, eliminate barriers to participation and achieve social cohesion in an ever-changing environment.

The manner in which a consistent and effective overall approach is developed varies considerably across countries. Consideration of how various countries with different structures and political traditions operate economic and social policy suggest that the system must be internally consistent, and must be suitable for the economy and society to which it is applied.

Through the 1990s, the first (macroeconomic) of these requirements was met by adherence to the ERM and transition to EMU. The Council argued that the second (distributional) of these requirements is best met by a negotiated determination of incomes and that, to be really effective, such a negotiated approach must encompass not only the evolution of pay, but also taxation, the public finances, exchange rate and monetary policy and the main areas of public provision and social welfare. In pursuit of the third (structural) requirement, the Council and others advocated a major programme of structural reform. The Council argued that such reforms are best achieved with the active consent and participation of those who work in public agencies and with the participation of affected citizens and groups.

The analytical framework was further developed in the 1996 *Strategy* report. In the context of globalisation, the Council argued that:

(i) Most of the policies which affect Ireland's prosperity and social cohesion are *supply-side* policies—i.e. those that improve quality, quantity and allocation of resources and capabilities;

(ii) Given rapid economic change, national policies must produce *flexibility*; and

(iii) Successful national supply-side policies, directed towards innovation, competitiveness and inclusion, depend on the high level social cohesion and co-operation that the state can both call upon and develop.

This suggested that once a consensus on macroeconomic policy is in place—and if it is reflected in government policy, wage bargaining and management—the main focus of policy analysis and development should be the supply-side measures that influence competitive advantage, social cohesion and societal well-being, and the institutional arrangements which encourage discovery and implementation of such measures.

4.2 RECASTING IRELAND'S CONSISTENT POLICY FRAMEWORK FOR 2003-2005

The Council believes that the consistent policy framework outlined above still provides a useful guide to the formulation of a strategic approach that can command the agreement of the social partners. However, in view of the new challenges noted above, the changing domestic and international environment and the evolution of policy, it is now necessary to describe Ireland's consistent policy framework in new terms. This requires, firstly, that we analyse and understand Ireland's experience in the past decade and a half—as has been done in Chapters 1 and 2 above. Secondly, it requires that we review and recast the relationship between the macroeconomic policy, distribution and structural or supply-side measures. Thirdly, it requires that we review and revise the content of policy within each of the three boxes (macroeconomic, distributional and structural).

4.2.1 The Changing Relationship between Macroeconomic, Distributional and Structural Issues

The relationship between the three categories of policy has changed over time. In the difficult economic period from the late 1970s to the late 1980s, the three existed in a vicious circle: the failure to adequately adjust the structure of the economy to international competition (combined, for some of the period, with adoption of a short-term orientation in public policy), created a fiscal crisis and rising taxation which, in turn, created distributional pressure in which both profitability and real take home pay were eroded.

During much of the period from 1987 to 2000, the three existed in a virtuous circle: the macroeconomic, distributional and structural developments readily supported and reinforced one another. The rapid 'growth of the cake', reduced the salience of distributional issues and itself produced a significant amount of structural change.

However, the long period of rapid growth brought the three elements into greater tension with one another, as structural and supply-side bottlenecks and problems in service delivery impacted on inflation, the public finances, wage bargaining and the value of fixed incomes. At the same time, macroeconomic developments, particularly the weakness of the euro and pro-cyclical policy, impacted on distribution, competitiveness and supply-side bottlenecks. This highlighted how critical structural and supply-side changes are if a consistent macroeconomic and distributional approach is to be maintained.

While the slowing of economic growth in the past year and a half might be thought to reduce tension between the three, since it relieves some of the most acute bottlenecks, this is a limited and temporary effect. In fact, the slowing of growth has added another strand to the tension between the three elements of policy. The shortfall of revenue has increased the difficulty of maintaining the public investment programme and improving public services. In a context of continued high inflation, this puts pressure on wage bargaining. Independently, the slowing of output and earnings growth means that attention tends to shift from 'growing the cake' to 'dividing the cake'. Distributional issues—over pay, prices, housing, service availability, rent earning, taxation and profits—become more salient (as is discussed further in Chapter 6).

These developments increase the importance of a consistent approach, yet make it more difficult to achieve. This is one way of characterising the challenge that government and the social partners now face. The difficulty makes it tempting to achieve a minimal consistency between macroeconomic and distributional approaches. Maybe structural and supply-side improvements are too hard to agree, to dear or too difficult. Maybe they can wait. The Council rejects this approach. A minimal consistency between macroeconomic and distributional approaches will not work:

- It will not work because social exclusion cannot be further reduced if the quality of services is not greatly improved (see Chapter 8 below);

- It will not work, because competitiveness cannot be sustained for long if infrastructure, R&D, utilities and a skilled flexible workforce are not available;
- It will not work for long as a distributional settlement because wage earners will continue to face high prices, poor services, expensive housing and long commuting times;
- In consequence of these three, it will not work as a public finance strategy, because government will be under short-term pressure from all sides and will not have up-graded the productive potential of the economy or the public service by appropriate supply-side measures, thus weakening its long-term budgetary position; and
- It will not work as social partnership, since it would not be social partnership, merely an old-style tri-partite deal of the sort that failed through much of the 1960s and 1970s. Partnership involves not only consensus, but also recognition of necessary change.

Consequently, a consistent policy approach must include a vigorous programme to improve structural and supply-side factors.

4.2.2 Redefining the Content of Macroeconomic, Distributional and Structural Approaches

The Council's proposals on macroeconomic policy are outlined in Chapter 5 below. The two key problems addressed there are inflation and the public finances.

The distributional issues addressed in the *Strategy* are:

- Wage bargaining;
- Poverty, exclusion, inequality and welfare; and
- The broad parameters of social provision, especially on health.

The Council's views on wage bargaining are outlined in Chapter 6 below.

The Council's proposals on poverty, inequality and exclusion are summarised in Chapter 8 below. It argues that Ireland's social welfare state needs to adopt a more developmental form than hitherto. Individuals and groups need more active supports as they seek to maximise the potential and minimise the dangers that attend major changes in employment, family patterns and demographic trends.

The social partners have a historic opportunity to now guide the evolution of Ireland's social assistance and social insurance systems to align and converge into a truly Developmental Welfare State that secures social inclusion while respecting economic exigencies.

The Council believes that structural/supply-side issues are now of central importance. The structural, supply-side and organisational challenges fall into three broad groups:

- Major national investments—in transport, childcare, information and communications technology and networks, energy, R&D and physical planning;
- The provision of services and regulatory regimes to citizens, enterprises and to voluntary groups; and
- The creation of flexible learning organisations that achieve continuous improvement, equality of opportunity and fair outcomes.

Given the wide range of urgent structural/supply-side needs, in Chapter 9 the Council identifies the common elements that arise in all of them. Its work suggests that there are three common elements:

- The need to ensure scope for the necessary investment to take place in these areas, while respecting the Council's budgetary strategy;
- The need to ensure a high quality or standard of service and value-for-money in infrastructure, public services and regulation and to make effective use of existing infrastructure; and

- The need to make the organisational and institutional changes necessary to achieve co-ordination of a range of cross-cutting policies and organisations.

This analysis is not presented as an alternative to the existing modernisation and devolution processes in the public system. We must explore how new ways of combining strategic direction, local innovation, transparency and accountability can be developed from the very significant change already underway in the public system, and how that can be built upon through a partnership process that delivers continuous adaptation and improvement in service delivery.

The Council sees three sets of related organisational and institutional challenges: in utilities and networked sectors, planning and infrastructure and services.

FIGURE 4.1
Three Sets of Institutional Challenges

Utilities and Networked Sectors	Planning and Infrastructure	Services
• Electricity; • Telecommunications; • Gas; • Parts of transport; • Waste management.	• Spatial strategy; • Infrastructure; • Local planning; • Local partnership; • Local development.	• Transport; • Health; • Life-long learning; • Housing; • Welfare; • Care services.

Exploration of the best arrangements in each of these areas is a central task for Government and the social partners. Willingness to adopt the best arrangements is the central test of social partnership.

At the same time, there is little point in an agreed long-term vision and strategy if the immediate reality is not addressed in a consistent way—consistent in three senses: internally consistent policies, co-ordinated action by all partners and policy that is consistent with long-term economic and social development. The current problems should be seen, and addressed, as instances of the enduring vulnerabilities identified in Chapters 1 and 2.

4.3 SHARED UNDERSTANDING AND A CONSISTENT APPROACH

The Council's work on a new *Strategy* report is driven by the conviction that there are huge advantages in a shared understanding of key economic and social mechanisms and a consistent approach across macroeconomic, distributional and structural policies. Without agreement on national priorities, each sector of the economy, and of society is likely to pursue its separate aims in the years ahead in ways that, taken together, would overload Ireland's economic performance.

Something of this kind occurred during previous periods of Irish economic strength, to everybody's eventual cost. In this regard, in its 1996 report, *A Strategy into the 21st Century*, the Council pointed out that:

> Although the Irish economy achieved significant economic growth, adjustment, modernisation and inward investment since 1960, these successes are qualified in important ways. Growth was not handled well. Awareness of the international environment was incomplete. The adjustment of indigenous enterprises to international competition failed more often than it succeeded. Job creation was insufficient, at times old jobs were lost at a remarkable rate and unemployment increased. High levels of savings and corporate profits were not matched by investment in the Irish economy. Inevitable adversities were allowed to become divisive and produced delayed and insufficient responses. Overall, there was an insufficient appreciation of the interdependence in the economy—between the public and the private sectors, between the indigenous economy and the international economy, and between the economic and the political (NESC, 1996a: 4).

This interdependence takes new forms in Ireland's current economic and social situation. Current pressures—to improve public services, undertake capital investment to address infrastructural deficiencies, achieve continuous improvement through partnership, maintain fiscal balance, devise effective reward systems, enhance competitiveness, eliminate poverty and reduce inequality in a context of high employment and provide for long term environmental sustainability—must be addressed in a consistent manner. The Council emphasises the importance of an integrated approach across key policy strategies (including the National Development Plan, the *National Anti-Poverty Strategy*, the *National Health Strategy*, the *Sustainable Development Strategy*, the *National Climate Change Strategy*, and the *National Spatial Strategy)*.

The Council wants to emphasise the inter-dependence between the economy and public policy, to which it also drew attention in 1996. In its 1996 *Strategy* report it said:

> Failures since 1960 seem to have arisen when sight was lost of a third inter-dependence: that between the economic and the political. By this is meant the idea that inconsistent claims on national output, and damaging actions, can arise from either economic actors or policy-makers, or from the interaction between them. The areas of taxation policy and exchange rate policy illustrate this graphically. Success requires that both economic actors and policy-makers adopt a strategic, long-term, and mutually consistent approach. Opportunist behaviour in either sphere can damage economic performance directly. In addition, short-term or narrow action in one sphere tends to prompt similar responses in the other. A key requirement of national strategy is to adopt an approach which ensures a long-term orientation of both public policy and private economic actors, and which achieves consistency between the two. Later sections of this report identify how this requirement can best be met (NESC, 1996a: 26).

Current developments illustrate that this observation has a renewed relevance.

In this *Strategy* report, the Council hopes to contribute to a new consensus on well-being, investment, services and competitiveness. The emphasis must be on generating returns for families, communities, workers and enterprises. Rather than focus on partnership itself, the Council emphasises that:

- With or without partnership agreement on the current model, Ireland has to devise a wage and reward system which is suitable for its type of economy and which achieves its social goals;
- Regardless of pay arrangements, public policy has to address a wide range of supply-side and distributional issues in a coherent way; and
- Whether pay is centralised or local, organisations in both the private and public sector have to enhance productivity and performance.

Consequently, the Council focuses its report on the substantive tasks outlined above, and particularly on ways in which their interaction can provide the basis of a coherent national strategy.

CHAPTER 5

MACROECONOMIC POLICY

5.1 INTRODUCTION

A small open economy requires a consistent set of macroeconomic, distributional and structural policies. This chapter outlines the Council's approach to macroeconomic policy. Section 5.2 reviews developments in the public finances and considers in broad terms the possible evolution of the public finances in the coming years. A central aim of macroeconomic and distributional policy is to achieve low inflation. Section 5.3 examines the factors behind the emergence of higher inflation in Ireland in recent years and policy options to secure low inflation. Finally, the Council's policy recommendations are presented in Section 5.4.

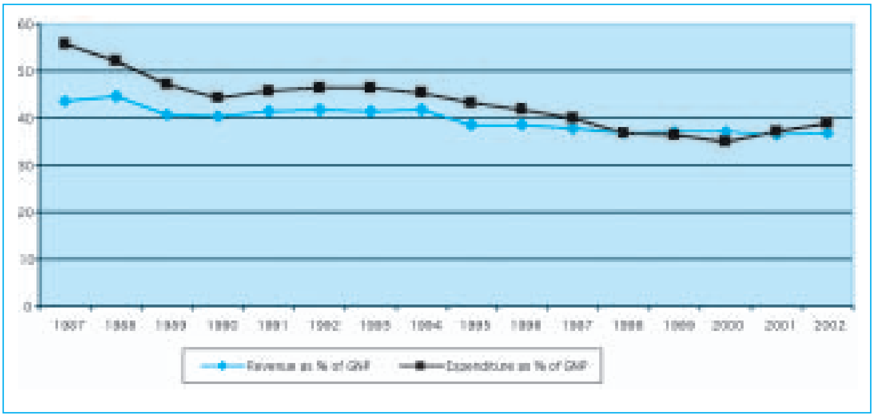
5.2 THE PUBLIC FINANCES

5.2.1 Public Finance Trends

The first half of the 1980s was a very difficult period for the public finances. Exchequer borrowing averaged close to 14 per cent of GNP and annual debt service costs were around 10 per cent of national income. To correct the imbalances in the public finances, the share of public expenditure in GNP was reduced. This share fell sharply by approximately eight percentage points from an underlying 54 per cent of GNP in 1987 (compared to 47 per cent of GDP for the EU average) to 47.2 per cent in 1989. The public expenditure share (gross current and Exchequer capital expenditure) of GNP increased modestly in the mid-1990s and has fallen since 1993. After several years of decline this share increased in 2001 and 2002; the 2002 share was close to 39 per cent of GNP (with declining debt service contributing about nine percentage points of the fifteen percentage point decline). The share of total current revenue in GNP has been more stable. After rising from 39 per cent of GNP in 1980 to 43 per cent in 1987, the share fell by about two percentage points in the late 1980s. It has fallen slowly in the 1990s, from just over 40.4 per cent in 1990 to around 37 per cent in 2002. Current revenue consists of tax revenue, PRSI and levies, non-tax revenue accruing to the Exchequer (including the surplus of the Central Bank, the National Lottery surplus, and dividends from State companies) and miscellaneous receipts of Government Departments known as appropriations-in-aid (current EU receipts are included as appropriations-in-aid). If one focuses specifically on tax revenue, this has shown even greater stability during the 1990s. The share of taxation in GNP in 2000 was 30.8 per cent, compared to tax revenue excluding motor vehicles duty (now given to local authorities) of 30.6 per cent in 1990. There was, however, a significant fall in the tax share in GNP in the past two years with a decline to an estimated 28.2 per cent in 2002. Factors influencing the tax share in GNP are discussed further below.

FIGURE 5.1

Total Government Expenditure as a Percentage of GNP, 1987-2002



Source: Department of Finance. The 2002 figures are outturn estimates from *Budget 2003*.

Government Balance and Debt

After falling sharply in the 1987 to 1989 period, the deficit[1] was stable for the first half of the 1990s. From 1995 it began falling and

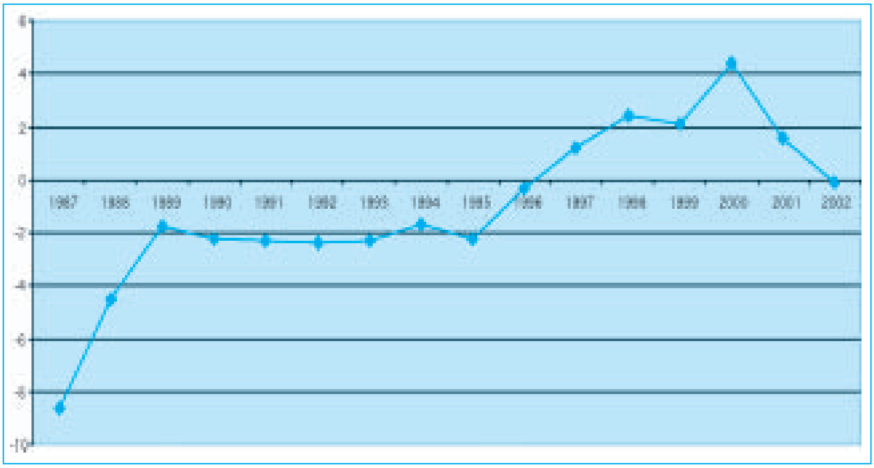
1. In discussing the deficit in this paragraph, the focus is on the EU definition of the General Government Balance (GGB) as a percentage of GDP.

moved into a surplus by 1997. The surplus continued growing and reached a peak of 4.4 per cent of GDP by 2000. The movement from a deficit of 2.2 per cent of GDP in 1995 to a surplus of 4.4 per cent in 2000 reflected the fact that there was a substantial decline in the expenditure share of GNP while the revenue share was fairly stable. Growth was very buoyant in this period so the decline in expenditure share co-existed with substantial expenditure growth. Since 2000 the surplus fell sharply, and there was a marginal deficit in 2002 of 0.1 per cent of GDP.

The national debt has fallen consistently from its peak level of 125 per cent of GNP in 1987 to an estimated 37.4 per cent of GNP in 2001.

FIGURE 5.2

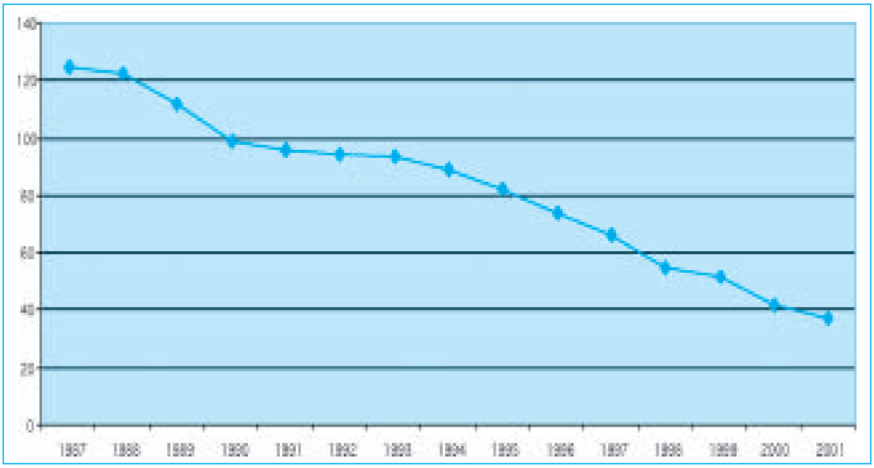
General Government Balance as a Percentage of GDP, 1987-2002



Source: Department of Finance.

FIGURE 5.3

National Debt as a Percentage of GNP, 1987-2002



Source: Department of Finance.

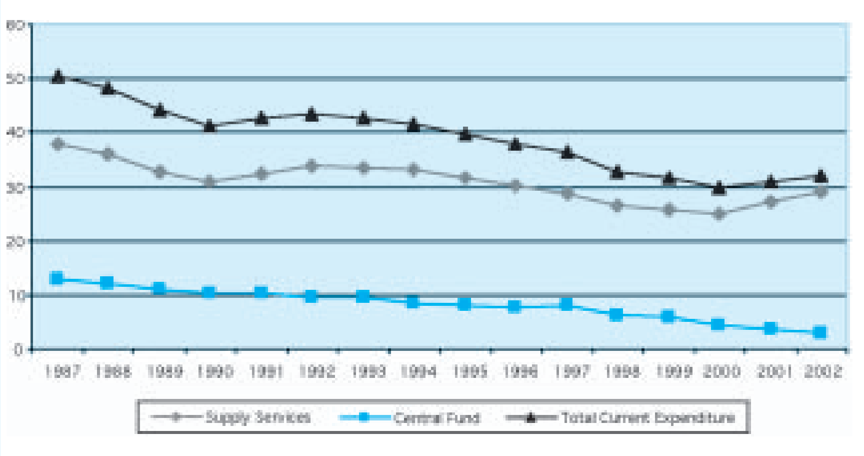
Current Expenditure

The budgetary data on current expenditure are divided into Central Fund expenditure (mainly debt service and EU budget contributions) and supply services (expenditure on services and benefits). The trend in these two elements of current expenditure as a percentage of GNP is shown in Figure 5.4. Central Fund expenditure as a percentage of GNP has fallen consistently from close to 13 per cent in 1987 to 2.8 per cent in 2002. Following the decline of the late 1980s, supply services expenditure as a percentage of GNP increased in early 1990s. It then fell from just over 33 per cent in 1994 to 25.2 per cent in 2000. It increased in the following two years to 29.2 per cent of GNP in 2002[2].

2. Supply services expenditure data quoted includes expenditure from the Social Insurance Fund (SIF).

FIGURE 5.4

Total Current, Central Fund and Supply Services Expenditure as a Percentage of GNP, 1987-2002

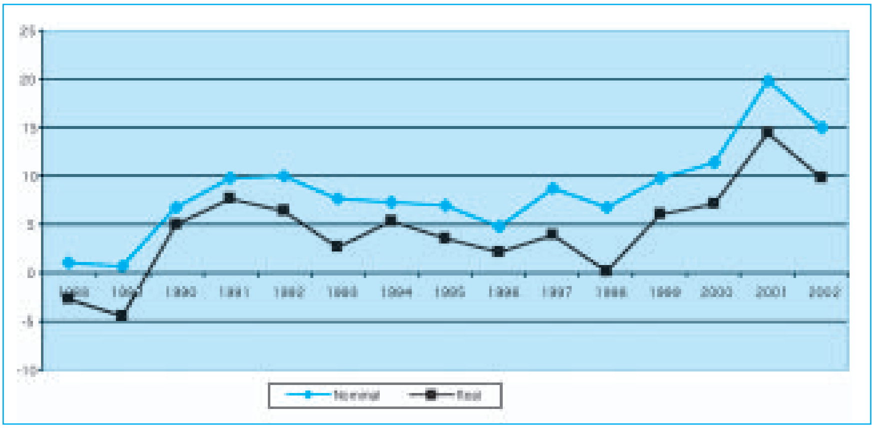


Source: Department of Finance. The 2002 figures are from *Budget 2003*.

While declining relative to GNP for much of the 1990s, supply services expenditure has grown in real terms throughout the 1990s. The growth has been particularly high in the most recent years. The average annual rate of growth of current expenditure between 1989 and 2001 was 9.1 per cent in nominal terms and 5.3 per cent in real terms. Growth rates have been particularly high in more recent years. The annual average increase between 1999 and 2001 was 15.5 per cent in nominal terms and 10.3 per cent in real terms. The increase in 2002 was approximately 15 per cent in nominal terms and close to 10 per cent in real terms.

FIGURE 5.5

Annual Percentage Change in Gross Supply Services Expenditure 1987-2002



Source: Calculated from Department of Finance expenditure data, using the GNP deflator. The 2002 figures are from the *2003 Estimates for the Public Services (Abridged Version)*, Dublin: Stationery Office. The 2002 deflator is from the *Quarterly Economic Quarterly*, Winter 2002, Dublin: ESRI.

The growth of supply services expenditure by function is shown in Table 5.1 below. It is worth noting that health, education and social welfare together comprise over 70 per cent of gross supply services expenditure and hence have a decisive influence on trends in current expenditure. Over the period 1989 to 2001, the average annual rate of growth in real terms was 8.8 per cent for health, 4.8 per cent for education and 3.2 per cent for social welfare. There have been particularly large increases in health in recent years. The level of health expenditure since 1997 has more than doubled in nominal terms to approximately €7.7 billion in 2002.

TABLE 5.1

Current Public Expenditure: Supply Services
Annual Percentage Change 1987 to 2002 in Real Terms

	1987-1989	1989-1994	1994-1999	1999-2001	2002	1989-2001	Percentage of Total, 2002
Economic Services	-11.4	6.0	3.1	17.8	-0.3	6.7	9.4
Infrastructure	-5.2	3.0	-8.4	20.8	7.5	0.8	0.5
Social Services							
Health	-1.9	8.3	6.8	15.3	10.4	8.8	25.4
Education	-1.1	5.8	3.0	7.3	10.2	4.8	16.2
Social Welfare	-2.1	4.3	0.9	6.7	15.3	3.2	31.2
Housing	-21.9	-32.0	44.8	64.0	-8.6	7.9	0.4
Subsidies	-6.3	-2.5	-11.3	18.8	5.5	-3.1	0.8
Subtotal	-2.1	5.3	2.9	9.9	12.2	5.1	73.9
Security	-2.3	4.8	2.8	6.2	3.1	4.2	7.9
Other	-4.0	6.0	7.3	9.3	8.8	7.1	8.3
Gross Total (real)	-3.2	5.4	3.2	10.3	9.8	5.3	100.0
Gross Total (nominal)	1.3	8.3	7.4	15.5	15.0	9.1	

Source: Calculated from *Revised Estimates for Public Services*, using the GNP deflator. The 2002 figures are from the *2003 Estimates for the Public Services (Abridged Version)*, Dublin: Stationery Office.

The composition of current supply services expenditure is shown in Table 5.2. It is clear that supply services expenditure is dominated by three major areas of social services: social welfare (31.2 per cent), health (25.4 per cent) and education (16.2 per cent). These three areas represented over 70 per cent of supply services expenditure in 2002. Housing is a minor item in current supply services expenditure but is a more significant element in capital expenditure. Expenditure on economic services was equal to 9.4 per cent of supply services expenditure in 2002. This category includes the current expenditure of agencies such as IDA Ireland, Bord Fáilte and support services for agriculture. Expenditure on security (army, gardai, prisons, and the legal system) represented 7.9 per cent of total supply services expenditure. Of the total increase in current expenditure over the 1989 to 2001 period, 30 per cent went to health, 16 per cent went to education, 25 per cent went to social welfare and the remaining 29 per cent went to all other services.

TABLE 5.2

Current Supply Services Expenditure by Function, 2002

	Expenditure (€ millions)	Percentage of Total
Economic Services	2,840	9.4
Infrastructure	144	0.5
Social Services		
Health	7,694	25.4
Education	4,893	16.2
Social Welfare	9,446	31.2
Housing	111	0.4
Subsidies	233	0.8
Subtotal	22,377	73.9
Security	2,405	7.9
Other	2,503	8.3
Gross Total	30,269	100.0

Source: Calculated from the *2003 Estimates for Public Services (Abridged Version)*, Dublin: Stationery Office.

Capital Expenditure

During the 1980s capital expenditure was cut earlier and more severely than current expenditure, while during the 1990s it has grown at a faster rate than current expenditure. Exchequer capital expenditure as a percentage of GNP was just over 5 per cent in

1987. It fell to 3.2 per cent of GNP in 1989. Over the 1990s Exchequer capital expenditure has grown faster than GNP, and was approximately 6.7 per cent of GNP (including the pension fund contribution) in 2002. Since 1999 Exchequer capital expenditure has grown at an annual rate of over 20 per cent in nominal terms.

TABLE 5.3

Composition of the Public Capital Programme, 2002

Composition of Expenditure	Expenditure (€ millions)	Percentage of Total
Sectoral Economic Investment		
Industry and Labour	418	4.5
Agriculture and Food	172	1.9
Fisheries	70	0.7
Forestry	131	1.4
Tourism	54	0.6
Subtotal	845	9.1
Productive Infrastructure		
Energy	1612	17.4
Telecommunications, RTE, Postal services	138	1.5
Transport	2415	26.1
Environmental Protection	619	6.7
Subtotal	4784	51.7
Social Infrastructure		
Hospitals	509	5.5
Education	604	6.5
Housing	1597	17.2
Government Construction, etc	922	10.0
Subtotal	3632	39.2
Total	9261	100.0

Source: Department of Finance (2002), *Public Capital Programme 2002,* Dublin: Stationery Office.

While current expenditure is dominated by social services spending, the largest element of the Public Capital Programme (PCP) is productive infrastructure (investment in transport, energy and telecommunications infrastructure). This accounted for 51.7 per cent of the PCP in 2002 (€4.8 billion). The largest element of infrastructure spending was investment in transport (26.1 per cent of the PCP in 2002). The next largest element of infrastructure investment was energy (17.4 per cent of the PCP). This mainly covered investment by the ESB and Bord Gáis Éireann and so could be considered as more commercial investment than pure public investment. The low level of investment shown for telecommunications reflects the fact that Eircom was privatised in 2000 so that its investment is no longer included in the PCP.

The other major component of the PCP is investment in social infrastructure (housing, education, health facilities and general government construction) which represented 39.2 per cent of the PCP in 2002 (€3.6 billion). The largest component of social infrastructure was investment in housing (17.2 per cent of the PCP) reflecting the recent expansion of public housing investment. Finally, investment in hospitals and education facilities represented 5.5 per cent and 6.5 per cent respectively of the PCP in 2001.

The remainder of the PCP is sectoral economic support (capital support for industry, agriculture and so on) accounting for 9.1 per cent of the PCP in 2002 (€845 million). The share of this element of the PCP has been declining in recent years.

TABLE 5.4

Public Capital Programme, 1980-2001
Annual Percentage Change in Real Expenditure

	1987-1989	1989-1994	1994-1997	1998-2000	2001	Percent of Total
Sectoral Economic Investment						
Industry and Labour	1.4	1.0	26.0	-2.4	-21.8	6.4
Agriculture	7.0	19.7	-3.4	-0.5	-27.7	1.8
Fisheries	2.2	-0.7	18.1	38.8	-25.0	0.8
Forestry	11.9	15.8	-5.6	8.5	-12.4	1.7
Tourism	33.8	23.0	13.2	-3.1	-23.5	1.0
Subtotal	2.9	6.7	16.0	0.9	-21.8	11.8
Productive Infrastructure						
Energy	-15.6	11.9	5.2	5.6	20.9	13.9
Telecommunications, RTE & postal services	5.2	-1.7	14.0	15.3	18.2	1.9
Roads, Sanitary services	-0.9	5.3	9.2	24.6		21.9
Transport	12.5	-0.4	5.5	31.3		10.3
Subtotal	-0.4	3.8	8.7	19.7	14.7	48.1
Social Infrastructure						
Hospitals	-13.9	2.7	21.6	18.8	16.5	4.9
Education	-27.9	9.1	4.1	11.1	0.3	6.6
Housing	-42.8	11.9	3.3	23.5	36.7	17.4
Government Construction	-19.6	12.7	12.8	23.6	10.6	11.2
Subtotal	-33.8	10.2	7.9	19.8	18.8	40.2
Total (real)	-10.8	6.2	11.0	16.4	10.9	
Total (nominal)	-5.7	9.9	15.9	26.2	20.4	100.0

Source: Calculated from Department of Finance data and *Public Capital Programme 2001*.

Note: The above trends in real expenditure have been calculated using the gross domestic fixed capital formation deflator taken from the ESRI databank and updated using CSO *National Income and Expenditure*

2000 and *Quarterly National Account*s (Q4, 2001). Until 1997 loans by the ICC and ACC Banks were included in the Sectoral Economic Investment part of the Public Capital Programme. For this reason this Table shows slightly different time periods than the corresponding current expenditure Table to achieve consistency. Investment by Eircom/Telecom Éireann was included in the PCP until the privatisation of Eircom in 2000. This investment has been excluded from the 1998 figures to achieve consistency for the 1998–2000 period. The health figures from 1997 include investment funded by Health Boards from property disposals. The increases for roads and transport in 2001 are not shown due to changes in classification of these items.

Revenue

It was noted above that the tax share in GNP has been remarkably stable over the past decade, although the years 2001 and 2002 are significant exceptions in this respect. The question arises as to how this stability was achieved, given the substantial income tax cuts that have occurred. This aspect of the tax system is discussed in the Report of the Tax Forecasting Methodology Group of the Department of Finance (1998). This report pointed out that there is a tendency for the tax share of GNP to increase in the absence of policy changes. The corporation tax base is particularly sensitive to growth in GDP and, if that is faster than GNP growth, in the absence of policy changes, corporate taxes tend to grow faster than GDP. The VAT base could also be expected to grow by more than GNP growth as higher VAT rates apply to high income elasticity goods (i.e., goods whose consumption rises are more than proportionately in line with income). The income tax system is progressive, so income tax will increase faster than GNP in the absence of policy changes.

The total tax share in GNP in the year 2000 was 30.8 per cent, approximately the same as the 1991 share (after excluding Motor Vehicle Levies from the 1991 total for comparability, as these are now paid direct to Local Authorities). The income tax share fell by 1.8 percentage points over this period. The most buoyant tax base was corporation tax; its share of GNP more than doubled from 2.2 per cent in 1991 to 4.4 per cent in 2000. This was the single biggest contribution to maintaining the total tax share of GNP despite the decline in the income tax share. There were also increases in the shares for VAT and stamp duties. The share in GNP of customs and excise, however, declined. These duties are set in nominal terms so revenue does not increase automatically in line with growth of GNP.

TABLE 5.5

Tax Revenue as a Percentage of GNP

	1987	1989	1991	2000	2001	2002	1989-2001 Annual % Change (Nominal)
Customs and Excise	7.8	8.0	7.0	5.1	4.4	4.4	5.4
VAT	8.4	8.8	7.6	8.5	8.2	8.5	10.2
Income Tax	14.2	12.7	12.2	10.4	9.7	8.8	8.4
Corporation Tax	1.4	1.4	2.2	4.4	4.3	4.7	22.0
Stamp Duties	0.9	1.3	0.9	1.3	1.3	1.1	10.9
Motor Vehicles	0.7	0.7	0.7				
Other (Capital Gains, Capital Acq., Ag., and Training Levies)	0.8	0.9	0.9	1.2	1.1	0.7	9.5
Total Tax Revenue (excl. motor vehicles)	33.5	32.9	30.9	30.8	28.8	28.2	10.4

Source: The 1991 data taken from IPA (2001), *Administration Yearbook and Diary*. The 2001 data are from the Exchequer Returns, January 2002 and the 2002 data are from Budget 2003. The data for 1987 and 1989 are from the Department of Finance. The revenue from the annual tax on motor vehicles now goes to local authorities. It is excluded from the total in all years to facilitate comparability.

Since 2000 the tax share of GNP has fallen substantially by approximately 2.6 percentage points of GNP. The largest fall was for income tax, which fell by 1.6 percentage points.

International Comparisons

The level of public expenditure in Ireland and other EU countries is shown in Table 5.6. If expenditure is measured in terms of GDP, the level of expenditure in Ireland at 35.4 per cent in 2002 was the lowest in the EU. When measured as a share of GNP,[3] public expenditure in Ireland in 2002 at 42.5 per cent was the third lowest among EU countries, with both the UK and Spain at 41.0 per cent and 39.2 per cent respectively.[4] The share of total government expenditure in the UK has expanded in recent years. Its share in 2000 was 36.9 per cent of GDP while the Commission forecast is that its share will increase to 41.7 per cent in 2004.

Even when expressed as a percentage of GNP for Ireland, this measure is subject to a number of significant limitations. Public expenditure as a percentage of output or income is not necessarily an indication of the resources actually devoted to the delivery of public services and benefits. Total public expenditure includes interest payments that are not available for the provision of public services. The level of national debt and interest payments in Ireland are relatively low. The second column in Table 5.6 shows the level of non-interest general government expenditure. Total non-interest general government expenditure in Ireland in 2002 was estimated at

3. The main difference between GNP and GDP is the profits of foreign multinationals with operations in Ireland. These profits are part of GDP but not GNP. To some extent these profits are part of the tax base as they are subject to corporation tax. However, they are not part of the other tax bases that constitute most of the total tax base.

4. The level of public expenditure as shown in Table 5.6 is higher than the figures shown in Figure 5.1 from national sources. The level of public expenditure as estimated by the European Commission is higher than that shown by the budgetary figures in Figure 5.1 as the budgetary figures refer to central government expenditure while the Commission figures refer to general government (central and local government). The Commission figures on public expenditure are close to but slightly higher than public expenditure as reported by the CSO in the national accounts. This is because of adjustments made by in the Commission's figures for reasons of international comparability. The largest single difference between the CSO and the Commission figures concerns the treatment of the imputed pension costs of public servants. The Eurostat figures include the estimated imputed costs of the future pension entitlements of public servants, which are not included in the national figures on public expenditure.

40.5 per cent of GNP, just over three percentage points below the EU average.

Total non-interest expenditure is still not a measure that shows the total resources that are spent on public services. Ireland has a major infrastructure deficit and a relatively high level of public investment. This high level of investment will provide benefits over time but is distinct from the provision of current public services and benefits. The most relevant measure of resources devoted to the provision of current services and benefits is current non-interest expenditure (see the final column of Table 5.6). Using this measure, current expenditure was around seven percentage points lower in Ireland compared the EU average in 2002. This comparison, however, is subject to a number of significant qualifications:

- First, part of the gap between Irish and EU levels is a reflection of Ireland's relatively young population that reduces expenditure in Ireland at present on pensions and health;
- Second, it takes no account of Ireland's lower defence needs – Irish expenditure on defence is about ¾ per cent of GDP, compared to an EU average of more than 2 per cent; and
- Third, it does not take into account the extent to which Ireland implements some policies in part through the tax system, for example, assistance with health insurance premiums, with mortgage interest and pension provision, rather than through direct public expenditure alone. Relevant Irish tax expenditures exceed 3 per cent of GDP. Comparable tax expenditures from other EU countries are not readily available.

The data are not available to make a comprehensive comparison of expenditure ratios in a way that would take full account of all of the above issues. If public expenditure is broadly defined to include tax expenditures and taking account of lower defence and expenditure on pensions, there may not be a substantial difference between the Irish expenditure ratios and the EU average. However, it should not be assumed that the EU average level of public expenditure (including tax expenditures) constitutes the 'correct' level of public expenditure.

TABLE 5.6

General Government Expenditure Measures as a Percentage of GDP, 2002

	Total Expenditure	Total Non-Interest Expenditure	Current Non-Interest Expenditure
Belgium	48.9	42.7	40.6
Denmark	53.3	49.8	47.0
Germany	48.9	45.6	41.7
Greece	47.4	41.8	32.6
Spain	39.7	36.8	32.0
France	52.9	49.8	44.7
Ireland (GDP)	35.4	33.8	27.3
(GNP)	42.5	40.5	32.7
Italy	47.3	41.5	37.9
Luxembourg	43.2	42.9	37.6
Netherlands	44.8	41.8	38.3
Austria	51.6	48.2	42.8
Portugal	46.1	43.0	36.3
Finland	49.9	47.3	42.3
Sweden	57.3	54.2	49.1
UK	41.2	38.9	36.2
EU15	47.2	43.7	39.6

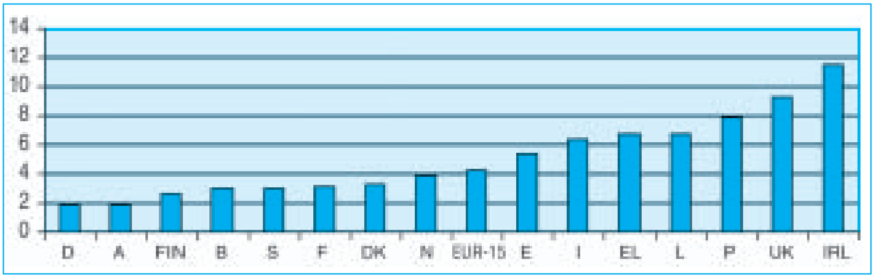
Source: European Commission (2002), *European Economy*, No. 4. The GNP-based figures for Ireland have been calculated by applying the ratio of GDP to GNP to the GDP-based expenditure figures.

In the mid-1980s both the share of public expenditure in national income and the overall public deficit in Ireland were above the EU averages. The share of public expenditure in national income has fallen in a number of EU countries (notably in the UK, Germany and the Netherlands) but the decline has been larger in Ireland. The greater decline in the public expenditure share in Ireland reflects the exceptional economic growth achieved in Ireland since 1987.

The actual growth rate of public expenditure has been relatively high in Ireland. Over the period 1995 to 2002, the annual average increase in expenditure at 11.5 per cent in nominal terms was the highest in the EU (see Figure 5.6).

FIGURE 5.6

Annual Percentage Change in Non-interest Current Expenditure in Nominal Terms, 1995-2002



Source: Secretariat calculations based on European Commission (2002) *European Economy*, No.4.

It is also of interest to consider the broad allocation of (non-interest) current expenditure. Expenditure on social protection expenditure in Ireland in 1999, at 17.2 per cent of GNP, was the lowest in the EU and just over 60 per cent of the EU average. Non-interest current expenditure in areas other than social protection (final column of Table 5.7) in Ireland at 12.8 per cent of GNP was almost one percentage point higher than the EU average (11.9 per cent of GDP).

Ireland's relatively low social protection expenditure is significantly influenced by demography. The fourth column of Table 5.7 shows social protection expenditure excluding expenditure on old age and survivors benefits. The gap in this measure among European countries is much lower than in relation to total expenditure. Social protection expenditure in Ireland, excluding old age and survivors benefits, was 12.9 per cent of GNP in 1999, around two percentage points below the EU average. The lower gap between Ireland and

TABLE 5.7

Current Expenditure Allocation as a Percentage of GDP, 1999

	Total Current	Current Non-Interest	Social Protection Total	Social Protection excluding pensions	Other Non-Interest Current
EU15	43.6	39.5	27.6	14.9	11.9
Belgium	47.4	40.4	28.2	16.1	12.2
Denmark	53.2	48.5	29.4	18.2	19.1
Germany	45.0	41.5	29.6	17.1	11.9
Greece	39.8	32.6	25.5	12.6	7.1
Spain	35.8	32.3	20.0	10.7	12.3
France	47.9	44.6	30.3	16.9	14.3
Ireland (GNP)	32.8	30.0	17.2	12.9	12.8
Italy	44.5	37.7	25.3	9.1	12.4
Luxembourg	36.8	36.5	21.9	12.8	14.6
Netherlands	42.8	38.3	28.1	16.4	10.2
Austria	47.4	43.9	28.6	15.0	15.3
Portugal	38.7	35.5	22.9	12.9	12.6
Finland	46.8	43.7	26.7	17.3	17.0
Sweden	54.4	49.6	32.9	19.9	16.7
UK	37.3	34.4	26.9	14.4	7.5

Source: Eurostat (2002), *Social Protection in Europe*, January and European Commission (2002) *European Economy*, No. 6.The GNP-based figures for Ireland have been calculated by applying the ratio of GDP to GNP to the GDP-based expenditure figures of Eurostat and the Commission.

the EU average when old age benefits are excluded is not purely a demographic effect; it also reflects relatively low pensions in Ireland compared to some other European countries. It is clear, however, that the dramatic differences in social protection expenditure in Ireland are mainly a reflection of very different levels of expenditure on pensions. Comparisons of social expenditure levels are also affected by other factors, such as whether or not benefits are subject to tax as well as varying reliance on tax expenditures. Social protection expenditure in the form of tax expenditures is not included in the figures quoted above; this has a significant impact on the Irish figures as the Irish reliance on tax expenditures in pensions and other areas is relatively high.

5.2.2 Previous Fiscal Policy Recommendations

The Council's recommendations in the 1999 *Strategy* report on fiscal policy were as follows:

- Policy should aim to maintain substantial budget surpluses close to present levels, while growth remains strong;
- Over the three years to 2002, the increase in current public expenditure should at a maximum, correspond to growth of GNP;
- In relation to capital expenditure, the Council supported a major construction programme of physical infrastructure including accelerated development of the national road and public transport system and a significant increase in the housing stock; the Council welcomed the broad thrust of the National Development Plan (NDP);
- The tax share of GNP should be kept close to existing levels; and
- The Council recommended reform of the public service pay determination system.

The surplus as measured by the General Government Balance (GGB) was 2.3 per cent of GDP in 1999. It then increased to 4.4 per cent of GDP in 2000 and has since fallen sharply to an estimated deficit of 0.1 per cent of GDP in 2002. Some decline in the size of the surplus was warranted given the slowdown of growth in the economy. However, a large part of the turnaround from a substantial surplus to a marginal deficit is not attributable to the slowdown in growth that has occurred.

The Council's recommendation that the increase in current expenditure should not exceed the growth of real GNP allowed for considerable flexibility for expenditure growth. It was a departure from earlier *Strategy* reports that had recommended very limited growth of current expenditure. This recommendation would have been consistent with nominal growth of around 36 per cent in current expenditure between 1999 and 2002. In the event, the increase in gross supply services expenditure between 1999 and 2002 reached over 53 per cent in nominal terms. Supply services expenditure as a percentage of GNP has increased by three percentage points since 1999 to over 29 per cent in 2002. Clearly, the increase in expenditure over the last few years was significantly larger than that recommended by the Council.

In 1999 the Council recommended that the tax share of GNP should be maintained close to its existing level. Since 1999, its share has fallen by around three percentage points. This is a significant fall in the course of three years and was not projected to occur in the budgetary projections. While the reasons for the extent of the decline are not fully understood, in part it reflects larger tax reductions than envisaged by the Council.

From 1999 to 2001, the Exchequer pay and pensions bill increased by 30 per cent and increased by a further 12.5 per cent in 2002. The increase in the pay bill reflects pay increases under Partnership 2000 and the PPF as well as the effects of increases in public service employment.

Pay increases raise the cost of public services. However, public service pay increases are to be expected in a growing economy. What is important is that pay levels in the public service do not exceed those in the private sector or drive economy-wide pay developments—directly or through their implications for the tax burden—and that there is continuing adaptability and co-operation with on-going change in delivering public services. The Public Service Benchmarking Body was established to oversee independent comparisons between the public service and the private sector pay levels. Combined with the linking of the final phase of the PPF with organisational performance these are welcome steps in modernising pay determination.

The very large increase in expenditure in recent years raises the question of what has been achieved with this increase. Health is the fastest growing area of public expenditure, as noted above. Much of the increase in health expenditure was absorbed by cost increases including higher pay costs but there has been a significant expansion of services as well. For example, the numbers treated in the acute hospital sector have expanded substantially and there has been a significant investment in services for people with intellectual disability with the creation of an additional 1650 residential places and 2300 day places for this group between 1996 and 2001. Nonetheless much remains to be done to improve health services. Higher social welfare expenditure led to a large increase in the value of social welfare payments; for example, over the period 1999 to 2002 the old age contributory pension increased by 30 per cent in nominal terms and almost 13 per cent in real terms.

While there have been improvements in some areas of public services the Council emphasises the importance of achieving improvements in the management of public expenditure to ensure that value for money is achieved. One aspect of this is the regular publication of information on outputs produced by public expenditure (see Section 5.4.1 below).

5.2.3 Principles and Priorities for Public Finance

The Council's position on the public finances is based on a range of principles. These principles are of three kinds: overall balance, expenditure and taxation.

Principles relating to overall balance

- **Sustainability:** the public finances must be managed on a sustainable basis. This means, among other things, that borrowing should only by undertaken if required for capital purposes, and only for projects that provide an adequate rate of return. Sustainability also requires that the public finances be managed such that the long term costs of an ageing population can be met without recourse to excessive levels of taxation.

- **Stabilisation:** The management of the public finances needs to take account of the stage of the economic cycle. At a minimum, the public finances should not add to cyclical fluctuations in the economy. When the economy is performing well, flexibility should be maintained in order to provide scope for some relaxation of fiscal policy in an economic downturn.
- **The EU Stability and Growth Pact:** Under this Pact, the Government is required to maintain the public finances "at close to balance or in surplus". The relevant measure for this purpose is the GGB, a measure that encompasses the social insurance fund and the pension fund, in addition to the Exchequer.

Principles on Public Expenditure

- In view of the significant infrastructural deficits, capital expenditure needs to be sustained at a significant level of GNP to address these deficits. A crucial part of this is the implementation of the NDP. Capital spending includes spending on both economic infrastructure, such as roads, as well as social infrastructure, such as investment in facilities for childcare and eldercare.
- Public expenditure should be sustained at a level that is sufficient to address key social deficits, subject to being consistent with the strategy on the overall balance and a tax level that will facilitate growth and employment creation. Public expenditure should be managed in such a way that the above goals are achieved in the most effective way and at a minimum cost. The Council is concerned that there are weaknesses in how public expenditure is managed. The Council recommends that measures be taken to improve the management of public expenditure (see Section 5.4.1 below).

Public service pay is a key element driving the growth of public expenditure. Public service pay accounts for approximately 39 per cent of gross supply services spending. The effective organisation and management of public servants, so that they provide services that meet the needs of society and the economy, is a critical priority for the Council. The system of public service pay determination needs to meet the following objectives:

(i) to facilitate high performance in the public service, including the effective development of the Strategic Management Initiative (SMI);

(ii) to provide pay settlements that are comparable to the private sector, taking into account differences in working terms and conditions; and

(iii) to promote competitiveness.

Public service pay determination is discussed in more depth in Chapter 6 on wage bargaining.

Principles on Taxation

The Council's principles in relation to taxation are presented in Chapter 7 below. These principles do not show an optimal tax share of GNP. However, in view of (i) the expenditure objectives outlined above and the target of maintaining the public finances close to balance on a general government basis; and (ii) the fact that the outcome for 2002 was a marginal deficit on a general government basis (around 0.1 per cent of GDP) there would not seem to be scope for reduction in the tax share of GNP. If all these objectives are to be achieved, the option of a modest increase in the tax share of GNP from its 2002 level should not be excluded. The Council supports a widening of the tax base in a number of ways, as discussed in Chapter 7 below. However any such increase should be modest, since a substantial increase in the tax share of GNP would be inconsistent with the Council's principles because it could damage the competitiveness of the economy.

Uncertainties and Vulnerabilities

Tax revenue growth is difficult to predict at this stage. Tax revenue growth has been very much lower than expectations in 2001 and 2002. The introduction of individualisation has weakened the historical relationship between tax revenue and economic growth as it has reduced the revenue yield from rising female labour force participation.

A significant vulnerability of the public finances in the short-term concerns the possible movement of the euro. Bergin *et al*. (2002a) considered that a 10 or even 20 per cent change could occur although the timing is difficult to predict[5]. The effect of a stronger euro is to impart a deflationary pressure to the euro area, implying a competitiveness loss to the Irish economy and the euro area generally. The effect of lower demand in the euro area (resulting from the loss of competitiveness) on the Irish economy is not taken into account in the analysis of Bergin *et al*. If the deflationary shock occurred after budgetary parameters have been set, the outturn for the public finances would be for a higher deficit than originally forecast (the real value of welfare payments and public service pay would also emerge as higher than projected).

Using the ESRI macroeconomic model, it is estimated by Bergin *et al*. that a 10 per cent euro appreciation with rapid pass through of the deflationary shock would add 0.5 percentage points of GNP to the government borrowing requirement (Bergin *et al*. 2002a). With slower pass through of the deflationary shock, the effect in the first year would be lower (around 0.25 percentage points) and would rise over a five year period to eventually have a similar impact. The effects of a 20 per cent appreciation would be to double this amount

The implication of this for the planning of the public finances is that the possibility of a sharp appreciation of the euro and other possible adverse shocks needs to be taken into account and sufficient flexibility built into the public finances to be able to absorb the consequent impact on the public finances. Each 1 per cent shortfall in growth is associated with a deterioration in the public finances of approximately half per cent of GNP (Fitz Gerald, 2000b).

5. From November 2002 to 4 March 2003 the euro appreciated by approximately 9 per cent.

BOX 5.1

Special Savings Incentive Accounts

Special Saving Incentive Accounts (SSIAs) will result in a cost to the Exchequer of over €500 million over the years 2002 to 2006, substantially more than originally estimated. The scheme was designed to encourage long-term savings. The scheme is of most benefit to higher income people, as such people are more likely to be in a position to make the maximum monthly contribution. Given that the scheme is in existence, it could be argued that its withdrawal would be unfair. However, to the extent that its withdrawal facilitated higher expenditure than would otherwise occur on socially useful services or infrastructure, this would provide a positive net contribution to social equity. The most significant disadvantage of withdrawal from an equity perspective would be its impact on employees on modest incomes who are using the scheme as a substitute for a pension.

5.3 INFLATION

Inflation has re-emerged as a concern in recent years. This section begins with an outline of trends in various measures of inflation in recent years. Attention then turns to the factors that have influenced inflation in Ireland. It is important that these factors are carefully identified and acknowledged by economic actors. Consideration is then given to the ways in which Irish inflation is a problem, economically and socially. Finally, the main policies to contain inflation are identified and discussed.

5.3.1 Inflation trends

The annual rate of change in the consumer price index (CPI) fell during the 1980s from a peak of over 20 per cent in 1981 to just over 2 per cent in 1988. It increased to 4 per cent in 1989 and has tended to fall somewhat during the 1990s, reaching a remarkably low level of 1.6 per cent in 1999. CPI inflation then increased more than threefold to 5.6 per cent in 2000 while it fell somewhat to 4.9 per cent in 2001. The rate of inflation for 2002 was approximately 4.7 per cent. In recent years the rate of inflation in Ireland has been substantially higher than the euro average (see Table 5.8).

Since 2001 it is mainly higher services inflation that accounts for Ireland having a higher rate of inflation compared to the euro average. Services inflation increased from 5.7 per cent in 2000 to 6 per cent in 2001 while core services inflation increased from 7 per cent in 2000 to 7.3 per cent in 2001. Services inflation for the euro area in 2001 was 2.5 per cent. Estimates by the Central Bank indicate that there was no difference in goods inflation in Ireland and the euro area in 2001 (2.5 per cent in each case).

TABLE 5.8

Goods and Services Inflation in Ireland and the Euro Area

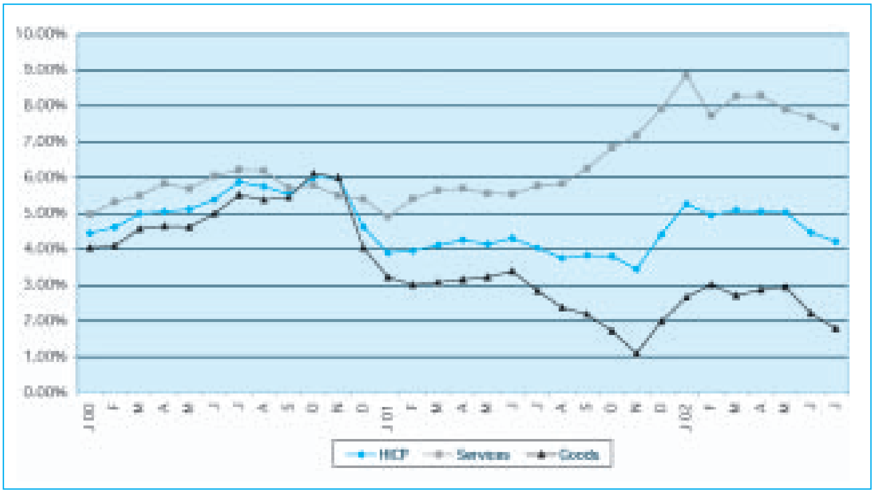
	Ireland			Euro Area		
	HICP	Goods	Services	HICP	Goods	Services
1997	1.2	0.7	2.2	1.6	1.1	2.4
1998	2.1	1.7	3.0	1.1	0.7	1.9
1999	2.5	1.6	3.8	1.1	0.9	1.5
2000	5.3	4.9	5.7	2.3	2.7	1.7
2001	4.0	2.5	6.0	2.5	2.5	2.5
2002	4.8	2.6	7.9	2.2	1.7	3.1

Source: Central Bank (provided by Terry Quinn).
Note: The 2002 figures are the average year-on-year increases in the months to August 2002.

Inflation in 2002 continued above the euro-area average with an average rate of CPI inflation of around 4.7 per cent. Again, it is mainly higher services inflation that has caused above average inflation in Ireland in 2002 although goods inflation was also almost 1 per cent higher in Ireland compared to the euro average. From its peak in January 2002, there was a modest easing of services inflation over 2002, particularly if one focuses on what the Central Bank refers to as 'core' services inflation. This excludes administered services (services whose price is mainly controlled by administrative decisions, such as health, education and public transport), alcohol services (not subject to normal market forces) and communications (different from other services as prices tend to fall due to technological progress). Significant increases in administered services prices (notably health and education) have delayed the reduction in the rate of services inflation.

FIGURE 5.7

Annual Percentage Change in HICP, Services and Goods Inflation 2000-2002



Source: See figure 5.6.

Euro Changeover

There has been some concern that the euro changeover provided an opportunity for unjustified price increases. This issue has been examined in a recent report prepared for Forfás (Pricewaterhouse Coopers, 2002). This report found that at an aggregate level in Ireland, CPI inflation during the euro changeover period did not appear to be unusual by reference to historical patterns. The evidence for this conclusion is straightforward. The rate of increase of the CPI during the changeover period, defined as September

2001 to March 2002 was 2.2 per cent. This was similar to the corresponding rate for the same period between 2000 and 2001 (2 per cent) and somewhat less than the rate for the corresponding period between 1999 and 2000 (2.8 per cent). The rates for this part of the year in earlier years (i.e., before 1999) were lower at a time when annual inflation generally was lower. The report also looked at an alternative measure, the ratio of prices for the January to March period relative to prices for the full year April to March. This ratio for January to March 2002 relative to the full year to March 2002 was 1.3 per cent. This was again similar to the ratio for the period 2000/2001 (1.2 per cent) and lower than the corresponding period 1999/2000 (1.7 per cent).

However, more detailed analysis of sectoral price trends did find indications of unusual price trends over the changeover period. Products and services identified as having unusual price increases included doctors' and dentists' fees, cinema prices, package holidays, pubs and restaurants, taxi fares and local authority rents. The report did not find widespread evidence of euro profiteering but there was preliminary evidence of profiteering in a number of services areas. Unusual price increases in the euro changeover period may reflect a convenience factor of bringing forward full year price increases to this particular changeover period. Where this is the case one would expect that future price increases would be lower than otherwise. The extent to which this is the case will only emerge over time and further research will be required to reach a definitive conclusion.

An examination of the changeover effect across the euro zone as a whole was undertaken by Eurostat, the Statistical Office of the EU. This study found that the euro changeover did not appear to have had a significant effect on inflation trends across the euro area generally. It pointed out that the rate of change in the euro zone index of consumer prices between the first six months of 2002 and the last six months of 2001 was 1.4 per cent. This was identical to the rate of change between the first six months of 2001 and the last six months of 2000 and little different from the corresponding rate for the 1999/2000 period. The report concluded that almost all of the prices increases over the period could be explained by a normal inflation pattern and some special non-euro factors; in particular, bad weather affecting fruit and vegetable prices, car and energy prices and some significant tax increases on tobacco. The report estimated that of the rate of inflation of 1.4 per cent over the changeover period, the contribution of the euro changeover most likely fell within the range of 0.0 per cent to 0.2 per cent (Eurostat, 2002).

5.3.2 Factors Influencing Inflation

In a small open economy, exchange rate movements and inflation in the main trading partners are key influences on inflation. However, inflation is not entirely determined through these influences. Much economic activity is non-traded and inflation in non-tradeables (mainly services) is influenced by the level of demand in the economy, and by wage and other costs. It is possible, in principle, to quantify the various direct 'beneficiaries' of increased prices (i.e., where the money goes), although there are no recent data available for Ireland.[6]

The increase in inflation in Ireland in recent years is not surprising, in view of the weakness of the euro, wage inflation arising from a tight labour market and the bidding up of the prices of fixed factors, such as property prices and rents. In addition to these factors, it is possible that there was a contribution to inflation from some traders taking advantage of the more buoyant economic conditions to achieve unwarranted increases in profits (profiteering)[7]. The role of this factor is not known. Provided there is competition, including freedom of entry, this can only be a temporary phenomenon: profits that yield an above average rate of return will attract new entrants

6. The composition of a unit of consumer expenditure in 1985 and hence of the 'beneficiaries' of higher prices were as follows: import prices (36 per cent), indirect taxes less subsidies (18 per cent), wages and salaries (25 per cent), agricultural profits (5 per cent) and profits/rents/depreciation (17 per cent). This disaggregation was provided by Professor John Fitz Gerald of the ESRI.

7. A recent Forfás study examined the impact on prices of the euro change-over. It did not find evidence of widespread profiteering but there was preliminary evidence of unusual price behaviour in a number of services areas.

into a sector and bid down excess profits. This points to the role of strong competition, and recommendations to strengthen competition are presented below. The factors that caused inflation are now easing. The euro has strengthened recently, demand is now weaker in the economy and wage inflation is easing in some sectors (see Chapter 6).

5.3.3 Problems Posed by Inflation

It is sometimes argued that inflation in a small part of the euro area, such as Ireland, is not a significant problem. The Council does not share this view. The key danger is that excessive wage and price inflation leads to a significant loss of competitiveness and a rise in unemployment. Such a rise in unemployment and loss of competitiveness would then place downward pressure on inflation. The key challenge is to achieve wage growth that is appropriate in an economy at full employment, while avoiding excessive wage and cost inflation that would cause an increase in unemployment.

Another problem posed by inflation is that it makes it more difficult to achieve co-ordination among actors in the economy. When inflation is higher than people have become accustomed to, it becomes more difficult to set prices and to reach agreement on appropriate wage increases. A possible consequence is that without any bad faith by either unions or employers, there is a perception that the PPF has either been breached or is ineffective. Consequently, inflation can erode confidence in the partnership process.

Inflation also affects the distribution of income. It poses a particular problem for elderly people without adequate pensions who rely on their savings, as real interest rates on a typical savings account are now negative. Unexpected inflation can have particular effects on groups whose income is set in advance in nominal terms. For example, inflation in the year 2000 was higher than expected and it turned out that the rate of increase for some social welfare payments was slightly below the rate of inflation.

The impact of inflation on any particular group or individual depends on their pattern of expenditure. Those whose pattern of consumption includes items that are showing rapid increases will experience above average inflation. Two items that have shown very large price increases are housing and childcare. Those who pay the full market price for housing on an ongoing basis and have significant childcare costs will at a time of rapid increases in these costs have a personal inflation rate higher than indices such as the CPI. Conversely, others will have a rate of inflation below the average growth in the CPI.

The impact of inflation varies across different economic sectors. The sectors most adversely affected by inflation are sectors that face inflationary cost rises but have limited ability to pass on the cost increases. Such sectors include the agricultural sector and parts of indigenous manufacturing that are exposed to international competition and have weak market power (e.g., clothing and footwear). High inflation reduces the income of those engaged in these sectors and can contribute to job losses.

5.3.4 Policies to Address Inflation

The Council is firmly committed to the achievement of a reduction in the rate of inflation. In particular, the Council is committed to ensuring that a wage-price spiral does not become embedded in the economy. The target of the European Central Bank is for a rate of inflation in the euro zone of 2 per cent.

The Council recognises that the future rate of inflation is uncertain, among other things reflecting uncertainty about exchange rate movements. One possibly is a large sudden increase in the value of euro relative to sterling and the dollar. This would have a beneficial effect in reducing inflation. However, if it were unexpected, a sharp appreciation could have a number of negative consequences. It would result in a loss of cost competitiveness with effects on exports and employment. If inflation turned out to be lower than expected at the time when wages and social welfare benefits were set, then real wages and welfare benefits would be greater than expected and the Government's budgetary position would be weakened.

The following are the main instruments that are potentially available to address inflation:

- Counter-cyclical fiscal policy;
- Wage determination and incomes policy;
- Competition policy and regulatory reform;
- Labour market policies; and
- Infrastructural capacity and planning.

Each of these is discussed briefly below.

Counter-cyclical Fiscal Policy

With the pooling of exchange rates and monetary policy instruments in the EU, the primary macroeconomic instrument available to manage demand is fiscal policy. It is well known that the effectiveness of fiscal policy is very limited in a small open economy such as Ireland. But this does not mean that it has no effect. Research suggests that fiscal policy in Ireland in recent years has been strongly pro-cyclical; i.e., it has added to the already strong growth in the economy (Duffy *et al*., 2001). This is an undesirable policy approach. The Council recommends that fiscal policy should contribute to the stabilisation of the economy.

For the most part, public services are funded by taxation and are not included in inflation as measured by the CPI. Nonetheless, the costs of public services do have inflationary implications. Excessive costs in the public service can lead to higher taxation and put upward pressure on wages. The Council considers that public services should be improved and recommends improved management of public expenditure. This requires, among other things, the focussing of expenditure on priorities, a stronger evaluation culture, the use of sunset clauses to eliminate programmes that are no longer serving economic or social priorities and improved accountability for what is achieved through public expenditure[8].

8. These issues are discussed further in the Council's recent report *Achieving Quality Outcomes: The Management of Public Expenditure*.

Wage Determination and Incomes Policy

Tighter labour market conditions seem to have been a key factor contributing to higher inflation in Ireland in recent years. With the economy at virtually full employment, it was natural that more of the benefits of economic growth were taken in the form of higher wages rather than increased employment. The strength of demand in the economy, in conjunction with rising wage and other costs, has increased prices in the services sector. Excessive price and wage inflation has led to a loss of competitiveness and a rise in unemployment. Approaches to wage bargaining are discussed in Chapter 6.

Employee financial involvement provides more flexible ways of allowing employees to share in the benefits of economic growth. Such schemes are not primarily aimed at the inflation problem but there are potential counter-inflationary effects. Employees who are able to share the benefits of higher profits are less likely to seek inflationary wage increases. The Council's view on this is outlined in Chapter 6, where wage bargaining is discussed.

Competition Policy and Regulatory Reform

Strong competition has numerous potential benefits. It can exert downward pressure on prices, encourage responsiveness to customer demands and promote innovation. Competitive forces can be impeded either through state-imposed regulations, such as those that existed until recently in the taxi market and still exist for pharmacies, or can be limited by collusion among private companies. Reforms to remove state-imposed obstacles to competition, and the pursuit of a vigorous competition policy to reduce private restrictions, can contribute to reducing inflation.

The Council strongly supports the strengthening of competitive forces across the economy through the more vigorous implementation of competition law and it supports the introduction of greater competition in sectors such as pharmacies, the drink trade and the professions. It recommends that the Competition Authority and the Director of Consumer Affairs be mandated and resourced, as part of a strategy against inflation, to prioritise investigations in sectors where prices do not appear justified by market conditions.

Investigations by the Director of Consumer Affairs would complement those of the Competition Authority. They could cover a wider range of areas and be conducted in areas where there was no reason to suspect that there was any breach of competition law, but where greater transparency could help to stimulate stronger competition to the benefit of consumers.

In some parts of the economy, the achievement of appropriate prices through open competition is not feasible due to the nature of the sector. The Council supports the regulation of markets where lack of competition or other market failures apply (see Chapter 9 below).

The large increase in insurance costs is a matter of concern for the Council. While the cost of insurance is affected by the general increase in costs across the economy, there are some specific influences. The Council supports the measures in the Tanáiste's reform programme to tackle excessive insurance costs, including measures to combat fraudulent claims, the reduction of legal costs and excessive compensation awards. In addition, there are a small number of insurance providers in the Irish insurance market. The Council supports the inquiry by the Competition Authority and Department of Enterprise, Trade and Employment into factors limiting the number of firms offering insurance in the Irish market.

Labour Market Policies

Inflation pressures emerged as the economy moved towards full employment. Policies that act to increase labour supply and address skills and labour shortages will tend to reduce wage inflation, which is also likely to weaken price inflation. Such policies include public employment services, active labour market policies (to help those experiencing social exclusion to re-enter the labour market), policies to encourage female labour force participation, policies that encourage workers to remain in the labour force and policies that facilitate immigration[9]. Immigration is discussed in Chapter 8.

9. The Council notes that the National Economic and Social Forum (NESF) is undertaking work on the participation of older workers in the labour market.

Infrastructural Capacity and Planning

While all public expenditure adds to demand (other things being equal), some forms of public investment are relevant to reducing inflation. In particular, the Council is aware that the cost and availability of housing is putting upward pressure on wages and it attaches a high priority to measures to improve affordability (see Chapter 9). Infrastructure investment that facilitates an increase in the supply of housing can help moderate inflation and alleviate congestion, a key constraint on competitiveness. While this investment may not reduce inflation in the short term, improving infrastructure is a preventive policy against inflation.

5.4 CONCLUSIONS

5.4.1 The Public Finances

Since the-mid 1990s, the expenditure share of GNP has declined while the revenue share was fairly stable. The tax share in GNP was remarkably stable over the past decade, despite the tax reductions that occurred. The buoyancy of corporation tax revenue helped offset the decline in the income tax share of GNP. This resulted in an increase in the surplus to a peak of 4.4 per cent of GDP in 2000. At the same time there has been substantial real growth of public expenditure. Over the period 1989 to 2001, the average annual real growth of expenditure was over 5 per cent.

The growth of expenditure since the publication of the Council's last *Strategy* report in 1999 has been substantially faster than recommended by the Council. The real growth rate of supply services expenditure has been around 10 per cent in the period since 1999 and the share of supply services expenditure in GNP has increased by three percentage points. The tax share of GNP also declined so that effectively the surplus in the public finances has been eliminated.

The Council acknowledges that higher public expenditure has been associated with improvement in the provision of many public services but emphasises the importance of strengthening the focus on the effectiveness of public expenditure in terms of the quantity and quality of public services. The information on what is produced with public expenditure should be improved. Other general reforms required in the management of public expenditure are discussed in a recent report of the Council (NESC, 2002c). Improving the management of public expenditure is an important priority for the Council.

Commonly used measures of public expenditure relative to GDP exaggerate the extent to which Ireland has low public expenditure compared to other EU countries. The very low apparent social protection expenditure in Ireland relative to GDP is mainly, although not exclusively, a reflection of lower public expenditure on pensions in Ireland.

The Council's Proposals on the Public Finances

The Council's proposals on the public finances are based on analysis of the medium-term economic and social requirements. Ireland's medium- and long-term development requires continued investment in public infrastructure of at least the current level of 5.5 per cent of GNP. The core elements of the Council's strategy for the public finances are:

- Continuation of infrastructural investment of at least 5.5 per cent of GNP in order to implement the NDP and other infrastructure projects;
- Public expenditure necessary to address the key social deficits, as identified in Chapter 8 below.

Meeting these goals will be very challenging. These key economic and social goals could be achieved in a number of ways: improved value for money and reallocation of existing expenditure to new priorities, a general government deficit (i.e., borrowing) or by increased revenue, or some combination of all three. The Council is strongly in favour of improved value for money and the allocation of expenditure in line with policy priorities. However, it does not consider that this will be sufficient to meet the objectives outlined above, so that the other mechanisms also need to be considered. The degree to which increased revenue to meet the priorities discussed above would be reflected in an increase in the tax share of GNP will depend on the rate of economic growth achieved, subject to the requirement of maintaining competitiveness. Likewise, the extent to which additional borrowing to fund capital investment increases the GGB as a per cent of GNP, depends on the rate of growth achieved. Consequently, a high priority must be given by all to growth-oriented policies and actions. Any increase in revenue must be achieved in ways that avoid disincentives to the deployment of mobile factors in productive activity in Ireland. Likewise, any increase in expenditure on current services must occur in a context of rigorous evaluation and public sector modernisation.

The Council, noting Ireland's obligations under the Stability and Growth Pact, believes that, taking account of the current constraints in the public finances and a growth rate that is below the economy's potential, in the short-term a modest level of borrowing (on a general government basis) may be unavoidable. With a deficit in 2002 of around 0.1 per cent of GDP and the prospect of modest growth in 2003, the challenge of stabilising the deficit at its current level should not be underestimated. The Council considers that the option of a modest increase in the share of taxation in GNP should not be ruled out. The Council expects growth to return to its full potential in the years covered by this *Strategy*. As growth returns to its full potential, the aim should be to restore balance in the public finances, with current public expenditure growing no faster than GNP and the debt ratio continuing its gradual decline.

In proposing this medium-term strategy for Irish policy, the Council also supports immediate adjustments necessary in the light of the shortfall in revenue. Some immediate adjustments are necessary in order to achieve a transition to lower expenditure growth. The Council emphasises that in making the transition to a lower rate of expenditure growth, the distribution of the burden should be fair—in particular, that those on the lowest incomes should not bear the burden of adjustment—and, as noted above, that the priorities identified above be addressed.

The Council emphasises that this strategy is only feasible if public policy, and the action of the social partners, are both strategic and fair. The Council's *Strategy* involves identification of priority public investments and priority improvement in services. The criteria used in identifying these priorities should be the extent to which increased expenditure contributes to supporting a sustainable increase in living standards and an improved quality of life, a fairer and more equal society and environmental sustainability.

Improving the Management of Public Expenditure

Given the very strong growth of public expenditure in recent years, the Council wishes to emphasise the importance of achieving better value for money in the public system. Higher public expenditure has been associated with an improvement in the provision of some public services and a significant increase in public employment. However, the Council is concerned about the lack of transparency of what is achieved through increased public expenditure.

Future public expenditure should be based on clear plans on what expenditure is to achieve and be followed by publication of much clearer information on, and greater accountability for, what has been achieved. Expenditure decisions should be based on clearly defined economic and social priorities. There is a need to develop a culture in which evaluation plays a much more significant role in spending. To achieve this, further progress is required on public service modernisation[10].

The EU Stability and Growth Pact (SGP)

The Council believes that there are good reasons for co-ordination of national fiscal policies in economic and monetary union. Fiscal policy in one member state can have spill-over effects on other member states. Too stimulatory a fiscal policy in the euro area requires the European Central Bank to tighten interest rates, with adverse effects on economic activity and employment in all member states. The need to treat economic policies 'as a matter of common

10. The Council's proposals to improve the management of public expenditure are outlined more comprehensively in the Council's recent report *Achieving Quality Outcomes: The Management of Public Expenditure*.

concern' has been recognised by successive Irish governments and the Irish people when they endorsed the Treaty of Rome and the Treaty of Maastricht.

Indeed, it is particularly in the interest of small member states that the Union has the ability to co-ordinate fiscal policy. This is graphically illustrated by the way in which the unilateral approach to fiscal policy adopted by Germany after unification forced an increase in German and then European interest rates, such that "the incipient boom in Ireland was halted in its tracks in 1990" (Fitz Gerald, 2000b: 56).

The European system of economic policy co-ordination contains a mixture of relatively hard and relatively soft methods of co-ordination, depending on the matter under discussion. The avoidance of excessive budget deficits is achieved through binding rules, set out in the Stability and Growth Pact (SGP), which can culminate in formal sanctions, including fines. By contrast, co-ordination of national economic policy through a set of 'Broad Economic Policy Guidelines' is relatively soft. Where a member state deviates from the Guidelines, the Council can issue a non-binding recommendation to the member state in question, which is not supported by any sanction.

The SGP played an important role in facilitating the transition to EMU and provides part of the framework for co-ordination within the eurozone. Aspects of the SGP have been criticised as inappropriate. The Council recommends that Ireland should develop its own view of the strengths and weaknesses of the SGP and participate constructively in discussion of it.

Uncertainties

The planning of the public finances needs to take into account the possibility of a sharp appreciation of the euro and other possible adverse shocks and sufficient flexibility built into the public finances to be able to absorb the consequent impact on the public finances. Each 1 per cent shortfall in growth is associated with a deterioration in the public finances of approximately half a per cent of GNP (Fitz Gerald, 2000b).

5.4.2 Inflation

The increase in inflation in Ireland in recent years is not surprising, in view of the weakness of the euro, wage inflation arising from a tight labour market and the bidding up of the prices of fixed factors, such as property prices and rents. The euro changeover does not appear to have had any significant impact on overall inflation, but there is evidence of unusual price trends in a number of services, including doctors' and dentists' fees, cinema prices, pubs and restaurants and taxi fares. The Forfás study did not find evidence of widespread profiteering associated with the euro but it is some concern to the Council that there was preliminary evidence of profiteering in a number of services areas (PricewaterhouseCoopers, 2002). The factors that caused inflation are now easing. The euro has strengthened recently, demand is now weaker in the economy and wage inflation is easing in some sectors.

The Council is seriously concerned that Irish inflation has been well above that in our main trading partners for some time now. While inflation can be part of an equilibrium process of adjustment, it can still be a significant problem. The key danger is that excessive wage and price inflation leads to a significant loss of competitiveness and a rise in unemployment. Such a rise in unemployment and loss of competitiveness would then place downward pressure on inflation. The key challenge is to achieve wage growth that is appropriate in an economy at full employment, while avoiding excessive wage and cost inflation that would cause an increase in unemployment.

The impact of inflation on any particular group or individual depends on their pattern of expenditure. Two items that have shown very large price increases are housing and childcare. Those who pay the full market price for housing on an ongoing basis and have significant childcare costs will at a time of rapid increases in these costs have a personal inflation rate higher than indices such as the CPI. Conversely, other people will have a rate of inflation below the average growth in the CPI.

Of the policies discussed to address inflation, the most relevant would seem to be fiscal policy and competition policy. The Council recommends that fiscal policy should contribute to the stabilisation of the economy. The Council emphasises the benefits to consumers of stronger competition in terms of the provision of quality goods and services at an optimum price. Stronger competition in the non-traded sector can make a contribution to lower inflation. It recommends that the Competition Authority and the Director of Consumer Affairs be mandated and resourced, as part of a strategy against inflation, to prioritise investigations in sectors where prices do not appear justified by market conditions. Investigations by the Director of Consumer Affairs would complement those of the Competition Authority. They could cover a wider range of areas and be conducted in areas where there was no reason to suspect that there was any breach of competition law, but where greater transparency could help to stimulate stronger competition to the benefit of consumers.

CHAPTER 6

WAGE BARGAINING

6.1 INTRODUCTION

There are a number of reasons why the wage bargaining component of Irish social partnership now requires careful consideration and analysis. Among these are:

- The move from ERM to full EMU;
- Shortages of labour in many areas of the private sector;
- The move to new systems of public sector wage determination;
- The limits to a strategy of exchanging pay restraint for tax reductions; and
- The need to consider what distribution of income is appropriate in a socially inclusive society.

Any such review should take account of international experience and developments in the analysis of wage bargaining systems. Section 6.2 summarises the main analytical approaches that guide understanding of wage bargaining systems. It highlights the benefits of a significant degree of co-ordination in wage determination. Section 6.3 reviews international developments in industrial relations and wage bargaining. This shows that in most EU countries falling union density has not been associated with a decline in collective bargaining; multi-employer bargaining at sectoral level remains the dominant pattern. However, it is also clear that it is rare for all bargaining to take place at one level, and most bargaining systems can now be characterised as multi-level negotiations. A most important development has been the emergence of 'social pacts' in many EU countries, similar to Ireland's social partnership programmes. Since a system of 'co-ordinated decentralisation' has emerged in many countries, Section 6.3 describes three examples of this—in Norway, Denmark and the Netherlands—that may have relevance for Ireland.

Section 6.4 identifies developments in wages and competitiveness in Ireland. This reveals steady growth of earnings and wages over the past decade and strong growth in recent years. When this is combined with an analysis of productivity trends and levels, it reveals a sharp deterioration of Ireland's cost competitiveness in recent years. This section finishes with a discussion of the shares of wages and profits in national output, distinguishing between high-technology foreign-owned sectors and the rest of the economy. Section 6.5 reviews wage determination and organisation in the Irish public sector. Section 6.6 identifies the options for Ireland.

6.2 ANALYTICAL APPROACHES TO THE STUDY OF WAGE BARGAINING

6.2.1 The Council's Approach

In its previous *Strategy* reports the Council has undertaken a detailed review of the analytical foundations of different wage bargaining systems (NESC, 1996a, 1999). Those reviews outlined the famous Calmfors and Driffill hypothesis: that extremely centralised and extremely decentralised wage bargaining systems were superior to intermediately centralised systems (Calmfors and Driffill, 1988). Attention was drawn to the argument that centralisation/decentralisation may be less important than co-ordination and encompassing agreements. It was also emphasised that a highly co-ordinated approach to wage bargaining is successful only where it combines strong institutions (necessary to give discipline and achieve encompassingness) with mechanisms that require organisations to come to terms with market forces (such as an independent central bank, export competitiveness, company-level institutions, appropriate relations between companies and the state). Most important of all, the Council drew attention to economic analysis which suggests that the centralisation or decentralisation of the bargaining structure may be less important than the approach which unions and employers adopt. The Calmfors-Driffil hypothesis shows the superiority of centralised bargaining, on the assumption that parties adopt a non-co-operative approach. Research by

Rowthorn suggested that if even a moderate degree of altruism is introduced—motivated by consideration of long-term, rather than immediate, self-interest and by social responsibility—then either fully centralised or moderately centralised may yield low unemployment and inflation (Rowthorn, 1992). The real difference between centralised and moderately fragmented bargaining structures may be their vulnerability to shocks. While a co-operative mood of play can produce good results with any bargaining structure, in the face of major shocks the parties may revert to less co-operative forms of behaviour which, in systems with weak co-ordination, can have serious consequences. This research takes some of the emphasis off the centralised/decentralised bargaining structure and places it instead on the degree to which unions pursue a wider national interest and their own long-term self interest. The Council concluded "the Irish experience suggests that such a co-operative mood of play is, in turn, shaped by the existence of a wide-ranging national programme which aligns economic actors to a particular policy approach and provides trade union members with guarantees on non-wage issues, such as taxation and social provision" (NESC, 1996a: 102).

6.2.2 The Benefits of Co-ordinated Wage Bargaining

From the international experience of wage bargaining, it is possible to identify three main arguments favouring co-ordinated wage bargaining. The first relates to unemployment, the second to shocks, the third to monetary union.

Unemployment

Several empirical studies have examined the relationship between bargaining co-ordination and unemployment (controlling for other factors) (see Calmfors *et al.* (2001) for an overview). Broadly speaking, half of the studies found that both fully decentralised and highly centralised bargaining systems were associated with a lower level of unemployment than intermediate bargaining systems. Incentives for wage moderation are strong at both low and high levels of co-ordination, because of the competition between firms (and the threat of job losses) in the first case, and the internalisation of externalities associated with wage increases (such as higher inflation and unemployment) in the second case. The other half of these studies found that more co-ordination always led to lower unemployment.

These studies suggest that a move over the long run from highly co-ordinated bargaining (as in Ireland, since 1987) to decentralisation would mean substantially higher unemployment, everything else constant. But everything else is not constant. Increased international competition may reduce the connection between intermediate co-ordination, since more intense competition means that wage bargainers at industry level will place higher weight on the risk of losing market share to foreign competitors. However, where international product market competition is absent (as in the public service), it would seem foolish to disconnect wage bargaining from national structures of formal or informal wage co-ordination.

Responsiveness to Shocks

There are a number of reasons as to why wage co-ordination can facilitate nominal wage flexibility when required in response to shocks. First, there is the social fairness argument made by Keynes: workers will resist nominal wage cuts, unless all wages can be cut simultaneously. Second, co-ordinated wage bargaining facilitates the synchronisation of wage deals. The absence of such synchronisation can be an obstacle to the adjustment of money wages in a decentralised system.

A recent empirical study by Thomas (2001) found evidence supporting the link between wage co-ordination and nominal wage responsiveness. This study found that the responsiveness of nominal wages to unemployment has decreased in countries that moved from high to intermediate bargaining co-ordination (such as, Finland, Spain or Sweden) while it has increased in countries that have moved in the direction of more co-ordination (Norway and Italy).

Monetary Union

If an asymmetric shock were to happen under monetary union, the 'one size fits all' monetary policy requires more flexibility (meaning rapid adjustment) in the deployment of other policy instruments. Fiscal policy is a possible response to divergent cyclical developments among the euro countries but is unlikely to be sufficient in itself to achieve stabilisation (and may be used to accentuate cycles). Hence, it is likely that *extra* or early wage restraint through co-ordinated policies may *come to be seen* as a necessary means of stabilising the economy. Even the desire to avoid the risk that occasional wage hikes occur 'by accident', the fiscal and employment consequences of which would be more difficult to handle in the EMU than earlier, could be a reason for precautionary policies. This would seem very relevant in the case of Ireland. It can be further argued that it will be much easier to achieve co-ordinated wage restraint when it is needed in times of crisis, if there is a degree of co-ordination also in more normal times.

The development of 'buffer funds' in Finland is a recent example of the use of bargaining co-ordination to facilitate adjustment in the new monetary context. These buffer funds consist of additional employer social security contributions in the upswing of the business cycle. The buffer funds are to be spent in recessions in order to prevent contributions from then having to be raised. These funds are controlled by the central labour market organisations. Sweden is considering a more ambitions system whereby there would be *ex-ante* arrangements in place to provide (in defined circumstances) cuts in money wage costs, without having to cut money wages.

In Ireland a number of proposals have been made for new mechanisms that could improve the ability of the economy to adjust to shocks and divergence between actual and expected outcomes. MacCoille and McCoy (2001) proposed that in a national agreement, the desired element of flexibility could be incorporated as an additional term. This more flexible term would be conditional on a range of *ex-post* outcomes in the economy over a range of variables. This proposal has merit, but there is a trade-off to consider between making pay increases more flexible and introducing overly complex formulas that may be difficult to understand and hence lack widespread support.

6.2.3 The Relation between Wage Bargaining and Monetary Regime

Within the analytical literature, a revised view is emerging of how wage bargaining works in European countries and how it can best be organised to achieve competitiveness, low inflation and employment. The starting point of this revision is the Calmfors-Driffill analysis of centralised and decentralised bargaining cited above and used by NESC in previous *Strategy* reports—an analysis which suggested that centralised bargaining or fully-decentralised bargaining were superior, in terms of unemployment and inflation, to industry-level bargaining. Iversen argues that this analysis takes insufficient account of the interaction between wage bargaining and the monetary/exchange rate regime in place (Iversen, 1999). He suggests that the economic effects of three different models of wage bargaining—fully decentralised, intermediately centralised or centralised—depend on whether government adopts an accommodating or non-accommodating monetary/exchange rate policy. This brings together two important fields of economic analysis which have, to date, been separate: the study of wage bargaining and the recently developed literature on central bank independence.

Iverson argues that there are two approaches to wage bargaining and monetary policy which are particularly conducive to low unemployment and strong economic performance:

(A) Intermediately centralised (industry or sector-level) wage bargaining combined with a non-accommodating monetary regime; and

(B) Centralised wage bargaining combined with an accommodating monetary regime.

The third approach to wage bargaining (C)—decentralised, firm-level, bargaining—can be combined with either an accommodating or non-accommodating monetary policy. It can produce low levels of unemployment, with high levels of wage inequality, but not as low a level of unemployment as can be achieved with other approaches to wage bargaining[1].

1. Iversen's analysis of decentralised bargaining differs from that of Calmfors and Driffill in allowing that firm-level bargaining can create wage push effects

This argument clearly involves a significant revision of Calmfors and Drifill's influential analysis of the advantages of centralised over intermediate-level and decentralised bargaining. This might suggest that most European countries can choose between A and B. A few European countries, such as the UK, have chosen C. However, Iversen then argues that a number of international developments have weakened the foundations of model B, centralised bargaining with an accommodating monetary policy. This model has become less feasible because:

- New flexible technologies and production techniques require more varied reward systems and greater inter-occupational wage flexibility;
- International capital mobility has made discretionary accommodating monetary policy less effective;
- The increased importance of service-sector employment means that fully centralised bargaining, with a compression of wage differences, will tend to restrict the growth of private services; and
- Fiscal pressure on governments limits their ability to secure full employment through the expansion of public services.

Consequently, Iversen says that his analytical and empirical analysis 'point to the possibility that intermediately centralised systems outperform all others if combined with an independent central bank' (Iversen, 1999: 71). Indeed, a significant number of countries have moved towards A, industry-level bargaining with a non-accommodating monetary regime. The accession of more and more countries to the ERM and EMU can be seen as evidence of the difficulty of operating an independent monetary policy. The move of a number of countries from fully centralised bargaining to industry-level or sector-level bargaining is seen as evidence that this is the best approach to combine with a tight monetary policy (see Section 6.3 below).

that yields unemployment. In contrast to their model, his theory allows there to be externalities of unemployment (see Iversen, 1999: 25-6).

6.3 DEVELOPMENTS IN EUROPEAN INDUSTRIAL RELATIONS AND WAGE BARGAINING[2]

6.3.1 Recent Trends in Unionisation, Militancy and Bargaining

In 1991, the OECD published a survey of trends in union membership during the 1970s and 1980s (Visser, 1991). One of its main conclusions was that in most industrialised market economies the post-war expansion of trade unions had turned into decline. On the basis of newer data, covering the 1990s, this conclusion can be confirmed: 1980 marked a reversal of the post-war trend of union growth in almost all European economies (Ebbinghaus and Visser, 2000). In total, European unions lost almost eight million members in two decades, nearly one-fifth of their combined membership in 1980. The (standardised) union density rate, calculated by taking the employed union members as a proportion of the employed dependent labour force, dropped by six points, from 37.6 to 31.9 per cent (Table 6.1), between the 1980s and the 1990s.

Cross-national differences in union density are very large and there is no evidence of convergence. The divergence in union density in Western Europe and in the OECD area—as measured by the coefficient of variation—has increased. Persistent and increasing cross-national differences in unionisation are *prima facia* evidence that union membership decisions must be seen in the context of institutions specific to *national* labour markets (Ebbinghaus and Visser, 1999).

Analysis suggests that the downward trend in unionisation is related to the rise in unemployment and to structural changes in labour market participation and employment, bringing in groups with a lower propensity to unionise (service workers, workers finding employment in small firms) and groups that go into non-standard employment (Calmfors *et al*., 2001; Checchi and Visser, 2001; Western, 1997). Another main finding is that unionisation trends in

2. This review of European industrial relations and wage bargaining was prepared by Professor Jelle Visser of the Amsterdam School for Social Science research. The interpretation of trends and development is that of Professor Visser.

TABLE 6.1

Union membership, density, and militancy, 1980s and 1990s

	Members (change in '000s)				Union density (%)			Militancy (volume)		
	1980-'89		1990-'98		1980-'89	1990-'98	trend	1983-'89	1990-'99	trend
Sweden	326	10.8%	-295	-8.9%	80.0	85.0	+	177	51	–
Finland	200	15.0%	-65	-4.3%	69.9	77.3	+	413	184	–
Denmark	147	9.2%	65	3.7%	77.8	76.3		165	180	+
Norway	92	9.9%	166	16.1%	57.5	58.1		92	86	
Belgium	-157	-9.6%	72	4.7%	50.9	52.7		22	32	+
Austria	-68	-4.7%	-150	-10.9%	52.1	42.1	–	2	4	
Germany (*)	-240	-2.9%	-3,643	-30.4%	34.2	30.4	–	26	12	–
Switzerland	45	-5.3%	-55	-6.7%	28.9	23.8	–	1	1	
Netherlands	-213	-14.0%	170	12.6%	28.8	24.2	–	15	23	+
Ireland	-62	-12.6%	27	6.0%	55.0	47.8	–	346	105	–
UK	-2,510	-21.5%	-1,932	-21.6%	46.1	34.4	–	337	32	–
Italy (**)	-1,233	-17.2%	-716	-11.9%	44.0	38.8	–	493	129	–
France	1,274	-38.8%	-18	-0.9%	14.7	10.1	–	76	36	–
Spain	-191	-16.2%	581	51.9%	10.5	17.3	+	691	351	–
Portugal	-450	-29.0%	-200	-20.0%	46.1	26.4	–	n.a.	n.a.	
West-Europe	-5,677	-12.4%	-2,039	-5.1%	37.6	31.9		218	66	–

Source: *Membership:* Ebbinghaus, B. and J. Visser (2000), *Trade Unions in Western Europe Since 1945*, London: Macmillan.

Union Density rates: Ebbinghaus and Visser, (2000) and OECD, *Labour Force Statistics,* Paris, for employment data.

Militancy: ILO, *Yearbook of Labour Statistics*, Geneva (own calculations).

Notes: (*) only West Germany until 1989; (**) without unknown membership of independent unions.

Membership: 'paying members' in employment, without unemployed, retired and self-employed members, in thousands; averages for 1980-1989, and 1990-1998.

Union density rates: membership as a percentage of wage and salary earners in employment, averages for 1980-1989, and 1990-1998.

Militancy: working days lost due to strikes and lockouts, per 1,000 employees; averages for 1980-1989, and 1990-1998.

the private and public sector have further diverged. On average, more than half of Europe's public sector employees are unionised, compared to less than a quarter of private sector employees. In many countries (e.g., Germany, Austria, Switzerland, the Netherlands, the UK, France and Portugal) the differences are three to one, or larger. The higher density rate in public and subsidised services has contributed to the advance of women in unions, since women make up an increasing share of employment in these sectors.

Worker Militancy

The downward trend in union membership is paralleled by the decline in worker militancy, measured as working days lost due to industrial conflicts, per thousand workers (Table 6.1). The same causes—unemployment; fiercer international market competition; structural changes in labour markets, declining share of mining and manufacturing—lie behind this trend. Strike data by industry (number of strikes, their length and size) show that the decline in militancy was significantly stronger in the private sector and that levels of militancy are now higher in the public sector. As in the case of union density, the large cross-national differences suggest the importance of institutional factors. There is little correlation between levels of union organisation and militancy. Unions may have access to other weapons other than strike action, like the referendum (e.g., Switzerland), or to be able to exert pressure through political (e.g., Italy, Portugal or Belgium) and corporatist (e.g., Austria, the Netherlands or Norway) channels.

Coverage of Collective Bargaining

There is a large discrepancy between union density and bargaining coverage, defined as the number of employees covered by collective agreements divided by the total number of employed wage and salary earners. On average, three out of four workers in Europe are covered by collective agreements negotiated by trade unions, whereas only one in three is member of a union (see Table 6.2). This 'excess coverage' serves to uphold union influence despite falling membership rates, but might represent a serious long-term risk, as the legitimacy of unions and union-negotiated agreements may come to be questioned.

TABLE 6.2

Collective bargaining coverage, centralisation, and co-ordination, 1980s and 1990s

	Bargaining coverage			Level(s) of bargaining			Intra-union coordination		Intra-employer coordination		Bi- or tripartite co-operation	
	'85	'95	trend	'83-'89	'90-'99	trend	'83-'89	'90-'98	'83-'89	trend	'83-'89	'90-'99
Sweden	n.a.	89	?	(1)-2-(3)	2-(3)	-	M-H	M	M	M-L	some	failed/ some
Finland	95	95		(1)-2-(3)	(1)-2-(3)		M-H	H	M	M	some	yes
Denmark	74	69	-	(1)-2-(3)	2-3	-	M	M-L	M-L	M	some	some
Norway	70	70	?	1-(2)-(3)	1-(2)-(3)		H	M-H	H	H	some	yes
Belgium	90	90		1-(2)-(3)	1-(2)-(3)		M	M-L	M-L	M-L	some	failed/ some
Austria	n.a.	99		2	2-(3)	-	H	H	H	H	yes	yes
Germany	90	92	?	2	2-(3)	-	M	M-L	M-H	M	some	failed/ some
Switzerland	53	37	-	2-(3)	(2)-3	-	M-L	M-L	M	M-L	some	some
Netherlands	78	83	+	(1)-2	(1)-2-(3)	-	H	M-H	M-H	M	yes	yes
Ireland	n.a.	n.a.	?	3	1-3	+	M-L	M-H	L	M	no/yes	yes
UK	64	40	–	(2)-3	3	-	L	L	L	L	no	no
Italy	85	82	-	2/3	2-(3)	+	L	M	L-M	L-M	no	yes/?
France	85	95	+	2/3	(2)-3	-	L	L	L-M	L-M	no	failed
Spain	70	78	+	2-3	2-3		L	M	M	M	yes/no	some
Portugal	78	71	-	2?	(1)-2?	+	L	L	M	M	no	yes

Source: *Standarised bargaining coverage rates:* Ochel, W. (2001), "Collective Bargaining Coverage in the OECD from the 1960s to the 1990s", Munich: Institute for Economic Research, except for Switzerland, see, Fluder, R. and B. Holz-Hart (1998), "Switzerland: Still as Smooth as Clockwork?", in A. Ferner and R. Hyman (eds), *Changing Industrial Relations in Europe*, Oxford: Blackwell, and Prince, J-C. (1994), *L'impact des conventions collectives de travail en Suisse*, Zürich: Schulthess.
Other variables: own scores (see text).

Notes: *Standardised bargaining coverage rates:* employees covered by collective agreements as a percentage of wage and salary earners, excluding workers barred from legal bargaining rights.

Levels of bargaining: level at which bargaining usually takes place; 1=central

bargaining; 2=industry or sectoral bargaining; 3=single employer, company, enterprise or plant bargaining; between brackets=unstable, occasional or dominated.
Intra-union coordination: Relative membership size of the main bargaining co-ordinator or unit (main confederation, or wage leading union, whichever applies) and degree of rivalry from contesting organisations or union agents with regard to norm-setting in wage bargaining. H=high; M-H=medium to high; M=medium; M-L=medium to low; L=low.
Intra-employer coordination: Relative membership size of the main bargaining co-ordinator or unit (main confederation, or industry federation, whichever applies) and degree of rivalry from contesting organisations or companies with regard to internal norm setting in wage bargaining. H=high; M-H=medium to high; M=medium; M-L=medium to low; L=low.
Inter-agency co-operation: Degree of co-operation between union and employer (peak) organisations (at the national or macro-level), with or without the government, as shown in a regular practice of concertation and social pacts.

On the basis of the data on coverage trends, shown in Table 6.2, there is no evidence of a decline in collective bargaining, contrary to the trend in union density. There appears in fact to be no relation between the level or trend of unionisation and the degree of bargaining coverage. The main exception in Europe is the United Kingdom, where the decline in bargaining coverage and union density appear to go hand in hand (Milner 1995)[3].

Multi-Employer Bargaining Still the Dominant Pattern

Since the 1940s, *multi-employer* bargaining had been the dominant type of wage setting in Western Europe. In all cases, including Britain and Ireland, bargaining patterns are quite distinct from the single-company bargaining patterns found in the United States and post-war Japan. As can be seen from Table 6.2, sectoral bargaining is still the dominant pattern in Europe today, though it is rare that all bargaining occurs at one level. Instead, most bargaining systems are characterised by *multi-level* negotiations. The two major exceptions are the UK, where multi-employer bargaining has disappeared in

3. The UK highlights two important conditions of high bargaining coverage: multi-employer bargaining leading to national or industry agreements which applied to all workers in the bargaining domain; and provisions for extending or enlarging the contract, through public intervention or organised pressure, to non-organised (Traxler, 1994).

nearly all sectors, and France, where company or enterprise bargaining over wages and working hours is of greater importance than sectoral or national bargaining. In Denmark, Sweden, Austria, Germany, the Netherlands and Italy (since 1993) sectoral bargaining is or has become dominant; in Portugal and Spain more intermittently so. In Finland, Ireland, Norway and Portugal central agreements incorporate wage guidelines; in Austria, peak associations influence the timing of negotiations; in the Netherlands targets are set through co-ordination within and among the confederations; in Belgium, legal prescriptions set tight norms for bargaining outcomes of central-level negotiators.

The 1980s was marked by a general and powerful thrust towards decentralisation, which was especially evident in the UK, but also in Sweden, the country that had long given primacy to centralised wage bargaining in pursuit of wage solidarity policies. France, Italy and Britain returned to decentralised bargaining, after unsuccessful experiments with concerted policies in the 1970s. Other countries where central level bargaining was ended in the 1980s included Denmark (1983), Ireland (1981) and Spain (1986). Nor did countries in which central-level negotiations or consultations continued in one way or another (Austria, Belgium, Norway, Finland, the Netherlands) seem immune to the decentralisation process. 'Softer' peak-level guidance (Austria, the Netherlands) or, where it failed, state intervention (Belgium 1981-85; Norway 1987-89) became more important. Some centralising policies, like a general (across-the-board) indexation of wages to consumer price inflation, which had become common in Europe from the mid-1960s, were reduced (Belgium after 1981; Italy after 1983-84) or ended (Denmark and the Netherlands in 1983, Italy in 1992; Sweden in 1993). Another decentralising thrust came from increased differentiation across sectors and the disconnection of public sector pay setting from wage bargaining in the private sector (Denmark, the Netherlands later also in Sweden and Italy).

Social Pacts

At first sight, the 1990s seems to have brought a reversal of the trend to decentralisation as a result of the increasing occurrence of national agreements and tripartite social pacts, formally, as in Ireland (five multi-annual pacts between 1987-2002), Italy (1992, 1993, 1995, 1996-97, 1998), Finland (1991-92, 1996-97, 1998-99, 2001), Norway (1993-1997, 2000), Portugal (1990, 1996, 1997-99), Spain (1996, 1997) and Greece (1997), or informally and on a more continuous basis, as in Austria and the Netherlands (Fajertag and Pochet, eds, 1997; 2000). Failed attempts included Belgium (1993, 1996), Germany (1996), France (1995-97), (Hassel, 2001). These agreements and pacts often involve the government and are typically intended to promote wage moderation and labour market and social policy reforms for the purpose of restoring competitiveness to the national economy and securing the participation in a hard currency regime (Ebinghaus and Hassel, 2000). Many of the successful pacts were negotiated in the 'peripheral' EU member states, outside the d-mark zone, in order to ensure membership of EMU 1999 (Pochet, 1999; Streeck, 1998).

The social pacts of the 1990s differ from the income policies of the 1970s and early 1980s (Regini, 1997). Rather than a 'political exchange', in which unions forego wage increases in exchange for increased public sector expenditure, compensating social policies and increased employment protection rights (the typical content of the 1970s social contracts), the recent pacts aim at *less* wage growth, *less* public sector growth, *less* costly social policies, and *less* employment protection, for some greater good in the future, like membership of EMU and macroeconomic stability as a condition for investment and employment growth, or a more employment-friendly welfare state. The incomes policies of the 1970s were without exception centralising, relocating decision-making power within labour market actors to higher levels, and usually brought in the state (Elvander, 1974; Flanagan *et al*., 1983). This happened everywhere except in Austria, Germany, Switzerland and Sweden, the four main countries where state intervention in collective pay bargaining is anathema. Income policies broke down because they overrated the taste for, or capacity of, centralisation in unions or employers' associations, and the capacity of states to foot the bill of increasingly expensive social or industrial policies.

The current social pacts across Europe are attempts to improve co-ordination, both among labour market actors and between private (wage, productivity) and public (monetary, fiscal) policies. In order to do so successfully, and continue doing so, central organisations need to have the co-operation and resources from their members (individuals, companies, member-organisations), and they must learn to trust each other (Visser, 1998a). When successful, social pacts do establish or influence mutual expectations and norms concerning the bargaining conduct of unions and firms, or the budgetary and fiscal policies of governments. In so doing, they do not formally constrain industry-level or company-level negotiations, nor do they prevent firms from designing different pay-systems and incentive structures (Regini, 1997). In this sense the Belgian income policies of the 1990s (Arq and Pochet, 2000; Hemerijck, Unger and Visser, 2000) and the Irish pacts appear exceptional, though in the two most recent pacts in Ireland incomes policies have become more loosely defined (O'Donnell and O'Reardon, 2000; Hardiman, 2000). Also, the Norwegian and Finnish agreements on incomes policies are exceptional insofar as they define the boundaries of legal industrial action in lower-level bargaining. This has no counterpart in the central agreements or accords that have been concluded between confederations in the Netherlands, since these do not constitute any legally binding text or commitment (Visser, 1998b).

Beginning with the Wassenaar agreement of 1982, the Dutch central agreements may be typical for the new trend in social pacts. They substitute informal consensual norms, moral suasion and inter-agency trust-building for formal centralisation of wage bargaining, in a situation when the general development towards lower-level bargaining has made centralisation unlikely. Through their impact on norms and expectations, these pacts do exert influence on the overall wage dynamics (moderation, long-term stability), while leaving the task of determining relative wage levels to decentralised negotiations. In the Dutch case, the successive central agreements increased the confidence of unions and employers in each other, increased their autonomy in wage-setting against the interference of the state, and have encouraged unions and employers to take further steps in decentralisation, below the level of industry bargaining (Hemerijck, Van der Meer and Visser, 2000). Traxler (1995) has labelled this development—"organised decentralisation", contrasting it with the "unorganised decentralisation" of collective bargaining found in Britain, the US or New Zealand[4].

Thus, what at first sight appeared to be a reversal of trends is in many respects a continuation of decentralisation, but with an important supplement: the realisation that, firstly, a certain measure of co-ordination is necessary to ensure that decentralisation is efficient; and, secondly, that bargaining outcomes and processes can improve when embedded in a process of social dialogue (Visser, 2001). The first point is related to what has been called the "hold-up problem" in bargaining (MacLoad and Malcomson, 1993), the second point to the dilemma faced by negotiators who must decide between a superior course of action and the distribution of costs and benefits (Scharpf, 1989).

Renegotiating contracts is costly, because they undermine the incentives for investment. Bargaining over the returns on investment after the investment is made places the investor in a disadvantaged position. If individual workers and firms delegate bargaining to outside institutions and cannot influence the result, this "hold-up" problem is minimised. The delegation of the right to adjust wage increases (not levels) to external agents breaks the linkage between the level of specific investments and bargaining power (Teulings and Hartog, 1998: 83). The empirical correlate is that non-market conforming wage differentials related to sector, firm size or tenure, which do not contribute to efficiency, tend to be larger under decentralised bargaining (Teulings and Hartog, 1998: 299). Company bargaining under control of the external union tends to suppress local rent sharing whereas unrestrained local unions encourage it. They "are drawn into this strategy as a moth towards the flame that would burn it" (p. 303).

Social dialogue, involving public and private actors, can be defined

4. Other examples of organised decentralisation include Austria (Auer and Welte, 2001; Blaschke and Traxler, 1998) and Denmark (Due *et al.* 1994, 1997; Scheuer, 1997).

as a process in which actors inform each other of their intentions and capacities, elaborate and exchange information provided to them, and clarify and explain their assumptions and expectations. This is not the same as bargaining, but provides a setting for more efficient bargaining by helping to separate the digestion of facts, problems and possible solutions from negotiating feasible courses of action and the distribution of costs and benefits (Visser, 1998a).

Recent developments in a number of countries are interesting, given the apparent underlying trend towards a more decentralised approach to wage bargaining. The Dutch government and the social partners have reached a new social agreement for 2003. For the first time in a decade, this new agreement includes a centrally agreed pay limit (2.5 per cent for 2003). The new agreement includes provision for tax and social security contributions. In Germany, the partners have negotiated a new agreement on pay across the public sector. There is evidence of a move to social pacts in Poland, Slovenia and Hungary.[5] It is too early to say whether these developments herald a new era of centrally negotiated wage settlements or whether the pressures for decentralisation will make themselves felt again.

Multi-level Bargaining, Wage Drift and Peace Obligations

In the Nordic countries local (company) bargaining is common during the currency of a central or industry agreement. These negotiations account for about half of the total wage increases (Calmfors, 1990; Elvander, 1990). Such proportions for local wage drift or local wage increases are not uncommon and need not be inefficient (Teulings and Hartog, 1998; Høgsnes and Longva, 2001); part is due to individual employers' attempts to adjust to market conditions or to set efficiency wages. In Norway, for instance, it has been shown that central bargainers have been able to anticipate the overall amount of drift and take this into account when setting the national norm (Rødseth and Holden, 1990). In other words, if worked to perfection, such a two-level bargaining model operates on either side of the 'hump' of the Calmfors-Driffill

5. http://www.eiro.eurofound.ie/2002/12/Feature/SI0212101F.html; http://www.eiro.eurofound.ie/2002/12/Feature/HU0212105F.html

(1988) curve, combining the advantages of centralisation and decentralisation. But for this beneficial outcome to occur it is essential that “the different levels are integrated so as to prevent them from mutually blocking their respective purpose” (Traxler 1994: 174).

A characteristic of local bargaining in the Nordic countries is that, with a central agreement in force, it takes place under a peace obligation. A similar condition applies to local bargaining in Germany, Austria, Switzerland, the Netherlands and Belgium. Collective agreements in these countries create rights and obligations both for the signing organisations and for their members. Whether strikes nonetheless occur, depends on the effectiveness of mediation procedures, inter-union rivalry and the tolerance of the unions for (short) strikes. Finland was long the ‘Nordic exception’ to peaceful industrial relations because of the political fragmentation of the union movement (Lilja, 1992). Norway appears least tolerant to strikes and is one of the few industrialised countries with compulsory conflict mediation (which is, under the rules of the ILO, only allowed in ‘essential services’). More important, probably, as a method to restrain maverick unions and employers, is the possibility, as exists in Denmark, of ending industrial conflicts by a single mediation procedure for the entire private (or public) sector, empowering the mediator to treat several settlements as one entity in the ballot (Elvander, 2000). Votes among union members over such proposals are typically aggregated across firms and sectors. This is a strong centralising element in an otherwise decentralised system of wage setting like for instance the Danish one.

In Table 6.1 we observe, however, that more working days are lost due to industrial conflicts in the Nordic countries and in Southern Europe than in Germany, Austria, Switzerland, and the Benelux countries. The reason may be that supplementary local bargaining in the latter countries is recent, less widespread and more subdued. Trade unions tend to defend their prerogative in wage negotiations against the mandatory works councils. Not having their own representative bodies in the workplace (with the exception of Belgium), unions in these countries must rely on works council members who depend on the entire workforce for re-election. This has made the trade unions in these countries half-hearted advocates of company bargaining even at the best of times.

Thus, the recent openings in industry agreements towards supplementary bargaining on working-time and pay issues in the 1997-2000 pay rounds in Austria, and since the New Course agreement of 1993 in the Netherlands, have been used only up to a point. In their survey of managers and staff, Auer and Welte (2001) found that many works councils in Austria were ill prepared for, or had great difficulties legitimising, lower wage increases than were considered standard for the industry. This may have been one of the reasons why employers, who advocate more flexibility and variable pay, were reluctant to make the works council rather than the external union their new partner in local bargaining. A similar reluctance, against local pay bargaining and involvement of the works councils, is found among Dutch employers (Teulings and Hartog, 1998). Dutch employers want more decentralisation because they believe that they need more flexibility, but they want to keep the union on board so as to not to endanger the precious low levels of conflict to which they are accustomed. Dutch unions, acknowledging the diversity among their (potential) members, are open to experiments with individualised bargaining over working time and pay, within the framework of so-called '*a la carte*' agreements, providing different menus from which individual workers can choose.

6.3.2 Some Examples of Co-ordinated Decentralisation

Norway

Norwegian researchers have argued that the 'renaissance of corporatist incomes policy in Norway' is the answer to the specific problem of containment of cost pressures in the oil industry in an economy in which domestic sectors, in particular public services, are the main employers. It can be argued that oil is to Norway what foreign direct investment from the US is to Ireland. It makes Norway both rich and vulnerable, given the strongly fluctuating oil prices and a large-sized public sector partly depending on oil revenues. Responsible wage setting is extremely difficult under these circumstances.

In the mid-1980s, following a sharp drop in oil prices, Norway found itself in deep economic trouble. After zero wage increases in 1987, followed by severe restrictions in 1988 and 1989, imposed by law, but with the cooperation of the central organisations, the government and the social partners launched a new policy (the so-called 'Solidarity Alternative') in 1993, based on recommendations of a government appointed committee in 1991. A five-year pact was to ensure the continuation of a strategy of wage moderation, combined with ambitious goals concerning competitiveness, productivity growth, lower unemployment and healthy public finances. The pact was successful; the unemployment target of 4 per cent, for instance, was reached long before the pact expired. But the very success of the pact made it impossible to agree on its renewal. Conflicting principles of 'equal pay' and a 'fair wage distribution' within the union movement, especially in the public sector and embodied in unaffiliated trade unions (over which the Norwegian Federation of Labour has little or no authority), appear to be major stumbling blocks (Dølvik and Stokland, 1992).

In Norway, collective agreements are renewed every second year, usually by way of central agreement and often with the support, or under threat of, the state (Norwegian employers still resist the decentralising trend among their counterparts in Sweden and Denmark; state intervention in wage formation is common in Norway, just as it is unthinkable in Sweden). But half of the total wage increases are negotiated at the local level. Such 'drift', which is not uncommon in multi-level bargaining (similar figures exist for Austria, Sweden or the Netherlands), is the outcome either of local bargaining or of individual employers' attempts to adjust to market conditions or to set efficiency wages. Local drift includes all changes related to job mobility and career development, and appears to be anticipated by the central negotiators. In other words, the interpretation that local drift undermines the central agreement is unwarranted. The flexibility of local bargaining makes central agreements possible, and central agreements contain the inflationary pressure of the oil sector from spreading across the economy. In other words, if worked to perfection, such a two-level bargaining model operates on either side of the ‘hump’ of the Calmfors-Driffill curve, combining the advantages of centralisation and decentralisation.

Central negotiations are almost inevitably dominated by a specific social agenda in addition to concerns for competitiveness and price stability, which means that special attention must be paid to low-wage employees and the goal of wage equalisation. Dissatisfaction from insiders who then defend their relative advantage with superior strike power is undoubtedly a potential threat. However, when there is a second bargaining round, or some covert adjustment in the firm, insiders need not worry too much about the central agreement and accept moderation as well as egalitarian outcomes (Høgsnes and Longva, 2001: 153).

In the public sector the Norwegian story is more complicated. Here, wage determination takes place in three different arenas. First, there are the main central negotiations, which follow the settlements in private industry. Next, there are ‘central adjustment’ negotiations. These negotiations focus on which occupations or sectors deserve extra wage increments given the outcome of the central wage settlement, labour shortages and past wage developments. The amount of money set aside for these negotiations, as well as for local negotiations, is agreed upon in conjunction with the main central negotiations. Unlike adjustment negotiations (which have a long tradition in Norway), *local* negotiations are a more recent element in the public sector. In addition to inter-union strife over wage distribution principles, the absence of objective principles for ‘ability to pay’ and of reliable measures of productivity among various groups of employees makes such conflicts more acute than in the private sector. Pay rises for skilled workers, in scarce supply, tend to be contagious, especially in the public sector, because employers cannot appeal to highly visible market signals to legitimate wage differentials. Nor is it easy to design schemes for gainsharing or introduce profit-related schemes in the public sector (but some innovative schemes in the Dutch public sector have linked pay incentive schemes to better services, greater client satisfaction, fewer complaints, etc.).

In the case of Norway, as in the Netherlands, it has been shown that, compared to earlier decades, the central union leadership finds it easier to advocate wage moderation, thanks to moderate decentralisation and flexibility combined with continued security. The key issue, then, is to create legitimacy for more flexible employment and wage policies in the public sector. Sectoral differentiation and a clear definition of employer responsibilities in the public sector, distinct from the government or the Finance Ministry, may constitute a necessary step on that road.

Denmark

Until the 1980s, the determination of wages in Denmark was marked by two central institutional features: (1) an extensive system of indexation linking nominal wage changes to changes in consumer prices; and (2) central negotiation of real increases of basic wage rates, combined with local bargaining and significant wage drift. With accelerating inflation, indexation payments represented a growing proportion of wage increases during the 1970s and the government's incomes-policy activity came to be focused on possible alterations, and finally, in the 1980s, the suspension of indexation arrangements. Moreover, after 1983 public sector employees could no longer expect automatic increases in their wages in parallel with growth of private sector wages.

All this is very comparable to the combination of policies (hard currency policy, tight fiscal policies, de-coupling of public and provide sector wages, wage moderation, and suspension of the indexation mechanism) that were adopted around that time in the Netherlands, after a troublesome trajectory of frequent but not very effective state interventions in wage bargaining, amidst rising unemployment, soaring public deficits, and a general loss of competitiveness (Visser and Hemerijck, 1997).

The Danish trade union federation LO (like its Swedish sister organisation) had been strongly oriented towards an egalitarian or 'solidaristic' wage policy. This was in tune with the preferences of its largest affiliate, the union of unskilled workers and the woman workers' union. The craft unions (in metal engineering) were usually able to restore their relative pay through compensatory movements in wage drift. Throughout the 1970s wage drift had accounted for more than 40 per cent of earnings growth. That a significant element of earnings emanated from unauthorised local bargaining eroded the standing of the central federations as a source of regulation. For employers, drift created an element of uncertainty in the development of labour costs once a central agreement had been signed; it was bound to lead to doubts as to whether one ought to continue negotiating central agreements that did not stick. Nevertheless, some wage drift may be unavoidable, as was shown in the case of Norway[6].

The Danish Parliament intervened and imposed a settlement in the wage bargaining rounds of 1975, 1977, 1979, 1985 and 1998. The positive side of such intervention and the rationale for it is that, in the short run, industrial peace is secured and major conflict avoided. There is a downside however. The 'peace obligation' in collective agreements has generally been justified on the grounds that agreements are subject to endorsement by the membership; this legitimacy is lost if settlements are repeatedly imposed by the legislator. Thus, it is argued by many observers that from a long-term perspective, intervention by parliament in collective bargaining must be minimal if the system is to work (Due *et al.*, 1994).

In addition to the rivalry within the union movement, central agreements lost their clout due to the limited authority and coverage

6. Another notorious case is Austria, where relatively centralised bargaining is known to produce considerable levels of wage drift without apparently being a source of great concern. One possible explanation is that the law confines works activities to narrowly defined issues, which must be dealt with in a co-operative manner. Since works councils are not formally authorised to negotiate wage increases, they can only conclude informal, (i.e. legally unenforceable), plant agreements on issues of pay. This somewhat restricts pay drift and makes it reversible, allowing for a relatively flexible adaptation of wages to the business cycle and to company performance. A similar institutional explanation pertains to Germany and the Netherlands.

of the employer federation. After a spell of decentralised bargaining, with higher real wage growth and even more local drift, employers and unions took various steps. In 1987 they signed a 'declaration of intent', jointly with government, in which they undertook to keep Danish wage increases below the level of Denmark's main trading partners. More important, perhaps, was the reorganisation of bargaining jurisdictions, from several hundreds, to some thirty, together with a concentration of employers' associations. Central-level negotiations have entirely stopped and all bargaining takes place sectorally, with additional bargaining in firms. In addition to these shifts in the level of bargaining, there was decentralisation in a further sense: a shift from standard job-related wages to person-related pay by means of the gradual replacement of what in Denmark is called the 'normal wage' by the 'minimum wage' system. Under the normal wage system the standard rates, negotiated at the sectoral or national level, cannot be improved through local bargaining. Under the minimum wage system, only minimum pay levels are regulated through sectoral bargaining[7]. In Denmark, local bargaining takes place more or less on an annual basis, but under a peace obligation, and takes the form of 'pay sum bargaining' over the 'aggregate size of the pay rise for the group of workers represented by the shop steward', leaving it to the management to allocate the award to individuals (Scheuer, 1997). Hence, it remains possible for management to link pay to performance or ability, and for stewards to assert their role despite the fact that the main bargaining process takes place outside the firm. This system is now also gradually making its way into the public sector.

An interesting aspect of the recent bargaining rounds in Denmark is the insertion of so-called 'social chapters' in addition to issues like training, maternity pay, leave systems and flexible working time. Following a proposal of the Public Conciliator, wage negotiations are encouraged "to consider appropriate suggestions to further the employment of persons who due to health problems, reduced working ability or long term absence from the labour market, cannot

7. This was originally the province of craft workers who could negotiate piece rates locally.

be employed in a full-time, normal job". Social chapters are typically not very detailed and are placed on the agenda of local negotiators by the central organisations, the Danish Labour Federation and its counterpart on the employers' side.

Sweden

The case of Sweden also illustrates the trend from central bargaining but also the limits of decentralisation. In the early 1990s, wage bargaining in Sweden remained relatively centralised thanks to the co-ordinating efforts of a government-appointed negotiating group and a coalition of trade unions. Following the troublesome bargaining round of 1995-96, when co-ordination among the unions failed; the industrial employers, confronted with rising wage costs and more conflicts, were ready to break new ground with the unions. In 1997 they signed the Industry Agreement, laying the foundation for a private mediation institute, and a sectoral Economic Council with four independent academic economists. This step has since been imitated in the public sector and became the basis for the new law on statutory conflict mediation in 2000, applying in industries such as building, transport, banking or commerce where unions and employers have thus far failed to create their own institutions. Elvander (1999: 24, 39) judges this the "most important innovation of the rules of the game for bargaining and conflict resolution on the Swedish labour marked since the Basic Agreement of 1938" and "a prerequisite for decentralised wage formation". This episode shows that the Swedish employers in engineering, who had been the strongest opponents of centralised bargaining in the 1980s and had wanted to end all industry bargaining in the 1990s, now realised that the need for industrial peace was stronger than that for flexibility. Another reason why employers did not press for further decentralisation was the wish to maintain control over wage costs. Calmfors (2001) sees the Industry Agreement as part of the preparation for Swedish entry into the EMU.

The Netherlands

There are many parallels between the Danish and Dutch histories of organised decentralisation, following a period of decline and recurrent state intervention in the 1970s and early 1980s. We need therefore not repeat the story here. In the context of a comparison with Ireland, it would seem of greater interest to concentrate on one aspect only: how Dutch collective bargainers have innovated their agenda in the face of part-time employment and new working patterns in dual earning families.

The Netherlands has been characterised as “the only part-time economy of the world, with a finger in the dike of unemployment” (Freeman 1998; Visser, 2002a). The Netherlands enters the 21st century as a “one-and-a-half-job-per-household” economy. This development is the result of recent, and rapid, change. Between 1977 and 1997 the number of one-breadwinner households decreased from 1.9 to 0.9 million, a decline from 51 per cent to 18 per cent of all households. The number of two earner households jumped from 1 to 2.4 million, or nearly half of all households. Households with two full-time jobs (‘double earners’) or two part-time jobs (‘half earners’) remain exceptional, however. The one-and-a-half combination has become most common, both in households with and without children, and is twice as frequent as elsewhere in Europe.

The Netherlands is admired for its ‘employment miracle’ (Auer, 2000; Schmid, 1997; Visser and Hemerijck, 1997). Between 1983 and 1997 the number of jobs increased at a rate of 1.8 per cent per year, four times the EU average. The expansion of part-time work was a strong contributory factor: three-quarters of the two million new jobs since 1983 were part-time jobs. Most of these jobs went to women and the female participation rate (in persons) jumped from 33 per cent in 1975 to 59 per cent in 1998.

Regarding part-time employment, Dutch trade unions initially shared the sceptical view of other European unions. The unions did not want to help to create a secondary and non-unionised job market. During the entire 1980s the union controversy between collective working-time reduction and part-time work continued. The reference group for the collective working hours campaign was the *male breadwinner*, for part-time jobs it was the *working mother*. Only by the end of the decade, when these groups became equally large in the public services, did a compromise solution emerge. In 1990 the main union federation abandoned the norm of the full-time working day and advocated diversity and pluralism combined with a "right to work part-time" for men and women, and equal rights for part-time workers. This was "the harvest of years of investment of women in the union movement" (Grunell, 1997: 101).

The fact that part-time work in the Netherlands is mostly voluntary helps explain the singular position of the Dutch unions in the European union spectrum. In Eurostat surveys, the Netherlands emerges as the country with the lowest share of involuntary part-time work. According to Eurobarometer data, part-time work is evaluated more positively by Dutch women than by their sisters elsewhere in Europe (with the exception of Denmark), as regards contractual status, tenure, perceived career chances, job satisfaction and social security, though on all these aspects part-time jobs attract lower scores than full-time jobs even in the Netherlands.

In a surprisingly brief period of time, the part-time issue has captured a place on the agenda of bargainers (Visser, 2002a). This shows the comparative advantage of co-ordinated bargaining: *if* central organisations agree on a particular agenda, their influence on legislators and on local bargainers is relatively large. Moreover, in the Dutch consultation economy, the central organisations, especially employers, have an incentive to stay ahead of legislation. That way they hope to wield more influence over any regulations that emerge and to demonstrate their importance to member organisations and firms. The social partners jointly argued that the spread of part-time employment should be halted, something that "might happen if part-time work remains concentrated in a limited number of sectors and jobs, or if small part-time jobs produce too limited income and career prospects" (Visser, 2002a). They advised that collective bargainers "shall improve" standards and that firms recognise a qualified right for full-time employees to work reduced hours, unless this cannot reasonably be granted on grounds of conflicting business interests.

Part-time jobs are *neither atypical nor flexible*, though they have increased the aggregate flexibility of the Dutch labour market. Most part-time employees are covered by collective agreements and most part-time jobs (81 per cent), compared to 91 per cent for full-time jobs, are standard jobs of indeterminate length, subject to dismissal protection. Controlling for sector, occupation and seniority, earnings differentials between full-time and part-time jobs have narrowed to 7 per cent. Folloing accoprance and promotion of part-time work, trade unions have had some success in the 1990s in easing the differences in job and social security rights between part-time and full-time workers. Government policy has worked in the same direction. As a rule, part-time workers pay *pro rata* social insurance contributions in exchange for *pro rata* entitlements. The 1990 tax reform reduced the basic tax allowance for breadwinners and integrated social security charges, thus lowering disincentives for second earners to take up more hours. In the first tier of the Dutch pension system entitlements are individualised, unrelated to earnings (covering about 40 per cent of average wages) and based on citizenship rather than employment, which is the system in which part-timers fare best. Hours limits for entry in occupational pension funds—the second tier—have been outlawed under the 1990 Pensions and Savings Act. In 1996, 91 per cent of all Dutch workers were covered by occupational pensions, which, when fully matured, guarantee 70 per cent of (last-earned or average) earnings.

Statutory minimum wages help to narrow wage differentials (Blau and Kahn, 1996)[8]. Normalisation of part-time work is supported by collective agreements, negotiated since the 'New Course' central agreement of 1993, favouring working time reduction and decentralisation of decision making over working time, with greater direct involvement of workers. This development is supported by recent legislation. Replacing legislation of 1919, the 1996 Labour Time Act sets wider margins for normal and maximum working hours, and allows deviation from statutory norms, within given boundaries, if there is a formal agreement with the unions or the

8. The 1/3 rule, under which employees working less than one-third of full-time hours were denied coverage under the national minimum wage (and holiday payments) law, was repealed in 1993. Similar exclusionary clauses in collective agreements have become unlawful under the 1994 Act against discrimination based on differences in working hours.

works council. In its introduction, the Act states that in a dual-earning economy, employees must be able to combine work and care, and therefore find variable and personal solutions in matters of working time.

Thanks to the one-and-a-half earner model, gender differences in Dutch households have decreased, but gross inequalities persist. In 1979, adult women living in households earned between 16 and 22 per cent of household income[9] while in 1995 their share had increased to 30 to 35 per cent. In 1979, a married women was financially fully dependent upon her husband in 72 per cent of all marriages, in 1991 this was true in 48 per cent of marriages. Time-budget data show that in one-and-a-half earner households with young children, men devote on average 10 hours, women 28 hours, per week to household chores and child care, whereas men tend to spend 18 hours more on paid work. As in paid work, the difference has narrowed, slowly. In 1997 women spend twice as many hours on household chores than men, against three times as many in 1975.

Two quite different policy choices seem possible. The first option is to push for reforms, allowing more women to participate in the labour market on the same terms as men, pressing in the direction of a *two-earner economy*. According to Plantenga (1996: 104) this might imply that “the same ‘care-less’ participation behaviour enjoyed by men is also advocated for women without a clear answer how to tackle the work and responsibilities normally associated with women’s lives”. This choice requires to some degree the ‘collectivisation’ of care provisions. There may be various good reasons for that choice: more labour market participation, in order to create more wealth and a financially robust welfare state for future generations; full economic independence of women, lowering the risk of poverty when divorced or in old age; and, finally, concern with the declining fertility rate in our societies. In the second option the perspective is turned around: “the stress is no longer on women to participate in the labour market in a ‘male’ way, but rather that men should participate in the labour market in a ‘female’ way, ergo, participate in care tasks”. In this *combination* scenario, part-time

9. The percentage depends on inclusion or exclusion of pensioners.

employment is "a positive strategy, because it may help to erode an employment system in which employees are assumed to have *no* caring obligations".

In the 1990s the Netherlands has shown the way towards an "employment friendly welfare state" (Ferrera *et al.,* 2000). The issue for the future is whether it can also create a "welfare friendly labour market". The combination scenario, favouring a voluntarily chosen thirty hours working week for men and women, is currently favoured, though in practical terms policies focus exclusively on encouraging female labour market participation and too little is done to help (partially) disabled people to retain employment, or fathers who want to work part-time. From a gender perspective, the key issue is the quality of part-time work; if part-time jobs offer a good quality alternative to full-time employment in terms of earnings, security and career prospects, then they should be sought by men of all ages. From the perspective of social inclusion, the key issue is upgrading small part-time jobs, with some trade-off between more security for (female and young) workers with weak labour market attachments and more negotiated flexibility for (male and older) workers in standard jobs (as in the '*flexicurity*' agreement of 1996).

This analysis of the Dutch experience suggests to Visser that agency for change in these areas is likely to come from outside the unions and employers associations, through behavioural changes in families, of women and in firms and perhaps through civic dialogue. But Dutch collective bargainers have also demonstrated that the timely acknowledgement of market changes that are largely beyond their power may help social partners and politicians to redirect social policies and attain outcomes that markets would not create on their own.

The Difficulties of Centralised Bargaining

The trends in industrial relations and wage bargaining reported above demonstrate that there are undoubted difficulties in both centralised wage bargaining and national co-ordination. These difficulties can be increased by a number of the trends identified above. As bargaining becomes more decentralised, co-ordination can become harder to achieve and can yield less benefits. With a continued trend towards lower unionisation, it becomes more difficult to maintain a high degree of co-ordination, as co-ordination will produce more favourable results the more employees that are encompassed. Lower membership may in the long run weaken the legitimacy of moderating wage agreements negotiated by unions.

Another long-term threat to national co-ordination is likely to be provided by the internationalisation of product and labour markets, which tends to liberate companies from their historical national roots. As a consequence, national governments will have less leverage to persuade companies to accept a joint policy. Increasingly, national frames of reference—as in a national wage policy that is developed for the sake of the national interest or social solidarity—may lose their economic, political and moral relevance for firms that are already strongly internationalised. This can put greater strains on the central organisations of employers and unions when they try to define national guidelines for policy.

This discussion suggests that bargaining co-ordination through social pacts and consensual norms may represent an unstable equilibrium, which may easily break down once the levels of unionisation and coverage of collective agreements fall below a critical level. Another way of phrasing this conclusion is that wage moderation through co-ordination may increasingly come to require government intervention and public policy support.

Pressures for some decentralised bargaining are likely to continue in the years ahead, since they reflect long-run trends in international competition, technological and organisation change, cross-industry mergers, desectoralisation, and growing diversity in labour markets. These pressures will probably be more pronounced in sectors where large firms are predominant. While acknowledging that the effects of this decentralisation process are uncertain and controversial, it should be stressed, also, that decentralised collective bargaining may coincide with the goals of unions and individual workers, when that gives them more involvement in sharing rules, or adds to choice over working hours, holidays, leave arrangements, and better reflects differences in preferences for leisure or income within a more heterogeneous working force. *'A la carte'* agreements, in which individual workers make a choice between various menus within the collective agreement (reflecting the different 'profiles' of workers with or without family responsibilities, older or younger workers, etc.), are an illustration of this. Of course, their introduction requires sophisticated management and well-developed personnel information systems. These developments partly explain why enterprise-level partnership and employee representation in firms have come onto the agenda of central negotiators in Ireland and many other countries.

While these general trends and associated difficulties and pressures apply to Ireland's partnership approach, a number of additional economic complexities have been identified, given Ireland's small size and economic position. It has been argued that Ireland's national partnership wage bargaining approach has, at different times, come under pressure from:

- Exposure to sterling movements;
- *Ex post* economic outcomes that differ from expectations; and
- The need to avoid pro-cyclical policy.

These pressures need to be adequately addressed in the evolution of Ireland wage bargaining system.

6.4 WAGE AND COMPETITIVENESS DEVELOPMENTS IN IRELAND

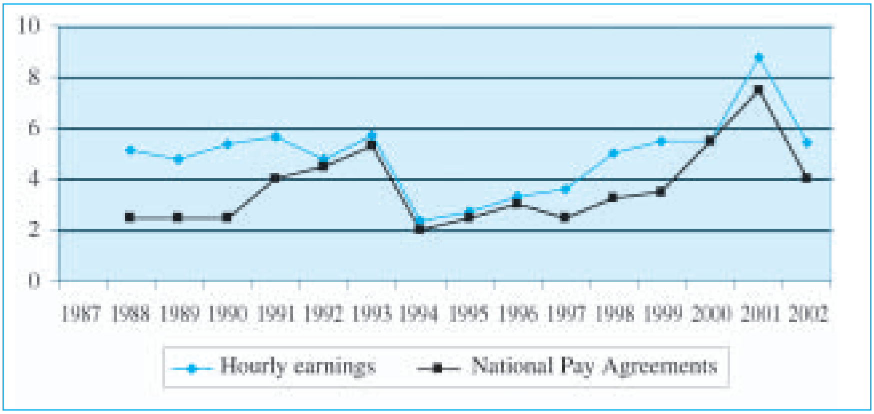
6.4.1 Wage Trends in Ireland

Since 1987, earnings have evolved in the context of national agreements. The econometric research on the influence of national agreements on wages is inconclusive. It has been pointed out by MacCoille and McCoy (2001) that average earnings across the economy have grown considerably faster than the increases provided for in national agreements. This is a significant observation in relation to average earnings. However, one would not necessarily expect a close correlation between average earnings across the economy and the increases in national agreements. The agreements refer to changes in basic pay rates rather than earnings *per se*. Regardless of the extent to which the agreement influenced basic pay rates, average earnings would be influenced by a range of other factors including structural and occupational change, pay increments, overtime, bonuses, profit-sharing, performance related pay, special pay increases in public service and so on.

For the manufacturing sector, the CSO produces an index of hourly earnings for industrial workers that adjusts for sectoral and occupational changes. This series abstracts from some of the factors other than basic pay rates that influence the trend in earnings. Growth in the series is compared to pay increases in the national agreements in Figure 6.1. It can be seen that for most of the period there has been a reasonably close correlation between the two series. The figure of 2002 refers to the annual change to June 2002.

FIGURE 6.1

Percentage Change in Manufacturing Earnings and National Agreements



Source: CSO, *Industrial Earnings and Hours Worked*, Hourly Earnings Index.

Notes: Average manufacturing earnings is an index of hourly earnings for all industrial workers in manufacturing. The manufacturing series is slightly different to that for all industries which also includes utilities and mining. In the period to June 2002, the corresponding increase for all industries was higher than manufacturing at 7.8 per cent. The full amount of the local bargaining clauses is included in the pay increases under the national agreements. In the case of the PESP the 3 per cent is spread over 1992 and 1993. For P-2000, the 2 per cent is spread over 1998 and 1999 (i.e. 1 per cent each). The increase for 2001 includes the additional 2 per cent agreed in the PPF review in 2000. The 2002 increase is the year-on-year increase for the first quarter. The 1 per cent lump sum under the PPF is not included.

Manufacturing covers a relatively small part of the economy. The trend in earnings across a range of sectors is presented in Table 6.3. Over the extended period 1988 to 2001, earnings for all employees in the industrial sector grew by an annual average of 4.9 per cent, somewhat faster than the growth in the financial services sector (4.6 per cent). The growth in earnings in the public sector (excluding health) was faster than in both of these sectors with annual average growth of 5.3 per cent. The fastest growth in earnings was for the construction sector with annual average growth over the period 1988 to 2001 of 7.1 per cent. More recent years have seen faster growth of earnings. For the period 1999 to 2001, the annual average growth in earnings was in the range 7.5 per cent for industry and over 10 per cent in the case of construction.

TABLE 6.3

Trend in Earnings by Sector – Annual Percentage Change

	Construction	Public Sector (excl. health)	Industry (All Employees)	Financial Services	Distribution/ Services
1988-01	7.1	5.3	4.9	4.6	n.a.
1999-01	10.3	8.0	7.5	8.9	8.3
2001 (q1)	10.6	9.8	6.7	11.5	10.4
2001 (q2)	9.3	10.2	7.8	15.6	8.5
2001 (q3)	10.2	10.8	9.5	13.2	8.2
2001 (q4)	5.2	8.1	8.6	9.8	5.1
2002 (q1)	11.0	7.1	6.0	11.8	2.5
2002 (q2)	10.7	5.7	5.7	7.5	3.0
2002 (q1)	€32,500	€36,400	€29,700	€36,100	€28,700

Source: CSO, Earnings and Hours Worked in Construction; Public Sector Employment and Earnings; Industrial Earnings and Hours Worked; Banking, Insurance and Building Societies: Employment and Earnings; Earnings in Distribution and Business Services.

Notes: Index of employee earnings in industry is a revised series provided by the CSO. Where available, weighted earnings indices have been used (public sector, industry) that give an indication of underlying earnings, but for construction and distribution/business services, actual average earnings are used.

The most recent quarterly earnings show that there has been a moderation in earnings growth. This is most evident in the distribution and business services sector where annual earnings in the period to June 2002 showed an increase of just 3 per cent. One factor depressing earnings in this sector is the slowdown in the ICT sector. 'Computing services' is included in this category and showed a fall in earnings of 1.9 per cent in the period to June 2002. Most of the other sub-sectors within distribution and business services showed modest increases; for example, the increase for distribution (incorporating retail, wholesale and the motor trade) was 4.2 per cent for the same period. There has also been a moderation in earnings growth in industry and the public sector, with the annual growth in the broad indices of weekly earnings in these sectors falling below 6 per cent in each case.[10] Earnings growth in construction and financial services has continued at high rates.

While the fastest growth of earnings has been in the construction sector, in terms of levels the highest earnings are in the public sector (€36,500 approximately) and financial services (approximately €36,100). These sectors were followed by construction with annual average earnings of approximately €32,500 and industry with €29,700. The lowest earnings were in distribution and business services (€28,700).

Analysis by SIPTU of pay settlements among its members in the private and semi-state sectors shows that the number of settlements above the norm (ABN) under the PPF has been greater than in previous agreements. A total of 207 such settlements, 16 per cent of all SIPTU settlements, covering just under 30 per cent of SIPTU members were recorded. Notwithstanding the higher number of ABN settlements, the PPF remains the benchmark for settlements in the unionised private sector.

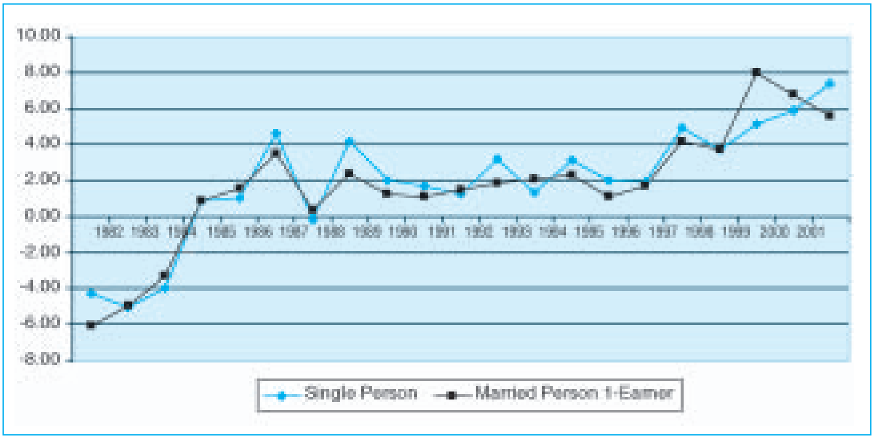
Industrial Relations News (IRN) recorded 53 ABN deals in the year to April 2002, a significant decline on the previous year when as many as 100 deals were recorded. While a slowdown in the number of ABN deals in the second year of a national agreement is a normal pattern, the decline is also a reflection of more difficult economic circumstances. Furthermore, an increasing number of firms appear to be securing productivity concessions in exchange for such settlements. SIPTU meanwhile has observed that since the start of the PPF 79 enterprise partnership initiatives have been concluded and 43 cases of 'inability to pay' the renegotiated terms of the PPF have occurred.

10. Hourly earnings growth for industrial workers has been higher than the increase for industry quoted in the text. The annual increase in the index of hourly earnings for industrial workers to June 2002 was 7.8 per cent. The data shown in Figure 6.1 refer specifically to industrial workers in manufacturing and the increase for this category to June 2002 was 5.4 per cent. The industrial sector includes manufacturing, utilities and mining.

The earnings data discussed so far have all been in nominal terms. From the point of view of living standards what is of most relevance is the trend in real take-home pay, that is nominal earnings adjusting for the impact of inflation and tax. There has been consistent growth in real take-home pay in the period since 1987. Between 1987 and 2001 the cumulative increase in real take-home pay for a single person on average manufacturing earnings was 60 per cent, while the corresponding increase for a married person (one-earner family with two children) was 54 per cent. These represent very substantial increases in real take-home pay. The cumulative increase in real take-home pay in the years from 1994 to 2001 was around 36 per cent (for both single and married persons). The increases in real take-home pay have been larger in the most recent years, with a cumulative increase between 1999 and 2001 of 14.5 per cent (single) and 13.1 per cent (married). The increases in real take-home pay are in marked contrast to the first half of the 1980s. During the seven years to 1987, nominal manufacturing earnings increased by 101 per cent, but real take-home pay decreased by over 7 per cent because of the impact of inflation and tax.

FIGURE 6.2

Annual Percentage Change in Real Take-Home Pay



Source: Department of Finance

6.4.2 The Minimum Wage

A National Minimum Wage (NMW) was introduced in 2000. Prior to its implementation, an ESRI report prepared for the Inter-Departmental Group on the Implementation of a Minimum Wage estimated that over the short-term a minimum wage of £4.40 (€5.59) would reduce employment and increase both unemployment and inflation (Nolan *et al*., 1999). In its *Strategy* document the Council (1999) also considered both the benefits and costs of introducing this 'floor' to wages. The Council highlighted in particular the predicted impact on women's labour supply, a rise of three percentage points compared to a 1.5 percentage point increase for men.

Within a year of introducing the NMW legislation, a survey undertaken by Nolan *et al*. (2002b) indicated that more than 95 per cent of firms viewed the NMW as having had no impact on the numbers they had subsequently employed. Furthermore, 96 per cent of all workers were by then earning an hourly rate equal to or above the NMW. They conclude that the minimum or sub-minimum wage did not appear to be a factor influencing the probability of a firm going out of business. Rather, 80 per cent of firms reporting increases in wages at the time of the survey stated that these reflected trends in the tight labour market. Meanwhile O'Neill *et al*. (2002) argue that the legislation has had a negative effect on employment for a small number of firms most severely affected by the legislation. However, they found that the size of these effects is still relatively modest.

O'Neill *et al*. (2002) highlight that individuals earning less than the NMW are concentrated in sales and personal services, reflecting a wider concern that enforcement of the NMW in Irish workplaces falls short of total compliance. This also resonates with the findings of Nolan *et al*. (2002b) that younger and female workers are most likely to experience low pay, the extent of this phenomenon being proportional to the size of the informal economy (Ioakimoglou and Soumeli, 2002). Identifying the number of low/under-paid workers in the Irish economy might also provide some clarification of the number and work conditions of non-nationals in the Irish economy.

The NAPS review framework document commits the Government to ensuring that the low paid have access to higher incomes and the opportunity to progress to better-paid employment (Goodbody Economic Consultants, 2001). The Council welcomes the recent second rise in the NMW and the associated sub-minimum rates as agreed under the PPF. The Council recommends that over time the NMW should be uprated in a manner that encourages people to enter and remain in the labour force and is consistent with Ireland's move to long-term prosperity and a more equal and socially inclusive society.

The percentage of the minimum wage that is exempt from tax depends on both the level of the minimum wage and the level of tax credits. The 2003 Budget ensured that 90 per cent of the annualised minimum wage continued to be exempt from tax. This is a welcome development. The Council recommends that tax credits should, at a minimum, be indexed to price inflation and should—as soon as circumstance permit—lift those on the minimum wage out of the tax net.

6.4.3 Developments in Productivity

A substantial part of economic growth cannot be explained by increased utilisation of factor inputs, primarily capital and labour. This part of growth represents improvements in the efficiency of production, namely productivity. Productivity is commonly defined as a ratio of a volume measure of output to a volume measure of input use.

The Council has recognised the importance of productivity as a measure of economic sustainability by its inclusion of labour productivity as a headline indicator in its recent report on national progress indicators (NESC, 2002a). In that report, the Council chose to measure labour productivity by annual growth rate of GNP per worker and absolute levels by GDP and GNP at constant market prices per person at work.

Over the past decade the growth in labour productivity in Ireland fluctuated considerably from year to year but has averaged close to

3 per cent per annum. This compares favourably not only with productivity improvements in other developed economies but also their levels of total economic growth. Where the data allow, labour input should be measured in terms of the numbers of hours worked as other measures such as numbers of persons employed will disguise changes in the numbers of part time workers, overtime, different working arrangements between countries etc. Over the last decade hours worked have fallen from an average of 42.8 hours per week as recorded in the 1990 Labour Force Survey to 37.9 by 2001. This is a decrease in the level of inputs of 10 per cent; this is akin to the addition of almost 1 per cent per annum to productivity growth.

The Importance of Sectoral Changes in Production

Labour productivity can, in principle, be separated into two components: the part taking place within sectors (or firms) and the part due to structural change arising from a growing employment share of sectors (or firms) with high levels of productivity. Structural change also takes place within sectors with a tendency for high productivity activities to increase their share of employment, and for low productivity firms to go out of business. One key area where such shifts are prevalent is the shift between low and high productivity activities between sectors of the economy and within sectors. Productivity growth in manufacturing has been substantially faster than in services, as shown in Table 6.4. The annual average increase in productivity for the manufacturing sector (based on value-added) for the period 1995 to 2000 was 9.5 per cent, compared to productivity growth of 2.6 per cent in market services. If productivity growth in manufacturing is defined with reference to output rather than value-added per person employed, the growth in productivity over the period 1995 to 2000 was even higher with real annual average growth of 12.2 per cent over this period. The agricultural sector also showed quite strong labour productivity growth of 4.6 per cent per annum over this period. Within the manufacturing sector, productivity growth in high-tech manufacturing was substantially faster than the rest of manufacturing.

TABLE 6.4
Productivity Growth (based on value-added)
Annual Average Percentage Change

	1990-95	**1995-00**	**2000-05**
Agriculture	2.5	4.6	3.1
Industry			
Manufacturing	6.5	9.5	6.6
Traditional	3.5	3.7	2.3
Food	5.7	2.7	2.8
High-tech	8.3	11.4	5.5
Building	1.8	-2.7	1.8
Utilities	3.3	7.0	6.1
Market Services	0.6	2.6	3.0
Distribution	-1.7	6.4	3.1
Transport & Comm.	3.7	7.5	4.6
Other Services	0.1	-0.7	2.4
Total Economy (GNP)	**2.5**	**3.3**	**2.7**

Source: ESRI *Medium-Term Review 2001-2007* on CD.

Notes: The productivity figures are calculated as real value-added per employee, except for the sectoral figures within manufacturing which are based on the volume of output per employee. The recorded decline in productivity shown in the building sector in this table reflects a number of special factors. First, it reflects a change in the composition of activity. There has been particularly strong growth in house building activity; this is more labour intensive than other construction activity such as road building. A second measurement issue is that the introduction of the QNHS in 1998 showed employment in the building sector at a higher level than previously estimated. These measurement issues could result in an apparent fall in aggregate productivity in the building sector, even if there is an increase in underlying productivity (due to factors such as more professional management). A third factor is that new regulatory requirements may have reduced productivity in the building sector.

Keating (2000) looks at the effects of the changes over the five main sectors in the National Accounts. He finds that over the period 1990 to 1999, there was at this level of disaggregation a structural effect of 0.3 per cent per annum. He also further disaggregates 13 sub sectors within the industry category which accounts for the period 1991 to 1998 some 0.9 per cent per annum. Given the proportion of GNP composed from industry this would approximate to an additional 0.3 per cent per annum, or 0.6 per cent per annum in total.

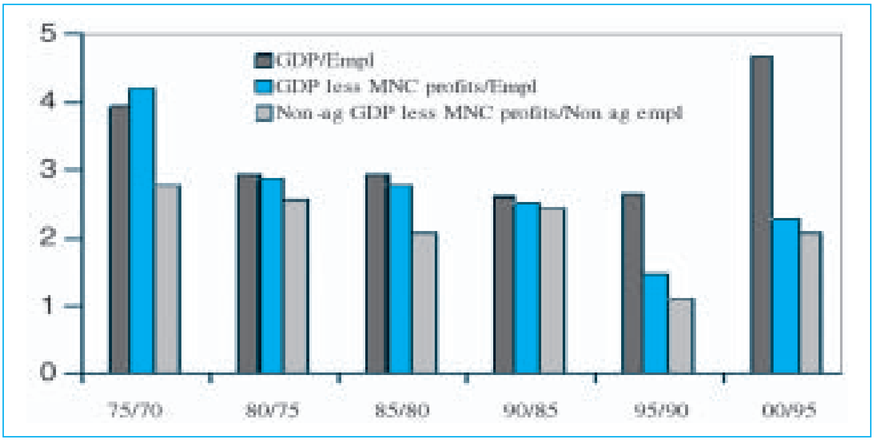
Two tentative conclusions can be drawn from the magnitude of such effects. Firstly that it is important to develop a pool of skilled and flexible labour which is able to adapt to technological and sectoral changes as they may develop in the wider international arena. Only then will we be able to maintain sustained levels of productivity growth and be in a position to react to sectoral shocks. Secondly, we must interpret trends with caution as changes in the sectoral composition of output can also imply changes in the natures and composition of inputs to the production process.

As a very open economy with a high level of foreign direct investment, Ireland has been particularly affected by the behaviour of multi-national companies (MNCs) and the apparently very high levels of value-added associated with their production. These very high levels of recorded productivity derive to a considerable extent from the use of imported intangible resources (technological know-how, brand values, R & D and so on). These sectors account for a very high level of manufacturing output but a small share of employment.

In a recent analysis of productivity growth in Ireland, Honohan and Walsh (2002) prefer to show in addition to calculations based on GDP per person employed an adjusted figure excluding all MNC profits as a refinement to using GNP per employee. This is shown in Figure 6.3, reproduced from their paper. Birnie and Hitchens (1998) point out the assumption that all profit outflows are the result of transfer pricing is undoubtedly an exaggeration but permits us to calculate an upper bound on the economic impact of the practice in Ireland.

FIGURE 6.3

Measures of Aggregate Productivity Growth



Source: Honohan and Walsh (2002).

Honohan and Walsh recognise that their approach is clearly an over adjustment, but they argue not a substantive one, and is preferable to simply using GNP to correct for the transfer pricing problem which does not allow for the complication of the rise and fall in net interest payments on government debt. The approach adopted, of course, fails to take account of the decrease in the number of hours worked which also contributed to productivity growth and which is highlighted above.

Although GNP per employee is not represented in the figure above it clearly falls between the measure for GDP/employee and the measures adjusted for the repatriation of multinational profits, the latter measures are under the 3 per cent growth in GNP per employee.

Productivity figures for indigenous enterprise also suggest that caution is warranted in interpreting recent favourable trends in output and employment as evidence of substantial performance improvement. It is clear, despite measurement issues, that the performance of indigenous enterprises lags far behind that of foreign enterprises in Ireland (see O'Sullivan, 2000 for a comparison) but given the scope for income shifting by the latter the comparison in fact tells us little about indigenous enterprises.

6.4.4 Relative Wages and Competitiveness

As a small and very open economy, competitiveness has a crucial influence on the performance of the Irish economy. Competitiveness is a multi-dimensional concept. Factors that influence competitiveness include investment in science and technology and the use of this knowledge in new and existing industries, the quality of infrastructure and the public service, the education system and skills of the workforce, competition policy, the incentives and support services provided to the enterprise sector, the adoption of advanced work practices and the quality of management. Notwithstanding the wide range of factors that affect competitiveness, wage costs have a key influence on competitiveness and employment growth, particularly in the short-term. Higher wages are one of the key benefits of economic growth and a strategy of competing on the basis of low wages is neither possible nor desirable for the Irish economy. It is, however, crucial that the evolution of wages relative to our trading partners is consistent with the economy's need for employment growth.

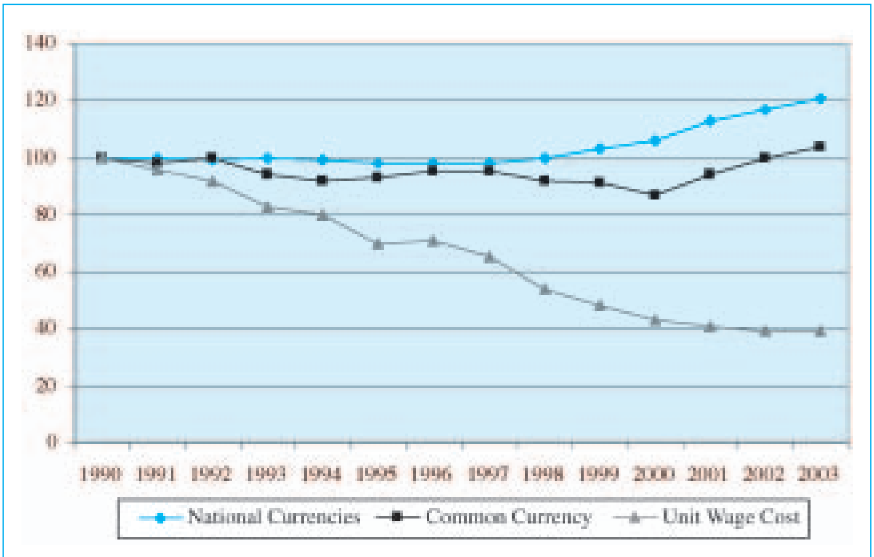
Wage Competitiveness in the Manufacturing Sector

Central Bank reports include comparative data on wage trends in manufacturing in Ireland and its major trading partners. These data show that for much of the 1990s nominal wage growth in Ireland (in national currency terms) was similar to growth in our trading partners. Since 1998, however, hourly earnings in Ireland have grown considerably faster than among our trading partners, so that earnings relative to Ireland's trading partners increased by 17 per cent between 1998 and 2002 (Central Bank forecast for 2002). The impact of this trend on competitiveness was partly offset by the weakening of the euro against the dollar and sterling. Relative hourly earnings in common currency terms increased more modestly by an estimated 8.7 per cent between 1998 and 2002. This process by which the impact of higher wage growth was partly offset by a weaker euro has reversed during 2002 and a stronger euro means that the impact of wage increases on competitiveness will be magnified.

Relatively strong productivity growth in Ireland could potentially provide a basis for relatively high wage increases. Unit wage costs incorporate the effects of both labour costs and productivity. The trend in relative unit wage costs for Irish manufacturing is also shown in Figure 6.4 in common currency terms. It can be seen that this measure has fallen consistently during the 1990s but this decline has now levelled off.

FIGURE 6.4

Relative Hourly Earnings in National and Common Currency Terms and Unit Wage Costs for Irish Manufacturing, 1990-2003



Source: Central Bank *Quarterly Bulletin*, Autumn 2002.

Relative unit labour costs expressed in common currency terms is probably the most comprehensive measure of cost competitiveness for most economies. However, in the Irish economy, it is subject to a number of limitations. The trend in this series is dominated by the very high productivity of a number of high-tech multinational sectors. Recorded productivity in these sectors reflects very high levels of imported intangible factors, as discussed above.

Because of the limitations of the standard unit labour cost measures, a recent analysis by the IMF (2002) focused on unit labour costs weighted by employment rather than output shares of the various manufacturing sectors. This reduces the impact of a limited number of high-tech sectors as these sectors have a much higher output than employment share. Unit labour costs measured in this way were fairly stable for the Irish manufacturing sector since 1995, in contrast to the large fall in the output-weighted measure. Since 2001, this measure showed a large increase in unit labour costs.

Using the IMF measure of relative unit labour costs, there was a modest improvement in competitiveness over the period 1995 to 2000, of around 10 per cent. This modest gain was mainly due to exchange rate movements, as unit labour costs in themselves did not fall. The modest gain in competitiveness up to 2000 was entirely reversed during 2001 when there was a sharp loss in competitiveness of over 15 per cent. While the employment-weighted unit labour cost measure is less subject to distortion by particular sectors, it still includes such sectors. If the chemicals sector is excluded the deterioration in competitiveness in 2001 was even larger. For 2002, the Central Bank has estimated that manufacturing earnings growth in Ireland continued to grow at a faster rate than its trading partners. If this were combined with a sharp appreciation in the euro, it would reinforce the negative impact on competitiveness.

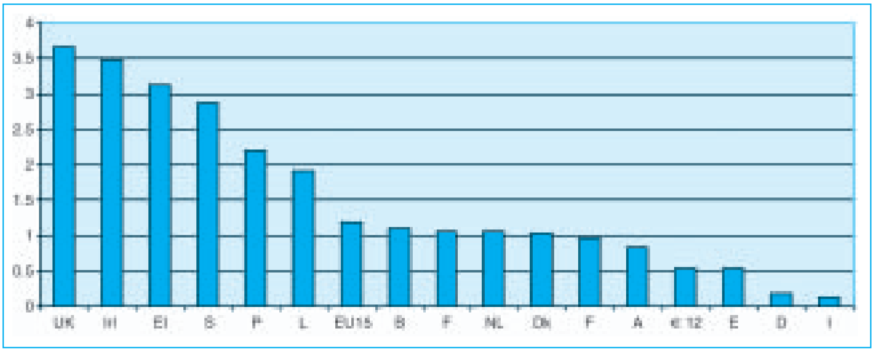
Economy-wide Earnings Growth

It is of interest to compare economy-wide earnings growth in Ireland to other EU countries (see figure 6.5). In *nominal* terms, the average growth of pay in Ireland was 7.75 per cent per year between 1998 and 2001, the highest in the EU. Over this period, the increase for the EU average was 3 per cent per year, while for the eurozone the average was 2.5 per cent per year. Inflation was also higher in Ireland, thus reducing the *real* value of this growth in pay. Comparative trends in *real* pay in the years 1998 to 2001 are shown in Figure 6.5 below. Over this period, the increase in real pay in Ireland averaged 3.5 per cent per year. This was the second fastest rate of increase in the EU, with only the UK having higher growth of 3.7 per cent per year. The average increase for the EU was 1.2 per cent per year, while for the euro area the real increase was just 0.5

per cent per year. These figures do not take account of tax changes or changes in public services.

FUGURE 6.5

Real Change in Gross Pay: 1998 to 2001 Economy-wide



Source: European Economy, No. 2, Table 23.

Recent Wage Agreements

In recent months, a number of European countries have reached agreement on modest wage increases. As noted above, in the Netherlands the social partners recently reached a new agreement that included a centrally agreed pay limit of 2.5 per cent for 2003. In Finland, the social partners signed a new two-year agreement in December, 2002 covering 90 per cent of wage earners. The new agreement increases wages by 2.9 per cent in 2003 and 2.2 per cent in 2004. In Germany agreement has been reached on a public sector pay deal that provides increases of 4.4 per cent over 27 months.[11]

6.4.5 International Comparison of Wage Levels

In assessing the absolute levels of remuneration it is important to distinguish between the employer costs of labour including employers' contributions to social security payments, which is important from an international competitiveness perspective for

11. Information on the Netherlands and Finland is taken from the European Industrial Relations Observatory Online, available at www.eiro.eurofound.ie. Information on Germany from the Financial Times, 10 January, 2003.

traded goods sectors and worker take home pay after taxes which can be used to acquire goods and services. Moreover, in assessing actual standards of living it is important to translate monetary values into real purchasing power due to price differentials between countries and also differences in the composition of direct and indirect taxes between countries.

Eurostat data on hourly labour costs in manufacturing show that costs for Ireland in 1999 at €15.60 were among the lowest in the EU, with just Portugal and Greece having lower labour costs[12]. Hourly labour costs as defined by Eurostat are inclusive not only of employer social security contributions but also include other costs such as training. These figures refer to 1999 so that above average growth of pay levels in Ireland since 1999 would have somewhat changed this position. These figures also refer to the manufacturing sector and the position can very substantially across the economy. The data show the position for the construction sector is different. Hourly labour costs for Ireland in construction in 1999 were €18.60. This was again at the lower end of the range among EU countries, but the gaps between countries were narrower than in manufacturing. Hourly construction costs for Ireland were similar to the UK (€19.70) and 85 per cent of the German level (€21.80). In terms of direct remuneration per hour in this sector, the Irish figure (€13.40) was seventh among 13 EU countries (Greece, Austria not included) and similar to levels in Germany and the Netherlands. Given the relatively high wage growth in Ireland in the last few years, hourly remuneration in this sector would by now exceed these countries.

More comprehensive data on economy-wide annual earnings and labour costs are also available from Eurostat. These data include all forms of employee compensation (including private pension contributions, benefits-in-kind) in all sectors of the economy. This table shows that on this basis that Ireland (€35,600) has employer labour costs that are fifth in the European Union. Gross labour costs in Ireland are slightly lower than the UK (€37,700). In terms of employee remuneration, the Irish figure was third highest in the EU.

12. Eurostat, *Hourly Labour Costs in 1999*, Statistics in Focus, Theme 3/2001.

The Council is also reassured of the reasonable accuracy of these forecast numbers given that for Ireland, at least, they appear to resemble numbers from current average weekly earnings as collated by the CSO, bearing in mind that the CSO weekly earnings figures do not include pension contributions or irregular bonuses.

TABLE 6.5
INTERNATIONAL COMPARISON OF AVERAGE EMPLOYEE EARNINGS AND GROSS LABOUR COSTS, 2002

Country	Average Employee Earnings	Gross Labour Costs
Luxembourg	€57,580	€62,572
Denmark	€36,299	€38,763
Ireland	€33,273	€35,644
United Kingdom	€32,349	€37,687
Belgium	€31,202	€41,547
Austria	€27,294	€34,340
Germany	€26,651	€33,010
Sweden	€26,311	€35,323
Finland	€26,207	€33,109
Netherlands	€26,160	€32,640
France	€26,111	€35,599
Italy	€21,781	€30,030
Spain	€19,929	€25,108
Greece	€15,925	€20,496
Portugal	n.a.	n.a.

Source: Calculated by dividing the national wage bill by the number of employees. The 2000 data (and 2001 where available) are from the Eurostat Cronos database. These have been updated using the annual change for 2001 (where relevant) and the 2002 forecast from European Commission (2002), *European Economy*, No. 2.

While employer costs are important from a cost competitiveness perspective, it is take-home pay and the goods and services that can be acquired for it that is the primary concern of workers. Preliminary and tentative analysis by the Council suggests that once adjusting for direct taxation, variations in the number of hours worked and the cost of living, Irish married couples on the average wage enjoy the fourth highest monetary standard of living whereas for a single person on 167 per cent of the average wage is seventh in a league of his European counterparts. The Council should stress that the analysis it has undertaken is indicative rather than definitive but that it appears to lend broad support to the recent work carried out by PWC for Forfás (PricewaterhouseCoopers, 2002) that suggested that Irish workers were the third best remunerated in the euro-zone post-tax and despite higher costs of living retain a purchasing power income above average. It also suggests that the Irish direct taxation system is somewhat more progressive in nature than our European counterparts.

6.4.6 Variation and Trends in Wage and Profit Shares

The recovery of the Irish economy in the late 1980s and through the 1990s was associated with an increase in profitability, as well as increased living standards and employment. Rates of profitability and trends in profit shares differ significantly across sectors. The trends in wage share in the main sectors and in the overall non-agricultural economy are shown in Table 6.6. This shows that while the wage share of total gross value-added fell by around seven percentage points in the overall non-agricultural economy, this was driven by trends in the manufacturing sector. The bottom row of Table 6.6 shows that wage share in the overall economy, outside of manufacturing, was broadly stable between 1991 and 1999.

Indeed, trends in wage and profit share also vary significantly within manufacturing. The falling wage share within manufacturing as a whole is mainly due to a number of high-tech sectors. This is illustrated in Table 6.7, which shows labour costs as a share of value-added in selected high-tech sectors and in overall manufacturing.

TABLE 6.6

The Wage Bill as a share of Gross Value Added in the Non-Agricultural Market Economy

	1991	**1994**	**1999**
Manufacturing	47.6	43.3	28.7
Building	78.1	77.5	67.9
Utilities	47.2	46.0	48.7
Market Services, excluding rents	45.6	45.8	47.6
Total	**48.6**	**47.0**	**41.4**
Total excluding manufacturing	**49.2**	**49.1**	**50.3**

Source: Calculated from the ESRI database.
Notes: Imputed rents on home ownership are excluded from market services and the totals shown. Data on imputed rents supplied by the CSO.

The high-tech sectors selected in Table 6.6 have: (i) a low labour share of value-added; (ii) rapid employment and output growth; and (iii) a high level of foreign ownership. The wage bill in these selected high-tech sectors fell from just over 20 per cent in 1991 to just under 11 per cent in 1999, while for the rest of manufacturing the wage share fell by around two percentage points, from 46.6 per cent in 1991 to 44.7 per cent in 1999. The selected sectors identified in Table 6.6 employed around 55,000 people in 1999, representing around 22 per cent of manufacturing employment and 3.5 per cent of total employment. Thus, sectors employing a low share of total employment account for most of the decline in the wage share in manufacturing and also in overall national output.

The evidence analysed above would suggest that the position is not substantially altered since the Council's 1999 analysis, which indicated that the capital income share was broadly stable, if adjustment was made for profit outflows (NESC, 1999: 241-2).

TABLE 6.7

Labour Costs as a Share of Value-Added in Manufacturing

	NACE code	1991	1994	1999
Other foods etc	154, 156, 1588, 1589	13.8	11.7	7.5
Other organic basic Chemicals	2414	10.4	6.8	3.6
Basic pharmaceutical products	2441	21.2	11.1	5.2
Pharmaceutical preparations	2442	32.7	23.5	13.4
Recorded media	223	7.3	12.3	11.1
Computers	30	31.1	37.1	28.4
Communications equip.	32	47.1	53.4	17.0
Total High-tech sectors		**20.4**	**18.6**	**10.7**
Other Manufacturing		**46.6**	**44.3**	**44.7**
Total Manufacturing		**39.0**	**35.5**	**24.9**

Source: Calculated from CSO revised time series based on the *Census of Industrial Production* (Census of Industrial Enterprises).

Note: The labour shares in this table are expressed as a percentage of gross value-added at market prices, while Table 6.6 refers to gross value-added at factor cost (i.e., adjusting for excise duties and other indirect taxes and operating subsidies). The former variable is not available in the *Census of Industrial Production*.

6.4.7 Financial Participation

The Council notes that financial participation of employees in businesses has gained increasing prominence in all EU member states over the last decade (Poutsma, 2001). As shown below, such schemes make gainsharing, profit sharing, share option or share purchase arrangements or some combination of these available to workers with the intention not only of securing a firm's viability but also promoting a culture of new dynamism (European Commission, 2002a).

While there is no single data source for the extent of such schemes in Ireland, recent data from the Revenue Commissioners indicate that the number of Approved Profit Share Schemes (APSSs), the oldest and most common financial participation option, has increased from two in 1984 to 391 today. In terms of workforce coverage, it has been estimated that up to 2001 236,559 employees, equivalent to 14.5 per cent of non-agricultural employment, have participated at least once in an APSS at one time or another.

SIPTU (2002) has estimated that 10 per cent of the economy-wide employments it negotiates with have agreed to at least one of these arrangements. During the PPF period 34 such schemes were established. However, this represents a fall in the number of schemes established when compared to the 83 implemented during Partnership 2000.

Figures for gainsharing and share ownership trusts, the latter given scope for expansion by the 1997 and 1999 Finance Acts, are less comprehensive again. Pendleton *et al*. (2001) note that over the course of 1999/2000 34 per cent of firms with 100+ employees had share ownership schemes in place (29 per cent of these same firms had profit sharing arrangements). They also note that while the development of business units with profit schemes in Ireland increased for the four occupational categories of 'management', 'professional', 'clerical' and 'manual', units while share ownership declined across all categories bar 'professionals'.

The emerging picture of those firms most likely to offer some form of financial participation, argue Pendleton *et al*. (2001), are large, domestically-owned entities with a stock market listing. Companies with such schemes tend also to have better lines of communication with employees and also invest more in training and a higher qualified workforce than those without.

Research has identified several potential benefits to firms from financial participation. There is evidence that it may contribute to an increase in productivity particularly if used in conjunction with other forms of employee involvement. There is also evidence linking financial involvement to lower absenteeism and it is associated with greater firm investment in training (Poutsma, 2001). Profit sharing in particular may also help to stabilise employment.

Above all these schemes offer workers rewards in excess of typical returns from employment but on condition of reformed work practices (Pendleton *et al*., 2001).

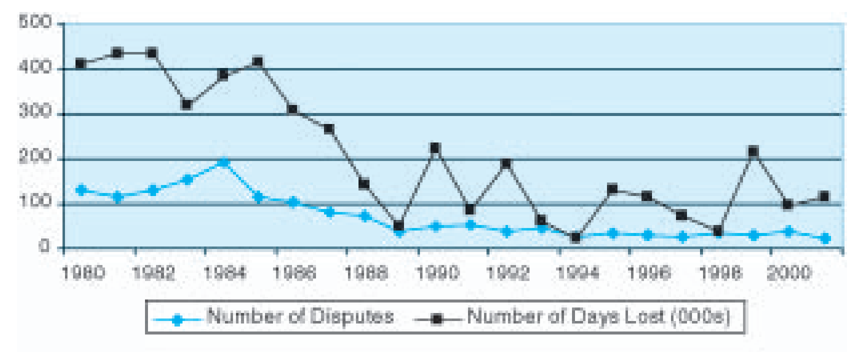
There is a natural link between financial participation and other forms of enterprise partnership. The PPF acknowledged the role of employee financial participation in developing and deepening partnership and increasing performance and competitiveness. It underlined this with the setting-up of a designated Consultative Committee to influence future policy direction on the issue in subsequent Budgets during the PPF's existence. While the downturn in the global economic climate illustrates that financial participation can mean employees sharing some of the risks as well as the benefits of changing profitability, the Council remains of the view that financial participation arrangements offer a real option to linking employers and employees in a unified effort to sustain business competitiveness and quality in work.

6.4.8 Industrial Disputes

An important motivation for social partnership agreements has been to achieve industrial peace. It is clear from Figure 6.6 that there has been a downward trend in the number of industrial disputes. It is noteworthy that the number of industrial disputes has remained low in recent years despite the move to full employment. The number of days lost to industrial disputes, although subject to greater variability, has also shown a downward trend. The unusually large increase in days lost in 1999 is a reflection of the nurse's strike in that year.

FIGURE 6.6

Industrial Disputes and Days Lost, 1980-2001



Source: CSO, *Industrial Disputes*.

6.5 WAGE DETERMINATION AND ORGANISATION IN THE PUBLIC SERVICE

6.5.1 Introduction

Public service pay is a very substantial element of public expenditure. The Exchequer pay bill in 2002 was €11.7 billion, an increase of 12.5 per cent from 2001. This represented about 39 per cent of gross current expenditure supply services. Since 1996, the Exchequer pay bill has risen by over 90 per cent. An analysis of the Exchequer pay bill by the Department of Finance for the period 1996 to 2001 showed that since 1996, pay rates accounted for two-thirds of the increase in the total pay bill. Health accounts for around 39 per cent of the pay bill and is the fastest rising element. Over the 1996 to 2001 period, the pay bill in health increased by 107 per cent, compared to an increase of 53 per cent for the rest of the pay bill.

It was noted above that average earnings in the public service (exclusive of the health sector) had, in the period since 1988, grown faster than other broad sectors of the economy, with the exception of the construction sector. In terms of pay levels, the level of earnings in the public service is higher than in other sectors. However, these are very aggregate comparisons and do not take account of the composition of public service and other sectors. Education qualifications are higher among public services employees: 52 per cent of public service employees have some form of third level qualification compared to 25 per cent of private sector employees. There is also a higher concentration of public service employees in professional and technical occupations. Almost half of public service employees (48 per cent) are in professional/associate-professional/technical occupations compared to 12 per cent in the private sector (Public Service Benchmarking Body, 2002).

6.5.2 Public Service Pay Determination

The growth of public service pay levels is determined by both general and special (local bargaining) increases. Two principles have been central to the determination of public service pay: (i) comparison with the pay of private sector employees doing similar work; and (ii) in the absence of such comparisons, the use of internal relativities.

The process of public service pay determination has proved unsatisfactory for a number of reasons. First, the maintenance of fixed relativities across different sectors of the public service created serious difficulties. Such relativities meant that attempting to increase pay for a particular group that might be required on the basis of changes in responsibilities or the need to recruit staff could result in very large consequent effects in other sectors where pay increases were not warranted. While it was noted above that two principles had governed the evolution of pay (external and internal comparisons), the principle of internal relativities had become the dominant one. Hence, the central focus in disputes about pay had become the issue of what other groups in the public sector had been paid.

A second problem that characterised public service pay determination was that the process of negotiating local bargaining increases had become a very lengthy and often divisive one. The difficulties involved can be illustrated with reference to the local bargaining clause of PCW (the 1994 to 1996 agreement). This agreement provided a local bargaining clause that was originally understood would provide increases of 3 per cent. This was subsequently modified to 5.5 per cent and a number of settlements were reached on this basis. However, the negotiations of the PCW local bargaining clause extended through the period of the next national agreement (Partnership 2000, 1996-1999). Settlements reached towards the end of this period including the nurses and guards were considerably higher than the earlier settlements. Those who had reached settlements at an earlier stage (who became known as the 'early settlers') sought an additional increase and were paid an additional 3 per cent at the start of the PPF period.

A third problem of traditional public service determination was the very weak link to the issue of performance. While some attempts had been made to address this, the dominant criterion had been internal comparisons, as noted above.

Another problem with public service pay determination that is shared with other human resource issues in the public service, is a very high level of centralisation. The recent evaluation of the Strategic Management Initiative (SMI) in the civil service by PA Consulting reported that many managers argued that they did not have the tools to reward excellence, to improve performance where it is deficient and to tackle non-performance (PA Consulting Group, 2002: 60).

The PPF sought to improve the process of public service pay determination in two ways:

- The parties to the PPF committed themselves, in return for the composite agreements on pay and tax, to the delivery of the modernisation programme outlined in the PPF. Specifically, an increase under the PPF of 4 per cent was linked to the agreement of specific performance indicators and the achievement of progress measured by their indicators; and
- The PPF provided for the establishment of the Benchmarking Body to undertake coherent and broadly based comparisons of jobs and pay rates across the economy and to make recommendations for benchmarked grades in the public service on the basis of this research.

Public Service Modernisation under the PPF

Under the PPF, each organisation in the public service was required to put in place performance indicators, using partnership structures. Assessment of progress in the achievement of the performance indicators was a matter for the Secretary General or equivalent in other organisations. To ensure standards were maintained, a Quality Assurance Group (QAG) was established in each sector identified for this process (the Civil Service, health, education and local authorities). The QAG had two functions: to examine the performance indicators that were agreed by the organisations, with a view to confirming that the agreements met the requirements of the PPF. Second, to consider progress reports from each organisation on progress made in relation to the targets set in the performance indicators.

Reports on progress made on the agreed performance indicators have been submitted to the quality assurance groups. Each QAG have at this stage all issued reports. The payment of the 4 per cent increase has been agreed across all sectors.

The report of the QAG for the Civil Service provides an illustration of how this process has worked. The report of this group found that the quality of the progress reports was excellent and that the reports clearly showed that a good deal of progress had been made in the year to April 2002. The reports indicated that more progress was required in the development and implementation of HR strategies. The group found that progress was slower than had been anticipated on introducing the new performance management system (the Performance Management Development System, PMDS) in some organisations. The group expressed concern about the degree of support given by parent departments to bodies under their aegis to implement PMDS.

In relation to the overall process, the group made the following observations. First, the overall quality assurance process gave a positive impetus to the rate of progress on modernisation. However, it was also pointed out that performance indicators are under-developed in most of the civil service and noted that the development of the Management Information Framework (MIF) (a new management information system for the civil service) should provide a considerable improvement in this respect. The group considered that it would be desirable to have more interaction between the group and the organisations in the process. It also pointed to the problem of a lack of weighting of the various performance indicators used.

Benchmarking

The recommendations of the Benchmarking Body are based on comprehensive research into pay and jobs in the public and private sectors. Information on pay in the public service was readily available to the Body. In order to examine jobs, the Body undertook job evaluation. This involves the measurement of demands and requirements of different jobs. Established job evaluation methodologies were available to the Board, but the scale and complexity of this task required it to develop its own scheme. The factors used in evaluating jobs were as follows: knowledge and skills, judgement, leadership and teamwork, responsibility and accountability, interpersonal/communication skills, and conditions and emotional demands. This scheme was applied to a representative sample of employees in the benchmarked grades, using rigorous sampling procedures. The body examined 3,944 jobholders from the public service. A further 5,363 jobs in the private sector were evaluated using the same methodology. Information on pay in the private sector was also collected by the Body's consultants. In its report, the Body paid a lot of attention to the requirement in its terms of reference to have regard to "the need to ensure equity between employees in the public service and the private sector" (Public Service Benchmarking Body, 2002: 14). Its pay recommendations were based on achieving this and it emphasised that these recommendations did not provide any basis for follow-on claims from the private sector.

The terms of reference of the Benchmarking Body also required it in reaching its recommendations to have regard, "to the need to ensure ongoing modernisation of the public service so that the public service can continue to adapt to necessary changes and to achieve greater efficiency and effectiveness" (p. 14). However, the Body considered that it would not be practical to link its recommendations to specific changes in work practices since this would require it to assess the position in relation to these for each position throughout the public service. However, the Body strongly recommended "that implementation of its pay award should be made conditional (apart from the one-quarter of any award to be implemented from the 1st December 2001 as agreed between the parties) upon agreement on the issues at appropriate local bargaining levels" (p. 65).

6.5.3 Future Public Service Pay Determination

In negotiating the PPF, the parties involved made significant efforts to address some of the key weaknesses that had characterised the traditional system of public service pay determination. In particular, the Council welcomes the approach in the PPF to linking some of the pay increases to verified progress in modernisation and change in the different sectors of the public service. This was a new initiative and there was considerable learning by all involved in the process. It is desirable that future negotiations on public service pay should seek to build on these initial steps in linking pay to progress achieved. This is not to imply that any change provides a basis for higher pay. Change in the public service as in the private sector is ongoing and in fact can often make work easier.

The following are some factors to be considered in the subsequent use of a PPF-style process linking pay awards and performance in the public service. First, it is desirable to make progress on the development of more robust performance indicators. The development and implementation of the MIF is important in this respect. Second, in the groups that monitor performance it would be desirable to have greater external representation in order to give higher weighting to the delivery of real change as seen from the perspective of the users of the service in question. Third, it is desirable to have a high level of interaction between the groups monitoring progress and the various public service organisations.

Human resource management (HRM) including pay is highly centralised in the civil service. The evaluation of the SMI in the civil service by PA Consulting Group found that many senior managers argued that they did not have the tools to reward excellence and to improve performance where it was deficient. Work is underway on legislation to allow for some decentralisation of recruitment in the civil service. There is also a review underway of the Civil Service Regulations Act, 1956 that could lead to some appropriate decentralisation of HRM regulations. The Council considers that some decentralisation of HRM issues in the civil service is desirable.

Changing customer preferences and expectations point to the need for greater organisational adaptability and flexibility. The need for greater organisational flexibility was recognised in the PPF including new forms of work organisation, multi-grade and cross-stream teams and broadbanding. The PA evaluation found that there did not appear to be much progress in addressing these issues. They noted that the distinction between general grades on the one hand and technical, professional and departmental grades on the other hand was virtually undiminished in most departments and there was little evidence of action being taken to address the range of grades across the civil service. The Council recommends that the issue of organisational flexibility should be advanced with greater urgency.

The Council is strongly committed to securing improvements in the delivery of public services. A public service that is fairly remunerated and characterised by a high level of organisation flexibility is a prerequisite for the achievement of this objective. The Council's recommendations on benchmarking are presented below.

6.6 OPTIONS FOR IRELAND

6.6.1 Analytical and International Guidance: Learning Ahead of Failure

In a changing international context it is not easy to derive clear principles from theory or identify which are the best countries to learn from. Nevertheless, both analytical developments and experience in other European countries suggest a number of lessons. The most important of these is one identified in earlier Council reports: that a shared understanding of the economic and social context, and of key mechanisms, greatly increases the probability of wage bargaining being conducted in a co-operative way, in which each party has an eye to their own long-term self-interest and the common good, and not to their short-term interest or purely sectional concerns.

The second lesson is that the chance of creating and maintaining a co-operative 'mood of play' depends as much on institutions as on the disposition of wage bargainers. Without supportive institutions, even altruistic wage bargainers can find themselves drawn inexorably into a zero-sum conflict or even a negative-sum situation, in which the attempt of each individual to rationally advance their interest can lead to a collective outcome that is worse for everybody. The relevant institutions range from the NESC, independent research bodies (such as the ESRI), the industrial relations machinery and law, the structures of bargaining, but also probably include institutions for training, life-long learning and enterprise-level partnership.

A third lesson, identified in a review of European wage developments prepared for the Council by Professor Jelle Visser, is that purely centralised bargaining is likely to come under pressure, both because of short-term economic conjunctures and underlying trends in markets, organisation and technology. A fourth lesson is that when tensions appear in centralised bargaining, there are significant benefits to moving to a form of 'organised decentralisation' or 'co-ordinated centralisation', rather than 'unorganised' decentralisation. The review prepared for the NESC by Visser concluded that "learning ahead of failure means that elements of variation and flexibility must be introduced before one of the sides in industry become disenchanted with centralised bargaining and its framework breaks down" (Visser, 2002b: 36).

The final lesson of international experience concerns some of the ingredients necessary to achieve a successful system of co-ordinated decentralisation. Visser suggests that to achieve successful devolution to lower bargaining levels, one needs stable partners, in whom one places confidence. Institution-building through organisational reform and mechanisms for conflict resolution are essential. Differentiation across sectors and, if it improves mobility, between geographic regions can improve the overall responsiveness of wage setting. The upgrading of public services—care provision, health services, housing and transport—helps the functioning of labour markets and gives people a better background for making real choices.

In addition to these lessons, there are significant trends in European industrial relations that might inform Irish developments. Prior to EMU national industrial relations generally followed two broad tracks. First formal cross border agreement among trade unions in continental countries to seek wage increases within specified parameters and thereby prevent social dumping known as the Doorn Initiative, backed by the European Trade Union Confederation, European Council and European Commission. Second, adoption of social pacts in peripheral or 'catch-up' countries (including Ireland) prioritising national competitiveness, addressing crisis situations and/or as preparation for EMU (Hassel, 2001; Calmfors, 2001).

Viewed together, these responses present something of a dichotomy between a 'Europeanisation' and 'marketisation' of pay. This dichotomy has recently attenuated as European countries 'recalibrate' national institutional arrangements in an effort to adapt to the new monetary and economic environment (Ferrera *et al*., 2000, Sisson, 2001; Waddington, 2001). Not by design, a common response has emerged across Europe based on adoption of hybrid responses entailing retention of domestic bargaining processes but reaching increasingly similar moderate wage settlements, a pattern termed "converging divergences" (Kauppinen, 2001; Arrowsmith and Sisson, 2001; Carley, 2002).

As EMU and economic coordination render labour cost and cost of living comparisons more feasible there are obvious competitive and normative reasons for setting wages in line with settlements reached in European neighbours. However, EU member states are free to set pay awards compatible with historical productivity differences and with an element of 'catch-up' on European counterparts. Since all EU member states face similar reform issues, the Council believes that trends in other member states should be taken into account in developing Ireland's wage bargaining system.

6.6.2 Wage and Competitiveness Developments

Since 1987 there has been a very substantial increase in real take-home pay and recent years have seen larger increases. The trend in real take-home pay is illustrated in Figure 6.2. Between 1987 and 2001, the cumulative increase in real take-home pay for a single person on average earnings was 59.8 per cent, while the corresponding increase for a married person (one-earner family, two children) was 53.3 per cent. Over the 1990s, the growth of wages in manufacturing in Ireland has been similar to our trading partners. In recent years, however, wage growth has significantly exceeded increases in our trading partners. This has occurred in the context of relatively high general price inflation in Ireland, as well as other pressures, such as housing affordability and high childcare costs. Until recently, the impact of wage increases on competitiveness was partly offset by the weakening of the euro. The trend in wage cost competitiveness varies significantly by sector, but overall there has been a sharp decline in wage cost competitiveness since 2001. Modest pay settlements have been reached in European countries in recent months (see examples outlined in Section 6.4.4). Other pressures on competitiveness include other cost increases, transport congestion and skill shortages. The decline in cost competitiveness is a matter of concern for the Council.

Notwithstanding some difficulties, the Council notes that the number of industrial disputes under the PPF has generally remained low. The Council recommends that voluntary codes to address the maintenance of essential services should be honoured by each sector.

6.6.3 Adapting Ireland's Partnership System to a New Context

With or without national partnership agreements on the current model, Ireland has to devise a wage and reward system that is suitable for its type of economy and which achieves its social goals. The key danger in wage bargaining at present is that average wage and price inflation continue up to the point where there is a significant loss of competitiveness, resulting in a rise in unemployment.

The pay determination system must meet a number of objectives. It must achieve outcomes that maintain cost competitiveness and full employment, including the ability to respond to shocks, such as would occur as a result of a sharp appreciation of the euro. It should avoid embedding inflationary expectations into the system and achieve outcomes that are consistent with a reduction in inflation. It must provide for an acceptable sharing of the benefits of growth. It must be consistent with high-performance work practices and associated reward systems. It must be consistent with a sustainable public finance position.

Wage Bargaining in Competitive Enterprises

The Council's conclusion is that these objectives are best met through co-ordinated wage bargaining, in which there is an element of co-operation and a focus on long-term interests. This implies a partnership approach to both the current conjuncture and longer term structures.

In the short-term, an effective system of wage bargaining must achieve a consistent and viable outcome, given the pressures of prices, housing costs, public service levels, rents, taxation, reward systems, international competition and profit levels. This would include taking into account wage developments in other euro zone countries and Ireland's principal trading partners. During the 1990s, this approach, used in many EU member states, did not seem appropriate in Ireland, given the rapid pace of economic growth and the dynamic structural change in the Irish economy. Now that growth has slowed—and Ireland's competitiveness is not automatically maintained by the virtuous circle described in Chapter 1—

comparison with wage growth in other countries may be a useful component of an effective wage determination system.

In the medium term, the partners should work with government to weaken the pressures listed above by altering some of the key parameters. This can be done by reducing inflation, improving those services that are now scarce and expensive, reducing the cost of housing, improving infrastructure and settlement patterns, extending gainsharing and widening the tax base.

An effective partnership agreement would, first, deal with the current conjuncture, in which the claims on economic output must be made consistent with one another and, second, alter the parameters of pay and profits by creating a shared understanding on key services, taxation and productivity.

Among the parameters that shape wage bargaining at any given time is the extent and pattern of financial participation of employees in business. Financial participation takes many forms, including profit sharing, gainsharing, share option and share purchase arrangements. In its 1999 *Strategy*, the Council observed that the incidence of profit sharing and related forms of financial participation in Ireland is increasing from a low base. It expressed the view that financial participation can help sustain business performance at enterprise level and economic performance at national level. Research suggests that financial involvement is closely associated with many of the other work practices that characterise high-performance enterprises. The National Centre for Partnership and Performance (NCPP) is undertaking research on the role of financial participation in organisational change and performance in Ireland.

While there has been some spread of employee financial participation in recent years, the Council considers that there is considerable scope for greater use of these arrangements. This would allow increases in income that are responsive to changing economic circumstances as well as supporting the gains that can be achieved through greater partnership at the level of the enterprise. The Council urges the social partners to actively promote and support more widespread financial involvement. This would occur in the context of Ireland's voluntary system of industrial relations.

The Minimum Wage

The Council believes that in setting out the parameters of any future wage bargaining arrangements the past and ongoing impact of the national minimum wage (henceforth NMW) must be considered. The Council recommends that over time the NMW should be uprated in a manner that encourages people to enter and remain in the labour force and is consistent with Ireland's move to long-term prosperity and a more equal and socially inclusive society. The Council also recommends that tax credits should, at a minimum, be indexed to price inflation and should—as soon as circumstance permit—lift those on the minimum wage out of the tax net.

Wage Bargaining in the Pubic Service

In its 1999 *Strategy* the Council argued that a stronger emphasis on the relationship between public service performance and pay is a key dimension of reform. The initial steps taken in the PPF to link pay to public service modernisation and reform should be built upon. It is now important that performance become the focus, rather than modernisation *per se*.

The Council considers that further devolution in relation to HRM issues in the civil service is desirable. The issue of organisational flexibility must be addressed with greater urgency.

Since its 1996 *Strategy*, the Council has emphasised that change must be seen as an ongoing process in both the private and public sectors and does not in itself provide a basis for pay increases. The Council recognises that benchmarking is an improvement on the earlier system of special pay awards and relativities and is potentially a step towards a more effective system of pay determination. If public servants are to be paid at levels similar to the private sector, then it is appropriate that they meet comparable standards of performance and accountability on an ongoing basis, having regard to enduring differences between the two sectors. The benchmarking pay awards involve substantial pay increases (an overall increase in pay costs of 8.9 per cent and an estimated gross Exchequer pay cost of €1.1 billion) that are designed to bring pay in the public service to levels comparable with the private sector. These new pay levels can only be regarded as sustainable if they are matched on an ongoing basis with high standards of verifiable performance. In a difficult public finance situation, such a large step-adjustment in public pay warrants a step-increase in flexibility and step-adjustment towards new systems of continuous improvement.

Conclusion

Current pressures on wage bargaining include inflation, high living costs, expensive housing and childcare, long commuting times and relatively limited public services**.** The Council believes that a satisfactory approach to wage determination is most likely to be achieved if it is part of a consistent policy approach to macro-economic policy and a vigorous programme to improve structural and supply-side factors. Taking account of the current environment and the experience of wage bargaining in Ireland and elsewhere, the Council is on balance of the view that a negotiated consensus between the social partners covering a range of issues, including incomes, is likely to be the most effective way of addressing both current pressures, especially those on employment, and medium-term challenges.

CHAPTER 7

TAX AND SOCIAL WELFARE

7.1 INTRODUCTION

The tax and social welfare systems have a key influence on economic and social well-being. The first sections of this chapter address tax policy. Section 7.2 outlines principles for the development of tax policy and Section 7.3 examines the structure and evolution of the tax system. Section 7.4 outlines principles for the development of social protection. Section 7.5 examines the current situation as regards the adequacy of social welfare payments while Section 7.6 discusses strategic directions which the Council believes should be followed over the coming years. The particular issue of child income support receives detailed consideration in Section 7.7. A final Section presents the Council's recommendations for changes in taxation and social welfare.

7.2 PRINCIPLES OF TAXATION

The Council proposes that the following principles should inform the evolution of the tax system:

- The tax system should facilitate economic growth and employment creation and, in particular, should not act as a disincentive to those on low incomes to take up employment;
- The tax system should be fair. There are two dimensions to fairness or equity. Horizontal equity means that people in similar circumstances on the same income should pay the same amount of tax. Vertical equity means that people on higher incomes should pay more tax;
- Tax bases should be as comprehensive as possible;
- The tax system, at a minimum, should not make it more difficult for firms to compete in domestic and international markets;

- Income from different sources—whether employment, self-employment, investment, or social welfare—should, as far as practical, be taxed in an equivalent way;
- The tax system should only be used to influence personal or business choices where there is a clearly defined justification for doing so, and where the tax system is an effective instrument for achieving this. Departures from neutrality should only take place where there are well defined externalities and where the benefits exceed the costs;
- Administrative and compliance costs should be minimised;
- The system of taxation needs to be able to adapt to changing economic circumstances; and
- The Council supports the continuation of earmarked social security contributions, but believes that compulsory social insurance contributions should be evaluated using the same criteria that apply to the evaluation of taxes.

7.3 STRUCTURE AND EVOLUTION OF TAXATION

This section describes the main features of the tax system and key developments in the period since 1987. It begins with an examination of the total level of taxation and its composition. The section then examines the main developments in income, corporate and capital taxes.

7.3.1 Level and Composition of Taxation

The level of taxation in relation to the size of the economy has fallen since the late 1980s. As noted in Chapter 5, this reduction has been substantially less than the corresponding reduction in the expenditure share. In 1990, total taxation was equal to around 40 per cent of GNP while by 2001 this had fallen to 34.5 per cent of GNP.[1] This reduction was concentrated in the period 2000 to 2001

1. This is based on the OECD definition of taxation and is inclusive of social security taxes and the tax receipts of local government. There is a discontinuity in the GNP series after 1990 which limits the ability to compare the tax share of GNP for years before and after 1990.

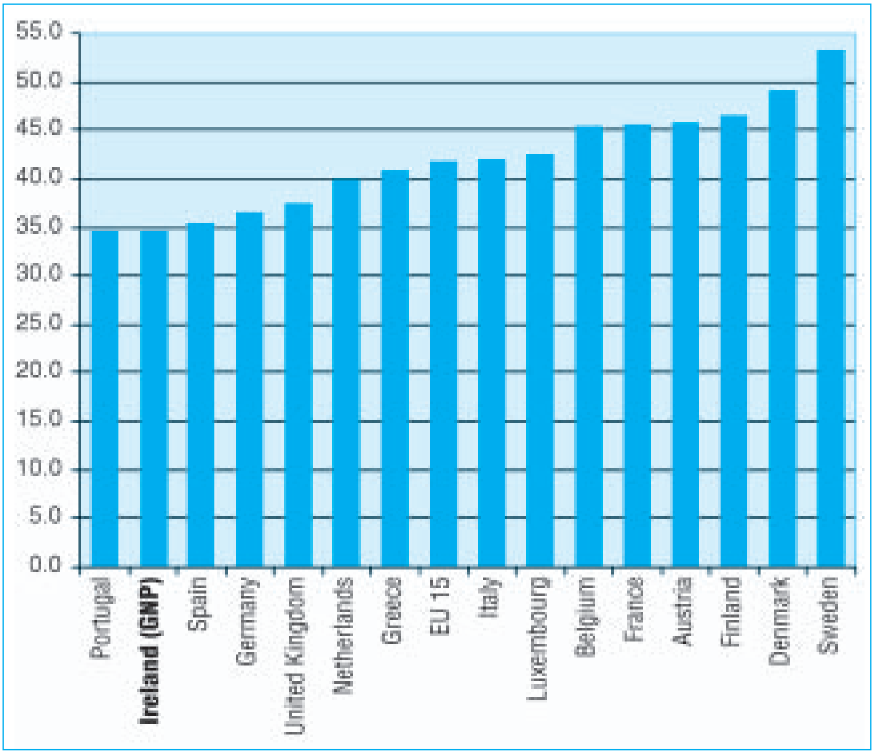
(and continued in 2002) when the tax share fell by two percentage points. Over the 1990s the tax share of GNP was fairly stable.

The tax share of GNP in Ireland (34.5 per cent) was significantly below the EU average of 41.6 per cent (of GDP) and lower than the figure for all other EU countries with the exception of Portugal, which had a marginally lower tax share of GDP of 34.1 per cent[2].

The Irish tax share was fairly close to the levels for the UK (37.4) and Germany (36.4 per cent). The highest tax shares in 2001 were for Sweden (53.2 per cent) and Denmark (49.2 per cent).

FIGURE 7.1

Total Tax Revenue as Percentage of GDP, 2001



Source: OECD, (2002) *Revenue Statistics 1965-2001*, Paris: OECD.
Notes: The figures for Portugal and the EU refer to 2000.

2. Due to the substantial level of profit outflows from multinational companies in Ireland, GNP is a better measure of economic activity than GDP for Ireland.

The main sources of tax revenue in Ireland are income tax (30.8 per cent of total revenue in 2000), social security taxes (13.6 per cent), taxes on goods and services (37.2 per cent) and corporation tax (12.1 per cent). Over time the composition of tax revenue in Ireland has become similar to other European countries, but some differences persist. The share of taxation accounted for by income tax in Ireland (30.8 per cent) was above the EU average (25.6 per cent). The Irish tax system relies significantly less on social security contributions (13.6 per cent in 2000) compared to the EU average (27.5 per cent) and also less than the UK (16.4 per cent). There is significantly more reliance on indirect taxes in Ireland (37.2 per cent) compared to the EU (30.0 per cent). The share of tax revenue accounted for by property taxes in Ireland (5.6 per cent) is similar to the EU (5.0 per cent) but significantly less than the UK (11.9 per cent). The share of corporation tax in total tax revenue in Ireland (12.1 per cent) exceeds the OECD (9.7 per cent) and EU (9.2 per cent) averages.

Local taxation is a relatively small share of total tax revenue in Ireland. In 2000, the share of local taxation in Ireland at 1.8 per cent was the lowest in the OECD with the exception of Greece (1.0 per cent). Other OECD countries with relatively low total taxation shares are the UK (4.0 per cent) and the Netherlands (3.4 per cent). The low share of local taxation in total tax revenue in Ireland is paralleled by the limited devolution of powers to local government[3].

7.3.2 Income tax

Declining Average and Marginal Tax Rates

The period since 1987 has seen substantial reductions in average and marginal tax rates. The changes in income tax (and PRSI) are

For this reason, the text refers to tax as a percentage of GNP for Ireland. Tax relative to GDP is used for other countries as this is the more widely used and available measure. Ireland is unique in the size of the gap between GDP and GNP, so that using the GNP measure for Ireland and GDP for other countries does not cause a significant distortion.

3. The figures in the preceding two paragraphs are taken from OECD (2002), *Revenue Statistics 1965-2001*, Paris: OECD.

illustrated in Table 7.1 which shows the average tax paid by an employee on various percentages of average industrial earnings. Average earnings for industrial workers in manufacturing (based on CSO weekly earnings) are taken as IR£10,070 in 1987 while average earnings are estimated at €24,800 in 2002 and €26,000 in 2003. Changes to discretionary tax allowances are ignored in this Table. For a single employee on average industrial earnings, the average tax rate fell by almost 20 percentage points in the period from 1987 to 2003. High income employees (as represented by those earning 250 and 500 per cent of average earnings) received similar (but slightly lower reductions) in their average tax rates, although the value in real money terms was substantially higher for such high earners. Some employees will have an increase in their average tax rate in 2003 (due mainly to holding the standard rate band constant in money terms), although this increase is very modest in comparison to the reductions that have taken place over several years.

TABLE 7.1

Average Tax Rate (Percent of Gross Wage) at Various Percentages of Average Manufacturing Earnings

	50%	100%	250%	500%
1987/88	22.0	35.4	50.8	54.9
1993/94	21.2	32.4	44.9	48.1
2002	2.4	16.1	32.8	38.5
2003	2.2	16.1	33.1	38.6
Change 1987-2003	-19.8	-19.4	-17.8	-16.3
Value of tax reduction	€ 2,574	€ 5,044	€ 11,570	€ 21,190
Income level in 2003	€ 13,000	€ 26,000	€ 65,000	€ 130,000

Source: NESC Secretariat calculations.

Notes: The value of the tax rate reduction has been calculated by applying the change in the average tax rate to the 2003 income level. It shows the difference between the tax paid in 2003 and the tax that would have been paid in 2003 if the 1987/88 average tax rates applied.

Following reductions in recent years, average tax rates in Ireland are now relatively low compared to other EU countries. Table 7.2 shows how average tax rates compare for a single person on average earnings in EU countries. It can be seen that for this category of taxpayer, tax rates were lower in Ireland than any other EU country, with the exception of Portugal, which has a marginally lower rate.

TABLE 7.2

Average Tax Rate for Single Person at Average Earnings

	1995	2001 (estimates)
Austria	27.0	28.5
Belgium	41.1	41.7
Denmark	45.2	43.8
Finland	38.0	32.4
France	27.4	27.0
Germany	40.5	40.6
Greece	17.6	18.1
Ireland	**29.2**	**16.9**
Italy	27.5	27.9
Luxembourg	25.6	24.8
Netherlands	40.5	33.0
Portugal	18.0	16.5
Spain	19.6	18.9
Sweden	32.6	31.7
United Kingdom	26.7	23.3

Source: *EIRI Review*, March/April 2002.

Marginal tax rates are also now substantially lower compared to 1987. In 1987, a single person on average industrial earnings had a marginal tax rate of 55.75 per cent (including PRSI and levies) while in 2003, the corresponding marginal tax rate is 26 per cent. This reduction is mainly due to the expansion of the standard rate band. Those earning 250 and 500 per cent of average earnings in

1987 had a marginal tax rate of 59 per cent while in 2003 this had fallen to 44 per cent (including levies, employees are above the PRSI ceiling at these income levels).

TABLE 7.3
Key Parameters of the Income Tax System
(€000s in 2003 prices)

	1987/88	1993/94	2003	Percentage Change 1987-2003
Effective Exemption Limit (single)	5506	6310	11600	112.5
Effective Exemption Limit (married, 1 earner)	11012	7534	19400	76.2
Effective Exemption Limit (married, 2 earners)	11012	7534	23400	112.5
Standard rate income limit (single)	15969	19169	28000	75.3
Standard rate income limit (married, 1 earner)	29890	36435	37000	23.8
Standard rate income limit (married, 2 earners)	31938	38339	56000	75.3
Basic Allowance (single)	6204	5716	11600	88.6
Basic Allowance (married, 1 earner)	10359	9529	19200	87.3
Basic Allowance (married, 2 earners)	12408	11432	23200	88.6
Tax rates	35%	27%	20%	
	48%	48%	42%	
	58%			

Source: NESC Secretariat calculations.
Notes: For 2003, the tax credit is shown in this table as a standard-rated allowance to facilitate comparisons with earlier years. In two-earner households, the standard rate band is transferable between spouses up to a maximum of €37,000.

The fall in average tax rates reflects a combination of changes in tax credits or allowances, bands, the rate schedule, PRSI and levies. The level of tax credits is particularly important for low income taxpayers. From 1987 to 1993/94, the level of basic tax allowances for an employee fell in real terms, but since the mid-1990s the level of allowances has increased substantially, giving an increase of 88.6 per cent in real terms over the extended period 1987 to 2003. The increase in tax allowances/credits has also meant that the income level at which one enters the tax system has more than doubled since 1987. In 2003, an employee becomes liable for income tax when earnings rise to €11,600.

The income level at which a single person (or a second earner) becomes liable for the higher rate of tax has long been of concern. This level has also increased significantly since the mid-1990s and a single person now becomes liable for the higher rate at an income of €28,000. Increases in the band in recent years were associated with the partial individualisation of the standard rate band (see below).

The tax rate schedule has been simplified since 1987 and rates have fallen. In 1987, there were three income tax rates (58, 48 and 35 per cent) while in 2003 there are two rates (42 and 20 per cent). There have also been significant changes to the system of PRSI and income levies. The rates of PRSI and levies have been reduced and lower income earners have been exempted from paying PRSI and the 2 per cent health levy. A reduced rate of employer PRSI for lower income employees was also introduced in the mid-1990s and the ceiling on employer PRSI contributions has been abolished. A significant change announced in Budget 2003 was the extension of PRSI and levies to benefits in kind. The changes made have tended to increase the progessivity of these charges.

Two major changes have occurred in the structure of the income tax system:

- The introduction of standard rated personal allowances in 1999 represented a major change to the way in which the income tax allowances operated, forming a move towards a tax credit system. From 2001, a full tax credit system has been put in place. This change means that subsequent increases in the tax credit will provide an equal reduction to most taxpayers. In addition, a fully developed tax credit system enables change in the structure of the tax system to be more precisely targeted at different types of taxpayers;

- The restriction of the transferability of bands between spouses began in 2000, as part of a move towards individualisation of the income tax code. Subsequently a £3,000 tax allowance was introduced for one-income families where a spouse is working in the home in a caring capacity.

The tax base

A feature of the income and corporation tax systems is a wide range of discretionary tax allowances and reliefs, as listed in the Appendix to this chapter. Some of these reliefs have been particularly beneficial to higher income taxpayers who have been able to legitimately reduce their tax liabilities to a very considerable extent.

In 1997, the Revenue Commissioners carried out a study of effective tax rates (i.e., tax liability divided by gross income) of high income earners based on a sample of 400 individuals with incomes over IR£250,000. The tax years examined in the study were 1993/1994 and 1994/1995. The study found that high income taxpayers were, in general, paying tax at well above the average effective tax rate for all taxpayers, i.e. 24% (see Table 7.4). However, the study also found that a minority of high earning taxpayers were engaged in substantial “tax planning” to reduce their income tax liabilities. The study concluded that capital allowances on buildings were the chief instrument used to achieve this. Provisions were subsequently introduced by the Minister for Finance in the Finance Act, 1998, that placed a cap on the amount of capital allowances a taxpayer could claim on investments outside their own business.

The Revenue Commissioners carried out a similar study in 2002 on the effective tax rates for high earning individuals based on the tax year 1999/2000. The effective tax rates of the top 400 earners examined in the 2002 study are also shown in Table 7.4.

The ceiling on capital allowance, mentioned above, was not fully in effect by 1999/2000. Nonetheless, the figures show an increase in the average tax rate paid by high earners; the percentage of high earners paying an average tax rate above 45 per cent increased from 8.8 per cent in 1994/95 to 13 per cent in 1999/2000. The 2002 study again found that it was property tax reliefs (including car-parks and hotels) that were most effective in reducing the tax rates of the highest earners.

TABLE 7.4

Distribution of Effective Tax Rates of Top 400 Earners (Percent of Total)

Effective Rate	1994/95	1999/00
Less than 30%	30.75%	29.2%
30%-44%	54.75%	57.8%
45% and higher	8.25%	13.0%
Information not available	6.25	
Total	**100%**	**100%**

Source: Revenue Commissioners (2002), Effective Tax Rates for High Earning Individuals.

Most of the property tax incentive schemes are due to expire in December 2004. In the Budget 2003, two tax relief schemes were extended (Town Renewal and Park and Ride), and the expiry date for two schemes (student accommodation and film relief) was brought forward. Capital allowances for hotels were reduced and the allowance for investment in holiday homes was abolished.

Of the tax reliefs listed in the Appendix, the largest in the area of personal taxation is that for pensions. Ireland is similar to many other OECD countries in exempting both the pension contributions made by employers and employees and the income of pension funds themselves, but Ireland and the UK are unusual in also exempting certain lump sum payments payable from the fund to beneficiaries on retirement (while taxing the pension itself). In this section, the results of analysis carried out by the ESRI for NESC is outlined. This exercise, utilising 1998 Living in Ireland (LII) Survey data, repeats work carried out by Hughes (2001) using survey data for 1994. The data for 1994 show that the top 20 per cent of employees, ranked by gross earnings, benefitted from more than 60 per cent of the tax foregone. Repeating the exercise for 1998, the ESRI looked at which employees are making pension contributions and where the tax relief then accrues in terms of position in the earnings distribution. They then look at where these employees are located in the household income distribution and the implications for where the tax foregone on employee pension contributions is concentrated in terms of that household distribution.

TABLE 7.5

Location in the Earnings Distribution of Employees with Occupational Pensions, and of Tax Relief on their Contributions, 1998

Decile by gross usual pay	% of those with occupational pensions %	% of total estimated tax relief on employee pension contributions %
Bottom	0.7	0.1
2	2.7	1.0
3	6.1	1.1
4	4.4	1.4
5	8.9	3.5
6	10.5	5.0
7	13.1	6.8
8	16.8	16.1
9	15.7	21.1
Top	21.1	43.9

Source: Supplied by the ESRI

Table 7.5 shows the location of employees with occupational or private pension entitlement in the earnings distribution, ranking by their reported usual gross pay. About 37 per cent were in the top one-fifth of the earnings distribution, and 23 per cent were in the bottom half. The Table then shows where this tax relief accrues in the earnings distribution. About two-thirds goes to the top quintile of the earnings distribution, while 7 per cent goes to the bottom half.

Table 7.6 shows the corresponding pattern, but with employees now ranked by the position of their household in the equivalised disposable income distribution (income of all household members, not just the earnings of the employee him or herself, is taken into account). Employees with pension entitlement are even more concentrated towards the top than was the case for the earnings distribution. About 41 per cent of the relevant employees are in the top two deciles and 57 per cent of the estimated tax relief accrues to that part of the distribution, while 5 per cent accrues to the bottom half. This reflects the fact that the lower reaches of the income distribution are dominated by households that do not contain any employees.

TABLE 7.6

Location in the Household Equivalised Disposable Income Distribution of Employees with Occupational Pension, and of Tax Relief on their Contributions, 1998

Decile by gross usual pay	% of those with occupational pensions %	% of total estimated tax relief on employee pension contributions %
Bottom	0.0	0.0
2	0.2	0.0
3	1.4	0.3
4	6.3	1.6
5	7.2	2.7
6	10.5	6.4
7	16.0	13.8
8	17.8	18.3
9	21.1	20.8
Top	19.5	36.0

Source: Supplied by the ESRI

The provision of tax relief in relation to pensions reflects a valid public policy objective to encourage people to make adequate provision for retirement. The QNHS for the second quarter of 2002 showed that only half (50.7 per cent) of those in employment had a pension scheme (occupational pension or personal pension plan) other than social welfare. Pension coverage among women in employment (44.2 per cent) was lower than men (55.4 per cent). The low coverage of pensions points to the need for policies to encourage pensions. The new personal savings retirement accounts (PSRAs) are designed to offer low cost and flexible plans to save for retirement and may improve the situation. The figures on the distributional pattern of tax expenditures on pensions presented above do not undermine the case for providing incentives for pensions, but do point to the importance of ongoing review of the extent to which the public resources committed to this area are achieving their objectives in an equitable and efficient manner.

The Finance Bill 2003 makes some changes to the tax regime governing pensions and the tax treatment of Approved Retirement Funds (ARFs). The Bill caps the tax relief available on pension contributions by imposing an annual earnings cap of €254,000 to income that qualifies for relief in respect of employee pension contributions. Additional voluntary contributions made by employees prior to retirement may now only be set back one year (instead of 10 years under previous rules), unless the contribution is provided for widows and orphans benefits, or is towards the repayment of benefits such as a marriage gratuity.

An ARF is an alternative to investing a pension fund in annuity or retirement. The income or gains made by an ARF remain tax free until a withdrawal is made. Arms length rules are being introduced by the Finance Bill to prevent investments in assets for personal use or benefit. Otherwise, there are no restrictions on the investments that can be made by ARFs.

7.3.3 Corporation Tax

Until recently corporation tax was based on a dual structure with a lower rate for enterprises in manufacturing and internationally traded services. This dual structure has been phased out over a number of years and from 2003 there is a single rate of corporation tax across sectors of 12.5 per cent for all trading income in general. Non-trading income is taxed at 25 per cent. The period since 1987 has seen strong growth of corporate tax revenue. Factors contributing to the strong growth of corporation tax have been the expansion of the highly profitable multinational sector, including international financial services and the widening of the corporation tax base. Notwithstanding the relatively low rate of corporation tax in Ireland, the corporation tax share of GDP in Ireland in 2000 (3.8 per cent) was equal to the EU average.

7.3.4 Capital Taxes

Capital taxes (capital gains tax and capital acquisitions tax) are a modest share of total tax revenue (2.7 per cent of tax revenue, excluding PRSI in 2002). The rate of capital gains tax (CGT) was cut sharply in the 1998 Budget from 40 per cent to 20 per cent. There was substantial growth of revenue since then, despite the lower rate. Up to 2002, relief against inflation has been provided in the application of CGT, i.e., only real gains have been taxed. This was changed in the 2003 Budget and the current position is that real gains are taxable up to December 2002, but all nominal gains made after 31 December 2002 are taxable. Rollover relief was also abolished in Budget 2003; this had provided relief from CGT in cases such as the replacement of business or farm assets. This Budget also introduced a measure to address the evasion of CGT through temporary non-residence.

Capital acquisitions tax (CAT) applies to gifts and inheritances. The current rate of CAT is 20 per cent. The rates of CAT have been cut sharply since 1987 when there were five rates, the highest of which was 55 per cent. Significant relief is provided in relation to CAT, depending on the relationship between the people involved. A child can inherit or receive gifts from a parent up to a threshold of over €400,000 without incurring liability for CAT. Additional relief is provided in relation to the inheritance of a family business, farm or shared private residence.

7.3.5 Conclusion

There have been substantial reductions in income tax since the mid-1990s. These reductions have significantly increased the income at which one enters the tax system and the income threshold for the higher rate of tax. Average and marginal tax rates have fallen substantially across income levels although the value of the income tax reductions has been greatest for those on higher incomes. The overall distributional impact of budget changes was discussed in Chapter 2. Tax reductions facilitated wage moderation and increased labour force participation and thus contributed to the remarkable employment growth that has been achieved. However, the scale of the reductions may have been larger than required to achieve this objective.

There continues to be a wide range of discretionary tax allowances that reduce the tax base. These allowances are of most benefit to high income earners. The benefit of tax relief for pensions is particularly concentrated on higher earners. Some measures have been taken in recent years to limit the ability of high income earners to use the available reliefs to achieve very low tax rates.

The most significant development in corporation tax has been the move to a single rate of corporation tax of 12.5 per cent. Despite the low rate of corporation tax, Ireland derives significant revenue from this source. Corporate tax revenue represented 3.8 per cent of GDP for Ireland in 2000, the same as the EU average in 2000.

The general trend in the area of capital taxation has been to reduce the burden of tax in this area although the revenue from CGT has increased. The low rate that exists for CGT provides an incentive to convert income into capital gains and is contrary to the Council's principles that income from different sources should be taxed in an equivalent way.

7.4 PRINCIPLES OF SOCIAL PROTECTION

The Council advances the following principles as important for guiding the development of social protection in Ireland in the coming years.

- A comprehensive system of social protection rests on four pillars: that provided by the state, what is purchased through the market, what is provided by the voluntary organisations of civil society, and the caring carried on within the family;
- The state's primary interest is to guarantee the quality of social protection and the attainment of outcomes and not to privilege one pillar over another;
- The state's action in protecting people from need should complement and not undermine the provision which people are able to make for themselves;
- The state has the responsibility to monitor the comprehensiveness and effectiveness of social protection and ensure that gaps and shortcomings are addressed;
- Social protection provided directly or indirectly by the state takes the form of public services, tax expenditures, income transfers, and activist measures;
- Where resources permit and economic initiative is not weakened by procuring them, universal public services are more effective in achieving social inclusion and supporting an efficient labour market than services targeted on need;
- Income transfers based on the insurance contributions of workers, their employers and the self-employed constitute an important sub-system of social protection, reflecting the central role of paid employment in generating wealth and solidarity within society;
- It is important that the regulations governing social insurance keep pace with changes in employment patterns and social risks;
- Income transfers based on need should be sufficient to enable individuals who are dependent on them to live life with dignity in their society; and
- Income transfers that leave people in need and economic distress neither foster the supply of workers needed by a knowledge-based, competitive, economy nor do they strengthen social attachment.

7.5 CURRENT SITUATION WITH REGARDS TO INCOME ADEQUACY

7.5.1 Broad Context: Changes in Income Poverty

The most basic type of social protection is that which ensures that people have a level of money income sufficient to meet their needs (other dimensions to social protection are reviewed in Chapter 8). Evidence that people's incomes are insufficient to raise them above poverty lines, therefore, is an important part of the context for reviewing whether, and which, changes are needed in how people are protected from income risks. Chapter 2 reviewed trends during the 1990s in the overall number of people falling below the different poverty lines. Here, we inquire more deeply into who these people are. Along with the contrasting developments in consistent poverty and relative income poverty already highlighted, there have, in fact, been significant changes in the composition of the populations experiencing each of them.

As consistent poverty was reduced in scale, it has changed markedly in whom it characterises (Table 7.7). In 1994, people living in households where the reference person was unemployed dominated the picture, both because of the exceptionally high level of risk they faced (a one in two chance) and because they accounted for almost one half of all people in poverty. By the year 2000, people in such households remained a severely disadvantaged group—they faced a poverty risk four times the national average (substantially the highest in the table) but now accounted for less than one-fifth of all the poor. However, two other groups now account for larger proportions of people in poverty: people living in households where the reference person is in home duties (35 per cent of all those in consistent poverty using the 70 per cent of median income line) and where the reference person is a low-paid worker (25 per cent).

TABLE 7.7

Percentage and Breakdown of Persons Below 70 Per Cent Median Income Line and Experiencing Basic Deprivation by Labour Force Status of Household Reference Person

	Percentage of Persons (Risk)			Breakdown of Persons (Incidence)		
Labour Force Status	**1994**	**1997**	**2000**	**1994**	**1997**	**2000**
Employee	3.2	3.6	2.7	9.1	16.1	24.9
Self-Employed	4.6	3.9	1.8	3.2	3.8	3.0
Farmer	5.5	1.0	1.5	3.3	0.8	2.0
Unemployed	52.5	42.7	22.1	45.0	39.0	17.3
Ill/Disabled	36.2	31.7	11.0	8.3	9.5	7.9
Retired	6.1	5.5	4.5	4.8	6.4	9.4
Home Duties	28.8	19.2	14.5	28.4	24.4	35.4
All	14.5	10.7	5.5	100	100	100

Source: Tables 5.10 and 5.11, Nolan *et al*. (2002a).

TABLE 7.8

Percentage and Breakdown of Persons Below 50 Per Cent Median Income Line by Labour Force Status of Household Reference Person

	Percentage of Persons (Risk)			Breakdown of Persons (Incidence)		
Labour Force Status	**1994**	**1997**	**2000**	**1994**	**1997**	**2000**
Employee	0.6	1.2	3.0	3.8	6.6	10.9
Self-Employed	9.9	10.7	14.2	16.2	13.0	9.8
Farmer	10.2	6.2	17.2	15.0	6.5	9.4
Unemployed	19.1	39.8	41.7	39.5	44.8	13.0
Ill/Disabled	10.1	27.5	48.3	5.5	12.0	14.2
Retired	4.0	2.1	14.1	7.6	3.1	11.8
Home Duties	5.7	8.9	31.8	12.5	14.1	30.9
All	6.0	8.6	13.8	100	100	100

Source: Tables 4.9 and 4.10, Nolan *et al*. (2002a).

As relative income poverty rose, it, too, has changed markedly in whom it characterises (Table 7.8). People living in households where the reference person is in home duties assume a new prominence here also; their risk of being below the 50 per cent of median income line rose from 6 to 32 per cent between 1994 and 2000, and they accounted for 31 per cent of all persons in that situation in the year 2000. The risk increased even more rapidly for persons in households where the reference person is ill or disabled, while it rose substantially for 'retired' households too. By the year 2000, people living in households where the reference person had a status outside the labour force accounted for nearly 60 per cent of all the people below the 50 per cent of median income line.

Policy Makes a Difference

The Council believes that the extent of the reduction in consistent poverty recorded since 1994 has been neither accidental nor automatic but is due to the operation of several factors: the expansion of employment, the reduction in unemployment, the increased purchasing power of social welfare payments, the improved design and delivery of social programmes, and innovative actions at local level. However, the extent of the reduction, the altered composition of those who remain in consistent poverty, and the recrudescence of severe income inequality, have profoundly altered the context within which strategy and policies for combating poverty and fostering social inclusion must now be formulated. The Council noted in 1999 that new thinking and policy innovations would be needed if social policy was to continue to record progress and keep abreast of the ways in which social disadvantage can reproduce itself in new forms, and that this would make large demands on actors and organisations in the social field (1999: 377, 437-8). In what follows, and in Chapter 8, arguments are developed and recommendations made that will hasten the development of social protection in line with a changing Ireland.

7.5.2 Specific Context: the Adequacy of Ireland's Lowest Social Welfare Payment

The adequacy of Ireland's lowest social welfare payment has been reviewed in successive studies.[4] It is frequently noted that there is no statistical or definitive answer which the social sciences can provide to what constitutes the minimum money income that is sufficient to allow a person 'to live life with dignity' in contemporary Ireland. The 1986 Report of the Commission on Social Welfare began a process in which the findings from poverty research of different types, fluctuations in the capacity and health of the economy, and values and political judgement interact to produce changes in the floor to Ireland's lowest money incomes. In this section, the Council would like to continue this process so as to help ensure that Irish society sets itself standards for its social welfare system that reflect the country's means and aspirations, and what is now known about how poverty evolved during the economic boom of the 1990s.

4. The first major attempt was that of the Commission on Social Welfare (1986) which applied seven different methods to establish that a minimally adequate income for one person, at 1985 prices, was in the range of £50 to £59 a week. Its conclusions were revisited by the ESRI ten years later (1996), which repeated some of the CSW methods and added others to establish a range of £68 to £96 a week in 1996 prices. In the following year, the NAPS (1997) adopted the lower end of the CSW range, up-rated for inflation, as its target, and this was achieved for the lowest social welfare payments in 1999 when they reached £72 per week. The specific but linked issue of a minimally adequate money income for an adult in retirement was taken up separately for people on the non-contributory state old-age pension by the National Pensions Board in 1998, which adopted the upper end of the ESRI range (£ 99 in 1998 prices) as a target and took the further step of expressing this as 34 per cent of Gross Average Industrial Earnings (GAIE). This was not a unanimous recommendation; the Department of Finance and employers' representatives did not support it, nor has it been adopted by Government. In 2001, the issue of the adequacy of the lowest social welfare payment was extensively reviewed by a working group set up under the PPF whose majority recommendation was that the lowest social welfare payment should be set at 27 per cent of GAIE, with employers' representatives and the Departments of Finance, and Enterprise, Trade and Employment again dissenting. Most recently, in 2002, the process of reviewing the National Anti Poverty StrategyNAPS produced the commitment, embodied in the Agreed Programme for Government of July, 2002, that the lowest weekly social welfare payment should reach €150 (in 2002 terms) by 2007. This target was equivalent to 30 per cent of Gross Average Industrial Earnings in 2002.

An incremental process of reducing complexity in the social welfare system and increasing fairness (providing similar levels of support for people with similar needs, notwithstanding the different reasons for them being in need in the first place) has taken the path of levelling up the lowest payments.[5] Six means-tested programmes currently pay Ireland's lowest weekly income maintenance payment for an adult, which is now received by approximately 250,000 people; another 35,000 adults and 207,000 children are indirectly dependent on its level (Table 7.9). The rate was €124.80 a week as of January, 2003, and the Programme for Government (July, 2002) has made a commitment to raise this to €150 per week in 2002 terms by 2007. The six programmes all apply to people of working age, some of whom have a status in the labour force while many do not. Being a member or not of the labour force is frequently not a fixed characteristic for many individuals. This can be particularly true for women, younger people (under 25) and older people (over 55), people whose participation rates are typically influenced by the overall level of unemployment and strength of aggregate labour market demand.

NAPS (1997) considered a life without poverty to require a sufficiency of "income *and resources*" (italics added) such that a person can live life with dignity in their society; it further specified that the resources in question can be "material, cultural and social". The Revised NAPS (2002) commits the Government to ensuring people have access to "sufficient income …to live in a manner compatible with human dignity" and specifies that such an income will be "the *net effect of all policies* impacting on income levels in the community (e.g., employment, tax, social welfare, pensions)" (no. 11, italics added).

5. The latest step was taken in January, 2002, when recipients of Short-Term Unemployment Assistance and Supplementary Welfare Assistance had a €2 per week discrepancy closed.

TABLE 7.9
Lowest Social Welfare Payment: Recipients, Dependants, and Expenditure, 2001

Programme	Number of recipients	Adult dependants	Child dependants	Expenditure on adults [€ 000]
One-Parent Family Payment[1]	77,142	0	123,047	412,159
Unemployment Assistance[2]	66,563	15,178	39,170	398,158
Disability Allowance[3]	57,655	4,732	13,206	322,648
Supplementary Welfare Allowance (basic payments only)[4]	29,167	6,785	19,306	96,403
Pre-Retirement Allowance[5]	11,807	4,372	2,084	81,038
Farm Assist[6]	8,380	4,093	9,878	42,835
Total	250,714	35,160	206,691	1,353,241

Source: *Statistical Information on Social Welfare Services, 2001.*

Notes:

1. One-Parent Family Payment is a weekly allowance paid to people who have the main care and charge of at least one child living with them (aged under 18, or under 23 if in full-time education). They must be bringing up that child(ren) without the support of a partner, and satisfy a means test. They benefit from a notable earnings disregard (the first €146.50 of weekly earnings is completely disregarded, and only one-half of the remainder of weekly earnings up to €293.00 per week is assessed as means).
2. Unemployment Assistance is a weekly allowance paid to people who are over 18 and under pension age (66), capable of work, available for work, genuinely seeking work, and able to prove that they are doing so in a prescribed manner. The weekly rate of payment depends on the amount of weekly means assessed.
3. Disability Allowance is a weekly allowance paid to people with a disability who are aged 16 or over and under age 66. The disability must be expected to last for at least one year and the allowance is subject to a medical suitability test as well as a means test.
4. Supplementary Welfare Allowance provides a basic weekly allowance as a right to people who have little or no income. Other than satisfying a means test, recipients must also be living in the State, have applied for any other

benefit/allowances to which they may be entitled, and have registered for work with FÁS if they are of working age.

5. People who are aged 55 or over and have been receiving Unemployment Benefit/Unemployment Assistance for 15 months or more, may opt to retire from the workforce and apply for Pre-Retirement Allowance (PRETA) which is a means-tested payment.
6. Farm Assist is a weekly means-tested payment for low-income farmers. Introduced in 1999, it has replaced the Smallholders Unemployment Assistance Scheme.

It is clear that a strong consensus that every member of society needs an adequate money income does not answer the question as to the proportion of it the state should undertake to provide, and whether—and which—conditions should attach. However, while non-monetary resources contextualise in a major way the significance of a given money income and people may receive income from several sources, the question remains as to what level of money income society believes government should be willing to provide, *given* the set of non-cash supports potentially available and *assuming* a single person had only that income on which to live.

The lowest rate of social welfare payment increased by 29 per cent in real terms over the nine-year period, 1994-2002.[6] One consequence of this is that, while recipients were 8 per cent below the 50 per cent of mean income poverty line in 1994, they were 17 per cent above the same line, up-rated for inflation, by 2002.[7] The scale of this real increase can take significant credit for the reduction in poverty since 1994. Several considerations support this conclusion. Ireland's poorest households generate next to no market income and are, therefore, wholly dependent on social welfare. Förster (2000: 84) found that the share of total earnings in the economy going to the bottom 30 per cent of the working-age population in the mid-1990s was 4.8 per cent in Ireland, the lowest in 15 countries he studied; he also found that Ireland's tax/transfer system was

6. The welfare rates compared apply to July, 1994, (£58.90) and January, 2002, (€118.80) respectively. Therefore, one half the inflation rate for 1994 and the full inflation rate for 1995 to 2001 inclusive constitute the change in the cost of living. The cumulative rise in the nominal welfare rate is 59 per cent and in the cost of living 23 per cent.
7. The 50 per cent relative income poverty line in 1994 was £64 per week.

particularly significant for bringing a large proportion of the nation's households across the income poverty threshold (see also Oxley *et al*., 2001). Simulation exercises have demonstrated that over one-half of the extra expenditure incurred in giving a generalised increase in welfare payments goes to the poorest 30 per cent of households (BIG, 2001).

TABLE 7.10

Ireland's Lowest Social Welfare Payment, and Various Standards of Comparison.

	January 2002	January 2003
1. Lowest Weekly Welfare rate of payment[1]	€ 118.80	€124.80
2. Gross Average Weekly Earnings of Industrial Workers (GAIE) [2]	€ 489.20	€521.49 (e)
1 as per cent of 2	24.3 %	23.9 %
3. Gross Weekly Earnings at statutory minimum wage (39 hours) [3]	€ 232.83	€247.65
1 as per cent of 3	51.0 %	50.4 %
4. 1994 relative income poverty line (up-rated for inflation)[4]	€ 101.10	€105.75
1 as per cent of 4	117.5 %	118%
27 per cent of GAIE	€ 132.08	€140.80

Source: Department of Social, Community and Family Affairs, Central Statistics Office and Living in Ireland Survey.

Notes:

1. The rate payable as of January in the respective year.

2. Gross earnings for all industrial workers (adult and non-adult rates of pay). Industrial workers include operatives, maintenance workers, storekeepers, packers, cleaners, basic supervisory staff, and apprentices. Earnings are gross (before income tax, PRSI, etc.) and include overtime, shift allowances, regular bonuses, etc. 2002 figure from CSO release (28 June 2002). Assumed increase of 6.6 per cent during 2003 (rate of growth in non-agricultural wage incomes assumed in ESRI Medium-Term Review's '*Slowdown Scenario*' [2001: Table B.4]).

3. Introduced in April 2000, the National Minimum Wage started at €5.59 an hour. Under the PPF, it was raised to €5.97 from 1 July 2001, and to €6.35 on 1st October 2002. There is a commitment, first formulated in the PPF, to remove people on the NMW from the income tax net. After Budget 2003, 90 per cent of their earnings are exempt from tax.

4. On the basis of the Living in Ireland Survey figures for 1994, the 50 per cent relative income poverty line was £ 64 per week (average disposable household income per adult equivalent, using equivalence scale 1.0/0.66/0.33, was £129). This is adjusted upwards by rises in the CPI from 1994 to 2002 inclusive.

The significant increases in real terms, and relative to a 1994 benchmark, of social welfare payments do not—of themselves—settle the question of adequacy in relation to need. In fact, there is, currently, no agreed methodology for calculating the budget that would enable a single adult to live with dignity in Ireland today, nor up-to-date research on—for example—the costs of rearing a child (BIG, 2001: 8.2.3). The lowest social welfare payment is about 24 per cent of Gross Average Industrial Earnings (GAIE, see Table 7.10); in 1994, it had been 23 per cent. The substantial increase in the purchasing power of the lowest welfare payment since 1994, therefore, has been accomplished while keeping it roughly constant as a percentage of GAIE. The context is the strong growth of 50 per cent in GAIE over the period in question.

The majority of the Benchmarking and Indexation Group "considered that the target of 27 per cent GAIE (on a current year basis) for the lowest social welfare payments was a not unreasonable objective" (BIG, 2001: 8.4.6). In 2002-03, 27 per cent of GAIE was about 12 per cent *above* the lowest welfare payment, and some 43 per cent *below* gross weekly earnings for a 39-hour week at the national minimum wage. In favour of this level of indexation with GAIE, it can be pointed out that (i) it is a more rational criterion of adequacy than increases on a somewhat arbitrary base, (ii) indexation with GAIE, while never a commitment of government, has been achieved since 1994 anyway, though at the lower level of 24 per cent, (iii) 27 per cent would still keep welfare income well below weekly gross earnings at the minimum wage. In favour of the traditional process of leaving the scale of the increases in social welfare to a Cabinet decision when budgets are being framed is that (i) this has proved capable of delivering a steady improvement in purchasing power of social welfare payments, and (ii) it guards flexibility for government in allocating additional Exchequer resources in the interests of the whole of society.

The Benchmarking and Indexation Group (BIG, 2001) estimated the Exchequer costs of raising the lowest social welfare payment to 27 (and 30 per cent) of GAIE in 2001 (Table 7.10). Its estimates show that some two thirds of the aggregate expenditure would go not to the recipients of the lowest payment themselves but are incurred when all other welfare payments are increased proportionately to maintain the existing differentials. It is, of course, a matter of values and political judgement as to whether costs of the order shown are acceptable in the light of the objective being pursued, i.e., a new method for establishing a floor to money incomes in Ireland. It is important to appreciate that a significant part of these costs will be incurred anyway as existing commitments are honoured (e.g., the €200 threshold for non-contributory OAP and the €150 threshold in 2002 terms for the lowest social welfare payment in 2007, further rises in Child Benefit, etc). In the absence of indexation to GAIE, it is also likely that the current budget-framing policy would feature some further degree of convergence with prevailing income standards in society anyway.

TABLE 7.11

Expenditure implications of raising the lowest social welfare payment to 27 per cent of GAIE, and adjusting the entire social welfare code accordingly, applied to the 2001 population (€ ’000)

Expenditure heading	**€ 000**
Assistance Payments	530
Insurance Payments	605
Child Benefit	382
Family Income Supplement	52
Total Social Welfare	1,568

Source: BIG (2001), Table 4.4

Some of the assumptions underlying these estimates could be revisited in ways that would significantly influence the Exchequer resources required. For example: preserving the existing pattern of relativities among welfare recipients (by January 2003, the non-contributory old-age was 15 per cent above the lowest assistance rate); the pro-rata extension of an increase in the lowest rate to Child Benefit, given the substantial increases that have occurred since 2001 and are planned; the assumption of static numbers. In the light of these observations, the figures in Table 7.11 can be regarded as outside estimates.

7.6 DEVELOPING SOCIAL PROTECTION IN LINE WITH A CHANGING IRELAND

7.6.1 The Adequacy of the Lowest Social Welfare Payment to Meet Basic Needs

The estimate that 5.5 per cent of the population is in serious income poverty (Table 7.7) is not, of itself, evidence that the level of the lowest social welfare payment is too low. Ineligibility for social welfare, or failure to avail of it, may make the level of the lowest social welfare payment irrelevant to addressing some pockets of poverty. However, that a household is in consistent poverty despite one or more social welfare payments being received by its members is strong evidence that the level of payment is too low and/or that social welfare recipients are finding it particularly difficult to combine receipt of their payment with income from other sources (principally earnings). Data from the Living in Ireland Survey for the year 2000 show that significant percentages of those in consistent poverty are, in fact, living in households in receipt of social welfare payments from different schemes (Table 7.12).

In addition to this type of evidence, the Council appreciates the findings in recent case studies demonstrating that individuals and families have unacceptably low living standards due to inadequate financial resources (Daly & Leonard, 2002; Richardson, 2001; Houghton and Hickey, 2001) and that high levels of demand are currently being experienced by statutory and voluntary providers of emergency services to people in need (particularly for Supplementary Welfare payments, housing, and charitable assistance).[8] Accordingly, it seems difficult to maintain that the current level of Ireland's lowest social welfare payment, where it constitutes a person's entire money income, is a sufficient income 'to live life with dignity' in contemporary Ireland. The Council points out that there is substantial international evidence that relatively generous rates of social welfare payments are compatible with high employment rates and good economic performance, and that the disincentive effects of social welfare more usually flow from aspects of programme design and delivery than levels of payment considered too high.[9]

TABLE 7.12

Percentage of Persons Below 70 Per Cent of Median Income and Experiencing Basic Deprivation in Household Receiving Social Welfare Payment.

Social Welfare Payment	1994	1997	2000
Old Age Pension	5.3	9.3	12.7
Unemployment Benefit/			
Assistance	59.6	56.0	30.3
Illness/Disability	11.4	18.0	23.4
Lone Parents Allowance	12.9	16.7	25.4
Widow's Pension	4.3	8.1	3.9

Source: Tables 5.14, Nolan *et al*. (2002a).

8. *Profile of Households Accommodated by Dublin City Council* (2002), jointly published by Dublin City Council and the IPA's Housing Unit.

9. When paid to unemployed people, see Esping-Andersen, 2002; Esping-Andersen & Regini, 2000; Spieza, 2000; Narendranathan & Stewart, 1993. When paid to lone parents, see Phipps, 2001; Forssén & Hakovirta, 1999; Björnberg, 1997.

7.6.2 The Adequacy of the Lowest Social Welfare Payment for Participation in Society

The Council believes that an adequate money income is a necessary but not a sufficient condition for many people to participate in society. The revised NAPS (2002) envisages its targets for social welfare as being "combined with an active social policy" (p. 9).[10] Its supporting Framework Document explains this broad approach as:

- To have in place a proactive policy of engagement with people of working age on social welfare, to ensure that, where possible, they have the opportunity to avail of employment, education and training options;
- To create new opportunities for unemployed people and marginalised groups to access employment and training;
- To eliminate any remaining gaps or disincentives to employment/training in the application of the secondary benefits system, so that, at a minimum, nobody is materially worse off as a result of taking up employment, training or education opportunities; and
- To ensure that those in low pay have access to higher incomes and the opportunity to progress to better-paid and more highly skilled employment. (Goodbody, 2001: 4.4.4).

Given that the large majority of people of working age in receipt of a social welfare payment now have a status outside the labour force (Table 7.9), this approach suggests that public policy should henceforth be willing to do more to support those among them with the capability and interest of participating more strongly in economic and social life. The Council supports this approach. Studies of older workers, women returners, and men in receipt of disability payments confirm that a status outside the labour force was not the direct choice of a significant number of them (Expert

10. The Final Report of the Social Welfare Benchmarking and Indexation Group (September, 2001) accepts that "an essential part of a strategy for income adequacy should be a proactive policy of engagement with people of working age on social welfare to ensure that, where possible, they have the opportunity to avail of employment, education and training opportunities" (2001: 8.4.9).

Working Group on Future Skills Needs, 2001a; Russell *et al.,* 2002; Beatty & Fothergill, 2002). For some, it was, rather, the end of a process of drift from displacement, through discouragement and disillusionment, to detachment from the workforce (e.g., Expert Working Group on Future Skills Needs, 2001a: 96-97).

The Council is concerned that no person of working-age should be given the impression—even as they receive income support from the state—that they are considered to have no talents or skills of value to society that society is keen they should use. Participation in the mainstream of society for people of working age generates self-respect and gains the respect of others. Higher employment rates, lower poverty rates and greater social cohesion are major societal benefits that result from respect for the individual.

However, other forms of participation also generate self-respect and gain the respect of others—caring for a dependant person, voluntary social or cultural work, returning to education, working in the social economy, etc. In support of these options, the Council considers that the ability of people to build up credits within the social insurance system—on foot of different types of socially valuable participation made within the home and the community—should be actively explored. Any such extension of the social insurance system needs to weigh carefully, on the one hand, the value of contributions to the common good that do not take the form of paid employment and the positive effect on social inclusion of according them the level of recognition implicit in credits and, on the other hand, justice towards the workers and businesses who are making paid contributions and the competing demands on the Social Insurance Fund.[11]

The payment of relatively high social welfare payments *and* the provision of practical supports to enable recipients progress is a strategy for which the Council would like to see the full range of social actors in Ireland share responsibility in helping to design and

11. These observations serve to underline the importance of the work being undertaken by the PPF working group whose brief is “to produce proposals for the development of a fully inclusive social insurance model which would facilitate combining work and family responsibilities in the context of changing working and social patterns.”

implement. The required evolution in designs and systems may require degrees of decentralisation and levels of participation by organisations closely involved with client groups which would be quite novel by Irish standards.

7.6.3 The Adequacy of Ireland's Lowest Pension for a Dignified Retirement

Earlier tables have provided evidence on how the relative income position of retired people changed during the 1990s (Tables 7.7 and 7.8). The percentage of people in households where the reference person is retired and who were in consistent poverty (below 70 per cent of median income and experiencing basic deprivation) dropped from 6.1 per cent in 1994 to 4.5 per cent in the year 2000, and remained below the rate facing the general population. However, the proportion of all people in consistent poverty who were in these households approximately doubled, to 9.4 per cent. When relative income alone is consulted, the risk of people in 'retired' households falling below 50 per cent of median income increased by a factor of 3.5 to reach 14 per cent and they accounted for some 12 per cent of all people below that line.

The risk of falling below the different income poverty lines in retirement has increased particularly dramatically for women. The share of women aged 65 or more below 70 per cent of median income and experiencing basic deprivation in the year 2000 was 8.5 per cent as against 4.1 per cent of men in that age group; 24 per cent of women aged 65 or over were below 50 per cent of median income as against 13 per cent of similarly aged men (Nolan *et al.*, 2002a: Tables 5.13 and 4.20. See Winquist, 2002, also). The gender gaps were nowhere as wide between men and women of working age.

These developments are a reminder of how easily people who have retired on fixed incomes can fall behind the average living standards of society, and even into relative income poverty, the more successful is the country's economic performance. It is also important to keep in mind that life expectancy continues to be lower for lower socio-economic groups. This raises a further ethical dimension to the expectation that they should save significantly out of their low incomes during their working life to support their own retirement.

7.6.4 Household Strategies and Social Welfare Payments

Table 7.9 shows that some 35,000 people were the adult dependants of people in receipt of Ireland's lowest social welfare payment in 2001. A Qualified Adult Allowance (QAA) is an addition to a social welfare payment made in recognition of another adult being supported by the welfare recipient and who is not her- or himself receiving any other social welfare. To qualify for the full QAA payment, the adult dependant must be earning less than €88.88 weekly (2002); the maximum QAA for people in receipt of social assistance is typically some 66 per cent of the main recipient's allowance. Women account for 95 per cent of all QAAs and only a very small number have availed of their right—and activated the procedure—to receive the payment directly. Where a dependant woman decides she would like to claim a social assistance payment in her own right (e.g., as unemployed), she gets no financial benefit from so doing; two independent claimants living together are each paid one-half of the aggregate amount that would have been received if one made a claim on behalf of both (this is a consequence of the 'limitation rule' introduced to ensure that cohabiting couples are treated the same as married couples. It does not apply to pensioners and recipients of disability allowances). In addition, the operation of the means test can see the value of any earnings by the woman being offset by reductions in her husband's welfare entitlements.

The current concept and administration of the QAAs developed during a period when the labour market and the taxation code were structured around the assumption of a principal (usually male) breadwinner. There are good grounds for believing that the social welfare code should harmonise more with labour market developments and with progress in individualising the tax code. For example, it can no longer be assumed that a fully-employed, low-skilled worker earns sufficient to support a household on his or her own (Esping-Andersen *et al.*, 2002), or that couples elect to have one of them earn full-time and the other work full-time in the home.

7.7 ENDING CHILD POVERTY

In many EU countries, rearing children increases the poverty risk facing households and makes it more difficult for them to escape from poverty (OECD, 2001a: Table 2.8). The evidence from the 2000 Living in Ireland Survey supports this general picture; lone parent and large (4 or more children) families faced risks of consistent poverty that were multiples of 3 to 4 times the risk run by the population in general.

TABLE 7.13

Percentage and Breakdown of Persons Below 70 Per Cent Median Income Line and Experiencing Basic Deprivation by Household Type.

	Percentage of Persons (Risk)			Breakdown of Persons (Incidence)		
Household type	**1994**	**1997**	**2000**	**1994**	**1997**	**2000**
1 adults	15.1	12.1	11.2	7.1	8.3	14.8
2 adults	4.0	6.1	3.6	12.5	8.3	9.6
3 or more adults	3.3	5.5	1.0	12.7	7.8	3.3
2 adults, 1 child	9.2	6.9	4.1	5.7	4.9	5.6
2 adults, 2 children	9.3	3.3	2.5	11.6	4.3	6.2
2 adults, 3 children	17.5	15.5	5.6	11.7	15.9	8.7
2 adults, 4+ children	35.6	33.9	16.2	9.5	18.5	20.5
1 adult with children	42.8	20.7	26.2	4.4	6.2	18.0
3+ adults with children	14.2	12.8	3.7	24.9	25.8	13.2
All	14.5	10.7	5.5	100	100	100

Source: Tables 5.8 and 5.9, Nolan *et al.* (2002a).

Lone parents and large families were the household types in which persons faced substantially the highest risks of being below 70 per cent of median income and experiencing basic deprivation in the year 2000 (Table 7.13). As the relative position of other households improved through the boom of the 1990s, these families came to constitute almost 40 per cent of those in consistent poverty as against 14 per cent in 1994. Looking at the risk of poverty by age, it is clear that currently the highest risk of poverty is in childhood (Table 7.14).

TABLE 7.14

Percentage of Persons Below 70 Per Cent Median Income Line and Experiencing Basic Deprivation by Age, Living in Ireland Surveys.

	1997	2000
Aged under 18	15.3	8.3
Aged 18-64	8.8	4.1
Aged 65 or more	8.4	6.6
All	10.7	5.5

Source: Table 5.12, Nolan *et al*. (2002a).

It is a substantial achievement to have reduced consistent poverty for children from over 15 per cent to around 8 per cent in the space of four years. Nevertheless, some 8 per cent of the nation's children were in consistent poverty after seven years of exceptionally strong economic growth and this is a cause of deep concern.

Consistently across OECD countries, children's poverty risks are seen to vary significantly with the labour force status of their parents and whether they are being reared by one or two parents (Oxley *et al*., 2001). The Living in Ireland Surveys establish that this is also the case in Ireland. Table 7.15 makes clear that the work/no work divide is much more significant to the poverty risks which children run than their being raised by one or two parents. A child being reared by a lone parent not in work has their poverty risk hugely reduced when that parent takes employment (from 44 per cent to 8.2 per cent in 2000). As will become evident in the discussion of childcare in Chapter 8, lone parents, however, find it more difficult than other mothers to access employment. Children being reared by two parents neither of whom is working similarly experience a huge reduction in the poverty risk they face when one parent takes employment (from 33.3 per cent to 9.7 per cent), but it is the movement of the *second* parent to take employment also (an option not possible in the lone parent household) which definitively alters the balance of poverty risk between one and two-parent households. This secondary significance of family structure relative to parental employment status is a pattern found in many OECD countries (Oxley *et al*., 2001).

TABLE 7.15

Risk of Consistent Poverty (below 60% Income Threshold and Basic Deprivation) for Children by Household Type and Labour Force Status of Parents.

		1994	**2000**
At Work	Two parents, both working	4.0	1.2
	Lone parent, working	9.8	8.2
	Two parents, one working	14.5	9.7
Not Working	Two parents, none working	72.5	33.3
	Lone parent, not working	69.3	44.0
Others		16.8	7.2
Total		25.2	8.2

Source: Table supplied by ESRI.

As the extremely high child poverty rates in 1994 for ‘work poor’ households in Table 7.15 suggest, the high unemployment rate of that period was the principal cause of child income poverty. The employment expansion since 1994 can be credited with having shifted many children out of the high-risk ‘Not Working’ categories to the lower risk ‘At Work’ ones. The rise in real disposable earnings would account for the reduction in risk for the ‘At Work’ categories, while improvements in the real value of social welfare payments presumably explain the reduction in poverty risk for the

'Not Working' categories. Table 7.16 highlights a significant consequence of this large shift of parents from unemployment or a status outside the labour force into employment. In 1994, a majority of poor children, about two out of three, were in households without work; by 2000, almost one half were in households with work. (Conversely 46.4 per cent of children in income poverty were in households where at least one parent was working.)

TABLE 7.16

Breakdown of Children in Consistent Poverty (below 60% Income Threshold and Basic Deprivation) by Household Type and Labour Force Status of Parents.

		1994	2000
At Work	Two parents, both working	3.6	5.9
	Lone parent, working	1.1	4.7
	Two parents, one working	21.8	35.8
Sub-total		*26.5*	*46.4*
Not Working	Two parents, none working	41.1	15.8
	Lone parent, not working	23.3	22.8
Sub-total		*64.4*	*38.6*
Others		9.2	15.0
Total		100	100

Source: Table supplied by ESRI.

The strong association of child income poverty with non-working parents in 1994 led policy to concentrate on helping low-income parents into employment and on ensuring that non-working parents were supported in ways that did not constitute a disincentive to take employment. The near equal allocation of poor children among parents at work and non-working parents in 2000 is a new situation. On the basis of the evidence in Tables 7.15 and 7.16, it can be concluded that parental employment remains important as the potential route out of poverty for children; however, nearly one half of all poor children already have a parent in employment and this suggests that support for low-paid parents in work has become as significant as tackling joblessness for making further inroads into child income poverty.

Studies done for Britain similarly underline the limits of a reliance on increasing parental employment and earnings alone for raising children out of poverty. One estimate is that over one half of the children in poverty in Britain have parents who cannot reasonably be expected to earn at a level sufficient to lift their children out of poverty. This is because some are already working full-time on very low wages while others are looking after at least one child aged under five, or are sick or disabled (Piachaud and Sutherland, 2000; Sutherland, 2000).

The major programme to increase Child Benefit that began with the 2001 Budget has been a significant measure from which children in poverty have benefited, whether their parents are in work or not. The Council appreciates that the programme originated in the childcare debate rather than from a primary focus on child poverty.[12] When data become available, the higher payments that began in June 2001 will be seen to have also gone some way in alleviating the plight of children in income poverty but it will be important to understand the role Child Benefit will have played.

For example, according to unpublished ESRI data, most poor families with children were more than €50 a week below the income poverty line in 2000. In 2001 and 2002, the weekly increase in child benefit totaled €14.68 for the one-child (lone-parent) family and €70.33 for the four-child family.[13] These increases equivalise to €11 a week for the one-child family and €24 for the four-child family, leaving considerable portions of the income gap still to be closed.[14] If the number of children in consistent poverty, as currently

12. The option of tax relief on childcare costs would have favoured families using paid childcare over those choosing parental care and would not have assisted low income families below the tax threshold. Child Benefit was therefore chosen as the vehicle to deliver assistance towards childcare costs to all families with children.

13. Child Benefit for a first and second eligible child was €53.97, €85.71 and €117.60 in Budgets 2000, 2001 and 2002 respectively; and €71.11, €109.20 and €147.30 for third and subsequent children.

14. Using Equivalence Scale A (1.0, 0.66, 0.33).

measured, drops significantly when data for 2002 become available, therefore, it will more likely be because Child Benefit enabled more households to pass the absolute part of the consistent poverty test (i.e., purchase a deprivation item) than because of any significant change it produced in their relative income position.

The scale of the planned additional resources announced for Child Benefit in 2001 (€1.27 billion initially over a three-year period but stretched to five in the Financial Statement of December 2002) has led the Council to give it careful consideration as a measure for tackling child poverty in this *Strategy*.

There are several legitimate and important objectives, other than alleviating child poverty, which the state can meet by allocating resources to child support. The principal one is horizontal equity by which the 'public good' aspect of children (Folbre, 1994) is recognised, the costs of parenting are to some extent 'socialised', and households without children subsidise those in which children are being reared; universal child benefit is the primary instrument for meeting this objective. The intention here is to subsidise, rather than fully cover, the costs of caring for and rearing a child; recognition of the primary role and responsibility of parents sees the state's function as one of subsidising rather than replacing parental support. This implies that, even if resources were unlimited, Child Benefit at a level that fully covered the cost of caring for and rearing a child would be undesirable and is not required by the principle of horizontal equity. The question of what proportion of the overall cost of children it is desirable Child Benefit *should* cover remains without a clear answer and may be deserving of more explicit discussion. In answering it, society gives tangible witness to some of its most profound values.

Child Benefit has important merits other than subsidising the costs parents incur in raising children. These are that, being a flat rate, it supports parents on low incomes more relative to their incomes than parents on high incomes; it is neutral with respect to the choices parents make as to how they provide care for their children; in almost all cases it is paid directly to mothers; its administration is efficient and receiving it is free of any stigma. The Council does not wish to detract from these positive features to Child Benefit. However, there is a significant opportunity cost in alleviating child poverty implicit in the distribution of Child Benefit, and it can be argued that relying primarily on it to make further inroads into child poverty does not give the needs of children in low-income households the priority they deserve.

TABLE 7.17

Distributional Impact of Increases in Child Benefit (2001-2003), Tax Units Ranked by Decile of Equivalised Disposable Income.

Tax Units[1]	Net Effect of Increases in Child Benefit Relative to Benchmark[2] (2001-2003)	Distribution of Total Increase in Child Benefit (2001-2003)
Decile	€m	%
Bottom	34	6
Second	57	9
Third	36	6
Fourth	75	12
Fifth	85	14
Sixth	83	14
Seventh	65	11
Eight	65	11
Ninth	57	9
Top	51	8
All	607	100

Source: Tables 6.4 and 6.6 in Callan *et al*. (2001).

Notes:

1. Simulation exercises using the ESRI's SWITCH model use a nationally representative survey of households in 1994 updated to reflect changes in population, labour force status and incomes. The calculation of the effects of tax changes is on the basis of 'tax units', which include single people and married couples without dependent children. Hence the term 'tax units' is preferred here even though 'families' is frequently used in ESRI reports themselves.

2. The Benchmark, against which the effects of the three-year increase in CB and continuing freeze in the nominal value of CDAs is measured, is the 'distributionally neutral' policy of indexing all tax instruments and welfare payments (including CDAs) to expected wage growth

Table 7.17 shows one estimate of where increases in Child Benefit, in fact, go in the income distribution. A simulation exercise using the ESRI's SWITCH model predicted that 28 per cent of the total increase in Child Benefit announced in December 2000 for the three budgets, 2001-2003, would go into the top 30 per cent of the income distribution, as against 21 per cent into the bottom 30 per cent. In fact, for each euro that the increases in Child Benefit brought to the bottom half of the distribution, slightly more than one euro was received by the top half. Clearly, the spread of receipts of Child Benefit across the income distribution reflects the presence of children at each level. It is because of this that the Council believes Child Benefit is more accurately viewed as an instrument for meeting the important objective of horizontal equity rather than as an anti-poverty measure.

Several measures target children in low-income families that are additional to the support provided by Child Benefit. Services in kind (e.g., access to child care, extra resources to schools in disadvantaged areas, etc.) can play an important role where they reduce children's exposure to potentially harmful consequences of low parental income. However, the provision of income support for children that is additional to Child Benefit and targeted on low-income households remains important to combating child poverty. Currently, this support takes one form for parents in receipt of social welfare and another for parents in low-paid employment. Child dependant additions (CDAs) raise the level of a parent's social welfare payment to reflect the number of children for whom they are responsible; Family Income Supplement and child additions to tax exemption limits increase the net earnings of parents who are earning at a low level.

Each form of targeted income support has characteristic problems (which underscore the attractiveness of Child Benefit): CDAs can create a disincentive to take employment as parents will lose them by doing so; the FIS increases the effective marginal tax rate facing low earners and can be a disincentive to earning more; finally, there are the problems inherent in making a smooth transition from one form of support to the other.

The disincentive effects of CDAs were given prominence in the early 1990s. As a result, the decision was taken in 1994 to freeze their nominal value. This has acted to offset some of the value to a subset of low income parents of higher Child Benefit; for example, in 2001, families receiving CB alone experienced a 59 per cent increase in their child income support whereas families in receipt of CB and CDAs experienced a 24 per cent net increase. The result of this freeze in the nominal value of CDAs and substantial increase in CB was to make 2001 the first year in which the weekly value of CB for a first and second child (€19.79) exceeded the weekly value of the lowest CDA (€16.76).

The Revised *NAPS* (2002) has articulated the extent of the income support that parents on the lowest incomes can expect to receive from the state. It adopts, as a target, the provision of combined income-support for children (CB plus CDAs) in poor households at a level that will, by 2007, be equivalent to 33 to 35 per cent of the minimum adult social welfare payment rate at that time. In fact, the provisions of Budget 2003 have raised the combined weekly income-support for children to some 37 to 42 per cent of the level of the lowest adult social welfare payment in 2003.[15] As the associated NAPS target of raising the minimum adult social welfare payment substantially by 2007 is implemented, the combined income support for children will also rise further, but by considerably less in relative terms. This can be illustrated by considering what would happen if the 2007 targets were brought forward and implemented in 2003 on top of what Budget 2003 already provided for: adults on the lowest social welfare payment would receive an additional 25.6 per cent increase in their weekly payment, there would be a 13 per cent

15. Child Benefit, as of April 2003, was €125.60 (first and second child) and €157.30 (third and subsequent children) monthly, and the lowest Child Dependant Increase was €16.80 weekly; these aggregate to €45.78 and €53.10 in weekly terms. The minimum adult social welfare payment was €124.80 a week from January 2003.

increase in combined income support for the 1st and 2nd child in low income households, and a 3.3 per cent increase for each 3rd and subsequent child. This uneven pattern of increases leaves open the question whether the standard being set for child income support in low income households is sufficient to secure Ireland's ambitions in, for example, eliminating child poverty and reducing educational disadvantage. An alternative way to formulate the standard would attempt to relate it to estimates of the cost of caring for and rearing a child in contemporary Ireland. For example, a 1992 study, up-rated to 2002 values, suggests that the combined support being provided low income families in 2002 was some 78 per cent of the actual costs of rearing an older child (Carney *et al*., 1994; CPA, 2002).

For these reasons, the Council believes that Ireland has still not found the best package of income support for children in low-income households. The CDAs are steadily losing their value for poor households; CB is not solely focused as a instrument for tackling child poverty—while it undoubtedly relieves some of the economic pressures in poor households, the scale of resources that would need to be channelled through it for it alone to eliminate poverty is not feasible; FIS benefits only children whose parents are in employment and the same is true for child additions to tax exemption limits; there are difficulties and delays that arise as families attempt the transition from receipt of CDAs to receipt of FIS. The Council is also aware that, while parental employment has been the single most important cause of the welcome reductions in child income poverty over the last decade, the same strategy is unlikely to be as successful in rescuing the significant number of children who remain in poverty. The design of a second tier of income support for children in poor families that would be neutral with respect to the work/no-work divide, therefore, has particular merit in the light of Ireland's new circumstances.

Some such new designs have been studied; for example, taxing child benefit and using the additional revenue to increase the level of the payments, or taxing a child benefit that is increased to compensate for the abolition of CDAs (Callan *et al*., 2001). The Expert Working Group on the Integration of the Tax and Social

Welfare Systems (1996), examined the case for a refundable child tax credit (named a Child Benefit Supplement) that would replace CDAs (but not FIS) and have the merit of being neutral with respect to the work status of parents. In simple terms, in households where income is very low such a credit takes the form of a cash transfer, in middle income households it takes the form of a tax reduction, while in households with very high incomes neither a cash transfer nor a tax reduction is received. The key parameters in the design of such a scheme are the level of the payment, the threshold at which it begins to be withdrawn, and the rate at which it is withdrawn. The Working Group acknowledged significant administrative implications because more people are drawn into income/means-testing but pointed to its progressive distributive impact and relatively light Exchequer requirements. Since the Working Group's report, Canada, Australia and the United Kingdom have returned to this issue and introduced a second tier of income support for children that specifically addresses the situation of low-income households where adults may move in and out of work.

The Council is aware of major political and constitutional sensitivities attached to bringing CB within the tax net; it suggests, nevertheless, that facts concerning the distributional impact of CB should be researched and routinely published.

It believes a particularly strong case exists for studying the advantages and disadvantages of merging CDAs and FIS into a single programme which would provide a seamless source of child income support to low-income families, with a withdrawal rate at a low level to minimise disincentive effects. A low withdrawal rate has the disadvantage that it brings more families into income/means-testing but their larger numbers and better means may contribute to ensuring that the procedure is minimally obtrusive and involves little or no stigma. One mechanism might be a refundable tax credit operating through the tax system for low-income families in the tax net, and as a cash payment to families below the tax threshold. An integrated child support payment targeted on low income families could eliminate the discontinuities in the present system in moving from welfare to work, but the challenge remains of designing one that would not suffer from a low take-up rate nor create a significant ‘poverty trap’.

Once in place, such a programme should receive priority in getting extra resources as and when these became available for child income support as this would ensure a targeting of resources on low-income families and those facing the highest risk of child poverty.

7.8 PROPOSALS

7.8.1 The Council’s Proposals on Taxation

Personal Tax

It is clear from Chapter 5 that the scope for personal tax cuts is very limited. The Council recommends that tax credits should, at a minimum, be indexed to price inflation and should lift those on the minimum wage out of the income tax net. Low income earners who do not pay any tax or qualify for social welfare payments do not derive any benefit when tax reductions or social welfare increases are provided in budgets[16], although they do benefit if increased tax credits keep them out of the tax net as their income increases. One possible way to transfer resources to this group would be to introduce refundable tax credits[17]. The feasibility and desirability of refundable tax credits are being addressed by a working group.

The Council has on several occasions expressed its concern at the highly complex system of tax reliefs and the lack of any clear principles in the evolution of these reliefs. The Council believes that such reliefs should only be introduced and retained where they provide clear economic and social benefits that exceed the costs of the reliefs. The Council recommends that tax expenditures should be considered in the current adjustment in public expenditure.

16. These low income earners do, however, benefit from the fact that being outside the tax net means that they receive the full benefit of gross pay increases.

17. Under refundable tax credits, if a person’s tax liability is less than the tax credit, this difference is paid to the taxpayer.

Furthermore, the Council recommends that tax expenditures should come within the scope of the existing programme of Expenditure Reviews. The Council is of the view that there is scope for the abolition of some reliefs that do not reflect economic and social priorities. The Council notes that many existing reliefs are standard-rated and recommends the extension of standard rating to other reliefs. A list of tax reliefs is presented in the Appendix.

Indirect taxes

In the absence of policy change, excise duties (set in nominal terms) will fall in real terms, thus resulting in a real tax cut. The Council recommends that excise duties should, as a norm, increase at least in line with inflation. If excise duties were used as part of the climate change strategy (see below), then duties on energy would also rise by more than inflation.

Environmental taxation

In its last *Strategy* report (1999) the Council expressed its support for a greater emphasis in tax policy on promoting environmentally sustainable development. The Council notes that one initiative in this area, the tax on plastic bags, was a notable success and believes that there is scope for the use of environmental taxes, charges and incentives in a range of areas, consistent with maintaining competitiveness. The design of environmental taxes, charges and incentives (including investment incentives) needs to pay close attention to equity, competitiveness and employment concerns. The design of these measures should also take account of potential differences in impact across regions and sectors and should not undermine the prospects of balanced regional development. The design of environmental taxation should take into account the need for international co-ordination.

The Kyoto agreement to reduce greenhouse gas emissions, with a view to addressing the problem of climate change, was ratified by Ireland and the EU in 2002. It is expected that a sufficient number of parties to the agreement will have ratified it during 2003, and the agreement will then enter into force. Hence, it is expected that the targets for reducing greenhouse gas emissions will shortly by legally binding with penalties for non-compliance. The Kyoto Protocol requires that Ireland limit the increase in its greenhouse gas emissions to no more than 13 per cent over the 1990 level over the period 2008-2012. It has been estimated that, in the absence of policy changes, Ireland's greenhouse gas emissions would be almost 27 per cent above the 1990 level by 2010 (Bergin *et al*., 2002b). Hence, Ireland faces a very demanding target of sharply cutting emissions over a short time period.

The Council notes that the Government has published its *National Climate Change Strategy*. There will be costs involved in reducing greenhouse gases, but the Council believes that Ireland should meet its commitments in this area. It emphasises the importance of an equitable sharing of the burden of adjustment, while seeking to minimise the impact on competitiveness and employment. Significant policy actions will need to be taken to meet these commitments. The Council notes the announcement in Budget 2003 that the Government has asked relevant government departments to advance plans for a general carbon energy tax, with a view to introducing this from the end of 2004. Full consultation will take place with interested parties. The Council considers that economic instruments, including taxes, negotiated agreements and emissions trading, have a key role to play in this area.

Economic instruments have a significant role to play in tackling traffic congestion. Commuting by car imposes significant costs on other road users, including those using public transport, so there is need to change incentives so that social costs are more accurately reflected in commuting costs. One useful initiative in this area was the provision of tax relief for the purchase of annual bus and train passes[18]. Road pricing has been implemented in Singapore and Norway and a congestion charge on traffic entering central London has been introduced.

In the context of the tax and expenditure principles outlined above, the potential for the use of user charges could be evaluated. In any

18. Some of the benefit of this incentive has been captured in higher prices.

evaluation of the role of use charges, the relevant considerations include:

- How charges can reflect the cost of providing environmental services (water, waste water and solid waste disposal);
- How charges can be volume-based;
- Their impact on the overall burden of taxes/charges; and
- Their impact on those on low incomes.

The case for considering the potential of volume-based user charges is that they might provide a way of encouraging efficient use of valuable resources.

Development Land Value Tax

The value of development land stems from the willingness of society to accept development and from the overall development of economic and social activity in the surrounding area. The Council therefore believes it appropriate that those whose assets gain in value from wider economic and social development should return some portion of their gain back to society. Property is an immobile factor, so that negative economic effects are minimised in comparison to the taxation of mobile factors of labour and capital.

One aspect of this is the increase in development land values generated by investment in new infrastructure. The benefits of the substantial programme of infrastructure investment that is now under way will accrue, to a significant extent, to these whose properties become more attractive as a result of this investment and hence appreciate in value. It has recently been proposed to use Section 49 of the 2000 Planning and Development Act to charge a levy on development land along a section of the Luas line. The Council regards this as an appropriate extension of the existing Local Authority levies for sanitation and roads. The Council supports measures of this nature to recover some of the increase in development property values generated by investment. It intends to undertake a further study of housing and development land policy. Among the issues to be considered are the relative mobility of different factors of production and appropriate taxation of windfall gains that arise from general economic and social development.

Tax Evasion

The practice of tax evasion has long been of concern to the Council. In recent years some of the means used to seek to evade taxation have been revealed, including bogus non-resident and Ansbacher accounts. The Revenue Commissioners are continuing their investigations in these areas and other matters revealed by tribunals. The powers available to the Revenue Commissioners were strengthened by the 1999 Finance Act and the Commissioners have used these powers to obtain information from financial institutions. Ongoing developments at EU and OECD level will in time lead to greater co-operation between national tax administrations. The Revenue Commissioners are seeking to negotiate agreements for the exchange of tax information with a number of offshore locations, including the Cayman Islands and Guernsey.

The Council regards the payment of tax liabilities as a fundamental obligation. There is a corresponding obligation of the authorities to ensure that the system of taxation is fair. The Council is committed to strong action to tackle tax evasion.

Conclusion

The Council believes that the tax system should facilitate economic growth and employment creation, while at the same time supporting social inclusion. To the extent that there is any scope for personal tax reductions, given the need for infrastructure investment and improvements in public services, the Council recommends that greater progress be made towards exempting those on the minimum wage from income tax.

Noting the significant developments in income, wealth and expenditure patterns which have accompanied economic growth, the Council recommends, with the aim of achieving further base-broadening, that the scope for new sources of revenue be kept under review.

7.8.2 Proposals on Social Welfare

The Adequacy of the Lowest Social Welfare Payment to Meet Basic Needs

Ireland's lowest rate of social welfare payment has increased much faster than the cost of living since 1994. Notwithstanding this, the Council still does not consider €124.80 per week (January 2003), where it constitutes a person's entire money income, is sufficient to live life with dignity in contemporary Ireland. It recommends that the government implement, as soon as resources permit and earlier than 2007 if possible, its commitment to bring this to €150 (in 2002 terms).

The Adequacy of the Lowest Social Welfare Payment for Participation in Society

The well-being of individuals in receipt of long-term social assistance, or otherwise wholly detached from the workforce, is the Council's primary concern in the area of social protection. Participation in the mainstream of society for people of working age generates self-respect and gains the respect of others. Higher employment rates, lower poverty rates and greater social cohesion are major societal benefits that result from respect for the individual. The Council recommends that this perspective should continue to inform Ireland's practice of 'activation', encouraging people to move from welfare dependence to work. It believes that, for a significant number of people of working age currently on means-tested social assistance, participation will involve employment. Consideration could be given to extending the supports currently available to those on the Live Register (to help them return to work, education or training) to more people of working age outside the labour force. But the Council accepts that other forms of participation can generate self-respect and gain the respect of others—caring for a dependant person; voluntary, social or cultural work; returning to education, etc.

The Adequacy of Social Welfare Payments for a Dignified Retirement

The Council welcomes the commitment in the Programme for Government (2002) to raise the lowest pension rate to at least €200 by 2007, and to introduce a personal pension entitlement for pensioner spouses currently in receipt of the Qualified Adult Allowance at the level of a full non-contributory pension. It recommends that the position of people dependent on state pensions relative to average living standards should be kept under active review.

Household Strategies and Social Welfare Payments

The social welfare code needs to harmonise more with labour market developments and with progress in individualising the tax code. The Council recommends that more rapid progress be made in ensuring that the social welfare code facilitates the choice of couples to make separate and independent claims. It suggests that consideration be given to abolition of the 'limitation rule', to remove the normative assumption of a household breadwinner underlying the current code. The Council also suggests that consideration be given to allowing those seeking *part-time* employment, because of caring responsibilities in the home, to register as seeking work. The ability of people to build up credits within the insurance system—on foot of different types of socially valuable participation made within the home (as carers, as assisting in a family business including a farm, etc.)—should be explored.

Ending Child Poverty

There is mounting international evidence that a dynamic, knowledge-based society is putting a growing premium on the quality of childhood, and that a society which does not accord high priority to tackling child poverty is, by omission, perpetuating major social inequality. In the light of this evidence, the Council recommends that government should pursue with even greater vigour its goal of eliminating child poverty from Irish society.

The Council welcomes the substantial increases in Child Benefit, which provides a significant degree of horizontal equity and has a role as an anti-poverty measure that is free of disincentive effects. It recommends that the design of a second tier of income support for children in poor families be actively studied in the light of Ireland's new circumstances.

APPENDIX

TABLE 7.18

Major Tax Incentives/Expenditures
(ESTIMATED TO COST MORE THAN €20M PER ANNUM)

	Numbers benefiting	Estimated full year Cost (€ million)	Base year from which costing derives	Notes
Capital Allowances				
Capital Allowances (includes business capital allowances and capital allowances to incentivise certain behaviour such as urban and rural renewal)	n/a	1,649	2000	(1)
Corporate				
Resort Relief	n/a	106*	2000	(2)
Group Relief	1,692	316	2000	
Pensions/Savings				
Exemption of the Income of Approved Superannuation Funds (Net of Pension Payments)	n/a	1,274*	1999/00	(3)
Employers' Contributions to Approved Superannuation Schemes	n/a	645*	1999/00	
Employees' Contributions to Approved Superannuation Schemes	n/a	456*	1999/00	
Special Savings Investment Accounts	1,170,200	525	2002	(4)
Retirement Annuity Premiums by Self-Employed	104,500	170	2000	
Pension Lump Sums	n/a	81	1999/00	(3) (5)
Exemption of Interest on Savings Certificates, National Instalment-Savings and Index-Linked Savings Bonds	n/a	82	2000	
Personal				
Child Benefit – exemption from income tax	n/a	272*	2002	

	Numbers benefiting	Estimated full year Cost (€ million)	Base year from which costing derives	Notes
Loans relating to principal private residence – interest relief	462,000	205	2003	
Relief in respect of Medical Insurance Premiums	533,000	160	2002	
Expenses allowable to Employees under Schedule E (work related)	856,900	61	2001	
Health Expenses Relief	99,900	38	2000	
Rented Residential Accommodation	n/a	31*	2000	
Investment in Corporate Trades (BES)	n/a	23	2000/01	(6)
Investment in Films	n/a	24	2000	(7)
Capital Taxes				
Principal Private Residence – CGT exemption	n/a	787	2002	(8)
Stamp Duty Relief for new homes	n/a	112	2001	
Exemption from CGT on occasion of Death	n/a	47	2002	(8)
Indirect Tax				
Disabled Drivers and Disabled Passengers Tax Concessions	7,500	38	2002	(9)
Farm Buildings and Land (VAT Refund)	n/a	30	2001	
Excise relief for local public transport vehicles	n/a	20	2002	(10)
Other Income Tax				
Exemption of income of Charities, Colleges, Hospitals, Schools, Friendly Societies etc.	n/a	87	2000	(11)
Artists Relief	941	30	2000	
Donations to Charitable Organisations	n/a	29	2000	
Relief under Profit Sharing Schemes	n/a	22*	2000	

NOTE: Figures accompanied by an asterisk * are particularly tentative and subject to a considerable margin of error.

(1) The cost shown for capital allowances does not include any cost associated with "unused capital allowances", that is, capital allowances which are not absorbed by a company in the accounting period in which they arise because they exceed the amount of the company's profits of that accounting period and which are available for offset. Unused capital allowances can be offset as losses against taxable profits arising in the previous accounting period and against certain profits arising in future accounting periods and can be offset against the profits of another company in the same group of companies.

(2) The Resort Relief figure relates to an exercise carried out by Revenue and is a very tentative estimate. The figure for the cost of the relief from its introduction until September 2000 (the scheme was introduced in January 1995) is estimated at €317.4 million; the figure shown is an annual estimate.

(3) In the absence of other information, tax has been assumed at the standard rate even though a different rate might be appropriate in many cases.

(4) This is on the basis that the level of investment in the most recent month for which figures are available broadly continues. As the scheme did not close until the end of April and more new accounts were being opened in the first four months of the year, the full year cost will be greater than the expected 2002 cost of €435 million. The expected full year cost is of the order of €525 million. The cost of the scheme is affected where participants die, withdraw from the scheme or vary their monthly contributions. The expected costs provided above assume that these variations will broadly cancel each other out. The SSIA scheme will end five years from when the first contribution was made, i.e. between 1 May 2006 and 30 April 2007.

(5) This is the most recent estimate provided by Revenue; it is not currently possible to capture this figure by way of tax returns.

(6) Due to an increase in the BES investment limit, there will be an additional cost of €3.7 million in 2002.

(7) Film Relief is scheduled to end on 31 December 2005.

(8) CGT is not payable where the capital gain is in respect of the disposal of a person's Principal Private Residence. The figure for the cost of this relief makes no allowance for the number of cases where the disposal of the property was on death, and would therefore be exempt from CGT even in the absence of this relief. The Revenue Commissioners have no basis upon which to estimate the proportion of disposals of principal private residences which are sales on the death of owners.

(9) Benefits here include refunds of VRT and VAT on the purchase of the vehicle, VAT (subject to a limit) on the cost of adaptations carried out, repayment of excise duty up to a maximum of 600 gallons and anyone with a primary medical certificate is exempt from road tax. Cost was €31.8 million in 2001 and is expected to rise to €38 million in 2002.

(10) This was €16.5 million in 2001 but has risen to €17.4 million in the nine months to end September 2002 and is estimated to amount to some €20 million in the full year.

(11) The cost of exempting the income of charities, colleges, hospitals, schools, friendly societies, etc. from income tax includes the sums repaid in respect of tax credits and income tax deducted at source (certain dividends, other investment income and payments received under covenant). It also includes the cost of exempting certain bodies from the deduction on income arising from government securities.

CHAPTER 8

POLICIES ON POVERTY, EXCLUSION AND INEQUALITY

8.1 INTRODUCTION

Social vulnerabilities attaching to Ireland's model of development have been discussed in Chapters 2 and 3, and the specific contribution of developments in taxation and social welfare to alleviating poverty and social exclusion in Chapter 7. This chapter reflects on policies other than income maintenance for tackling poverty, social exclusion and inequality and contains the Council's analyses and recommendations for how they should be further developed over the coming years. Section 8.2 reflects debate within the Council, and which it would like to see continued and deepened across society generally, about the nature of the interdependence between social and economic policy and the extent to which the internationalisation of the Irish economy is blurring the distinction between the two. Section 8.3 reflects on the *National Anti-Poverty Strategy* (NAPS) at its half-way point and makes some observations with a view to helping it become more effective in reaching its targets and securing its outcomes. In Section 8.4 the Council acts on its belief that it has a duty to clarify some of the complex issues surrounding the identification and invocation of socio-economic *rights* in framing and implementing policies to combat poverty and social exclusion. Section 8.5 highlights the significance of legislation and institutions that promote equality. Section 8.6 introduces, and Sections 8.7 to 8.11 systematically address, *four cross-cutting themes* which the Council believes link the many faces and complexity of disadvantage and exclusion at present, and where solid progress is particularly needed over the coming years. These areas arise out of the Council's reading of Ireland's social development trajectory in Chapters 1, 2 and 3 and also of current trends in other advanced industrial societies; international research and experience is used where appropriate to illustrate the nature and significance of the theme in question. Finally, in Section 8.11, the Council recommends that indicators of deprivation and poverty should be kept under review, and explores some reasons for revising the current measure of consistent poverty and adopting a measure of income dispersion as a further macro-level indicator of social inclusion.

8.2 ASSESSING DEVELOPMENTS SINCE 1999

8.2.1 Employment is a bulwark against social exclusion: the labour market approach

In the European Union, a deeper awareness developed during the 1990s that the modernisation of social policy is integral to enabling a dynamic and competitive knowledge-based economy to develop. This is for several reasons. Higher participation rates increase the resources available to deal with the challenges of ageing populations, and social policy can help to raise participation rates. Well-designed social policy can make the best of human resources, liberating people for participation in the economy whom preconceptions and prejudice had considered 'unemployable'. When labour markets are tight, well-designed social policy has the added advantage of minimising the recourse to low skilled immigration with its potential to fuel social tensions if groups in the national population continue to feel they are unable to access decent jobs. Finally, it is easier to introduce reforms that increase flexibility in the labour market and facilitate company restructurings when people see that social policy ensures no-one is 'set aside' but has their living standards and ability to re-enter the economy protected.

8.2.2 Society is more than an economy: the social needs approach

A mistrust of what becoming a dynamic and competitive knowledge-based economy under conditions of globalisation entails for social inclusion developed in parallel with the stronger appreciation of social policy as an 'investment'. Again, several factors are generating this. A strengthening focus on each individual's skills and productivity has pulled the threshold for entry to the formal economy above the heads of a significant minority of people. A gap is widening between the market rewards of people with knowledge and other assets that are highly valued in international markets and a second group who must effectively enter into competition with workers in, or from, regions of the world where living standards are very much lower. The emphasis on higher employment rates can push people into the formal economy without properly acknowledging their ability to make valued social contributions outside of it. Finally, there is a perception that attaining competitiveness can entail rolling back standards of social protection and levels of public service which had been painstakingly constructed in earlier decades.

The Council considers that a notable achievement in Ireland since 1987 is the recognition by the social partners of what is valid in each of the above perspectives and their acceptance that social and economic policies are mutually reinforcing. On the one hand, the real living standards of those on Ireland's lowest incomes have been steadily raised, regardless of the level of unemployment or degree of pressure on the public finances. On the other hand, the pivotal role of employment in reducing poverty, inequality and social exclusion has been appreciated and widening access to employment, and improving its quality have been, and remain, central to the attainment of social objectives.

This complementarity between economic and social policies has been particularly evident since 1999 in the largely positive interactions between the National Employment Action Plan and the NAPS, for which a supportive context was provided by the continuing strength of the economy into 2001. Significant social deficits still remain, however, partly the legacy of the past and partly the result of the very speed and nature of the economic growth that Ireland enjoyed until 2001. In addition, changes in employment patterns and to the family, and population ageing, are creating new vulnerabilities that require new methods and more resources for social protection. Chapter 2 listed the specific social vulnerabilities that still attach to Ireland's development model and

Chapter 3 argued that the slower economic growth and greater business uncertainly that developed in the second half of 2001 and characterised 2002 have contributed to allowing several of them to materialise together.

The Council is aware, therefore, of differing perceptions as to whether, overall, Ireland has become a fairer and more just society in step with its improved economic circumstances. Without detracting from the major social advances made possible by the extensive growth of the 1990s, therefore, it is of the view that opportunities and outcomes are still not fairly distributed across Irish society. It is aware that poverty and social exclusion in Ireland have multiple aspects and are the end products of processes that undermine the well-being of individuals, families, social groups and communities. An unacceptable incidence of social risks and levels of need still arises for:

- Children;
- Young people;
- Lone parents;
- Women;
- People with low levels of education or skill;
- People who are ill or with disabilities;
- Travellers;
- Migrants and members of ethnic minority groups;
- Older workers; and
- Older people.

The Council believes substantial further progress is necessary—and feasible despite the economic slowdown—in implementing its vision of an inclusive society, where all members can participate fully in activities that are considered the norm and where a strong commitment to social justice protects vulnerable social groups and individuals from systematic exclusion (NESC, 1999: 48-49).

8.3 THE IRISH NATIONAL ANTI-POVERTY STRATEGY

The NAPS has been a significant development in the Irish social policy process. In its first formulation (*Sharing in Progress*, 1997), it was presented as "a major cross-departmental policy initiative by the Government" in the design and implementation of which the voluntary and community sector, the social partners, users of services and people with first hand experience of poverty would be consulted and participate. It has a ten-year horizon (1997-2007); an extensive mid-term review and revision was concluded in early 2002, which resulted in a reformulation of the Strategy for the period, 2002-2007 (*Building an Inclusive Society*, 2002).[1]

There are several reasons why it is difficult to identify the direct and additional *net* impact of NAPS to the reduction in poverty of recent years, which has been documented in Chapters 2 and 7. Attainment of its key targets requires the mobilisation and successful coordination of a large number of actors (public, private and voluntary; national, regional and local); when targets are attained, or not as the case may be, it can be difficult to identify why. NAPS is partly an attempt to ensure that *existing* programmes and activities of government (including budgets) are aligned and cohere more strongly in the interests of anti-poverty objectives; it can be difficult to distinguish what might have happened anyway from the greater effectiveness procured by NAPS.[2] Finally, the first period of NAPS

1. The new formulation draws on a more developed and detailed 'Framework Document' published in November 2001. This *Review of the NAPS Framework Document,* by Goodbody Economic Consultants, synthesises the comprehensive preparatory work among the social partners that went into the review process. The Framework Document also draws on the Department of Social and Family Affairs' *National Action Plan against Poverty and Social Exclusion* (June, 2001) that was submitted to the European Commission in the midst of the NAPS review process in order to meet timetables agreed at the EU level for progressing the development of the open method of coordination in the area of social inclusion. The shorter document, *Building an Inclusive Society* (February, 2002), however, is the one which contains the government's official response to the mid-term review of NAPS.

2. For example, at the national level alone, NAPS can be variously interpreted as having been partially supported or offset by features in parallel developments such as the National Employment Action Plan, the National Development Plan and the different Budgets.

coincided with a period of exceptionally strong expansion of employment and rise in living standards, which serves to make the identification of its independent influence a difficult exercise.

Nevertheless, the Council regards NAPS as an important landmark in Irish social policy history and the moment when a multidimensional and dynamic understanding of poverty and social exclusion was endorsed by all organs of government as a shared concern, and a practice of consultation and partnership with individuals and groups affected by poverty was embraced. The first five years of NAPS have undoubtedly given the objectives of reducing poverty, social exclusion and inequality a higher profile than they would otherwise have had in government departments not primarily dealing with the socially disadvantaged, placed a formal leadership role on the Department of Social and Family Affairs, and provided a wide range of non-governmental organisations, including in the community and voluntary sector, with new opportunities for contributing to the shaping of national policies.

In the Revised NAPS (2002), the Council notes and welcomes the following new elements in particular:

- **The recognition that new factors keep emerging which fuel poverty and social exclusion until they are identified and redressed.** In 1997, the key factors identified were educational disadvantage, unemployment, income inadequacy, and the particular persistence of poverty in identifiable urban and rural areas. By 2002, it was acknowledged that extensive economic growth had made access to housing/accommodation and to health services, and difficulties facing members of ethnic minority groups (including racism), significant additional factors contributing to the risks of poverty and social exclusion in Irish society;
- **The stronger emphases on access to quality public services as having a major role to play in combating poverty and social exclusion, on discrimination and the denial of equality as factors limiting access to services and employment, and on the need to accommodate diversity** in the provision of

public services. These emphases effectively accept that, while eliminating social exclusion is a task touching on all sectors of society, a specific type of leadership must come from the public sector;

- **The key remit envisaged for local government in developing social inclusion strategies at local level.** Progress in redesigning policies at the national level and in building capacity at the local level, although by no means complete, has proceeded faster than complementary developments in the role of local government in combating social exclusion in the early years of NAPS. The stronger role envisaged for local government should increase the effectiveness of the inputs from national and local levels;
- **The acknowledged need to incorporate more formally the role of the community and voluntary sector and of volunteering in general.** In innovating pilot programmes which may subsequently be 'mainstreamed', providing services that are closely tailored to client groups on an on-going basis and producing challenging research, the community and voluntary sector has characteristic strengths that public planning and budgeting should allow for from the beginning;
- **The inclusion of the family as an actor in the social process.** The growing diversity of the family has not lessened its huge importance in the lives of individuals and the development of communities. The second term of NAPS will be the stronger for giving more explicit attention to programmes that work through families; and
- **The commitment to raise the lowest social welfare payments to €150 per week (in 2002 terms) by 2007.** Developmental programmes cannot substitute for adequate money incomes in the present. The Revised NAPS effectively regards an adequate income, not as the prize for which people in poverty can be asked to participate in programmes, but as a condition of effective participation and one that increases the likelihood of achieving sustained self-reliance.

The Council makes some preliminary observations, which might help NAPS to become more effective in reaching its targets and securing its outcomes.

- **The implications of making entitlement and access to a range of quality public services a key element in NAPS—and of committing service providers, users and the social partners jointly to setting standards and agreeing on monitoring procedures—should be more fully articulated and explored**. This issue is wider than social exclusion and touches on the levels of taxation the Irish people will embrace, the complementary roles envisaged for the public, private and non-profit sectors in delivering services, and the manner in which the accountability of each sector to service users is best ensured.

- **All parties need to attend to the task of devising arrangements that can achieve effective implementation of the strategic programmes set out in the NAPS.** Arguably, the more global are targets, the more articulated and detailed have to be the strategies for reaching them; otherwise, little will be learned from attaining or missing them. The nature of some targets (for example, reducing socio-economic inequalities in health) is a particular challenge to strategy formulation given that the jury of scientific opinion is either still out on what is effective in addressing them or suggests that attaining them is largely the by-product of progress in securing social integration more generally;[3]

3. The following are some authoritative viewpoints from within epidemiology: "Lower socio-economic status (SES) is probably the most powerful single contributor to premature morbidity and mortality, not only in the United States but world wide. …Although the progress toward understanding the pathways for the health-damaging effects of lower SES is encouraging, clinicians and researchers now face a daunting implication. Instead of simply targeting risky health behaviours, any effective intervention to ameliorate the impact of lower SES on health and disease will need also to reduce hostility, depression, and social isolation—and perhaps to correct autonomic imbalance as well." (Williams, R.B, 1998). "The current social, occupational, and national inequalities in health will not be much influenced by health education, for they reflect the way that societies are organized. We already know what is desirable; the obstacles to its achievement, which prevent the majority from

- **Government departments and state agencies need to do more to ensure their engagement in local partnership arrangements is real rather than formal.** Where each aspect of the programmes and budgets of public bodies is centrally controlled, the engagement of local officers or representatives at local level in the design and implementation of cross-cutting local strategies may only be superficial. National and local government need to plan to allow real space for effective partnership by its officials in area-based strategies;

- **Care should be exercised less a growing procedural complexity make it more difficult to maintain clarity of purpose and a central focus on outcomes.** Process-fatigue can result when formal requirements for complying with procedural norms become onerous; they also take time and energy from activities that are more directly linked to changing outcomes on the ground;

- **An evidence-based approach to policy making (including impact assessment) should be adopted, recognising its dependence on appropriate information, as highlighted by the Council in its *Review of the Poverty Proofing Process* (NESC, 2001).** The most telling argument for mainstreaming a pilot project or other innovation with resource implications should not be aspects of the programme design or the nature of the beneficiary organisation(s) but evidence that the sought-for outcomes for people at risk of poverty and exclusion are effectively and efficiently procured;

- **A more formal and institutionalised role for the community and voluntary sector in deliberating policy, providing services and evaluating outcomes has implications that need to be more fully articulated and embraced.** In consultation with the entire community and voluntary sector, and respecting

having what some already enjoy, are substantially economic, industrial, and political… A radical approach aims to remove the underlying impediments to healthier behaviour, or to control the adverse pressures. The first or medical approach is important, but only the social and political approach confronts the root causes.". (Geoffrey Rose,1992: 100, 105).

its diversity and dynamic nature, there should be an openness to revise procedures where this would ensure new voices are heard, the first-hand knowledge, expertise and commitment of the sector are more effectively drawn on, and services supported by public funding reflect the highest public standards;

- **The contribution that improving the quality of employment can make to achieving the 2002 targets should be maximally allowed for.** Giving more people the opportunity to hold jobs was a major strategy for overcoming poverty and social exclusion over the first five years of NAPS. This should be complemented with a greater focus on ensuring that vulnerable individuals have positive experiences within their jobs (e.g., retaining them, finding opportunities to learn and progress, etc.) over the next five years;
- **The impact of changes to the family, and the contribution of the family as an actor should be more fully integrated into NAPS analysis and policy.** A focus on the family should not be held back on simply because it was a hugely sensitive issue for public interventions in the past. The new diversity in the family and the way major economic and social changes are impinging on family life make it appropriate and necessary that the needs of all types of families be studied and opportunities to support them in their vital functions (Fahey, 1998) actively explored because of the potentially far-reaching effects that can result from successful family interventions;
- **The challenge of the new cultural diversity in Irish society—and of how to ensure the necessary conditions for the successful integration of ethnic minority groups and migrant workers—requires greater attention.** A significant number of the people granted refugee status or leave to remain in Ireland and of the low-skilled workers who have come from outside the EEA are exceptionally vulnerable because of their unfamiliarity with Irish society, limited social networks and other factors. International and Irish research should inform preventive strategies for minimising the dangers of their social exclusion;

- **There should be more attention given to the overall pattern of distribution in income, state benefits, services and tax expenditures, in order to ensure the creation of a more equal and inclusive society and the need to surmount two-tier systems and the development of 'solidarity without equality' (Ó Riain, 2000).** It remains the case that public support to people who are socially disadvantaged is more visible than the significant level of support which also goes to more advantaged sections of society. Informing people more fully of all that the state is providing by way of social support can contribute to greater solidarity and public support for raising the lowest standards; and

- **The NAPS should be aligned fully with the EU National Action Plans for Social Inclusion (NAPincl) and should be included in the Open Method of Co-ordination developing (OMC) across the EU.** As in other areas, there is good evidence that policies for tackling social exclusion in Ireland will benefit from the discipline and systematic comparison involved in participating in peer review at the EU level. It should be a once-off and not insurmountable challenge to subsume the timetable and review procedures of NAPS within those that have been adopted at the EU level for the National Action Plans for Social Inclusion.

8.4 RIGHTS

8.4.1 The Council's 1999 Strategy Report

In its 1999 *Strategy* Report, the Council identified the importance of citizenship rights and obligations. Citizen rights encompass not only the core civil and political rights but also social, economic and cultural rights which are embedded in our political culture and which underpin equality of opportunity and policies on access to education, employment, health, housing and social services (1999: 55). Both sets of rights bring obligations with them.

The Council pointed out that, while civil and political rights and obligations are now generally uncontested in Western European countries, there is far less agreement on social, economic and cultural rights and obligations. It noted that some of these rights may enjoy less support than civil and political rights and those social rights that have a more universal potential uptake, such as education. Furthermore, the obligations associated with social, economic and cultural rights are less clearly defined than the obligations associated with civil and political rights (NESC, 1999: 77-78).

The Council made clear that, in its view, social inclusion is not based on a set of specific rights understood in a justiciable sense. "We are referring to equal access to those social benefits and services that are taken for granted by members of society—this means access to benefits and services and participation in decision-making that are not linked to social and economic status" (NESC, 1999: 78). In 1999, the Council also addressed the question of standards against which progress should be judged. Reference to international declarations and charters proposes a rights basis on which progress on equality should be judged and aspirations directed. The Council recognised that "the identification of rights without benchmarks may be an empty exercise" (p. 76). Indeed, "rights are not just a question of access to services but have implications for the quality and effectiveness of services as reflected in outcomes" (p. 76).

8.4.2 Recent Developments

In recent years, there have been a range of developments which require the Council and Irish public policy to give further consideration to the issues of social and economic rights. These include:

- The agreement on the EU Charter of Fundamental Rights as a political declaration by the European Council;
- The second periodic report of the UN Committee on Economic, Social and Cultural Rights on Ireland's implementation of the International Covenant on Economic, Social and Cultural Rights (see UNCESCR, 2002);

- The incorporation of the European Convention on Human Rights (ECHR) into Irish law;
- The establishment of the Human Rights Commission in July 2002, in accordance with the Good Friday Agreement;
- The Supreme Court decisions in the *Sinnott* and *T.D.* cases in 2001 (see Whyte, 2002);
- The review of NAPS, which linked the question of citizenship rights to the specification of detailed standards on access to services; and
- The study prepared for the Council of Europe, *Access to Social Rights in Europe* (Daly, 2002).

These developments point in diverse directions. Consider, for example, the contrast between the views of the UN Committee on Economic, Social and Cultural Rights and the Supreme Court. The UN Committee recommended that Ireland incorporate economic, social and cultural rights in the Constitution to make them justiciable, expressed concern that Ireland "has still not adopted a human-rights based approach to the NAPS" and argued that Ireland has an "obligation to make the Covenant rights enforceable in domestic legislation" and "a legal obligation to integrate economic, social and cultural rights into NAPS" (UNCESCR, 2002). On the other hand, the Supreme Court struck down decisions of lower courts on socio-economic rights, questioned the idea that implied socio-economic rights could be found in the Constitution and limited the role of the courts on ground of the separation of powers.

As a result of these and the many other developments listed above, there are now highly divergent views and expectations about social, economic and cultural rights and the potential for what is often referred to as a 'rights-based approach' in social policy. Some, drawing on the UN Committee and other arguments, seem to believe that the declaration of a right is the key to securing it. Others, drawing on the Supreme Court, seem to believe that re-asserting the separation of powers is sufficient to address complex, enduring and acute social problems. The result is an unsatisfactory debate on socio-economic rights. The Council believes that a much more productive dialogue on social problems and rights is possible. This requires two things, at least; first, some recognition of the complex issues involved and, second, exploration of the relation between rights and public policy and institutions.

8.4.3 The Complex Meaning, Justification and Institutionalisation of Rights

In discussion of rights a distinction is often made between:

- **First generation rights:** the traditional liberties and privileges of citizenship, covered by the first 20 articles of the United Nations' Universal Declaration of Human Rights (UNDHR), such as free speech, religious liberty, the right not to be tortured, the right to a fair trial and the right to vote;
- **Second generation rights:** the socio-economic rights also outlined in the UNDHR, such as the right to a standard of living adequate for health and well-being, including food, clothing, housing, work, medical care, education and necessary social services, and the right to security in the event of unemployment, sickness, disability, widowhood, old age or other lack of livelihood beyond control; and
- **Third generation rights:** the rights of communities and whole peoples, including language rights, the right to national self-determination and the integrity of culture and ethnicity (Alston, 1987).

The Council emphasises that there are complex philosophical, political, legal and practical issues involved in the identification, creation, legislation and vindication of rights, especially social and economic rights. These are briefly outlined below.

The Basis on which Socio-economic Rights are Defended

The first complex issue is the very basis on which socio-economic rights are defended. There has been much debate on the grounds that support assertion and protection of core civil and political rights, and increasing consensus on the idea that they cannot be established on universally valid foundations (see Waldron, 1984; MacIntyre, 1981; Rawls, 1993). However, as noted below, core civil, political and human rights have proved themselves to be resilient in the face of philosophical scepticism (Ingram, 1994). While a case for socio-economic rights can be derived from the arguments that support civil and political rights, they are usually considered to require different and additional arguments. These arguments vary, as does their acceptability to people and social groups with diverse interests and convictions. Consequently, the case for specific socio-economic rights cannot be taken as self-evident. Or, put another way, where the case for a socio-economic right is widely considered to be virtually self-evident, this is almost always a very general principle—such as the right to adequate shelter or education—and the case for a particular interpretation or implementation of the right cannot be taken as self-evident (Curran, 2002). In either case, this is important because, as noted below, the effectiveness of socio-economic rights depends, to a significant extent, on a degree of public support (see below).

The Relation of Socio-economic Rights to Civil and Political Rights

While some difference between socio-economic rights and civil/political rights has long been recognised, understanding of the similarity/difference between the two is evolving. A strong distinction between the two was asserted by some, and was sometimes used to challenge the validity of socio-economic rights. A direct connection between the two was asserted by others, and used to argue that acceptance of civil and political rights must imply acceptance of specified socio-economic rights. Neither position has proved very robust, and there is now a more nuanced view of the relation between the two. This includes recognition that each can be seen to require the positive establishment and maintenance of costly administrative frameworks (Waldron, 1999:234).

The Relation Between Rights and Duties

There are complex issues in identifying what duties arise from the existence of socio-economic rights. It is generally the case that to invoke a right for some person is to state a duty for some other person. The fact that those who hold rights also hold obligations should not obscure this basic relation between rights and duties. But, it has been pointed out that the tightness of the relation between rights and duties does vary. We may think of a determinate socio-economic right without specifying a determinate duty incumbent on some person or persons in particular. While this point disposes of the objection that there can be no determinate right unless it is correlated with a determinate duty, it also implies that asserting a right can only be a first step in ensuring that a particular need is met. It has been argued that each right is best thought of as not correlative to one particular duty, but as generating successive waves of duty, some of them duties of omission, some of them duties of commission, some of them too complicated to fit easily under either heading (Waldron, 1999).

The 'Air of Absolutism' in Some Rights Discourse

There is a tension between the 'air of absolutism' that can attend rights discourse, and the modern consensus that rights reflect a particular historical, economic and social context (Waldron, 1993: 26; Dorf and Sabel, 1998: 446). Waldron observes that "An unhappy feature of the language of rights is that it expresses demanding moral claims in a sort of 'line item' way, presenting each individuals case peremptorily, as though it booked no denial, no balancing, no compromise" (Waldron, 1993: 26). That feature of rights has always troubled those who are sensitive to the fact that individuals live in a social environment where the things that they may reasonably expect must be adjusted constantly to reflect similar expectations on the part of others.

The Distinction Between Moral Rights and Legal Rights

There is a need to distinguish between moral rights and legal rights. To say that someone has a moral right to something is sometimes thought to entail the idea that they "ought to have a legal right" to it. However, it may be more appropriate to think that it implies that "the law ought to be such that they get it". There are many policy and institutional ways in which something may be secured legally for someone, without them having a *legal right* to it. A socio-economic right—such as that to a standard of living, health or housing—may or may not emerge as a specific or legal constitutional guarantee.

Rights Cannot Provide an Escape from Scarcity and Compromises

It needs to be recognised that assertion of rights cannot provide an escape from scarcity, trade-offs, balances and compromises, including conflicts between rights themselves. Part of the appeal of rights is that they seem to cut through the trade-offs that characterise utilitarian calculations of aggregate social benefit or cost. But if rights themselves conflict and require to be balanced they do not, in themselves, offer an escape from calculations of benefit and cost. This is an important part of the distinction between civil/political rights and socio-economic rights. Socio-economic rights often imply significant re-distribution of resources.[4] The procedures and institutions that protect civil and political rights may or may not be appropriate, effective or legitimate in deciding on such re-distributive matters.

The Dependence of Effective Socio-economic Rights on Public Support

Although the case for social and economic rights cannot be entirely grounded in social consensus, there remains an important sense in which effective rights are dependent on their widespread acceptance. As March and Olsen say "rights and authorities are capabilities easily enshrined in formal rules but more difficult to maintain in day to day political life" (1995: 92). In their view:

> Rights and authorities are protected, interpreted and enforced by a structure of norms and institutions that depend almost entirely on public support for their ability to function. Any protection can be ignored and, being ignored, does not exist. Support by any one citizen depends on expectations of support from others, expecta-

4. As noted above, this distinction is not total. For example, civil and political rights also re-distribute resources and power between citizens.

> tions that depend on the perception of those rights and authorities as meeting shared standards of appropriateness. Both the strength and the occasional fragility of rights and authorities stem from this reflective property of legitimacy. And while the process maintains the norms and institutions that assure stability, it also provided arenas in which rights and authorities are continually being negotiated and renegotiated, interpreted and reinterpreted. Controversies over and discussions about legitimate rights and authorities constitute an important part of the democratic political process (March and Olsen, 1995: 93).

This underlines the need to build consensus on those goods, services and procedures that people can be considered to have a right to (see below).

The Distinction between Socio Economic Rights, Judicial Review and a Bill of Rights

It needs to be recognised that commitment to socio-economic rights does not necessarily entail commitment to judicial review, a Bill of Rights or insertion of socio-economic rights in a constitution. As noted above, socio-economic rights can be secured by a variety of legal, policy and institutional methods. Each has strengths, weaknesses and unintended consequences. These need to be openly examined. Some of the complexities of judicial determination are noted below.

The Tension between Constitutional Rights and Democracy

It has long been recognised that there is a degree of tension between constitutional rights and democracy. Put simply, constitutional provisions put certain principles and rights beyond the reach of democratic majorities and legislatures. There are, of course, compelling arguments that constitutional protection of civic and political liberties is, on balance, protective of democracy. As a consequence, most democracies are constitutional democracies and judicial bodies and functions are seen as an integral part of the institutions that define democracy. But this does not dissolve the tension between constitutional provisions and democracy in a range of substantive areas. This is undoubtedly so in many of those social policy areas that are addressed by socio-economic rights. This tension needs to be recognised in the discussion of socio-economic rights.

Constitutionally Defined Socio-economic Rights and Policy Revision

There is also a tension between constitutionally defined socio-economic rights and normal functions of revision, reform and innovation in public policy and law. While it can be argued that a moral right should be defined as a legal right, some go further and suggest that it should imply a constitutional right. This is often seen as an extra level of protection. While this is often so, it is not always true in reality. Indeed, there are several reasons why a constitutional provision or Bill of Rights may be counterproductive. "One lesson of American constitutional experience is that the words of each provision of the Bill of Rights tend to take on a life of their own, becoming the obsessive catchphrase for expressing everything one might want to say about the right in question" (Waldron, 1999, 220). The gain from embodying a right in a constitutionally entrenched Bill of Rights, in terms of immunity against wrongful legislative abrogation, may be more than offset by the "loss in our ability to evolve a free and flexible discourse of politics" (*ibid*.). The other side of the coin of constitutional immunity is a *disability*: in effect, a disabling of the legislator (and other institutions) from their normal functions of revision, reform and innovation in the law and public policy.

The Distinction between Rights, Recognition and Human Sympathy

Some argue that there is a distinction to be made between rights, on the one hand, and recognition of a common humanity or human sympathy, on the other. In her essay "Human Personality", Simone Weil wrote:

> If you say to someone who has ears to hear: "What you are doing to me is not just", you may touch and awaken at

> its source the spirit of attention and love. But it is not the same with words like"I have a right…" or "you have no right to." They evoke a latent war and awaken the spirit of contention. To place rights at the centre of social conflicts is to inhibit any possible impulse to charity on both sides. (Weil, 1986, quoted in Gaita, 1998).

Her purpose was not to say that rights, as commonly conceived, claim too much, but that they claim too little. For, she continues:

> Relying almost exclusively on this notion, it becomes impossible to keep one's eyes on the real problem. If someone tries to browbeat a farmer to sell his eggs at a moderate price, the farmer can say: "I have the right to keep my eggs if I don't get a good enough price". But if a young girl is being forced into a brothel she will not talk about her rights. In such a situation the word would sound ludicrously inadequate (*ibid*).

The Australian philosopher, Raimond Gaita, sees Weil's point as showing that acknowledgement of someone as fully human is an act of justice of a different kind from those acts of justice which are rightly described as forms of fairness. "Fairness is at issue only when the full human status of those who are protesting their unfair treatment is not disputed" (Gaita, 1998: 81). He argues that if you are taken as 'one of us', then you can mount claims based on rights to an equitable distribution of goods or access to opportunities. "If, however, you are regarded as sub-human, then it would be ludicrous for you even to consider pressing such claims, unless as a device to dramatise the radically different kind of equality that is really at issue" (*ibid*). This is not to say that the law has no role in achieving recognition of human status. It may well be the case that the law or a judicial ruling is the critical and indispensable step towards recognition of the humanity of a previously excluded group, as in the famous Mabo case on Aboriginal rights in Australia (*ibid*). In any case, Weil's distinction between rights and the 'impulse to charity' may not be valid in all cases. Indeed, we know from experience that there is an interaction between rights and respect for others: while it is often the case that an ethic of respect is the source of a right, sometimes statement of a right helps create an ethic of respect.

But the proposed distinction between rights and recognition does suggest that we think carefully about the ability of rights claims to secure the social outcomes we seek in the most effective way. While the position outlined by Weil and Gaita can imply a degree of scepticism about rights, as sometimes discussed, it does not imply scepticism about social justice or about compassion and acknowledgement of our common humanity. Nor does the emphasis on compassion and recognition, pressed by Weil and Gaita, imply responsibilities only for individuals rather than the state and public policy. Acknowledging that compassion is not a virtue that can be exhibited by the state, and only in a secondary sense of the word can compassion be a virtue of a community emphasis, Gaita says:

> But justice is a virtue attributable to states and to communities. In the kinds of examples I have been considering, it partly consists in the creation of institutions which ensure, to the extent that is humanly possible, that our state and civic institutions should not be the cause of such suffering on our fellow citizens that we should be ashamed of ourselves if compassion were fully to reveal it to us (Gaita, 1998: 84)

The link between rights and institutions is explored further below.

Specified Socio-Economic Rights and the Right to Participate

There can be a tension between highly specified and precise socio-economic rights and the right to participate in the shaping of policy, conditions and rights. It would seem contradictory to think of people as worthy of rights and yet deny them a say in what their rights are and how they should be vindicated. Socio-economic rights that are specified very precisely in constitutional provision, statute or judicial findings can limit the involvement of the affected people in the definition and vindication of their rights. This is more than just a logical point. The increasing complexity of social and economic problems, volatility of conditions and diversity of situations has made it more difficult for any high-level authority (be it a constitution, a court or a legislature) effectively to specify the way in which a particular problem should be solved. As noted in Chapter 3, in many areas effective policies can only be agreed, analysed and changed in the context of doing them. This is reflected in the trend, evident across the democratic world, towards involvement of groups and citizens in policy design, monitoring and implementation. It needs to be recognised that this has implications for how we think about socio-economic rights and equality and the mechanisms we create to secure them. It draws attention to McCrudden's idea of 'equality as participation' (McCrudden, 2000)

Tensions Within Justiciable Systems of Socio-Economic Rights

As noted above, the Council does not does not view social inclusion as based on a set of specific socio-economic rights understood in a justiciable sense. In identifying some of the complexities of rights, it has emphasised that social rights are often secured through policy and administrative measures. Where socio-economic rights are justiciable, a number of additional tensions and complexities can arise. These include:

- Tension between the legal pursuit of unique remedies or damages and the social policy need for enduring systemic remedies;
- Tension between the argument from principle or precedent, that is the focus of judicial decision, and considerations of aggregate welfare that resolve trade-offs and compromises inherent in complex policy issues;
- Tension between the court's instruction to a defendant, such as a public agency, and the deliberation among a range of stakeholders that characterises much public policy making and implementation;
- Tension between the occasional court hearing and the continuous monitoring that is necessary in a well run organisation or policy sphere;
- Tension between the expertise and limited managerial capacity of the court and the deep sectoral expertise necessary for effective social policy; and

- Tension between courts' traditional tendency to specify *operating rules* for public bodies that are found to have violated rights and the *standards* and *outcomes* that are becoming the focus of the best policy systems.

These tensions must be taken into account in any discussion of socio-economic rights. They do not make justiciable socio-economic rights impossible, since various types of courts in various countries (including Ireland) are moving towards new types of rulings. In these rulings, courts specify general standards rather than operating rules, and delegate to the affected parties (including administrators, professional but also the citizens whose rights have not been secured) the task of solving problems.

The Mutual Dependence of Rights, Capacities and Identities

Despite debates on the foundation of rights, there is fairly widespread agreement that rights, certainly core civil and political rights to freedom and equality, are part of our identity as members of democratic societies (Dorf, 1996). This identity is determined jointly with the capacities of individuals and groups to exercise citizenship or personhood (Raz, 1986). The extension of rights to new groups involves recognition of their capacities and redefinition of their identity.

The Need for a New Conception of Rights

There is a need to find a conception of rights, and an approach to rights, that can both recognise the many complexities outlined above, and still acknowledge the widespread conviction that rights ought to be respected and the belief that their extension and evolution is closely associated with enlargement of our understanding of humanity and citizenship (Dorf and Sabel, 1998). Some elements of such a conception are outlined in Section 8.3.5.

Conclusion

The Council remains convinced of the validity of core socio-economic rights. However, in view of the complexities listed above, it does not presume that they can always deliver the *simplicity* that is sometimes supposed to be their main advantage (see UNCESR, 2002). Rights are subject to disagreement (NESC, 1999:77-78). Many social rights, like social services, are best achieved when they are co-produced by the citizens themselves. Complex social and economic problems require complex solutions, many of which can only be discovered in practice.

8.4.4 The Link between Rights, Institutions and Commitment: a Loop not a Line

Experience worldwide shows that the reality of rights depends on the creation of effective institutions and policies. This is true of both socio-economic rights and civil and political rights. It is also clear that rights require a commitment; indeed, without establishing a widespread commitment, it is hard to establish a right. Furthermore, as noted above, even when a legal right has been established, its effectiveness is heavily dependent on its widespread acceptance.

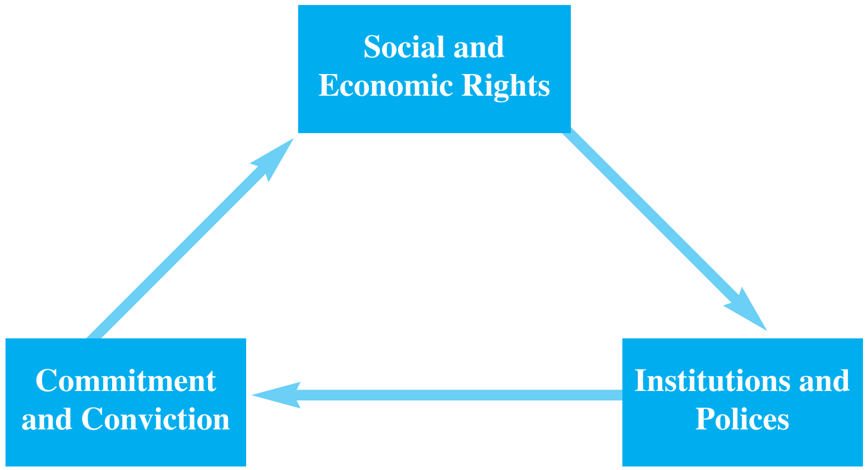
Experience suggests that the connection between commitment, rights and institutions/policies is a loop, not a line[5]. This is illustrated in Figure 8.1. Furthermore, it seems possible to enter that loop anywhere. A right may be established by proclaiming it, but that is rarely achieved. A right may be established by directly persuading society of the priority that should be given to ensuring that citizens receive a certain good or service. That is certainly one way in which socio-economic rights are created. It is also common for socio-economic rights to emerge from the creation of institutions and policies. Indeed, that was precisely the argument of T.H. Marshall in his celebrated paper on the UK welfare state as a system of socio-economic rights (Marshall, 1964). In Ireland, this process is demonstrated, for example, by the development of Rape Crisis Centres. A gap in existing health and police services was identified. Institutions were created to provide these services—and,

5. A somewhat similar approach is adopted in the Council of Europe's report *Access to Social Rights in Europe*: "The underlying view is that access to social rights forms a chain whereby the declaration and framing of the right, the process whereby it is to be realised and the activities and resources necessary to realise it …are all interconnected" (Daly, 2002:31).

just as important, to demonstrate that they could be provided and how they could be provided. This, in turn, led to widespread expectation that such services should be available. These services, and the types of respect and procedures implicit in them, are now seen as a right.

FIGURE 8.1

The Interconnection of Rights, Institutions and Commitment



The Council sees the challenge of social and economic rights as involving the challenge of creating effective institutions and policies for social and economic services. This implies that we focus on the connection between rights and standards.

8.4.5 Rights and Standards

An important contribution to the Irish debate on social and economic rights has been made by those who propose that we explore the connection between rights and standards. It has been argued that if social and economic rights are to be delivered in practice then it is necessary to:

- Develop specific, detailed norms in relation to these rights;
- Establish how these norms or standards are to be monitored;

- Clarify obligations of the state in relation to each of the norms e.g. by reference to indicators and benchmarks;
- Establish accessible, transparent and effective mechanisms of accountability in relation to each of the norms or standards; and
- Ensure that all members of society are fully aware of the rights and standards that they are entitled to expect.

The Council endorses these proposals. The question is: at what level, and by what procedure, are standards to be set, performance to be monitored and accountability to be secured? The challenge outlined above, while it can be seen as the challenge of socio-economic rights, is nothing less than the challenge of finding more effective approaches to public administration, citizens' participation and accountability, especially in the social area.

High-level comparisons of how health, education or welfare in Ireland compare with other EU countries have a role. But standards and benchmarks that not only tell how things are, but also how they can be improved, are much more specific and detailed. This can include comparison of the effectiveness of different approaches to administration, service provision and client/community participation.

The link between socio-economic rights, standards and public reform was emphasised in the Framework Document of the Revised NAPS. The consultants drew attention to the fact that, across the EU, there is now a major quality improvement drive underway in the public services, ranging from standards set at the national level to those locally developed. Increasingly, indicators are being developed to measure good quality and user entitlements. Much of the debate about citizens' rights is focused on client participation, information on the level and type of services to be provided and the requirement that service delivery agencies set quality targets and report their performance against them (Goodbody Economic Consultants, 2001:90). They emphasised that much of the work emanating from the SMI process in the Irish public service is inspired by such values.

This focus was reflected in the Revised NAPS. It said "detailed standards in relation to access to services will be set out". Accordingly, the NAPS will:

- Move towards formal expressions of entitlement;
- Monitor, by means of indicators, access to services; and
- Continue to pursue a much greater focus on effective outcomes and indicators to monitor outcomes.

The Council sees these as key challenges now.

Conclusion

The Council believes that, working in the context of the National Economic and Social Development Office (NESDO), it has a duty to clarify some of the complex issues surrounding socio-economic rights, listed above.

Given the link between rights and standards, the Council proposes that Irish policy, and any new national programme, should contain a process to explore how standards of public service can be better be identified, monitored, achieved and improved in order to vindicate socio-economic rights. This will require considerable extension of the progress made in the SMI and Delivering Better Government and will require the active involvement of all the social partners. The new public agencies—such as the National Disability Authority, the Equality Authority, the National Childrens' Office, the National Consultative Committee on Racism and Interculturalism, Comhairle, the Social Services Inspectorate and NESDO—may have a role in this most important process.

8.5 EQUALITY

Achieving equality is a central element of the NESC vision for a successful society. The Council recognises the achievements made to progress equality in Irish society through the adoption of equality legislation and through the establishment of the equality institutions. However, inequality, discrimination and exclusion persist across the nine grounds and in some instances may have significantly increased. In order to achieve a more equal society, the Council, in line with NESF, identifies each of the following as important spheres (NESF, 2002b):

- **Legislation:** National legislation has a proven role in the pursuit of equality and the effectiveness of legislation should be kept under review, in the light of the experience of implementing the current legislation. Incorporating EU Directives has often provided an opportunity to enhance our equality legislation and may do so in the future. Groups and agencies should be required to produce and implement equality policies and action plans;
- **Institutions:** Strong and widely respected institutions with adequate resources and the full backing of the State are crucial to realise equality;
- **Mainstreaming:** The mainstreaming of equality and evidence-based policy making should lead to significant changes in how services are designed and delivered and how the underlying policies are devised and implemented. For mainstreaming of equality to be effective requires an increased capacity within the civil service and public agencies to engage with and work on equality issues;
- **Participation and decision-making:** The current emphasis is on putting in place new structures to promote participation by the broad community and voluntary sector. Realising objectives of social inclusion, equality and true participation requires (a) specifically targeted supports to marginalised groups and their organisations and (b) institutional change at both operational and policy level in order to ensure that these participatory structures bring about real and sustainable change; and
- **Monitoring and review:** To realise equality within the economic, political, socio-cultural and affective contexts demands monitoring and review procedures, covering all aspects of the equality infrastructure. This requires planned systems for the gathering and analysis of equality data.

Key determinants of progress towards equality will be the strength and authority of the institutions charged with promotion of equality and, across a wide range of policies, the ability to recast national frameworks and institutions in the light of local innovations.

8.6 CROSS-CUTTING AREAS INVOLVING NAPS AND OTHER STRATEGIES

The Council is concerned that the public at large, and those involved in policy delivery, may find it hard to see how the multiple initiatives—consisting of the NAPS, the *National Employment Action Plan*, the *National Health Strategy*, the *National Children's Strategy*, and others—relate to one another and the overall direction in which they are taking Irish society. In calling attention to four cross-cutting themes in Sections 8.7 to 8.10 below, the Council is not seeking to deflect attention from the agenda set out in the Revised NAPS. However, the Council believes that these four areas, in particular, cut across the many faces and complexity of disadvantage and exclusion at present, and that solid progress on these four fronts will impact favourably on every aspect of the social inclusion and equality agendas. The four areas are:

- Ending child poverty and educational disadvantage;
- Building a new infrastructure of care;
- Improving the prospects of those who undertake low skilled work; and
- Responding to new population flows and cultural diversity.

Each of these is now addressed.

8.7 ENDING CHILD POVERTY AND EDUCATIONAL DISADVANTAGE

The economic boom of the 1990s occurred in a country that was young by the standards of the advanced industrial world. The share of Ireland's total population aged under 6 was high throughout the 1990s (OECD, 2001b) and, in 1996, the single largest ten-year cohort in the population was aged 10-19 years (CSO, 1999). The multiple ways in which an era of rapid economic growth and social change can affect children and young people in particular, therefore, need to be carefully studied and monitored at the present time. There are grounds for serious concern. For example, significant numbers of young people are abusing alcohol and smoking at levels which may damage their lives (ESPAD, 2001); suicide has replaced road traffic accidents as the principal cause of death in the 15-24 age group (CSO Press Release, 16 May 2001); there is a widespread perception that many local neighbourhoods have become less 'child friendly' (NCS, 2000); the incidence of type-2 diabetes among children has significantly increased, a condition previously associated with being overweight in middle-age and frequently attributed to a sedentary lifestyle and high-sugar diet (*Irish Independent*, 06/11/02); some young people's school performance is being significantly undermined by the extent of their part-time working (Morgan, 2000; MacDonagh, 2002).

Independently of these particular factors giving children and young people greater prominence in Irish social policies, other advanced industrial societies, despite having fewer children and young people than Ireland and less spectacular economic growth rates in the recent past, are still devoting growing resources to studying and improving the quality of childhood and adolescence. This is largely for two sets of reasons which have been succinctly summarised by Shonkoff and Phillips (2000) for United States policy-makers and service providers. They point to "two profound changes over the past several decades" which have coincided to produce "a dramatically altered landscape for early childhood policy, service delivery and childrearing":

> First, an explosion of research in the neurobiological, behavioural and social sciences has led to *major advances in understanding the conditions that influence whether children get off to a promising or a worrisome start in life*. These scientific gains have generated a much deeper appreciation of: (1) the importance of early life experiences, as well as the inseparable and highly interactive

> influences of genetics and environment, on the development of the brain and the unfolding of human behaviour; (2) the central role of early relationships as a source of either support and adaptation, or risk and dysfunction; (3) the powerful capabilities, complex emotions, and essential social skills that develop during the earliest years of life; and (4) the capacity to increase the odds of favourable developmental outcomes through planned interventions.

and

> Second, the capacity to use this knowledge constructively has been constrained by a number of *dramatic transformations in the social and economic circumstances under which families with young children are living* …: (1) marked changes in the nature, schedule, and amount of work engaged in by parents of young children and greater difficulty balancing workplace and family responsibilities for parents at all income levels; (2) continuing high levels of economic hardship among families, despite overall increases in maternal education, increased rates of parent employment, and a strong economy; (3) increasing cultural diversity and the persistence of significant racial and ethnic disparities in health and developmental outcomes; (4) growing numbers of young children spending considerable time in child care settings of highly variable quality, starting in infancy; and (5) greater awareness of the negative effects of stress on young children, particularly as a result of serious family problems and adverse community conditions that are detrimental to child well-being. (2000: 1-2, italics added)

While the social and economic circumstances of Irish families are not the same as in the USA, the trends Shonkoff and Phillips summarise find echoes in Irish studies too (National Forum on Early Childhood Education, 1998; *National Children's Strategy*, 2000; McKeown and Sweeney, 2001). What is true for other advanced industrial societies applies to Ireland too. In the first place, the unfolding of a knowledge-based society is putting a growing premium on the quality of early childhood and of schooling; if we do not accord a high priority to protecting both we are seriously compromising our ability to maintain our national prosperity. Secondly, if we do not ensure that households in which children are being reared have access to incomes and services adequate to enable children develop without major mishap we are, by omission, perpetuating major social inequality.

The Council appreciates the common interest of the National Children's Office, the forthcoming National Office of Social Inclusion, the Combat Poverty Agency, the Department of Education and Science, voluntary organisations and many health, educational and early childhood initiatives in ending child poverty and tackling educational disadvantage. It emphasises the pivotal significance of these issues in limiting the perpetuation of social disadvantage and providing a solid foundation to Ireland's future prosperity. Its recommendations on how child income poverty should be further reduced were outlined in Chapter 7, but the Council is aware that child poverty is not just economic. For example, the Annual Report 2000 of the Chief Medical Officer focused on children's health and establishes that poverty is the most important social factor associated with poor health among them. It concludes that improving children's health will not hinge primarily on more medical services but on better social policy: "specific policy measures which redistribute resources, provide opportunities and services for families with children, especially poor children, will do most to create better child health." (2001: 7). Notwithstanding this, the Council notes the call by the Chief Medical Officer that "basic universal health provision, such as free access to primary care for all children, should be considered" and recommends that further analysis be made of this possibility.

An issue closely related to child poverty is educational disadvantage. Educationalists and labour market economists have become steadily more aware of the major and lasting significance of poverty in early childhood. For example, there is evidence that under-performance in secondary school can be addressed more efficiently and cost-effectively by income interventions in early childhood than by scholarships or subsidies in the teen years (see Box 8.1). The interpretation of this evidence emphasises the nature of underperformance at secondary school and early school leaving as a culminating moment in a drift that begins much earlier. Conversely, in the lives of students who do well at school, a cumulative preparation is seen to take place from infancy onwards giving them a good level of school preparedness and the taste for education that makes their choice to complete secondary schooling and transfer to third level come relatively easily. James Heckman (2000) concludes as follows:

> Children whose parents have higher income [in early childhood] have access to better quality primary and secondary schools. Children's tastes for education and their expectations about their life chances are shaped by those of their parents. Educated parents are better able to develop scholastic aptitude in their children by assisting and directing their studies. The influences of family factors that are present from birth through adolescence *accumulate over many years* to produce ability and college readiness. (italics added)
>
> *Research in Economics*, 54, pp.3-56.

By contrast, children whose lives begin in poverty are less likely to do well at primary school, more likely to enter secondary school with insufficient standards of numeracy and literacy, and, thus, more likely to encounter problems in secondary school and to seek reasons for leaving. A report by the UNICEF Innocenti Research Centre observes that "a family's social, cultural and economic status tends to act like a rifle-barrel setting an educational trajectory from which it is difficult to escape" (2002: 21). Difficult but not impossible, for the same report emphasises that "attempts to mitigate educational disadvantage need to begin even before a child starts school" (24) and that schools themselves can also make a significant difference with some national educational systems managing much better than others to reduce the disparity in educational outcomes of their students.

There is also a new awareness that social disadvantage in later life—such as periodic unemployment, social welfare dependency, poor health, conflict with the law—can frequently be traced back to poverty experienced in childhood and that educational underperformance is a major causal pathway. This grounds the conclusion: "those who begin life with insufficient schooling or motivation to learn will, in a knowledge economy, in all probability face a difficult life course of low wages, poor training opportunities and precarious employment. Even well designed activation policies are unlikely to correct this" (Esping-Andersen *et al*; 2001:20).

BOX 8.1

Parental Income and Children's Educational Attainment

One US longitudinal study had data on income and other variables in the lives of 1,323 individuals from their infancy until they reached the ages of 20-24 (from the Michigan Panel Study of Income Dynamics). The authors wished to establish whether parental income varies in its significance in predicting a young person's likelihood of completing schooling, *depending on when in the child/adolescent's life span it was received.*

The variable to be explained was whether an individual had completed secondary schooling or not. They were able to distinguish the average level of parental income in the person's home during early childhood (ages 0-5), middle childhood (ages 6-10), and adolescence (11-15). They controlled for the mother's schooling, family structure, race, sex, and the age of the mother at the birth of her child.

Average parental income during the ages 11-15 *was* statistically significant in predicting the likelihood of completing secondary school (coefficient 0.06).

Average parental income during the ages 0-15 was also statistically significant, and had an effect nearly *twice as great* (coefficient 0.11).

> When average parental income during ages 0-5, 6-10, and 11-15 were entered as separate and independent variables, *only income in early childhood* had a significant effect and it was greater than income averaged over the whole 0-15 period (coefficient 0.14). Early childhood emerged as the crucial period when the level of parental income has its most significant effect, with later periods no longer having significant effects.The authors describe the implication of their findings as "remarkable" and concluded: "the only stage for which parents' income significantly predicted completed schooling is early childhood. Thus, the only reason that parents' income during adolescence or middle childhood predicts completed schooling is apparently that income during those periods is correlated with income in early childhood."
>
> (Duncan and Brooks-Gunn, 1997)

The causes of underperformance at school can be summarised as economic, social and systemic (i.e., lying within the educational system itself). On the economic front, the level of income in households, particularly during early childhood, the security of parents' employment (particularly the avoidance of unemployment) and the extent of part-time working on the part of teenagers, are seen to influence a young person's chances of doing well educationally. On the social front, parents who themselves did not stay in school long, are struggling with financial difficulties, rearing their families in disadvantaged neighbourhoods, in conflict with each other, or belonging to ethnic minorities insufficiently integrated into society, are less likely to be in position to provide their sons and daughters with the full range of supports they need to do well at school. On the systemic front, there is evidence that, while in school, the benefit young people extract from it has much to do with their social background rather than their level of intelligence or ability, i.e., the curriculum, pedagogy and 'culture' of the school suits some young people more than others.

In Ireland, the target of increasing the percentage of young people completing the Leaving Certificate to 90 per cent by 2000 (NAPS,

1997) has not been met; it reached 82 per cent in 2000 (NESF, 2002a). Some 15 per cent of young people were finishing school with their Junior Certificate only and a further 3 per cent with no qualification at all. There are considerable grounds for concern, therefore, that almost one in five young people are leaving the educational system without the preparation they need to become fully integrated into working life. Many of them will face increasingly bleak prospects in adult life because of their underperformance at school. The buoyant labour market of the 1990s has had an unintended and perverse effect. It created a supply of 'youth jobs' among others, and young people who found school of little relevance to their needs were particularly likely to abandon education in order to seize the status and freedom that comes with earning.

It is imperative that all young people should receive a foundation in their schooling on which they can build satisfying lives as adults. The Council supports the view that education consists of personal and social development, as well as career development and preparation for a productive role in the economy. The interests of those who will *not* complete the Leaving Certificate, as well as of those who, upon completing it, will *not* transfer to Third Level, must also be served by the educational system. International evidence suggests that success in reducing educational disadvantage is closely linked to success in diversifying what is on offer *within* the senior cycle of secondary education (in curriculum, courses and pedagogies) to cater for a wider range of student intelligences and abilities. The Council underlines the importance of the on-going work of the National Council for Curriculum and Assessment in this regard. It is pointed out that the 1997 target to raise the Leaving Certificate completion rate to 90 per cent did not adequately reflect the legitimacy of interventions outside the mainstream school setting (Goodbody, 2001), and the Council supports the view that youth organisations should be supported in widening "non-formal provision for early school leavers" (NESF, 2002a). The options available to early school leavers should include their being able to return to education under conditions that are attractive to them (for example, through a form of modularisation of the Leaving Certificate, such as is currently available only to adults).

Because early school leaving is more properly seen as the culmination of a long process of failure, low self-esteem, poor adjustment, low aspirations, low intellectual stimulation and poverty, rather than as an event, it follows that a holistic approach is needed which incorporates the school without leaving it all to the school. The Council points out that combating early school leaving and educational disadvantage is an objective requiring the integrated response that local partnership can help provide.

Despite over two decades during which social class inequalities in educational participation have been of concern, the evidence is that relative inequalities have declined little, and that the stark contrasts which used to characterise participation at secondary level have moved on to characterise third level participation and performance. Active parental selection of schools means that schools are more likely to reinforce existing social inequalities than contribute to reducing them. The Council believes that the objective of greater equality remains important to the quality of Irish society and the foundations of its prosperity. It is confident that the elimination of child poverty and the embrace by the secondary school system of the interests of young people not progressing to the Leaving Certificate will prove to be important milestones in achieving greater equality, and it underlines the urgency of these issues.

The broader vision of the Council encompasses a time when all children in Ireland, no matter the social and economic circumstances of their parents, will be able to avail of comprehensive health services, pre-school facilities and neighbourhood amenities on an equal footing. It advocates this objective for egalitarian reasons and because it believes Ireland simply cannot afford not to do so. It will be far more difficult to construct a dynamic, knowledge-based and competitive economy if a significant section of the population is condemned to marginality.

8.8 BUILDING A NEW INFRASTRUCTURE OF CARE

Changes in the world of work and to the family are combining to erode the traditional patterns by which Irish society maintained what is, arguably, the most important infrastructure of them all, that supporting caring. Children, young people, older people, people with disabilities, and sick people could traditionally rely on the availability of a household member, almost always a woman, to provide a first and often sufficient level of care, leaving quite subordinate roles to state services or purchased market services. This is no longer feasible for a growing number of households, nor is it a just and fair expectation to hold of women as a gender. Women have entered the workforce in growing numbers but the caring that is available from public and market services has not expanded at a proportionate rate. As a result many women are under exceptional pressure trying to balance work and their responsibilities in the home; others feel they have had unfairly to opt for one to the exclusion of the other because sustainable options for combining paid work with caring responsibilities do not exist. Mothers in the higher socio-economic groups can experience that the requirements of a professional career tend to penalise a preference for part-time work, job-sharing, flexi-hours, or leaves of absence for family reasons; mothers in low-skilled services employment can find that their working conditions increasingly sap the energy they bring to the work awaiting them in the home (Murphy-Lawless, 2000).

8.8.1 Context

Three observations serve to underline the pressure that has come on traditional arrangements for caring in Irish households. The economic boom had a dramatic effect in accelerating the rise in female participation in the Irish workforce.[6] This rise was almost totally driven by the changing behaviour of women who had completed secondary school; the participation rates of lesser educated women did not rise from its low level while that of women

6. In the eight years prior to 1994, the female participation rate (ILO basis) rose by just over 4 percentage points (from 33.8% to 38% between 1986-1993). Over the next eight-year period 1994-2000, it rose by ten percentage points to reach 48% (Sep-Nov, QNHS). This rise has been despite a secular decline in the participation rate among the 15-24 year old women, reflecting their rising rates of participation in education.

with a third level education had consistently been high before the economic boom (Duffy *et al*. 1997). In second place, by the standards of other northern EU member states, an unusually high proportion of the jobs that Irish women took in the 1990s were full-time rather than part-time. For example, in 2001, the full-time equivalent employment rate of Irish women was 4 percentage points higher than in the Netherlands, even though the latter country had a female participation rate that was 10 percentage points higher (European Commission, 2002b). In third place, the rise in women's participation rate associated with the economic boom was particularly rapid for the mothers of young children. The Commission on the Family (1998) examined Labour Force Data for 1996 to establish that young families (households with children aged under 15) were twice as likely to have both parents working as older families.

Table 8.1 confirms how rapidly women's employment rates have risen during and after the economic boom. Lone parents record the most dramatic rises; since the year 2000, they have become consistently more likely to hold employment when their children are aged 5-14 than women with a husband or partner. When the child is aged under 5, the employment rate of lone parents is relatively low and comparable to that of older women, suggesting that more of them care for their children full-time and see few real alternatives. Since 1998, more than 50 per cent of women with a child aged under 5 and a husband or partner in the home are holding employment.

These observations are enough to explain why the time budget of parents, and of mothers in particular, and their ability to balance work and traditional caring roles within the home were under acute strain by the end of the 1990s. The interaction of these developments throws light on the relatively sudden appearance of a strong demand for childcare since 1994.

TABLE 8.1

Women's Employment Rates (ILO basis) by Composition of Family Unit, 1995-2002.

Composition of Family Unit	1995	1998	1999	200	2001	2002	2002/1995
Husband & wife/Couple: without children							
Woman aged under 45	79.1	85.8	86.9	88.9	88.9	88.3	1.12
Woman aged 45-64	22.1	29.6	30.9	34.2	35.7	38.1	1.72
Husband & wife/Couple: with children							
At least 1 child aged under 5	42.2	50.7	53.4	55.4	54.6	55.2	1.31
All children aged 5-14	40.5	52.2	56.6	57.4	59.1	61.1	1.51
All children aged 15 or over	22.6	31.9	34.2	36.8	39.2	41.8	1.85
Lone parent with children							
At least 1 child aged under 5	20.2	40.6	40.3	45.2	45.0	43.1	2.13
All children aged 5-14	39.6	56.5	55.6	66.3	67.2	67.9	1.71
All children aged 15 or over	14.8	22.0	25.5	27.2	28.4	29.3	1.98

Source: QNHS, March-May, of each year.
Note: Employment status for 1995 is PES. Otherwise based on ILO status,

Quite apart from Ireland's particular circumstances, however, the international evidence is that the unfolding of the knowledge-based, services economy generally is driven disproportionately by women (Esping-Andersen, 2002). They constitute a more important source of new entrants to the workforce than men, the younger cohorts of women now have higher educational attainments than their male counterparts, and a significant proportion of the new services jobs coming on stream are, in effect, the way in which the market or the public sector is compensating for the demise of the home duties and caring formerly carried out by women in the home. With or without the boom, therefore, Ireland would have had to face the implications for social protection, inclusion and equality of the erosion of the traditional infrastructure of care provided by women in the informal economy.

The Council notes that a gap has already opened in Ireland between the preferred and actual number of children which women are having (Esping-Andersen, 2002: 64) and points out that, while the large families of Ireland's recent past were frequently associated with poverty for children and drudgery for women, it is not optimal to move to a situation in which obstacles are created for people in forming families of their own choosing (by incompatibilities between motherhood and work, difficulties in accessing housing, and the growing costs of rearing children). Several EU member states accept that a contributing factor to their very low birth rates and acute pressures of demographic ageing has been the accumulation of factors dissuading women and couples from starting a family.

The Council regards the rise in the participation rate of women in the Irish economy as reflecting and reinforcing an enduring and far reaching transformation in Irish society generally. "All is changed, changed utterly" not just for women but for men and children too, not just for the economy but for family and social life as well. The crisis in care, therefore, is much deeper than the economic issue of how employers can access the skills of people whom caring responsibilities are making unavailable. It touches on values fundamental to society, the value put on children, on people for whom participation in the economy is unrealistic and on the health of family life. Several issues—the shortage of child care facilities, the need for family friendly workplaces, the particular difficulties facing one parent households, the isolation and lack of recognition experienced by many carers of young children or other dependant household members, the postponement of motherhood and decline in the birth rate, the lower earnings and poorer labour market histories of women—are each manifestations of this crisis. The Council believes that, cumulatively, they constitute a compelling reason why Ireland should press forward with the revolution in gender equality that has begun and ensure that its social and economic policies genuinely facilitate parents in choosing how they can accord the age-related needs of their children the priority they want without either parent having to turn away from a satisfying and interesting career.

While education drives women's participation rates, their caring responsibilities for young children, other things being equal, constrain the types of employment which some of them can take. The full range of influences on women's decisions to participate or not in the formal economy is, in fact, quite complex.

Doris (2001), for example, established that low skilled women's participation in the workforce is particularly sensitive to the likely wage they can expect and that, for women in general, each child aged less than four years reduces the probability of participation by about 17 percentage points (in 1998). Children of primary school age have a smaller but still strong negative effect (10 percentage point reduction in probability per child for low skilled women, 6 percentage points for skilled) whereas older children (aged 13-18) appear, if anything, to increase the probability that they participate in the workforce. Doris interprets this as evidence that, as children get older, the urgency for a mother of spending time with them weakens as their school hours lengthen while, at the same time, the children get more expensive, increasing the mother's need for additional income.

Russell *et al*. (2002), studying women in home duties, found that the single biggest predictors of which of them were seeking work were (in order of the size of the effect of those factors which were statistically significant and positive) how recently they had last held a job, being in receipt of a payment as a lone parent, being in receipt of Unemployment Assistance, having been involved in education or training the previous year, and having a youngest child aged 5-12. The biggest predictors of who was *not* seeking work, on the other hand, were being in receipt of a payment for sickness or disability, being aged over 55, having never married, being aged 45-57, and having a youngest child aged under 5.

Ireland is in process towards, rather than having arrived at, a sustainable balance in how a modernised welfare state, the private sector and voluntary organisations complement each other to ensure a solid infrastructure of care services, one that would address the reality of care in family lives and free women in particular to access employment opportunities of a type and in a way that does not endanger dependant household members.

8.8.2 Child care

The Council regards the growth in childcare places under the Equal Opportunities Childcare Programme (EOCP) of the National Development Plan, 2000-2006, as not adequate to meet the scale of need. By November, 2002, it had supported 40,840 new places or just under 20 per cent of the estimated total needed (210,000 places). The Council notes that 37 per cent of the seven-year budget has been allocated to achieve this, yet believes that the core constraint in the medium term continues to be the capacity of the childcare sector to bring new places on stream. The Council recommends that funding should be increased when and as there is the capacity to use it and that the lead agencies in administering the EOCP should be pro-active in ensuring growth in the number of successful applications to use its funds.

The Council underlines the urgency that attaches to this issue. It believes that parents are currently paying too high a price, in emotional and health terms as well as financial, for the absence in this country of the types of services which are widely available in other advanced societies. The Council would like to see high quality child-care facilities for pre-school children becoming available across the nation within a realistic timescale and welcomes the challenge in the targets set at the Barcelona European Council (2002). It believes that here, as in other fields, the weakness of local government in Ireland poorly positioned the country to respond with the decisiveness and effectiveness that profound social change required.

The Council welcomes the triple objectives of the EOCP, viz. to improve the quality of childcare, to maintain and increase the number of childcare facilities and places, and to introduce a co-ordinated approach to the delivery of childcare places. It does not believe, however, that attention to quality and the improvement of existing facilities should lessen the urgency of substantially increasing their supply.

It welcomes the establishment of the County Childcare Committees and the comprehensive approach they have taken in their five-year Strategic Plans (2002-2006). A network covering the state has been established, in which all stakeholders are represented and for which standards and outcomes have been set and are monitored. The Council believes this partnership approach at local authority level offers the real prospect of childcare services becoming available to all parents, and of stemming the development of a two-stream system that divides and separates local children on the basis of their parents' income. It recommends that the relative achievements of the different County Childcare Committees be monitored in order to identify as quickly as possible what works in Irish circumstances. It recommends that the Inter-Departmental and Inter-Agency Synergies Childcare Group, through which the several government departments and state agencies with a brief in this area co-ordinate their work, use the SMI framework to formulate a clear national policy that will ensure the best guidance and fullest support to the County Childcare Committees.

This policy should include a national policy on childminders that will enable people with skills and experience in caring for children and parents with needs for childcare services to efficiently find each other. Such a policy could provide childminders with more status and better prospects and parents with more security in the quality and reliability of the service. The Council notes the simplicity and attractiveness of the innovation by FÁS whereby it pays childminders, sourced by its trainees, directly for their contribution to freeing people for participation on its mainline programmes.

The Council believes that a variety of different models for providing childcare should be fostered, and that it is the quality of the service that counts, not the origin of the service provider. It recommends that the County Childcare Committees actively examine the development of a template for childcare centres run as social associations that would increase the capacity of voluntary and community groups to attract funding. It also recommends that serious consideration be given to public-private partnership arrangements with commercial providers to widen the social mix being catered for through their centres and justify a higher public subvention to their construction.

The Council notes the particular shortfall to date in proposals to develop after-school services for older children (where school authorities and parent groups might be expected to have a particular interest). It recommends that the Department of Education and Science pay particular attention to identifying and surmounting any obstacles that may make the use of otherwise idle school buildings available and appropriate for after-school child minding.

8.8.3 Care of Older People and People who are Ill or With Disabilities

A particularly successful innovation has been the introduction of the Carer's Allowance, and the provision of respite care to carers by the Health Boards. Over 19,000 people now receive the Allowance and the Council considers it a headline example of how Ireland is building a new infrastructure of care. The Council underlines the continuing need to enhance the status of carers and to facilitate their transition into further employment, education, training, when they so wish it. It is important that Ireland learn from best international practice as to how the population of working age can be supported in responding to the needs of the 'oldest old' (80+) and the growing number of them who are chronically ill and physically or mentally frail.

Currently, only acute cases of need requiring a person to leave employment are catered for. The ability of workers to access caring services for older people or people with disabilities in more tailored ways remains restricted, and the Council urges that the necessary services be fully developed. Priority should be given to promoting and enabling maximum independence and autonomy for both older people and people with disabilities within the design and provision of care.

8.8.4 Family friendly employment policies

In its 1999 *Strategy*, the Council said "the introduction of parental leave was an important first step in helping parents to reconcile work and family responsibilities. It should also promote equality of opportunity for women who tend to be the primary caregivers by building greater flexibility into working arrangements". The Council noted that parental leave in Ireland is unpaid and considered that "this gives rise to serious equity concerns as it is unlikely that low income parents will be able to avail of parental leave because of the implied loss of earnings" (1999: 299).

The Council welcomes the extension by eight weeks of paid and unpaid maternity leave (March, 2001) and the extensive review undertaken of current provisions governing parental leave (April, 2002). It notes that a number of issues concerning maternal and adoptive leave are outstanding. It notes the diversity of EU practice in this field and the current difficulties that have been experienced in reaching consensus on what further legislative measures Ireland should take. It further acknowledges the other important steps that have been taken in helping people to reconcile work and caring responsibilities, viz., the Carer's Leave Act, 2001, and the Carer's Benefit Scheme.

In order to make paid work truly compatible with having children, most mothers need jobs that are reasonably secure and have flexibility in their hours. Generally, maternal employment is positive for mothers' well-being and that of their children (Hoffman and Youngblade, 1999) but, if mothers can source only stressful and insecure jobs, this can have negative, secondary effects on children's development. If there is not to be a segmentation in the labour market between jobs suitable to women and those suitable to men, the employment conditions of men must also become more compatible with greater co-parenting on their part. Women should not have to confine themselves to segments of the labour market because it is only in them that they find hours and conditions of work that are compatible with domestic responsibilities. Where lone parents have poorly marketable skills and responsibility for pre-school children, the evaluation of the net effect of their moving from welfare to work should include an assessment of its effect on child development. The wider issue of the quality of employment is addressed further below.

The Council believes that the agendas of competitiveness and equality overlap more than they differ and that empirical verification of the benefit—in reduced absenteeism, lower staff turnover and higher productivity—of family friendly employment policies that are properly structured and agreed would contribute to greater consensus. It recommends that experience in selected countries with high standards be more intensively studied and that intermediate policy objectives be considered to keep policy reform moving in this area, e.g., ensuring couples have the option of keeping one parent with an infant from birth until its first birthday, through the aggregation of maternity and parental leave, agreeing a list of flexible working arrangements and by encouraging employers to provide at least one of the agreed arrangements to workers with pre-school children.

There have been other single but important steps in building a new infrastructure of care. Since its introduction in late 1990, the number of recipients of Carer's Allowance has grown by more than 2,000 a year and, by 2002, some 20,000 people were receiving it. The provision of respite care to them has become more widely accepted and allowed for by the Health Boards. The Council is sympathetic to the view that receipt of a Carer's Allowance might give people access to the social insurance system for certain benefits. The intention would be, not to break the link between participation in the workforce and entitlement to social insurance benefits, but to recognise that to care for certain people on a full-time basis is, in effect, to participate in the national workforce.

The Council recommends that progress in all these areas be accelerated rather than slackened because of its appreciation that women, family life and children are continuing to experience exceptional stress in Ireland arising from women's and men's difficulties in balancing work and home responsibilities. It regards the major change that is taking place in how the dependant members of Irish families are cared for, and its consequences for women, as also strengthening the case for facilitating women to make independent social welfare claims as discussed in Chapter 7. It points out that, for the Irish economy to remain attractive to internationally mobile knowledge workers, and for companies to be able to attract and retain workers with significant caring responsibilities, greater progress needs to be made in facilitating employees to balance their work and home lives.

8.9 IMPROVING THE PROSPECTS OF THOSE WHO UNDERTAKE LOW SKILLED WORK

8.9.1 The context

The most remarkable feature of the economic boom of the 1990s was not the attainment of sustained high economic growth but the extent of the employment expansion associated with it. A net 450,000 jobs were created during the 1990s, profoundly gain-saying even apparently solidly-based and, by the standards of the time, benign predictions (Industrial Policy Review Group, 1992). Some 335,000 of these jobs were in the services sector, mainly private market services of which some, in turn, were high-skilled and high-productivity jobs while others were low-skilled and low-productivity. This bifurcation in the type of services jobs that came on stream means, on the one hand, that the graduates of Ireland's schools, universities and institutes of technology experienced that a stronger economy needed and rewarded their skills more than before. On the other hand, however, the full extents of the rise in employment rates, inroad into unemployment and reduction in poverty were achieved only because a substantial number of Irish people with relatively low skills made the transition from welfare-dependency or a status outside the labour force to job-holding.

This employment-intensive nature to Irish economic growth was unexpected. Higher productivity on the part of a slowly growing number of people in employment had described Ireland's pattern of economic growth from 1960 to 1993. During the 1980s, the Irish services sector had generated fewer jobs in relation to its GNP by comparison with other OECD countries (NESC, 1993b; Tansey, 1998). It is now clear that, in addition to high economic growth, it took the cumulative impact of lower taxes (particularly on low earnings), improved incentives for welfare recipients, wage moderation, the erosion of anti-competitive practices and, in general, an improved environment for small and medium-sized enterprises to allow low-productivity service jobs to expand alongside their high-productivity counterparts to the extent that they did. The Council believes that the social partnership process developed since 1987 played an important role in facilitating these changes and allowing Ireland's economic growth to become more labour intensive.

Turning to international experience, the Council notes the different approaches that countries have taken towards low skilled jobs and their role in helping achieve social inclusion (see Box 8.2)

BOX 8.2[7]

Different Approaches to Low Skilled Jobs

A Scandinavian approach has relied principally on recruiting relatively low skilled workers to expand public services, such as childcare at municipal level, to meet the new needs of households arising from high employment rates and the diminished time budget of both men and women for caring and housework generally. The services are funded from general taxation. From one viewpoint, this approach is simply moving activities from the informal into the formal economy but, in the process, impressively high employment rates for low-skilled and older workers, and extremely low gender differentials in earnings, were achieved. The approach, therefore, considerably abetted

7. The summary in the box is drawn from several sources. For a major, in-depth review, see Scharpf and Schmidt (2000).

social inclusion. However, it prospered best when the private sector could absorb relatively easily the high taxation that was involved. More difficult international trading conditions have exposed weaknesses in the approach; there is little incentive for skill-upgrading, the private services sector remains underdeveloped, and net outward rather than net inward investment is likely to ensue.

A Continental European approach has set consistently high standards for employment. Employment brought a relatively generous set of entitlements and levels of social protection, both for the individual worker and her or his dependants. This social protection was funded by insurance charges levied on the employment contract. In so far as the majority of jobs were high-productivity and full-time, and most 'breadwinners' were able to find one, the approach provided extensive social protection. However, global competition has eroded the share of high-productivity, manufacturing capacity being located in Europe and, in the new services economy, a significant proportion of jobs are unable to carry high insurance charges and remain viable. Employment prospects for the least skilled are choked off. Passive income transfers are relied on to ensure social inclusion of the low skilled while such low paying private market services as develop rely to a significant extent on immigrant workers.

An Anglo-Saxon approach has placed emphasis on allowing private market services to absorb low skilled workers viewing such employment as having a major role in bringing about social inclusion. The employment contract is minimally regulated so as not to lessen the demand for low skilled labour, and welfare policy is aligned with employment conditions. The alignment involves different mixes of restrictions to welfare and incentives to hold low paying jobs. This approach generally results in a dynamic market services sector and low welfare dependency among people of working age. Its weaknesses are that a substantial proportion of the jobs which people with low skills hold do not offer the types of opportunities for personal development, intrinsic job interest, adequate income or reasonable stability that tend to be assumed in arguments that employment *per se* is an effective source of social integration.

The Council does not believe that Ireland constitutes a clear example of the Anglo-Saxon approach. In particular, the steady improvement in the purchasing power of social welfare payments for people of working age and their potentially long duration fall outside this approach. When unemployment was high and the pressure on fiscal resources acute, Ireland continued to protect the real living standards of people who were jobless; the welcome fall in long-term unemployment from 9 per cent of the workforce in 1993 to 1.2 per cent in 2001 can be interpreted, in line with the argument in Chapter 7, as, in part, a tribute to this solidarity. However, the Council believes that further success in reducing poverty and securing social inclusion, through a continuing emphasis on employment, now needs a more careful analysis of the conditions under which the expansion of relatively low skilled jobs in market services can be a key element in the strategy. The emphasis must shift from employment *per se* to the quality of jobs. The objective of social inclusion implies that criteria such as, for example, exiting the Live Register or achieving a job placement are insufficient of themselves to confirm success and that some evidence of the quality and, above all, sustainability of the employment which people take is needed. The Council recommends that Ireland be to the fore of European Union efforts to develop meaningful indicators of the quality of work as integral to monitoring progress in attaining social cohesion (European Commission, 2000a).

There is evidence at national level and in specific programme evaluations that people leaving unemployment or a status outside the labour force to take employment are much less likely to experience poverty or social exclusion. This is not just because many of them are able to enjoy higher money incomes but because they may also experience that other, non-monetary benefits to job-holding are significant; these include the provision of a framework to their use of time, of social contacts wider than their home/neighbourhood provide, and of opportunities for personal development and skill acquisition. In addition, they are frequently conscious of a higher social status and have a heightened sense of belonging to, and participating in, society (Gallie, 2002) It is for these very reasons that organisations seeking equality and full inclusion in society for socially disadvantaged groups (people with disabilities, Travellers, refugees and asylum seekers, ex-offenders, older people, etc.) make access to employment on the same terms and conditions as the rest of the population a key element of their programmes.

8.9.2 Vulnerable groups

Barriers to employment, however, still exist for groups of working aged people in the Irish population. The low national rate of unemployment conceals much higher unemployment rates and, perhaps more significantly, high levels of discouragement from entering the workforce among such different groups as people with disabilities, older workers, people in receipt of supplementary welfare, Travellers, women in home duties, young people disaffected from school, adults with mental illness, lone parents, ex-offenders, and people recovering from substance addiction. Each of these groups has particular and multiple problems but they are alike in facing obstacles to their employment prospects (European Foundation for the Improvement of Living and Working Conditions, 2002a). These obstacles arise in part from limited skills and personal and family problems but also from poor living conditions, lack of access to education and transport, discrimination by employers and local labour market conditions.

Pervasive technological change and more intense international competition have impacted on most parts of the national labour market to create a situation where people unable or unprepared to adopt unfamiliar jobs, different work patterns and new skills required by the knowledge economy are increasingly at risk of holding only precarious employment or none at all. The Council believes that the identification of the specific groups at risk and the design of a holistic strategy for each of them have become essential if their social inclusion is to be strengthened through employment. The holistic strategy must cover the availability and attractiveness of work, the balance of financial incentives, education and training, and availability and access to services such as care, transport and counselling (European Commission, 2002c). In this context, the Council notes the major significance of the work of the EQUAL Development Partnerships and the Supported Employment Programme for people with disabilities.

8.9.3 Women returners

The Council would particularly like to highlight the contribution that women with low levels of educational attainment have made to national progress, and are expected to make. "The story of Ireland's economic transformation rests in part upon the story of women returners" (Russell *et al*, 2002).[8] From 1994 to 2000, the numbers of women in home duties fell from approximately 581,000 to 531,000, and from 43.4 per cent of adult women to 34.8 per cent. Table 8.2 is based on data from the Living in Ireland Survey in 1994 and 1998, broken down by sex and educational level. It shows that, while the employment rate of low skilled men in the open labour market hardly changed over a five-year period of rapid economic growth, that of low skilled women rose markedly and even outpaced the rise in employment among their higher skilled sisters. Recourse to temporary employment schemes grew markedly for the low skilled of both genders. The increase in the employment rate for low skilled women (open labour market and schemes combined) came largely at the expense of their being engaged in home duties, rather than unemployment. This is a consequence of how women report their labour market status, such that they often make transitions directly from "outside the labour force" to employment without ever having been recorded as unemployed. By contrast, the increase in the

8. Women returners are women who enter or re-enter employment, education or training having spent a period in full-time caring or home duties.

employment rate for low skilled men (which only occurred thanks to a rise in the number on temporary employment schemes) was associated with a fall in their unemployment rate.

TABLE 8.2
Principal Economic Status of Women and Men, Unqualified and Qualified

	Women				Men			
Status	**Unqualified**		**Qualified**		**Unqualified**		**Qualified**	
	1994	**1998**	**1994**	**1998**	**1994**	**1998**	**1994**	**1998**
Employee	20.5	28.8	55.8	63.1	52.2	51.4	78.4	84.9
Temporary Employment Scheme	0.4	3.6	1.4	2.6	4.9	7.4	1.8	2.7
State Training Scheme	0.5	0	0.3	0.7	1.1	0.8	0.6	0.1
Seeking First Job	1.1	0.8	0.3	0.3	2.7	2.2	1.2	0.5
Unemployed	2.1	2.5	3.3	2.4	26.8	22.7	11.5	5.0
Sub-total (Participation in Labour Force)	*24.6*	*35.7*	*61.1*	*69.1*	*87.7*	*84.5*	*93.5*	*93.2*
Retired	0.1	0.6	0.3	0.3	11.6	14.5	3.3	3.0
Home Duties	75.4	63.7	36.4	27.4	0.7	0.8	0.2	0.2
Education	0	0	2.0	3.1	0.1	0.3	2.5	3.2
Total	**100**	**100**	**100**	**100**	**100**	**100**	**100**	**100**

Source: Doris, A. in McCoy *et al.* (2001) *Quarterly Economic Commentary*, ESRI, Dublin. Based on data from the 1994 and 1998 LIIS.

Note: Qualified Individuals have at least a second level qualification (Group Certificate or Higher), unqualified individuals have none. Those unemployed may be participating or not participating depending on whether they are actively seeking work.

The Council is aware that attaining the EU target of an employment rate for women of 60 per cent by 2010 will make the largest demands on women with low levels of education whose current employment rate is far below the 60 per cent threshold. Their social inclusion through employment, however, raises particular issues, exemplified by what is known about the obstacles they face and the types of employment which women leaving home duties are in fact entering. The obstacles include the responsibility many have to care for young children, disincentives arising from the tax and social welfare systems, and an erosion of skills and confidence caused by being out of employment for a long time (NESF, 2000). These obstacles explain in part the types of jobs which women returners take. Analysis based on the 1995-1999 Living in Ireland Surveys throws a relatively rare light on the quality of employment that they are entering (Russell *et al.,* 2002). The principal findings include:

- Women pay a penalty of "downward mobility". They re-enter the workforce in jobs of lower social-economic status to those they originally left in order to assume full-time caring roles in the home;
- Lack of flexibility on the part of their employer in allowing them to align working hours with caring responsibilities often prompted their exit in the first place;
- Many work in low-paid jobs in catering, cleaning or childcare, areas which are an extension of the unpaid work they undertook in their homes;
- Lack of accessible and affordable childcare hampers their return;
- Low educational attainments weaken their position in the labour market.

Russell *et al.* (2002) also found that about one-half of women in home duties had no link with the social welfare system whereas the other half did, with nearly 30 per cent being in direct receipt of a welfare payment (principally one-parent family payment, disability assistance and unemployment assistance) and another 20 per cent in receipt of a Qualified Adult Allowance. In seeking to understand what prompted women in home duties to seek employment, and what subsequently facilitated them to access education, training or an employment scheme, it emerges clearly that contact with the social welfare system is beneficial; women who are independent actors in the social welfare system are more likely to see themselves as potential labour market participants. This is probably due to a variety of factors: they have access to a range of positive supports with both the Live Register and receipt of the One Parent Family Payment acting as "gateways" for them; they are exposed to information and may see themselves differently when recognised as autonomous adults; they are obliged to seek work and have a greater chance of financial disincentives being smoothed for them.

The Council believes that this evidence further strengthens the case made in Chapter 7 for facilitating more women in making independent social welfare claims and ending any normative assumption in the social welfare code that households are supported by a principal breadwinner.

8.9.4 A focus on the quality of jobs

As employment rates climb higher, and the targets for them too, it becomes more important to ensure that the conditions under which job-holding contributes to reducing poverty and fostering inclusion and equality genuinely obtain. In many countries, as unemployment and welfare dependency have declined, attention has shifted to the quality of the jobs that formerly unemployed people and welfare recipients are holding. Employment, which is of extremely short duration, does not allow a person to escape poverty, provokes a level of stress that impacts negatively on personal health and household harmony, and leads to de-motivation and a lessened interest in improving skill levels or furthering education, is clearly not what is intended when people with relatively low skills are encouraged to leave welfare for work. Once they are off the welfare roles, an interest should be retained in monitoring their progress in the labour market.

The Scandinavian, Continental European and Anglo-Saxon systems of social protection are all being challenged to address the issue of whether it is desirable that people with a low productivity as seen by the market should hold jobs and, if so, under what conditions. There is a widespread concern that the jobs which people leaving extensive periods of unemployment or welfare dependency behind them are entering are frequently not "the types of jobs that could be expected either to reverse long-term skills deficiencies or to provide the motivation and security required to ensure employment stability." There is a growing awareness that "an effective set of policies for social integration needs to take into account not simply the quantity of jobs, but also how to improve the quality of low-skilled work." (Esping-Andersen *et al*., 2001: 137, 112).

An objective (of NAPS) is to provide maximum opportunity for the most vulnerable members of society to gain employment and to progress to better-paid and more fulfilling employment. This will involve providing a range of life-long learning options designed specifically to assist people currently in low-paying jobs to acquire the requisite skills. (NAPS, 2002: 13)

It is in this context that the Council recommends that priority be strengthened over the coming years to improving the quality of the employment experience for those who take relatively low-paying jobs. This will require paying close attention to three aspects of job-holding at the lower end of the labour market: making work pay, targeting low skilled workers for training and further education, and sensitively activating people whom a prolonged period without employment has distanced from work readiness.

In continuation of the perspective outlined in Chapter 7, the Council notes the evidence that extremely low rates of social assistance, of themselves, are a poor incentive to take employment and more likely to lead to de-motivation, a deterioration in skills, and a general erosion in social belonging. It is also aware that the fear that high levels of social protection necessarily undermine work motivation is not supported by the comparative evidence (Gallie and Paugam, eds., 2000; Layte and Callan, 2001); on the contrary, where eligibility conditions are framed and monitored in such a way that they reflect positive expectations of people in receipt of welfare, high levels of social protection and a strong employment commitment co-exist. It is also to be noted that in-work benefits are frequently found to be more effective in bringing low skilled people to hold jobs than stringency or sanctions applied to their receipt of welfare. (Esping-Andersen *et al*, 2001; Phipps, 2001; Forssen & Hakovirta, 1999; Moffitt, 1992; etc.)

8.9.5 Making work pay

Ireland has made a lot of progress in ensuring that relatively modest earnings are not reduced by taxation or the withdrawal of social supports. Particularly significant developments in recent years have been the retention of secondary benefits allowed for a period under the Back to Work Allowance and Back to Education Allowance Schemes; the significant level of the earnings disregard in the One Parent Family Payment at the time it was introduced; switching the basis of calculation for eligibility to Family Income Supplement from gross to net earnings; the institution of a national minimum wage; raising the threshold at which workers become eligible for income tax, lowering the starting rate and widening the band to which it applies. Ireland currently compares favourably with other European countries in its tax treatment of low earnings (NEAP, 2002; European Commission 2000a).

The cumulative effect of these measures has, undoubtedly, facilitated the extent of the take-up of employment on the part of relatively low skilled workers and confirms that their employment commitment and employability was stronger than some commentators feared. The Council points out how important it is that Ireland should continue to pursue policies that ensure that relatively low skilled work pays. The Irish economy has a significantly larger incidence of low pay than many of its European neighbours with, for example, more than 7 per cent of all women workers being paid at the national minimum wage in 2001 (NEAP, 2002). It is also clear that the decision by women to seek work and to take a job offer is particularly responsive to the wage rates on offer (Russell *et al*, 2002). Finally, it should be pointed out that the earnings of one low skilled worker are increasingly unable to support a household and that either the household has to have more than one earner or receive complementary social supports. For these reasons, the Council recommends progressing—as soon as circumstances permit—with implementing the decision that has been taken in principle to remove workers on the National Minimum Wage completely from the income tax net. It also cautions against allowing the financial incentives to hold relatively low-paying jobs deteriorate by, for example, not up-rating earnings disregards in line with inflation or unduly tightening eligibility to retain secondary benefits. In this context, consideration should be given to the position of low-earning employees. The level of the minimum wage itself must be kept under review and adjusted appropriately.

8.9.6 Targeting low skilled workers for training and further education

The consequences of Ireland's previous era of chronic labour surplus and high rates of long-term unemployment are still underestimated and it has to be accepted that, until recently, considerable efforts at retraining the long-term unemployed did not have major results (ESF,1998). This has been the experience of other countries too: "the attempt to re-skill the unemployed in a relatively short period of time can only have limited results in a context in which people have spent long periods of their working lives without learning new skills or maintaining their basic learning capacities" (Esping-Andersen *et al.*, 2001: 97). Even buoyant aggregate labour market demand can bypass people whose former work experience, family commitments, local labour market conditions, and previous experiences of education and training have singularly ill equiped them for accessing the new types of employment opportunities that become available. In fact, as the unemployment rate has fallen, more companies have begun to comment that the quality of people available for recruitment is lower and that "the appropriate skillsets, not just for specific employment, but for the workforce in general" can no longer be taken for granted (Forfás, 2000: 4. Also 19, 22). This is a challenging observation.

The international experience is also that people who begin their working lives with low educational attainment and few qualifications are the least likely of all workers subsequently to benefit from further education or training (OECD *Jobs Stud*y, 1994). Again, the Irish experience echoes this, both because low skilled workers are more likely to be in small enterprises where less training is provided anyway and because already more educated and skilled workers have a stronger capacity to benefit from the formal courses on offer. In the light of the substantial factors which bias company training towards the already more educated and skilled, the Council recommends that the National Training Advisory Committee consider ways that might influence companies to target the least skilled members of their workforces for training. It also recommends that consideration be given to enabling small firms to co-operate, on a geographical or sectoral basis, in some form of shared training resource for their employees. The work of the Task Force on Life Long Learning should also be fully considered.

8.9.7 Respecting diverse employment contracts

Low-skilled workers seeking entry (or re-entry) to employment today are those who most experience the diversity of employment contracts that have come to characterise the knowledge-based economy and its services sector in particular. They are disproportionately likely to be offered work that is part-time, temporary or fixed contract, and featuring flexible hours or shift work. It is particularly important for them, therefore, that employment legislation and social protection should no longer be based on the assumption that a “real” or “decent” job is full-time and permanent; the ultimate criterion of a decent job, justifying its full proportionate protection, should simply be that it genuinely needs to be done.

In this context, the Council regards the introduction of the Protection of Employees (Part-Time Work) Act 2001, as an important milestone in extending improved protection to almost 300,000 part time workers, many of whom are women. It recommends that attention be increased to studying the working hours of new and relatively low-skilled entrants to the workforce and to their progression in the employment contracts offered them. For example, it is aware of a great deal of debate about the role of temporary work as a stepping stone to regular employment, with some taking the view that training or placement in workplaces can overcome employers’ hesitancy to hire people who have been unemployed for long periods, despite a lack of clear research to support this position (Storrie, 2002). Transition rates from temporary to permanent work appear to be greatest for prime age men (European Foundation for the Improvement of Living and Working Conditions, 2002b), while both young and older temporary workers run significantly higher risks of subsequent unemployment. Nevertheless, in some Member States (for example, Austria and Belgium) temporary work agencies are used as a tool for integrating vulnerable groups, such as older workers, long-term unemployed and people from ethnic minorities, into the labour market. The opportunity to earn a wage while gaining experience with different jobs and employers can make agency work an attractive option for marginalised or stigmatised groups.

8.9.8 Sensitive activation

An important way in which the employment expansion in Ireland has been harnessed to promote social inclusion has been through the implementation of aspects of the European Employment Strategy, principally its emphases on minimising the flow into long-term unemployment and on activating people in open unemployment. People passing thresholds of time on the Live Register (6 months for those aged under 25 since September, 1998, and 9 months for those aged 25-55 since July, 2000) have been referred by the Department of Social and Family Affairs to FÁS for interview and a fresh assessment of the options open to them and the steps they were taking to access them. This process has had clear results on the macro level; for example, of the more than 26,000 people referred in 2001, 35 per cent left the Live Register for a job, FÁS training or an educational programme, and another 27 per cent left for unspecified reasons (NEAP, April 2002). The Council welcomes this evidence that wider and more enriching options are being provided people than the indefinite receipt of a welfare payment (see Box 8.3). It endorses the underlying philosophy of activation is one of reciprocal obligations: welfare recipients are expected to accept employment, training, and community care offers in order to receive benefits, while the state accepts its responsibility to provide payments that are adequate and the services that enhance the employability of recipients.

BOX 8.3

Perspectives on Activation

"The main aim …is to allow, and encourage, people who have been long-term welfare dependent to test employment options and regain a foothold in the labour market while retaining some degree of financial security during the early years of employment or self-employment" (NAPincl, 2001: 3.28.1).

"The imperative of mobilizing labour supply among older workers (55-64) should be mutually compatible with their requirements for equality and social justice, thereby facilitating choice when the time comes to make the decision whether to stay in work or reap the benefits of pension entitlements they have gained over their working life" (NEAP, 2002: 3.5)

The Council notes how important it is to make a realistic assessment of the actual circumstances and personal characteristics of working age people who are in receipt of social welfare. It accepts that activation may come too late for some, and be too early for others, while urging great caution in using the term "unemployable". While a basic income and/or types of sheltered employment are the most humane societal responses in some cases, the Council is of the view that high support programmes in which employers participate and partnerships such as EQUAL can produce the optimal outcome for a great number of people. The Council welcomes in particular the recognition of the several purposes which came to be served by the Community Employment Programme, viz., preparation for work in the formal economy, sheltered employment and the provision of needed local services. When making changes to CE it should be clear how these purposes will continue to be met by other programmes if not by CE.

To strengthen the case that the Council made in Chapter 7 for extending the philosophy and practice of activation from people who are openly unemployed to people currently outside the workforce, the Council notes the relative absence of sophisticated evaluations of outcomes where some programmes are concerned. The evaluations the Council has in mind would pay less attention to having left the Live Register at a point in time and more on ascertaining the nature and prospects of the new situation in which people find themselves; they would attribute flows or placement rates to programmes only after having clearly identified control groups (to ascertain how much of what happened would have happened anyway); they would pay attention to the experience of people themselves as well as to programme objectives.

8.10 NEW POPULATION FLOWS AND CULTURAL DIVERSITY

8.10.1 The context

A notable development over the four years, 1999-2002, has been the growth in the numbers of people living in Ireland, for defined or indefinite stays, who have come from countries outside the EEA and the English-speaking world.[9] Frequently, their countries of origin feature cultures and levels of economic development markedly different from that of Ireland. The Council is aware that the theme of cultural diversity consequent upon these population inflows is something which public service providers across the spectrum—in education, health, housing, social support, and policing—are now having to address, as well as trades unions, churches and other bodies in civil society. The speed with which these inflows materialised is illustrated by applications for asylum: new applications peaked at 10,938 in the year 2000 whereas they had numbered 362 for the whole of 1994. The scale of what developed is illustrated by work permits: an estimated 40,000 work

9. The EEA consists of the EU States plus Norway, Iceland and Liechtenstein. The English-speaking world refers principally to the USA, Canada, Australia and New Zealand whose nationals tend not to experience major difficulties in integrating into Irish life.

permits were issued in 2002, a figure beginning to rival the annual outflow from the national educational system (46,000 in 2002).

The legal status of those from outside the EEA currently living in Ireland varies widely depending on whether they are asylum seekers awaiting a decision on an application or appeal, have been granted refugee status or leave to remain, are the holders of work permits or work visas, are students with a right to engage in casual work, or—in a number of cases that is impossible to ascertain—are people with no legal status and living clandestinely. Their social status in Irish life probably varies just as widely, depending on whether they are skilled or unskilled workers, expert or hesitant in their command of English, and—most regrettably of all in the Council's view—on their race and other cultural characteristics.[10]

The cumulative impact of the different inflows has taken some Irish people by surprise and there can be a failure to appreciate that the great majority of those from countries outside the EEA whom they see on the streets are workers who have been actively sourced by public and private sector employers in Ireland, students attracted by the successful marketing of Irish educational services abroad, the parents of an Irish-born child, the spouses of Irish or EU citizens, visitors, or refugees whose cases for asylum Ireland has been happy to accept.

The principal reasons for entry into Ireland on the part of those from countries outside the EEA are:

- As tourists, students or for business;
- As workers;
- As spouses, parents[11] or children of people with a legal right to be in the state; and

10. A valuable first discussion of immigration into Ireland is in NESF Report No. 19, November, 2000.

11. People given leave to remain on the basis of having an Irish born child numbered 1,428 in 1999, 1,515 in 2000 and 3,174 in 2001. At the end of 2001, 5,500 applications were in hand. See Department of Justice Equality and Law Reform , Annual Report 2001.

- As refugees and asylum seekers whose permission to remain in the state is temporary while their applications to remain longer are processed.

Adults from countries outside the EEA who remain in the State for more than 3 months, whatever their reason for entering or the likely duration of their residence, are required to register with the authorities. People seeking asylum—though not required to register—get specific temporary residence certificates. Consequently, a good indication of the cumulative presence of people from countries outside the EEA is provided by Table 8.3. Children (aged under 16) and people not complying with the legislative requirement to register are additional to the figures shown.

TABLE 8.3

People From Countries Other than the EEA in the State, 1998-2001

Year	Registered non-EEA nationals of countries outside the EEA[1]	Applications for asylum[2]
1998	22,546	4,626
1999	29,646	7,724
2000	47,262	10,938
2001	90,446	10,325

Source: Department of Justice equality and Law Reform , *Annual Report 2001*.

Notes: 1. These exclude children (aged under 16), the female spouses of Irish nationals and persons seeking asylum. Top 5 nationalities: China, United States, Nigeria, Phillipines and Latvia.

2. Top 5 nationalities: Nigeria, Romania, Moldava, Ukraine and Russia.

People seeking asylum at any one time are declining significantly as a proportion of the total number of people from non-EEA countries living in the state; they were one fifth of the total in 1998 but just over 11 per cent by 2001.

8.10.2 Asylum seekers whose claims are being processed

The most vulnerable among the non-EEA nationals living in Ireland are asylum seekers who have applied for refugee status and are awaiting a decision on their status. This is for several reasons: some of them have left behind situations in their home countries, and/or had harsh experiences in reaching Ireland, which can have deeply traumatised them; once in Ireland they find themselves under suspicion of being economic migrants seeking to evade immigration controls; their differential treatment by the Irish state (direct provision, fingerprinting, denial of the right to work, liability to deportation, etc.) marks them out as a special group and can lower their status in the eyes of some people.

BOX 8.4

Asylum seekers and refugees

People seeking asylum as refugees must have a "well-founded fear of persecution" in their own country which has left them temporarily stateless so that they are seeking the protection of another state under the terms of the 1951 Geneva Convention. Since April, 2000, a system of dispersal and direct provision for asylum seekers has applied in Ireland. Persons claiming asylum are accommodated with full board at a reception centre in Dublin for one to two weeks before being allocated accommodation at regional reception centres dispersed around the country while their applications are being processed. They receive the equivalent of pocket money (€19 weekly per adult and €9.50 per child, in 2002) and are not entitled to social welfare allowances (other than Child Benefit). They are not permitted to leave their allocated accommodation unless the circumstances are exceptional. Fingerprinting of applicants over 14 years of age began in November, 2000, in a bid to deter multiple applications and several EU countries have done the same. A Government decision in July, 1999, allowed an estimated 3,563 asylum seekers who had been waiting for over 12 months by that that date for a decision on their applications to take up employment while their cases were being determined. New applicants for asylum after that date are explicitly denied permission to take up employment while their claims were being processed. Some EU

Member States allow asylum applicants to work subject to various conditions but the Irish authorities have judged that doing so would create a significant “pull” factor, put further pressure on the asylum processing system and continue to delay recognition for genuine refugees in need of protection.

Work permits and visas

In filling job vacancies in the Irish economy with workers from outside the EEA, Ireland has relied principally on work permits. These are given for a maximum of a year at a time; when renewed, they are counted as new permits. The employer, not the prospective employee, applies for the permit and the employer should be prepared to demonstrate that it has not been possible, in spite of reasonable efforts being made, to fill the vacancy with an Irish or other person for whom a work permit is not required. A permit is supposed to be granted when the employer has no alternative but to employ a person from a country outside the EEA. As the work permit is granted to a person to work for a given employer and only for that employer, the worker is not free to sell his or her labour on the open labour market.

By contrast, prospective employees in countries outside the EEA can themselves apply for work visas and work authorisations in specific sectors of employment identified by the Irish authorities as experiencing substantial labour shortages. Visas and authorisations are usually granted for a period of two years and are renewable. While the application must be accompanied by a job offer from an employer in Ireland, holders of working visas and of work authorisations are allowed to change their employers within the same skills category after arrival in Ireland as long as they continue to have authorisation to work and reside in the country.

Students

People from countries outside the EEA who have permission to remain in the State as students are entitled, under a ministerial decision of April, 2001, to take up casual employment for the duration of their permission to remain. Casual employment is defined as up to 20 hours part-time work per week or full time work during vacation periods. The entitlement ceases upon the expiry of their permission to remain as a student and their being in casual employment does not, in itself, entitle them to further permission to remain. As a student, it must be established that the person has enrolled in private education, has paid fees and has sufficient funds to support him-/herself. "The relaxation on access to casual employment will facilitate students who have come here, not alone financially but also in social terms and in terms of improvement in their language skills. Participation in part-time employment, even of a type not directly related to the course of study, can enhance the overall experience of studying in a foreign country" (Minister for Justice, Equality and Law Reform, April, 2001)

The Council has an undivided and impartial concern for civil liberties within the state and believes that arrangements governing asylum seekers should be exceptional only in so far as they are strictly necessary, and should be kept under review.[12] It notes that the total recognition rate of asylum-seekers (i.e., decisions to grant refugee status the first time or on appeal, and decisions to grant leave to remain on humanitarian grounds or relations of kin, expressed as a percentage of all decisions taken including rejections) was low by EU standards at the end of the 1990s (Hovy, 2001: 14), that it stood at some 16 per cent in the year 2000 and may have risen further since then.[13] The Council commends the steep learning curve which the authorities and civil groups in Ireland have climbed in this regard, and the rapid development of an institutional

12. "In accordance with the 1951 Geneva Convention, it is important to afford refugees swift, effective protection, while making arrangements to prevent abuse of the system and ensuring that those whose asylum applications have been rejected are returned to their countries of origin more quickly" (Conclusions of the European Council Presidency, Seville, June 2002).

13. Background Briefing Note, September 2002, Department of Justice, Equality and Law Reform.

and policy framework to deal with requests for asylum that rose from less than 500 a year in 1995 to 1,000 a month in 2002.

The single best way to bring asylum-seekers to enjoy the same treatment and rights as others in the state is through ensuring the speedy, courteous and impartial processing of their claims. The Council recommends that the resources necessary to ensure this should always be a priority for government and that civil society in general, and community and voluntary groups in particular, be encouraged and facilitated in every way possible to form contacts with asylum-seekers in the state and foster public understanding of their situation.

The Council considers that the arrangements in place are generally fair and reasonable, while scope remains to continue learning from best practice in other countries. It notes how much could be learned from research into the particular factors underlying the large proportion of asylum applications from Nigeria and Romania (53 per cent in 2000, 47 per cent in 2001) and believes such research and close attention to the experience of other countries could increase Ireland's ability to anticipate future developments. It supports continuing exploration of alternatives to the current ban on employment for asylum-seekers, which would enable them to use their time in a manner more constructive for themselves and their host society.

8.10.3 People granted refugee status or leave to remain

It is important that members of ethnic minority groups granted refugee status or leave to remain should be facilitated in participating fully in mainstream society as speedily as possible. It is clear that the low skilled among them can be particularly vulnerable to exploitation if they are unfamiliar with the English language, ignorant of Irish standards and patterns of behaviour, without kin and other social networks, and inured to hardship by low living standards in their countries of origin. The Council recommends that the relevant authorities pay particular attention to ensuring that the terms and conditions of their employment, access to accommodation and—where it applies—protection of their human rights and civil liberties comply with national standards. Standards of accommodation are also of concern and close monitoring by organisations and support groups is to be welcomed. It is clear that the ease with which an individual who is lawfully present in the state can be integrated into Irish life will be crucially affected by the ease with which he or she can benefit from family reunification. The Council commends the special measures which local authorities and community and voluntary groups are taking to ensure the recognition and successful integration of refugees and the members of minority ethnic groups.

8.10.4 Skilled and unskilled migrant workers

An important element in sustaining Ireland's high economic growth has been the arrival of skilled and unskilled workers from outside the European Economic Area. Where skilled migrants recruited by the private sector are concerned (e.g., computer technicians and language specialists), they are easing skill shortages, making it more attractive for international companies to continue expanding in Ireland and slowing the rise in earnings inequality that would otherwise occur (Barrett *et al*., 2002). When they are recruited by public sector employers, their contribution reduces shortages and enables public services to be improved. When they are low skilled and work in the market services sector, the evidence is that queues are shorter and services are available which simply would not be provided otherwise.

The Work Visas scheme illustrates well the extent to which workers from outside the EEA have come to support the implementation of Irish policies. It was introduced in June 2000 as a fast-track alternative to the work permit regime so as to facilitate recruitment of overseas nationals in sectors experiencing particular skills shortages and initially used largely to source ICT workers and nurses. In June, 2001, an Action Plan to expand the capacity of the construction industry and deliver on large physical infrastructure projects under the National Development Plan was successful in increasing the number of building professionals and town planners from non-EEA countries. In May 2002, further professions were added to those eligible for work visas to help address shortages of professional medical, health and social care staff in the Public Health Service (doctors, radiographers, speech and language therapists, hospital pharmacists, social workers, etc.). This was to support the delivery of the National Health Strategy and public health employers subsequently undertook concerted, overseas recruitment campaigns.

In a similar fashion, it is clear that the strengthening of Ireland's scientific and research base, an objective that is integral to the economy's future, and the effective utilisation of funds allocated for that purpose to the Programme of Research in Third Level Institutions (PRTLI) and Science Foundation Ireland (SFI), will need an inflow of researchers from overseas as the current flow of Irish research graduates is simply insufficient. Pro-active policies to attract researchers from abroad in the face of stiff international competition are, therefore, being advocated (Expert Working Group on Future Skills Needs, 2001b).[14] Many countries are aware that their attractiveness to researchers and graduate students from overseas is important to their relative performance in science and technology and, thus, to their economic growth (International Mobility of the Highly Skilled, OECD, 2001c).

As for the more numerous work permits, Table 8.4 shows the degree to which sectors of the Irish economy became reliant on workers from outside the EEA during 2002.[15]

14. Boekholt *et al*. (2001), *Benchmarking Mechanisms and Strategies to Attract Researchers to Ireland*. A study for the Expert Working Group on Future Skills Needs and Forfás. Technopolis-Group.

15. Work permits granted each year include renewals of permits for people already in the state; these have been rising as a proportion of the annual totals. For example, while some 36,000 work permits were issued in 2000 and 40,000 in 2001, the actual inflow of new workers into the state net of renewals was steady at 23,500 in each year.

TABLE 8.4

Total Vacancies and Work Permit Applications Submitted to FÁS, January to September inclusive, 2002.

Type of economic activity	Number of vacancies	Number of work permits sought	Work permits as % of vacancies
Animal, Land, Marine, Mining & Exploration	2,989	2,394	80%
Hotel, Tourism, Travel & Catering	11,967	7,170	60%
Factory, Production & Related Services	5,076	2,870	57%
Social, Health, Welfare, Childcare	2,501	1,017	41%
Trades & Related Occupations	5,947	2,183	37%
Cleaning, Security & Maintenance	4,728	1,503	32%
Purchasing, Warehousing, Transport, Distribution	2,333	696	30%
Sales, Marketing, PR, Advertising & Property	4,258	927	22%
Professional, Administrative, Clerical	5,885	745	13%
Total	**47,632**[1]	**20,156**	**42%**

Source: FÁS (2002), Table 1.2

Note: 1. Areas of activity with less than 1,000 vacancies are not displayed but included in the total at the bottom of the table.

42 per cent of all vacancies notified to FÁS during the first nine months of 2002 were accompanied by applications for work permits. The sectors of the economy for which these workers were being sourced suggest that Ireland is already capable of repeating the experience of other countries, i.e., resorting to low skilled migrants to carry out work where the pay and conditions have become increasingly unattractive to the indigenous population. The

area of activity with the highest reliance on permits (animal, land, marine, mining & exploration at 80 per cent) includes several employments with demanding physical conditions. The area responsible for the largest absolute number of permits (hotels, tourism, travel and catering—accounting for 7,170 applications or 36 per cent of the total) is a labour intensive sector where relatively low pay and demanding hours do not obviate the need for good social skills.

The Council points out that the synergy between immigration and Ireland's economic and social objectives can be threatened. It is threatened, most obviously, if ignorance is widespread of the significant contribution which migrant workers are making to the economy. It is threatened if the system of work permits and visas, or the conditions under which students from overseas can take employment, are abused. It is threatened if the living and working conditions of low-skilled non-nationals are allowed to depart from prevailing Irish conditions, or if particular low-skilled employments become overly associated with the work of non-nationals. It is threatened if interest and inventiveness in working with groups of Irish people considered 'hard to employ' are lessened because bringing workers from overseas is a faster and more expedient solution to employers' needs. The Council is deeply concerned that the Public Employment Service (FÁS) should find grounds for thinking that some employers in Ireland are substituting domestic unskilled workers with cheaper foreign labour because of the latter's lower expectations concerning wages and conditions, and that part of the rise in youth unemployment during 2002 may be attributable to these employers' preferences for Work Permit recruits rather than young Irish persons (FÁS, 2002: 33-34). It supports a close scrutiny of the current system of work permits, and shares the view that a system is preferable which would be driven by a medium-term assessment of skills shortages in the Irish economy rather than the inventory of current vacancies (FÁS, 2002).

While the Council is of the opinion, overall, that the work of low-skilled non-nationals in the Irish economy and their presence in Irish society is of modest proportions and has a strongly positive nature for immigrants and host society alike, it is aware that tensions have been allowed to develop in other European countries between the economic case for a greater reliance on immigrant workers and the social case for proceeding more slowly. Ireland should learn from international experience that a social divide can easily arise between those who favour a tolerant attitude towards a multicultural society and those who are against one. The successful implementation of NAPS in Ireland, thus, becomes an integral part of ensuring a measured approach to immigration and comprehensive policies for the integration of migrants. The Council believes the experience of other EU Member States should be studied in this regard so as to encourage the development of pre-emptive policies in Ireland that will ensure a continuing welcome here not just for low-skilled labour but for the persons who provide it.

The Council underlines the importance of the National Anti-Racism Awareness Programme and the National Action Plan against Racism as they seek to counter prejudice, better inform the Irish population, and ensure that Ireland's legislative and institutional frameworks for providing social protection and promoting equality extend effectively to all non-EEA nationals in the state.

8.10.5 Cultural diversity

The Council believes that a vibrant Irish society is one which is plural and capable of on-going transformation through embracing cultural diversity as much as by initiating economic and social innovations. It welcomes the perspective on integration provided by the Interdepartmental Working Group on the Integration of Refugees in Ireland (1999): "Integration means the ability to participate to the extent that a person needs and wishes in all of the major components of society, without having to relinquish his or her own cultural identity". The Council would like to stress that cultural identities are neither immutable nor impervious to the society within which people are living. On the one hand, it is important that Irish society appreciate the limitations of a mono-cultural model and not accept that any public service or institution should presume upon assimilation to established and majority symbols, meanings, values and norms. On the other hand, it should learn from international experience that respect for cultural identity does not, and should not, mean the fragmentation of society with, for example, the embracing of identity politics (Young, 1999). A society that is culturally diverse does not mean that society becomes a space to be occupied by strictly equal cultures which are largely autonomous from each other and essentially engaged in reproducing a distinct way of life for their members. On the contrary, the Council believes that society is stronger when interaction and mutual influence between the cultural groups within it are at a high level and where the set of values, norms and behavioural patterns common to membership of the society is as wide as possible. This is consistent with each group having a right to their cultural identity and expression.

8.10.6 Responses to the new population movements into Ireland

The Council notes that there is no authoritative overview available of the scale, composition and net implications for the Irish labour market and society of the net population movement taking place between Ireland and countries outside the EEA and English-speaking world under the different headings. It recommends that government draw up, in consultation with all interested parties, a clear national policy on migration from outside the EEA. This national policy is needed because the cumulative impact of different developments (the strength of the economy in the 1990s, European integration, economic globalisation, political instability around the world) has generated a level of net migration that has taken some people by surprise. The Council believes that government should respond by being more pro-active in outlining what is happening, linking it to choices which the Irish people have made (for prosperity, solidarity within Europe, and shared responsibility for global imbalances), explaining its beneficial effects, and specifying what government is doing to manage it.[16]

16. A significant study underlining how heterogeneous migrants are and how a proper policy should reflect that was produced for the UK government in January, 2001. Glover *et al*, 2001.

A national policy on migration would be based on a realistic appraisal of the forces increasing population flows between non-EEA countries and countries such as Ireland, and of the scope for policy to manage this development. It would be informed by international research on the economic and social benefits and costs of migration, and constitute a further expression of Ireland's strong commitment to foster equality in its society and appreciate different cultures. The policy would, among other things:

- Set a framework for population inflows through different routes of entry (work permits, work visas, student visas, asylum seekers, people granted refugee status or leave to stay, family reunification, etc) which is conducive to economic and social development;
- Specify the types of contribution sought, currently and in the future, from skilled and unskilled migrant workers to Ireland's economic and social life;
- Embrace in a proactive manner Ireland's responsibilities under international and European law;
- Specify mechanisms that achieve integration in a way that is consistent with Ireland's anti-racist policy and respects the dignity and rights of all members of society;
- Specify (after a review and any necessary adjustments) the instruments, procedures and resources needed by the Irish authorities to regulate inflows into the state and protect the interests of those legitimately present within it;
- Identify whether and which specific supports and services are needed by people from outside the EEA. This would include estimating the implications for social services, from the provision of interpreters and language teaching to housing, education and health, of the scale and composition of the population inflows;
- Acknowledge and make practical provision for the important role of organisations and groups in civil society in achieving the satisfactory integration of immigrants into local communities;

- Ensure satisfactory data is gathered and research carried out to track the social progress of immigrants in Ireland; and
- Strengthen Ireland's participation in shaping and monitoring the common immigration policies of the EU.

The Council is ready to assist the government and other bodies, including within the EU, in developing a more adequate analytical framework for thinking about migration policy and helping to create a consensus in Irish society on this issue.

The Council underlines the importance of respect for, and effective enforcement of, the laws governing entry into Ireland for non-EEA nationals and of the conditions and regulations governing their stay. It welcomes the conclusions of the Seville Council of the European Presidency, June 2002, which sees a greater commitment to supporting the economic development of poorer regions surrounding the current EU as an integral part of a response to current immigration flows.[17]

8.11 MONITORING SOCIAL INCLUSION

It is important that uncertainty in 2002 about the prospects for the world economy and concerns about the budgetary position in 2002-2003 should not prevent further improvements being made in the capabilities of the Irish social policy process. The Council believes it is time to consider alternative measures to monitor poverty in what is a profoundly changed society. Indicators of deprivation and poverty should be kept under review. It recognises that the development and adoption of new measures would warrant the adoption of new targets also.

17. "An integrated, comprehensive and balanced approach to tackle the root causes of illegal immigration must remain the European Union's constant long-term objective. With this in mind, the European Council points out that closer economic cooperation, trade expansion, development assistance and conflict prevention are all means of promoting economic prosperity in the countries concerned and thereby reducing the underlying causes of migration flows."

8.11.1 Revisiting the measure of consistent poverty

The concept of "consistent poverty", first adopted by NAPS in 1997, is widely esteemed because it usefully combines a person's or household's current relative income position with evidence of enforced basic deprivation (NESC, 1999: 381, 439). The overall concept is not challenged by querying the usefulness for monitoring future trends of the eight items that were originally adopted by applying factor analysis to data obtained through the ESRI's 1987 *Survey of Household Income, Poverty and Usage of State Services* (column 1, Table 8.5).

Nolan *et al*. (2002a) point out that the levels of lack of the eight items adopted in 1987 were so low by 2000 (column 2, Table 8.5) that it will be "difficult to capture further progress empirically" (2002: ix). Six of the eight items were lacked by less than 2 per cent of sample households; random variation, they consider, will be indistinguishable from real change posing "potentially serious problems" for the continued use of the consistent poverty measure as currently constructed (p. 54). The eight indicators of basic deprivation were repeatedly seen to be valid—from their adoption in 1987 until 2000—in reliably identifying people with characteristics that conformed with a clear conceptual understanding of poverty (experiencing economic strain, psychological distress and fatalism). Looking forward from 2000, however, the argument is that the low levels of need now recorded by these indicators mean they will not reliably or usefully monitor how deprivation is further affected by social change. (Nolan *et al*. also point out that developments in the one remaining item that has a significant level of lack, viz. "Debt problems arising from ordinary living expenses", will dictate the poverty trend. Even what it is recording on its own may be unclear as higher living standards may change what people mean by "ordinary living expenses").

The Council believes that the implications of these shortcomings in the current measure of consistent poverty (which NAPS, 2002, has retained) need to be frankly addressed and soon. The credibility and usefulness of monitoring poverty targets will be undermined if the camera remains trained on what may no longer move; it will also be undermined if the reasons for moving to a revised set of basic deprivation indicators are not widely understood and effectively communicated. The Council is keen to support the emergence of measures for monitoring poverty that are adequate to the circumstances of a new Ireland. It is, after all, central to the conception of poverty as relative that expectations and perceptions of need will change over time as general living standards rise.

TABLE 8.5

Items Constituting Indicators of Basic Deprivation, Current and Alternative Lists

1987 items	Percent households lacking (2000)	ECHP-SILC items	Percent persons lacking (2000)
(1)	(2)	(3)	(4)
Meal with meat, chicken or fish	1.0	Meal with meat, chicken or fish	1.0
New not second hand clothes	3.3	New not second hand clothes	3.0
Without heating in past year	1.8	Keeping home adequately warm	3.3
Debt problems arising from ordinary living expenses	5.6	In arrears on rent, utilities and Hire Purchase	6.6
Two pairs of strong shoes[1]	1.0	Replacing any worn-out furniture	13.6
Roast once a week[1]	1.9	Having friends or family for a meal once a month	6.3
Warm waterproof overcoat[1]	0.9	*A week's annual holiday away from home*[2]	25.3
No substantial meal in past two weeks[1]	1.0		

Source: Nolan *et al*. (2002a: Tables 7.1 and 7.3)

Notes: 1. These no longer appear on the proposed new list based on ECHP/SILC.

2. It has a deprivation rate almost twice as high as for any other item and, thus, on its own would significantly influence the extent of poverty recorded; this is undesirable in a single item. It is also considered to be more open to the influence of taste than the other items. For these two reasons, the ESRI advocate dropping it.

Nolan *et al.*(2002a) apply the same technique (factor analysis) that led to the identification of eight items from 1987 data to data that have been available since 1994 for Ireland and most other EU member states through the European Community Household Panel (ECHP). (The different—but not hugely so—questions formulated in 1994 for the ECHP have the added advantage looking ahead that they will continue to be used to gather data at regular intervals through the new EU-Survey of Income and Living Standards (SILC) that is replacing the ECHP.) Their analysis allowed seven items on which data are gathered by ECHP/SILC to be identified as consistently associated with a dimension of basic deprivation (column 3, Table 8.5) and to appear as "serious candidates" as an alternative set of indicators for future monitoring purposes (p. 57).

TABLE 8.6

Percentage of Persons In Consistent Poverty, Using Current and Revised Measures

Measure of Consistent Poverty	Percentage of Persons in Poverty		
	1994	1997	2000
Below 70% median income and experiencing basic deprivation (old list)	14.5	10.7	5.5
Below 70% median income and experiencing basic deprivation (new list)	18.3	15.5	10.5

Source: Nolan *et al*. (2002a: Table 7.5)

When the proposed alternative list of indicators of basic lifestyle deprivation are used in place of the original list of eight items, the picture of how poverty has fared in Ireland during the economic boom changes. An example is shown in Table 8.6; almost the same percentage of the population escaped poverty (8 to 9 per cent) but the threshold is higher—more were below it in 1994 and remain below it in 2000.

It is also important to ask about the subjective characteristics of the people who, as a result of adopting the revised list, become included as ‘poor’. As already mentioned, the validity of the old list was periodically confirmed by establishing that people lacking the items in question did in fact report levels of difficulty in making ends meet, dissatisfaction with their economic situation, and record levels of distress which distinguished them from the general population (column one, Table 8.7). It is a matter of judgment whether the ‘additional poor’ whom a revised list of basic deprivation indicators would create have subjective characteristics that suggest they are significantly more similar to the ‘old poor’ than to the ‘consistently non-poor’ (compare column 2 with columns 1 and 3 in Table 8.7). It should, however, be pointed out that, in addition to its usefulness in monitoring developments from 2000 onwards and enabling cross-country comparisons between Ireland and other EU-member states, the proposed new list still enables us to identify and include among the ranks of the poor people who are not only lacking the items in question but six times more likely to be exposed to severe economic strain and twice as likely to be experiencing significant psychological distress than people who are not poor (column 2 versus column 3, Table 8.7). The contrast between the subjective characteristics of all people classed as consistently poor under the revised list (column 4) with the non-poor (column 3) is sharper still.

An understandable interpretation of what is at stake in revising the measure of consistent poverty in this way is that a society with higher overall living standards, and expectations, is “relaxing” its measure and raising the threshold to make it harder for a person to be officially classified as ‘poor’. This is only part of what is happening; if regarded as the whole explanation, it risks giving the original list of eight basic items an elevated normative and/or scientific status that was never claimed for them, lessening the import of the social comparisons and “shame” (Adam Smith, *The Wealth of Nations,* 1776) that are at the heart of the experience of poverty, and not addressing the requirements of a measure which is to help monitor developments. The Council has no final position on how the measure of consistent poverty should be revised in order to retain credibility and usefulness in monitoring the level of deprivation in Irish society in the years ahead. It supports making progress and securing consensus in doing so as soon as possible.

TABLE 8. 7

Percentage of Persons Exhibiting Subjective Characteristics of Poverty Using New and Old Indicators of Basic Deprivation

Subjective Indicator of Poverty	Percentage of Persons in 2000			
	Consistently poor[1] by old list	Added to consistently poor by new list	Not consistently poor by either list	Consistently poor by either list
	(1)	(2)	(3)	(4)
Great difficulty making ends meet	33.9	13.9	2.2	24.4
Not satisfied at all with economic situation	38.1	35.4	9.2	34.1
Above GHQ threshold	32.7	29.4	14.6	32.4

Source: Nolan *et al*. (2002a: Table 7.9)
Note: 1. below 70 per cent of median income and experiencing basic deprivation.

8.11.2 Incorporating measures of income dispersion into the monitoring of social inclusion

In second place, the Council believes that a country, which has integrated as rapidly and successfully into the international economy as Ireland has, should be particularly sensitive to evidence that money incomes that are seriously below levels generalised throughout society can constitute a significant erosion in the quality of life, for the individuals concerned and for everyone, and should, therefore, be closely monitored as part of social inclusion strategy.

A variety of different social studies underline the damaging effects on people of living life on money incomes that are an extreme distance from the levels prevalent in their societies (Wilkinson, 1996). It is not necessary that they be unable to buy food or afford heating; the damage is done by the way in which living on a very low income can undermine their control over their lives, self-esteem, sense of belonging to society, motivation and interest in the future, and keenness and ability to participate in social activities. Epidemiologists, in particular, (who study the causes of differences in the life expectancy and health of social groups) point to evidence that people living on very low incomes in the 'high cost environment' of advanced societies today can so internalise the constraints, frustration and stress of their situation that their immune systems are damaged, their lives are more punctuated by ill health and they die younger (Williams, RB, 1998; Mitchell *et al*., 2000[18]). The mechanisms (termed "psychosocial") through which a low relative income can undermine individual well-being are similar to those considered to be operative and linking poor health and low socio-economic status, poor health and workplace stress, and poor health and the absence of social ties (Kawachi & Berkman, 2001: Bosma *et al*., 1998, 1997; Siegrist, 1996; Marmot *et al*., 1991).[19]

NAPS (2002) has stated that "progress in relation to the proportion of the population falling below relative income lines, particularly

18. Williams, RB (1998), "Lower socio-economic status and increased mortality". *Journal of the American Medical Association*, June 3. vol 279, No. 21: 1745-1746 (editorial); Mitchell, R., M. Shaw & D. Dorling (2000), *Inequalities in Life and Death: What if Britain were more equal?* The Policy Press.

19. Marmot, MG., G. Davy Smyth, S. Stansfeld, *et al* (1991), "Health inequalities among British civil servants: the Whitehall II study". *Lancet*. 337: 1387-1393; Siegrist, J. (1996), "Adverse health effects of high effort/low reward conditions". *Journal of Occupational Health Psychology*. 1: 27-41; Bosma H., MG Marmot, *et al* (1997), "Low job control and the risk of coronary hearth disease in the Whitehall II (prospective cohort) study". *British Medical Journal*. 314: 558-564; Bosma, H., R. Peter & J. Siegrist (1998), "Two alternative Job Stress Models and the Risk of Coronary Heart Disease". *American Journal of Public Health*, vol. 88. 1: 68-74; Kawachi, I. & L.F. Berkman (2001), "Social Ties and Mental Health". *Journal of Urban Health*. September.

for a sustained period, will be monitored… in line with the indicators agreed in the EU Joint Report on Social Inclusion" (10). One of the seven indicators relating to social cohesion being considered by the European Commission [European Commission, (2000a: 594] is a measure of the degree of income dispersion—in practice, the income quintile ratio (S80/S20) which compares the share of a country's income received by the highest earning 20% with the share received by the lowest earning 20%. This is because wide inequality—of itself—can reflect poor levels of social cohesion, erode social capital, and heighten the risk of social exclusion for those at the lower end of the income distribution (NAPincl, 2001: 4.3.1). A variety of different social studies underline the damaging effects on people of living life on money incomes that are an extreme distance from the levels prevalent in their societies. The Council supports the adoption of some measure of income dispersion in Irish society as a legitimate focus of social policy.

TABLE 8.8

Distributive Impact of Budgetary Policy, 1997-2002

Budgets	**Quintiles of Disposable Income Per Adult Equivalent (% change over benchmark)**					
	Bottom	**2nd**	**3rd**	**4th**	**Top**	***All***
Budgets 1997-1999	4.5	7.9	10.9	10.7	9.8	9.5
Budgets 2000-2002	3.3	3.9	6.9	6.5	7.0	6.2

Source: Callan, Keeney & Walsh (2002).

The Council notes the evidence that budgetary policy since 1997 (the year of the formal adoption of NAPS) has not made a particular priority of income redistribution nor achieved a sustained improvement in the relative income position of the poorest households (Callan, Keeney & Walsh, 2002; Callan, Keeney, Nolan & Walsh, 2001). Table 8.8 compares the changes produced by decisions announced in budgets with what is termed a "distributionally neutral" stance (what would have occurred if all welfare rates and tax allowances had been indexed in line with wage growth). Thus, it does not show the actual changes in incomes that occurred as a result of budgets but the difference between what did occur and a hypothetically neutral budgetary stance. The pattern that emerges is clear: budgetary policy has had the effect of increasing incomes in the bottom two deciles but has increased income in the top two deciles by significantly more.

Budgetary policy, of course, is framed to meet other and, arguably, more important objectives for people who are socially disadvantaged than the immediate redistribution of income, such as promoting economic growth, increasing the employment intensity of that growth, securing greater equality in opportunities, and raising the lowest living standards. In fact, there are difficult to quantify trade-offs between these objectives and the redistribution of income at a given moment in time. In the medium to long-term, a more equal distribution of *market* income (for which evidence was adduced between 1994 and 1998 in Chapter 2) can be interpreted as evidence that these other avenues through which budgetary policy is supporting NAPS are having an effect. The short-term distributive impact of budgets, therefore, is by no means the sole criterion by which their alignment with NAPS can be assessed.

Nevertheless, it is noteworthy that the immediate redistributive impact of the prevailing budgetary stance between 1997 and 2002 can be characterised as having contributed to widening inequality in the income distribution over what would have happened if the policy stance had been to index welfare payments and the tax structure in line with wage growth.

In this area of money incomes falling far below the levels prevailing in society, the Council believes Ireland should welcome the challenge of being strongly linked—through the European Union—with countries that have strong traditions in maintaining some boundaries to the degree of inequality in the distribution of income at a national level. While data on income distribution is contained in the calculation of the Gini coefficient (for example, Table 2.10 in Chapter 2), there is as yet no consensus on how the data should be interpreted, i.e., the significance of the figures. For example, how high does a Gini coefficient have to be (or how strong a deterioration has to be recorded in it) for it to be accepted as requiring redress? The Finnish Economic Council, for example, believes that "as a rule, income differentials (measured by the Gini coefficient) are considered small if the figure is below 25, and large if it is over 30" (2002: 3).[20] The Gini coefficient for the distribution of disposable income in Finland was 20.7 in the mid-1980s and rose by 10 per cent to 22.8 in the mid-1990s, a rise largely due to an economic recession in that country in the early 1990s (Table 8.9). In Ireland, by contrast, the Gini marginally improved over the same period but that meant it came down to a level of 32.4 in 1994. We know that it increased again with the start of the economic boom and was 33.8 in 1998 (Table 2.10, Chapter 2).

TABLE 8.9

Inequality Indicators for the Entire Population, Selected European Countries, mid-1990s

	Gini Coefficient mid 90s	Increase in Gini mid 80s – mid 90s	P90/P10 Decile Ratio mid 90s
Denmark	21.7	-1.1	2.7
Finland	22.8	2.1	2.8
Sweden	23.0	1.4	2.7
Netherlands	25.5	2.1	3.2
Belgium	27.2	1.2	3.2
Ireland	32.4	-0.6	4.2

Source: Table 2.2, Förster (2000)

The standards set by other small northern EU member states are exacting but the Council believes systematic comparison with them will be beneficial. The benefits will include, not just higher living standards for that section of our population living on the lowest incomes, but a more cohesive society in which a wider and deeper acceptance of interdependence facilitates a greater social capacity to

20. Finnish Economic Council (2002), *Labour Market Exclusion, Income Distribution and Poverty*. Prime Minister's Office.

live with the demands of constantly reinventing the economy and flexibly transforming institutions in a global age.

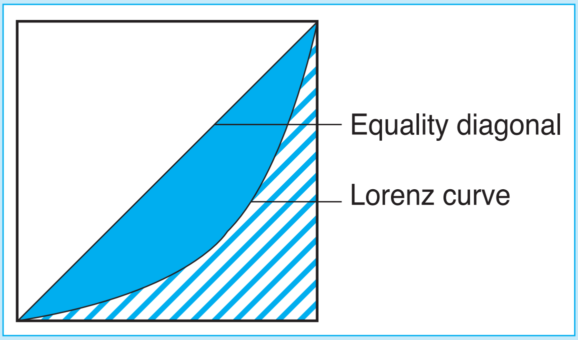
The development of greater co-ordination in setting objectives and targets, devising strategies and policies, and monitoring outcomes, for social policy that will emulate the process EU member states are currently following in employment matters (the 'open method of coordination', OMC) will have the full backing of the Council.

BOX 8.5

The Gini Coefficient

The Gini coefficient is based on the Lorenz curve, a cumulative frequency curve that compares the distribution of a specific variable with the uniform distribution that represents equality (Figure 1). This equality distribution is represented by a diagonal line, and the greater the deviation of the Lorenz curve from this line, the greater the inequality.

Areas for calculation of the Gini Coefficient



When applying this index to income distribution, the cumulative proportion of the population is generally shown on the X axis, and the cumulative proportion of personal disposable income on the Y axis. The greater the distance from the diagonal line, the greater the inequality.

The Gini coefficient is calculated in terms of how far the actual distribution deviates from an equal distribution of incomes across all households. The higher the Gini coefficient, therefore, the greater the degree of income inequality; 0 represents perfect equality and 1 total inequality. The actual value corresponds to twice the area between the Lorenz curve and the equality diagonal (Figure 8.2).

The significance of changes in the Gini coefficient can be expressed in terms of a hypothetical redistribution. For example, the difference of 2.1 percentage points in the Gini coefficient reported in Table 8.12 for Finland (and the Netherlands) would have been brought about if each income unit below the median in the mid-1980s had transferred 4.2 per cent of mean income to each income unit above the median over the period in question. In other words, the difference in Gini coefficients between two periods is one-half the value of a hypothetical lump-sum transfer divided by the initial mean income, this transfer going from each income unit below (above) the median to each unit above (below) the median (Förster, 2000: 11).

CHAPTER 9

INFRASTRUCTURE, PUBLIC UTILITIES AND SPATIAL DEVELOPMENT

9.1 INTRODUCTION

It is clear that Irish society has been undergoing a sustained structural transformation from an economy centred primarily on agricultural output to an industrial and increasingly service orientated economy with an associated growth in large scale settlement, with agriculture retaining an important role in rural areas. Consistently high levels of economic growth over the last decade have brought their own problems, particularly given the speed with which such a transformation has taken place and the pace at which institutions and the public policy machine have been able to adapt. Nowhere has this been more marked than in the area of spatial planning, infrastructural development and the creation of sustainable communities and affordable accommodation. Demographic factors, a reversal of many decades of emigration, and an increasingly urban society have all contributed to the difficulties society now faces. The quest for affordable levels of housing has driven people further from work, giving rise to longer commuting times, increased inequalities and deterioration in the balance between work and the family.

In its 1999 *Strategy* (NESC, 1999), published contemporaneously with the National Development Plan (NDP), the Council identified what it believed to be five areas of crucial importance in Ireland's infrastructural deficit: housing; public transport; roads; cultural and recreational infrastructure; and telecommunications infrastructure. Some three years on it is now timely for the Council to once again consider the current state of the infrastructural deficit in Ireland and the progress that has been made on the achievement of the targets set down in the NDP. Infrastructure plays an important part in the economic and social development of society and an infrastructural deficit imposes upon society constraints that may undermine spatial balance, international competitiveness or social inclusion and restrict consumer choice. The delivery of infrastructure in a timely manner, and of appropriate quality, would allow Ireland to cement the levels of income achieved to date, continue to grow into the future and to deliver a more inclusive society. It is for this reason that the Council has included as an indicator Infrastructural Expenditure per Capita in its recent report on *National Progress Indicators* (NESC, 2002a).

In particular, it is important to note that infrastructural priorities may undergo relatively rapid evolution. In addition to the five priorities listed above from the 1999 *Strategy*, the Council notes two additional priorities in 2002: energy and waste management. It is important to recognise that, while the priorities may change relatively quickly, the supporting investment to address deficits may take many years.

In addition to the identification of a number of sectoral infrastructural deficits this chapter also considers the role of public utilities, the role of finance and cost recovery for infrastructural projects and the regulatory and spatial institutions required to deliver infrastructure.

9.1.1 Ireland's Infrastructural Deficit

In his review of infrastructural investment Gramlich (1994) suggests there are at least four ways to determine a shortfall in infrastructure capital:

- Engineering assessments of infrastructure needs;
- Political measures based on voting outcomes;
- Economic measures of return; and
- Econometric estimates of productivity impacts.

It is clear that these measures may be in conflict and that a recognised engineering or economic need may not be met because of lack of political will or because of political opposition. However, even without a comprehensive evaluation along the lines of any of these measures it is clear that, while progress has been made in some areas, Ireland is currently facing an infrastructural deficit as identifiable through the absence of a road network of sufficient quality to link major settlements, the possibility of future electricity generation shortages and a low level of communications connectivity within the country. Infrastructure contributes to the Council's vision as outlined in Chapter 3 in a number of respects. It facilitates the dispersion and concentration of economic activity through physical linkages thus increasing both economic and social opportunity. Enhanced infrastructure also leads to an improved quality of life at individual locations. An infrastructural deficit, and in particular physical infrastructure linking settlements, must itself be measured in the context of balanced regional development and settlement pattern.

9.1.2 Conceptual Approach

Five main analytical ideas inform the Council's analysis of infrastructure, utilities and housing:

- Society's concept and goal of spatial balance evolves in response to the dynamic of economic and social development;
- The current approach to the funding of infrastructure, and cost recovery following its completion, is built upon a set of conventions and we should be open-minded to changes in our approach;
- In regulating utilities we have to resolve issues of two kinds. The first concerns the balance between single utilities and multi-utilities, whereby one firm engages in the provision of many services with associated economies of scope and scale. The second concerns the balance between short-term cost containment and profit, on the one hand, and long-term or strategic provision, on the other;
- The Council can envisage a set of institutions which is more centralised, in a few key respects, yet much more decentralised in general; and

- In regulating public utilities there is a spectrum of institutional arrangements, running from pure competition to intra-organisational change, rather than a single model capable of meeting public policy goals.

Each of these is briefly described below.

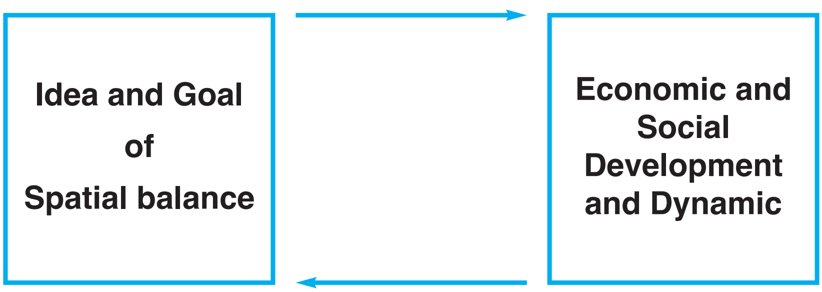
The Interdependence of 'Spatial Balance' and the Economic and Social Development

The Council believes that our idea and goal of spatial balance evolves in response to the dynamic of economic and social development. The idea of 'spatial balance' or a desirable spatial pattern does not constitute a timeless goal against which we can compare actual developments. The pattern of economic and social development has a spatial dynamic that includes strong tendencies to agglomeration and some tendencies to dispersal. These vary from one period of development to another, depending on the dominant technology and other factors. This spatial dynamic is not a law of nature, beyond deliberate human influence, but nor is it entirely within the control of policy. While the spatial pattern can be significantly altered by public policy—as Ireland's development shows—such policies must 'cut with the grain' of the patterns of economic and technological development that prevail at any particular point in time.

Consequently, a sensible idea or goal of spatial balance must evolve. This idea is represented graphically in Figure 9.1.

FIGURE 9.1

The Interdependence of 'Spatial Balance' and Development



For example, while our idea of spatial balance once involved a wide dispersal of population based on the maximum number of family farms, it might now involve sufficient city and town development to sustain economic activity and population in each region of Ireland (NESC, 1994).

Likewise the Council believes that the set of infrastructural requirements and the appropriate spatial balance are interdependent and evolve over time. It is only with an understanding of the true benefits and costs of spatial diversity—economic, social and environmental—that infrastructural requirements can be determined. Yet it is also the evolution of infrastructure, including the evolution of settlement patterns and associated economic and social development that shapes our current thinking about appropriate spatial balance. It is clear that there is inter-dependence between these elements that runs in both directions.

The Variety of Institutions to deliver infrastructure and spatial balance

It is an ongoing challenge to find the appropriate balance between local, regional and national decision makers in infrastructural and spatial planning and provision. While the Council is in favour of more devolution to the local level in many policy areas, infrastructure and spatial planning is a national issue and therefore requires national co-ordination. A major challenge is to devise institutional arrangements which combine national strategy with regional co-ordination and local devolution. The devolution of decision making to the appropriate level is one of the twelve principles of sustainable development identified by Comhar (Comhar, 2002).

Ireland has a fragmented set of regional and local institutions combined with a set of unclear and underdeveloped linkages between them. The Council believes that national authorities have a strategic role in planning, particularly in planning major infrastructural projects. This needs to be informed by local communities and by those at local government level to ensure that development builds quality localities and communities.

There is significant interaction between land use and infrastructural requirements. The spatial distribution of housing, workplaces, shopping, educational establishments and other services has a major impact on the infrastructure required to provide essential services. The Council suggests that high priority be given to devising institutional arrangements that can co-ordinate spatial planning and infrastructural provision to deliver a more sustainable pattern of settlement and land use.

Funding and cost recovery for infrastructure

Infrastructure must be paid for, whether through general taxation by today's generation, or future ones, or through charges for access to infrastructure.[1] To the extent that government borrowing is not possible, or deemed undesirable, alternative means to finance the necessary infrastructure must be considered. The existing financing of infrastructure and the recovery of costs is based on a set of conventions that differ across sectors and are somewhat arbitrary in nature. It is important to recognise that these conventions can be modified.

The Council recognises the importance of many of the services provided by national infrastructure and hence the universal nature of their provision. It was for this reason that many of these services evolved under state planning and ownership. In the provision of some services, precedent has dictated that access charges, where applicable, are levied on a uniform basis (e.g. line rental for voice telephony), whereas in other cases a more incremental, or cost reflective, approach has been adopted (e.g. initial access and ongoing payments for access to the electricity grid).

No one principle of pricing is superior in all cases and therefore a case-by-case analysis is required. However, the Council cautions against the introduction of purely cost-reflective pricing without consideration of the other important objectives to be fulfilled through the provision of infrastructure. Where models of cross-subsidy are employed to meet such objectives, consideration should be given to the possible distributional and efficiency effects.

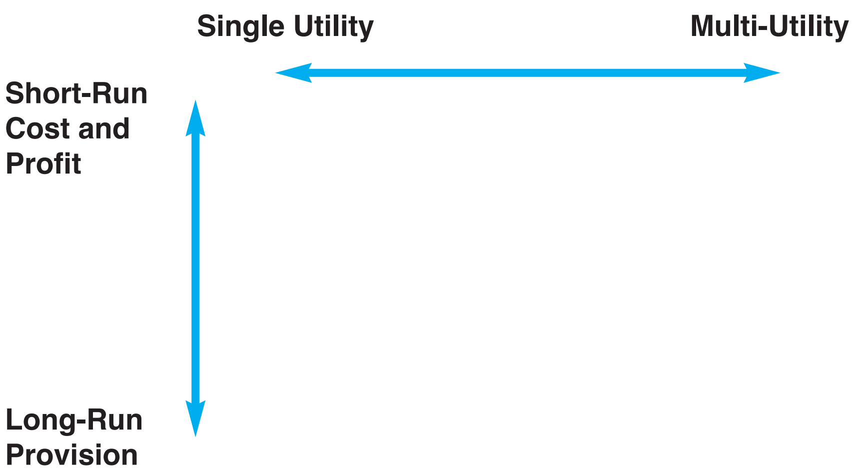
1. Future charges can be recovered over a variety of time periods and differently from different customer classes.

The Spectrum of Challenges in Regulating Utilities

An important challenge for Irish society and policy is to find the best manner of regulating public utilities and networked industries. The background to, and nature of this challenge is described in section 9.4 which explains the European dimension in service and utilities. While the issues involved are complex, and vary from one utility to another, they can be seen as lying in two dimensions, as described in Figure 9.2. The first dimension runs from single or separate utilities (electricity, telecommunications, water etc.) to provision of several utilities by each company, often called a multi-utility approach. In choosing within this spectrum we must balance maximum competition (likely to be achieved by a large number of service providers) against maximum efficiency (which may rely on the exploitation of the synergies between utilities or on the exploitation of economies of scale within a single sector). The second dimension runs from short-term cost containment and profit, at one end, to long-term or strategic provision, at the other. Again the mix of competition, regulation and strategic state intervention varies.

FIGURE 9.2

The Spectrum of Challenges in Regulating Utilities



The Spectrum of Regulatory and Institutional Arrangements

In regulating public utilities there is a spectrum of institutional arrangements available. These run from pure competition, through various forms of regulated and virtual competition, to public audit, but also include arrangements to ensure high-performance and flexibility within the organisations that provide utilities and services. This spectrum is represented graphically in Figure 9.3.

FIGURE 9.3

The Spectrum of Regulatory and Institutional Arrangements

Pure Competition	Regulated Competition	Virtual Competition	Public Audit	Partnership Framework and SMI	Intra-Organisational Change

There are doctrinal positions which lead some people to place all their faith in one model, whether it be a single-minded belief in competition or a defence of traditional models of public ownership and provision. In the Council's view, the various social and economic goals cannot all be neatly met by reliance on a single approach. Although better contracts and incentives can improve things, there is no perfect contract or set of incentives. Consequently, there is no avoiding organisational performance and the search for structures and routines that achieve organisational change (Miller, 1992). Later in the chapter the Council reviews the existing debate on regulated and virtual competition and raises some new issues concerning public audit and the institutional arrangements necessary to ensure high-performance.

Three Common Elements

The overarching theme of this chapter is one of balancing the choices society makes between policies and programmes which deliver today and those which provide for sustainable development into the future. This requires that we create policy frameworks and institutional designs that ensure that society makes the best possible use of the resources available to it. The Council believes that despite the disparate infrastructural needs there are common elements that arise in all of them.

As indicated in Chapter 3 the Council identified these common elements as the following:

- To ensure the necessary investment takes place;
- To ensure a high quality or standard of service in infrastructure, public services and regulation; and
- To achieve the necessary institutional and organisational change.

Within this, the Council believes there are trade-offs to be made between the pursuit of a series of policies with a short-run focus and those that encompass a long-term view of societal development. There is also a need to balance the benefits of policies that emphasise a cross-sectoral and cross-cutting approach to policy making, and the associated synergies, with an approach that recognises that there is no unique set of institutions or models that will optimise all possible policy decisions. Questions such as these are already being addressed within the context of the regulatory framework for utilities. Regulators, be they state controlled or independent, must balance short term cost and long term gains, and the need to develop a vibrant and sustainable industry with the demands of customers for a better quality service at lower costs.

The Chapter is arranged as follows. Section 9.2 examines the development of settlement patterns, increasing urbanisation and the role of both the planning system and the *National Spatial Strategy* (NSS) in identifying and delivering balanced regional development. The following five Sections identify some key infrastructural priorities in housing, energy, transport, communications and waste management. Current policy programmes are discussed and potential shortfalls identified for each sector. Elements from the experience of each sector, and the common elements between all of them, are taken up in the elaboration of the overarching theme of the chapter which is expanded in Sections 9.9, 9.10 & 9.11. Section 9.9 discusses the evaluation and financing of infrastructural projects in general, Section 9.10 looks at how the projects, once identified can be delivered in an efficient manner and Section 9.11 outlines the institutional arrangements to ensure efficient delivery.

9.2 PLANNING AND SPATIAL BALANCE

In large part, it is the desirable regional pattern of social and economic life that determines the need for infrastructural investment to link settlements and communities. This section examines recent changes in land and planning policy and suggests areas for further consideration in fostering sustainable communities of tomorrow. Land is ultimately a fixed factor and cannot be created or destroyed. Land also differs from other factors in that it is non-mobile in nature and therefore much less subject to distortion through taxation or other measures than more mobile factors such as labour or, in particular, capital. It is up to society as custodians of the land to make the best available use of the land to maximise its goals—economic, social and environmental.

9.2.1 A Population on the Move

> One of the paradoxes of urban economic development is that resident households desire the personal consumption of space in all of its pleasant varieties, and strive to limit the indulgence of this desire by their fellow citizens. Each household seeks to consume private space as a location and surrounding garden for a residence, and can generally be expected to devote a considerable portion of income towards its acquisition. When others do this, however, the process is sometimes strenuously opposed and decried as "sprawl". The tension is made more severe in times of rising incomes and/or falling transportation costs because these tend to encourage an increase in the private consumption of land (Cheshire and Sheppard, 2002).

It is clear that Ireland has recently begun to experience "urban sprawl" with an increasingly monocentric society focused on Dublin with regional development in Cork, Limerick, Galway and Waterford. So called "commuter houses" for Dublin are now being sold some 60 miles away from the capital and the increased traffic congestion which has resulted from increased commuting, including the increase in long distance commuting where few alternatives to private car transport are available, has slowed traffic movement in major cities to little more than would have been achieved by horse and cart a century ago. The recently released preliminary figures from Census 2002 illustrate the point, with the greatest increases in population in Meath (+22.1 per cent), Kildare (+21.5 per cent), Fingal (+17 per cent) and Westmeath (+13.8 per cent). Dublin suburbs have also shown enormous growth with the Dublin suburb of Lucan almost trebling in size, while Blanchardstown-Blakestown increased by 61.9 per cent. Some 40 per cent of the population, including the majority of immigrants, are living in the greater Dublin area. It may be neither possible, nor desirable to counteract such growth which is, to a significant degree, self-perpetuating. Settlement must develop in line with consumer preferences not only for areas of open countryside but also a desire to consume private space. The question is how to devise a policy to achieve spatial balance that does not try to counteract the agglomerative forces of social cohesion and market development and yet make other regions more attractive, in combination with a drive to more concentrated development in the Dublin area.

The census also provides some evidence of the regeneration of inner city Dublin and the reversal of many years of population decline in the inner city boroughs and this can be seen as some success for the measures introduced to engender urban regeneration. Most inner city areas recorded an increase in population, although this was offset by some decline in more mature suburbs associated with demographics and the family life cycle.

While we have been aware of the need for the development of a balanced regional policy since the time of the Buchanan report in the 1960s, successive National Development Plans or programmes of rural development policy have failed to integrate all elements of spatial balance adequately. The Council has long recognised and identified the need for analysis of overall settlement patterns and clarification of policy goals concerning settlement, including in its report on *New Approaches to Rural Development* (NESC, 1994).

The planning system exists to foster well-developed communities, curb undesirable development, and to regulate for market failures in the provision of development. The Planning and Development Act, 2000 expresses the purpose of the planning system to provide in the interest of the common good for proper planning and sustainable development including the provision of housing. The ultimate relaxation in supply would be to abolish the current system of planning and let the owners of land and developers decide upon development. The Council believes better, not less planning is required in order to curb the urban sprawl that has emerged from the current regime.

To be effective the planning system must integrate the needs of local communities with overall national policy objectives. It must be able to process the demands of society for increased development in a timely manner and it must ensure that development takes place in a co-ordinated fashion that meets the requirements of continued economic and demographic growth. The planning system in Ireland has for too long been subject to inconsistency at the local level, and a lack of transparency and has succumbed to the pressures placed upon it by pressure groups with vested interests.

Two particular problems identified by the Council are urban sprawl and single rural dwellings. The large number of single dwellings can raise a number of problems. One such problem is that a development premium is built into the land price making it more difficult to purchase land for agricultural purposes, on a commercial basis.

Rural development in Ireland has been characterised by a dispersed village pattern and rural hinterlands are a key component of the overall spatial hierarchy. It is possible to distinguish between housing needed in rural areas by persons closely linked to, through family or other connections, or working in rural areas from housing desired by persons living and working in urban areas, including second homes. As a general principle, subject to good planning practice in matters of location and design, the planning system should endeavour to accommodate rural-generated housing needs to sustain the rural community.

However, settlement must develop in line with consumer preferences not only for areas of open countryside but also their desire to consume private space. Equally, housing policy should, as far as possible, facilitate economic and social mobility. The challenge is to devise a policy to achieve spatial balance that does not restrain the dynamic of economic and social development, yet makes regions more attractive.

9.2.2 A National Spatial Strategy

In 1994 the Council drew attention to the critical need for the development of national settlement policy. The Council further developed its views on the importance of a national spatial framework in its 1999 *Strategy:*

> A National Spatial Development Strategy (NSDS) would provide a framework for the operation of the three principles of infrastructural development—comprehensiveness, co-ordination and 'long-termism'. It is through this principled approach that the objectives of infrastructural developments are most likely to be achieved. A NSDS would provide a framework for analysing relationships between changes in land use, economic activity, population and infrastructure. It would also provide a basis for correcting past mistakes that have resulted in uneven development between the East (especially Dublin) and the rest of the country that has led to damaging economic and social problems in both areas due to congestion and marginalisation. By having a national orientation, it would recognise that the country is composed of many different spatial units (national, regional, local, urban, rural, suburban etc.), where no unit is subsidiary to any other, but the workings of the whole are enhanced by the co-ordination and integration of its constituent parts. And, while a NSDS would provide an appropriate framework for considering infrastructural issues, this would not be the only role of the NSDS. Fundamentally, it would seek to provide a means for devising a co-ordinated and integrated response from a spatial perspective to broader goals such as maximising economic performance, social inclusion and environmental sustainability. (NESC, 1999: 457)

The Council therefore welcomes the fact that the NSS has now been published (Department of Environment and Local Government, 2002b). The NSS sets out the explicit objective of providing an overall national framework for dealing with spatial issues, within a sustainable national economic and budgetary context and within an ‘island of Ireland’ perspective, which can contribute to the enhancement of national competitiveness and a high quality environment. In particular, the NSS is designed to improve the effectiveness of public investment in infrastructure and other relevant services around the country.

As noted in Section 9.1 our idea of spatial balance evolves over time as the variety of centrifugal and centripetal forces in the economy and society change and interact. Over the last two centuries economies of scale and agglomerative forces have brought together activity in the form of large manufacturing plants and extensive settlement patterns, whereas activity prior to this was based around a more micro-enterprise cottage industry approach. The information revolution, and the ability to conduct business in more remote locations, with fewer transportation costs, and the ability for knowledge to traverse space more easily introduces opportunities for business and settlement to become more dispersed again.

The Council believes that a national spatial strategy should provide a number of inputs to assist national development:

- It should provides a systematic analysis of spatial trends within Ireland over recent decades;
- It should add significantly to our knowledge of activities in different geographical areas and shed light on the relative economic and social performance of each area;
- It should provide a template for the development of the country over 20 years that provides a balanced approach across all sectors and regions;
- It should propose a coherent strategy for managing the spatial dimension of Ireland’s economy and society, focusing on the development of a number of strategic locations for certain kinds of investment; and

- It should provide an implementation framework to be led by the Department of the Environment and Local Government, but encompassing a wide range of public agencies within the overall framework.

In line with its earlier work on national and rural development, the Council emphasises that a successful regional and settlement strategy will be of benefit to all areas and interests. Experience shows that a zero-sum view of spatial development, in which progress in one area is seen as a loss to other areas, is not only divisive but also short-sighted, since it is at odds with the dynamic of regional development. Consequently, it argues that spatial strategy that meets the requirements listed above should not be seen as creating winners and losers.

The NSS should be seen as a framework document and an overall strategy under which other public sector policies and programmes should be tailored and with which they should be consistent. The NSS seeks to promote certain strategically located places as part of an all-Ireland network which will energise the potential of both urban and rural areas. It seeks to do this through the strengthening of existing gateways, almost all of which were in the Southern and Eastern region, (Galway in the BMW region) combined with a strengthening of the pivotal international role played by Dublin, and by establishing four new national gateways in the Border, Midland and Western region. In addition, the NSS identifies nine strategically located medium sized hubs which will support and be supported by the gateways and link out to wider rural areas.

The NSS encompasses a long-term horizon of nearly 20 years and its importance, and strategic nature, should be considered in that regard. The Council emphasises the need for the NSS to be supplemented and supported by regional planning guidelines, which should draw on relevant local plans and strategies such as City and County Development Board strategies.

The NSS seeks to adopt a framework of polycentric development across Ireland, opposing the concentration and critical mass that has developed along the Eastern seaboard. It is more than simply a designation of selected settlements, but encompasses the inter-relationships and infrastructural provision between designated centres of development and their supporting hinterlands. The NSS does not seek to prescribe an exact formula for each centre's development, nor does it purport to suggest that all such designated centres should be treated in the same manner.

Economic activity, investment and job creation represent the most significant influence on spatial patterns. Accordingly, the location, concentration and distribution of economic activity will have a crucial bearing on the ability of the NSS to achieve balanced spatial development. Those areas designated for development will need to be supported by all relevant stakeholders to help foster clusters of economic activity which may give rise to spill-over benefits for both firms and workers.

Combined with the economic and education spheres, social and cultural factors providing a good overall quality of life are important elements which determine what makes an area attractive to live and work in. The NSS sets out key considerations for evaluation and priorities with respect to housing development to meet the needs of local communities, while balancing the needs of society as a whole, and establishes a hierarchy of access to social infrastructure that will help foster social capital and give the greatest access to the greatest number of services in the most cost effective manner.

The Council welcomes the focus of the Strategy on a limited number of key development centres supported by regional and local development plans. While it would be possible to be more selective the Council recognises that there is significant dispersion and low density of settlement in Ireland and that the networks for inter-connectivity between settlements are weak, and these will have been key considerations in arriving at the designated settlements.

In providing infrastructure to facilitate development of particular towns, there can arise a kind of 'chicken and egg' problem: it is hard for the town to develop high technology industry and services until the infrastructure is in place and it is hard to justify heavy infrastructure investment until there is a demand for it. Parties may have to take the risk of developing "stranded assets" to ensure further development follows. Therefore, infrastructure providers should work together to avoid the possibility of the development of a low level equilibrium of high prices and low demand as described by the Council later in this chapter. As such, it is imperative that government departments and agencies put in place mechanisms to ensure that the NSS is embedded into policy decision making. The Council urges the necessary statutory and other mechanisms be put in place to ensure this happens.

The NSS, translated into action and supplemented by local and regional plans and initiatives, provides us with the opportunity to place the spatial dimension at the heart of infrastructural, enterprise, employment and settlement policies and to counter some of the uneven concentration of population and activities in the past. The Council emphasises, however, that a wide variety of different agents will be required to co-ordinate their approaches to development if a balanced regional approach is to succeed. Therefore working out the appropriate institutional arrangements will be a major challenge. It will include members of the development agencies, regional and local planners but also providers of the necessary communications infrastructure, energy infrastructure, transport development and higher education sector. The Council returns to the issue of institutional arrangements in spatial development below.

The Council believes that a national spatial strategy involves new approaches at several levels: national strategic investment, regional planning and local government. There will have to be regional planning guidelines in all areas, following the example of the guidelines for the Greater Dublin Area and a harmonisation of area boundaries across agencies. An integral part of the national spatial strategy will be improved system of local government and changes to land use regulation.

It is neither possible nor desirable to force a particular regional pattern of development on Ireland. There are benefits to firms, workers and citizens from some concentration and from the services and facilities that can only be supplied to a critical mass. Some such benefits were identified in the Council's previous work on the clustering of economic activity and the associated spillovers (NESC, 1998). Indeed part of our current problem arises from the fact that people do not bear the full costs that their actions impose upon society in the form of infrastructural development, congestion and environmental degradation. The Council believes that these costs should be considered by planners in seeking to achieve spatial balance. The Council will return to the issue of infrastructural pricing below.

9.2.3 Planning and Development

The Council welcomes the enactment of the Planning and Development Act, 2000 which consolidated into one act all nine planning and development acts enacted since 1963. It has made substantial steps toward structured development planning at a regional and local level, streamlined the system and placed sustainable development at the heart of the planning system. The Act requires the preparation of Development Plans every six years which shall, in so far as is practicable, be consistent with such national plans, policies or strategies as the Minister determines relate to proper planning and sustainable development.

In addition, a planning authority may at any time, and for any particular area within its functional area, prepare a local plan in respect of that area in particular for those areas which require economic, physical and social renewal and for areas likely to be subject to large scale development within the time of the plan. Finally, where in the opinion of the Government, specified development is of economic or social importance to the State, the Government may by order, when so proposed by the Minister responsible, designate one or more sites for the establishment of a Strategic Development Zone to facilitate such development.

The introduction of such plans should lead to more structured development not only locally but regionally and nationally as well. The Council wishes to caution against supply orientated planning in favour of planning that recognises all aspects of sustainable communities, economic, social and environmental.

One key component in Section 48 of the Act concerns increased transparency in respect of development levies tying them to the particular infrastructural projects associated with the development. Another concerns the introduction of a new system for the provision of affordable housing by developers. Yet another is concerned with "special" development levies associated with the granting of planning permission where infrastructural development has conveyed a value upon the land. There are possibilities for the extension of all these mechanisms.

These are measures by which society now captures a portion of the increase in the value of land which results from planning decisions and permissions. In addition fiscal measures such as the taxation of capital gains and the application of VAT on housing also convey a proportion of the land value back to society. The value attributable on development land stems from the willingness of society to accept development in place of open space and in the overall development of economic and social infrastructure in the surrounding area. The Council therefore believes it appropriate that those who gain from society's willingness to accept such development should return some portion of their gain back to the overall enhancement of society.

9.3 THE HOUSING MARKET

The focus of this chapter is spatial development and land use policy rather than housing. However, it is clear that housing is an important component of infrastructural development and that the demands on development land and demands for housing are inextricably linked.

A primary objective expressed by the Council in 1999 was "the provision of sufficient affordable housing so that as far as possible every household enjoys real choice between housing tenures, each of which offers good physical standards at a price or rent that the household can afford" (NESC, 1999:489). A number of trends in housing stock, house building and affordability are documented in Chapter 2. The Council believes that there are a number of interrelated problems which must be addressed to deliver a sustainable housing market. These include supply and demand balance, affordability, urban sprawl and single dwellings.

Housing demand is determined not only by price but also by demographic change, immigration and changes in the patterns of household formation. Demand is also driven by rising employment and incomes, but tempered by the affordability of dwellings, which includes elements other than price alone, and which may impact on household formation behaviour.

Social and affordable housing represents the single largest infrastructure component of the National Development Plan (NDP). The NDP proposed to increase the local authority housing stock by about 35,500 over the 2000-2006 period, to substantially expand voluntary housing activity from 500 to 4,000 units per year and to provide up to 2,000 units per year under the local authority affordable housing scheme and shared ownership schemes (NESC, 1999). The target for local authority completions and acquisitions was subsequently raised to 41,500 by the Government in June 2000. The table below examines progress in 2000 and 2001 against these targets with the interim local authority targets being based on the earlier total target of 35,500.

Preliminary evidence[2] would suggest some further progress towards targets in the first six months of 2002 with 1,468 local authority houses completed, a rise of 13 per cent over the same period in 2001 and 383 houses acquired by local authorities during the first six months. There were some 7,916 houses in progress, as opposed to 7,486 at the end of 2001. In addition, voluntary housing completions have risen from 514 to 630, a 22 percentage point rise over the same period in 2001. The total target under the Economic and Social Infrastructure Operational Programme is due to rise by only 5.5 per cent to 8,750 units in 2002.

2. Based upon the second quarter data contained in the Housing Statistics Bulletin, June 2002

TABLE 9.1
Social Housing Completions vs Targets

	2000		2001	
	Target	**Actual**	**Target**	**Actual**
Local Authority Completions and Acquisitions	4,000	3,207	5,000	5,022
Shared Ownership Scheme	1,000	1,190	1,000	1,611
Affordable Housing Scheme	1,000	86	1,000	272
Voluntary Housing Output	1,000	951	1,250	1,253
Total	**7,000**	**5,434**	**8,250**	**8,158**

Source: Economic and Social Infrastructure Operational Programme (2000) and Department of environment and Local Government, *Housing Statistics Bulletin* (various)

It is clear that to gauge changes in the local authority housing stock one must also consider the disposal of local authority dwellings. Considering sales of 1,844 dwellings in 2000, 1,411 in 2001 and 1,257 in the first six months to June of 2002, in excess of 4,500 dwellings have been disposed of over the period of the NDP to date. These dwellings obviously remain part of the housing stock and often provide accommodation to previous local authority tenants. Similarly houses acquired by the local authority would once have been inhabited by non-local authority tenants and will therefore contribute to a demand elsewhere in the system. Thus, as neither of these provide net additions to the housing stock the number of new local authority houses completed, excluding acquisitions and disposals, might provide a better measure for the assessment of social housing provision.

The National Economic and Social Forum (NESF) carried out a study entitled *Social and Affordable Housing: Building the Future* in 2000. This focused on the delivery of housing as a public service and increasing the availability of affordable housing. Social and affordable housing is now available through a variety of means: subsidised costs of owner occupation in publicly and privately owned housing; rental of publicly owned housing; supplemental rental payments for the renting of private sector accommodation; the provision of housing units through the voluntary sector. Each of these means of delivery has a part to play in meeting the need for social and affordable housing units. At a minimum, the Council wishes to see that the necessary funding and support is made available to deliver on those commitments already made under the National Development Plan and elsewhere.

The Bacon Reports, commissioned by the government, endeavoured to address declining affordability through corrections in the supply and demand balance. The supply of houses has grown at unprecedented rates in recent years, with an increase in the number of new houses from just under 39,000 in 1997 to 52,600 in 2001. This period has also witnessed comparable growth in the number of local authority and voluntary housing completions rising from 8.7 per cent of total completions in 1997 to 9.3 per cent of total completions in 2001. While the supply and demand balance appeared to even out somewhat in 2001, evidence for 2002 suggests that the housing market is once again buoyant, at least in some segments of the market.

The need to ensure an adequate supply of housing is clear given the need for an additional 40,000 units per year over the next decade as highlighted by the ESRI in its Medium Term Review 2001-2007 (Duffy *et al*. 2001) or up to 500,000 new households over the next decade as identified in the NSS. It is also evident that demand is not simply a question of numbers but involves higher standards in terms of design and the urban environment combined with increased quality in construction and energy efficiency (Barlow *et al*., 2002). The Council welcomes ongoing initiatives to improve construction and design quality, combined with improved safety conditions.

The Council recognises that assessment of affordability is not straightforward and must take into account not only rising prices and incomes, but also changes in the cost of borrowing and any relaxation of credit constraints and intergenerational equity transfers that may be present. What is clear, however, is that the increased burden that has arisen as a result of rapid price growth has fallen on a particular segment of society and has affected the overall wealth distribution between owner-occupiers and other tenures.

9.3.1 Affordable Housing Measures under Section V of the Planning and Development Act

All forms of social and affordable housing have an important role in meeting our housing needs. One form is that provided for under Section V of the Planning and Development Act, 2000, which sets out measures for the provision of 'affordable housing' in the context of the local authority development plan. This measure is dealt with here as it is essentially a development land measure. It acts as an effective tax on the market for development land and ought to reduce the willingness to pay for this land.

The proposal aims to overcome some of the problems traditionally associated with the provision of local authority housing, such as the dichotomy between ownership and custodianship and poor levels of maintenance, by creating a variety of tenures within developments. The Council supports such measures and believes that they can foster a more integrated community and society and help to avoid pockets of local deprivation experienced in the past. The Council would, however, like to draw attention to what it believes are a number of ways in which in the proposal in its current form could be improved.

The Council notes that the scheme provides for asymmetric gains in the event that property is subsequently sold, which may reduce its value in building up the stock of social housing

Firstly, if the dwelling is sold in the first ten years of occupation then the occupier will benefit to the extent of their share of ownership in the property, where the property has risen in value, but will be protected in their entirety from any capital losses upon sale. Secondly, where the property has been in occupation for more than 10 years, the amount to be returned to the local authority falls on a sliding scale by 10 per cent per year until after 20 years the property is owned in its entirety by the occupier, with no outstanding liability to the local authority. This permits a "super-normal" return to the occupier compared to a "standard" owner occupier assuming the property grows in value in line with general house price inflation. It also acts as a very strong incentive to remain in the property from years 10 to 20, stronger indeed than is present in the first ten years of occupation. This has the dual effect of discouraging household mobility in this stage of tenure as well reducing the social housing stock, or associated funds, available to local authorities for that purpose.

A further potential difficulty with the proposal is its discretionary nature; the local authority is to decide the "affordable" housing need in the area before specifying the number of units to be designated under the affordable housing scheme. Prosperous areas may be officially recorded as having little unmet demand for affordable housing despite the fact that property prices may be high in such areas and outside the reach of the vast majority of households. This might reflect the fact that underlying divisions mean that these areas contain few inhabitants who would qualify for social housing. To this extent the new approach is unlikely to create the integrated community which the Council believes the legislators envisaged.

BOX 9.1

The Debate on the Affordable Housing Scheme under Part V of the Planning and Development Act

The Council wishes to highlight the various arguments it sees in favour of, and against, such a scheme.

The **proponents** of such a scheme might put forward a number of arguments including:

That mixed housing is socially desirable and reduces ghettoisation and areas of social deprivation.

That there is substantial profit made on new housing by both builders, and particularly landowners, and that this economic rent can be extracted without the creation of distortion in the housing market.

That this is an extension of public-private partnership and can result in public housing stock of a better quality built in a more efficient manner.

Counterbalancing these arguments might be the following:

Overall social welfare may be reduced if the welfare of the previous private occupiers of such new build schemes is reduced by the fact that a proportion of the housing is in the social housing stock. From a Pareto efficiency perspective this may not be the best use of the scarce resource (prime building land) and it may be theoretically possible to affect a transfer to make everyone better off.

Mixed housing may not be appropriate, particularly given the differing circumstances faced by the occupants of such mixed housing schemes including access to private transport, and hence (possibly) the non-viability services on which occupants of such "affordable housing" rely and which may require "critical mass" to maintain viability. It is important, however, to distinguish between car use and ownership.

The non-distortionary impact may not translate to brownfield land (i.e. predominantly urban land previously developed) where the betterment has already been eroded and where affordable housing may be most required. Therefore, the new measure may affect the supply of such houses on brownfield land (or indeed possibly give rise to intertemporal/ witholding effects on all land supply).

There may be better approaches which could be adopted by local authorities to raise revenue for affordable housing (e.g. planning gain or compulsory purchase orders) or by central government (e.g. Greenfield taxes).

Sale of the dwelling imposes asymmetric risks on the local authority vis a vis the occupier, the sale takes the dwelling out of the social housing stock and occupiers of such dwellings may have reduced labour mobility due to the opportunity to benefit from 'supernormal' profit.

Finally, it is important to note the cost of the scheme for local authorities, as highlighted by several recent high profile cases, and the cost to the local authority, in return for the limited numbers of units of affordable accommodation likely to be delivered. Consideration should be given to the idea that ownership of such affordable units be transferred to local authorities for a lower fee. However, this could have negative consequences on the economic efficiency of developing brownfield land where the existing use value may already be significant.

The Council believes that if the current mechanism under Part V transpires to be the preferred option for delivering affordable owner occupied housing, its implementation should be strengthened. The Council notes the recently published Planning and Development (Amendment) Bill, 2002 amending Section 96 of the Planning and Development Act, 2000. This Bill extends a large number of planning permissions granted prior to the introduction of Part V which were due to expire, and provides for the possibility for the required affordable housing, or associated lands, to be provided by the developer in conjunction with a development at another location or by payment of an equivalent monetary value to the relevant local authority and in addition provides for a levy of 0.5 to 1 per cent of the value of a dwelling constructed in lieu of the social and affordable housing provision relinquished through the non-application of Part V.

It is too early to say what the likely effect of the Amendment Bill will be, just as there is little evidence on the like success or failure of the provisions in the original Act. The restoration of permissions about to expire in the Amendment Bill may help secure future overall housing supply although it does not in itself guarantee this. It is clear that policy is not only seeking to ensure overall housing demands are met, but is also aiming to achieve both an increased quantity of social and affordable housing and increased integration of such housing into the overall housing stock. The various measures in the Amendment Bill may give scope for an increase in the quantity of social and affordable housing compared to what might have been achieved under the initial Act. At the same time, it is possible that the provisions in the Amendment Bill may reduce the degree of social integration in new housing developments. It will be important to monitor on-going developments. While it is not sensible to achieve integration at any cost, the Council believes that the continued integration of social and affordable housing in the spirit of the 2000 Act should remain the norm. Meanwhile, increased emphasis should be placed on the provision of social housing by other means and of other tenures.

In 2002 the Council noted that "It is now widely accepted that housing shortages are one of the main constraints on Ireland's continued economic growth and competitiveness, as well as a threat to social cohesion and quality of life" (NESC, 2002b: 142). Given the importance of housing and land in shaping national competitiveness, social cohesion and quality of life, and the possible inadequacy of existing policy, the Council proposes to undertake a thorough review of land and housing policy after the completion of this *Strategy* report.

9.4 THE EUROPEAN DIMENSION

The infrastructures and services discussed in this chapter are considerably shaped by European Union treaties and regulatory regimes. Consequently, this section briefly outlines the nature of the European dimension in these areas.

The Treaty of Rome (EC) of 1958 identified the creation of a common market as a primary goal of the European Economic Community. It defined a common market as an area in which there is free movement of goods, persons, services and capital. In reality, however, the treaty dealt with goods and services very differently: setting detailed liberalisation obligations for products but very little for services. Partly because of this, the history of the EC differs sharply between the two: whereas the common market in goods was achieved by mid-1968, little or nothing was accomplished in services until the mid 1980s and progress is ongoing (Pelkmans, 1997). Some reasons for this difference are identified below.

The different treatment of products and services in the Treaty of Rome (EC) took the following form. To create a common market in services it would be necessary to facilitate the sale of services across frontiers and the right of service providers to establish branch offices in other member states. While the treaty chapters providing for free movement of services seemed to be generally applicable, in reality, the most important services where excluded from it. Transport services were dealt with in a separate section of the Treaty, designed to create the Common Transport Policy. Financial service liberalisation was conditional upon "the progressive liberalisation of movement of capital" (Article 61.2). Major services, such as telecoms and postal services, were effectively removed from the services chapter because of certain provisions within the competition title of the treaty. While the core articles on competition prohibited restrictive practices and abuse of dominant position (the famous articles 85 and 86 of the Treaty of Rome) important exemptions were also identified. In particular, Article 90 stated that companies operating "services of general economic interest or having the character of a revenue producing monopoly" could be exempt from the rules of competition. This was widely interpreted as exempting national telecommunication, postal, transport, gas, electricity and water services from both the competition and common market regimes. It is from these provisions that the term 'services of general economic interest' (SGI) derives.

This situation meant that the creation of the European Community had minimal impact on the public sector in each of the member states. In like manner, the original treaty formulation had minimal impact of the welfare state in each of the countries joining the Community. While there was a high level agreement on the creation of a genuine common market, there was an implicit political consensus that both the public sector and the welfare state remained the preserve of the member states and that three elements of the common market—free movement of persons, services and capital—would only be achieved after extensive further negotiation (Laffan *et al.*, 2000).

There are a number of reasons why the Treaty of Rome treated products and services so differently. First, in the late 1950s internationally tradable services formed a small share of total service activity. Second, services are generally recognised to contain numerous “market failures”, such that a pure market regime would yield undesirable outcomes. Among the market failures in services are asymmetric information between buyer and seller, economies of scale in network sectors such as energy, telecommunications and railways, and the tendency towards considerable market power, as evident in banking and some other financial services. Consequently, everywhere services tend to be subject to more regulation than product markets. In Europe, this often took the form of state ownership of major utilities, such as energy, telecommunications, transport and postal services. The highly regulated aspect of services helps explain why they were treated differently in the Treaty of Rome and why movement to a common European market was much slower. The creation of a common market would require member states to harmonise the complex regulatory regimes governing the different services. By contrast, the common market in many products could be created by removal of obstacles, such as tariffs. Indeed, where the creation of a common market in goods also required harmonisation—concerning, for example, safety of machinery or food products—progress in creating a common market was also slow. There is a further reason why the treatment of services has been different. Many services have complex technical sector-specific characteristics which means that they cannot easily be harmonised or liberalised by general treaty provisions, regulations or court decisions.

The exemption of most services from the common market dynamic meant that, for several decades, Europe did not have to confront the difficult issue of how or where the boundary between the private business and the general economic interest should be. Or, put another way, Europe did not have to define the boundary between the economic and the social. Most public utilities remained in state ownership and the member states asked them to meet public service and universal obligations, in return for state financial support for both operating costs and capital investment.

This situation was altered significantly by the European internal market programme, launched in the mid 1980s. There was a growing recognition that the common market in industrial goods remained incomplete and the common market in services, capital and labour was scarcely begun. The internal market programme consisted of 300 legislative measures to deepen the internal market in goods, establish an internal market in services, make real the free movement of workers, and enforce Community principles in public procurement, state aids and competition. Three principles underpinned the internal market programme:

- Mutual recognition where possible;
- Minimum harmonisation where necessary; and
- Qualified majority voting on internal market matters;

In applying these principles to network sectors, account had to be taken of the many sector-specific complexities noted above. This required that the Community formulate a sectoral policy in each of these areas, expressed in a range of directives and regulations. One element common to many service and network sectors was the transfer of regulatory authority to new independent regulatory bodies. Hence the establishment of many such bodies in Ireland in the past decade (O'Donnell, 2000).

The implementation of the internal market programme, particularly its extension to public utilities and network sectors, reopened the question of "services of general economic interest". What constitutes a valid service of general economic interest? What public service obligations should public utilities have? What degree and form of state subsidy should be allowed to meet these general economic interest and universal service obligations? How could the guarantee of SGIs within each member state be made consistent with intra-Community trade and non-discrimination? Consequently, the issue of SGIs has become the subject of much discussion at European level, including in the Convention and Future of Europe (Héretier, 2002). Indeed, the move to create a European internal market in services has also prompted a debate on how social services—such as hospital, dental and optical services—are to be provided (Leibfried and Pierson, 2000).

In recent years, the EU and its member states have been working to identify the best way to balance the provision of SGIs with the creation of a genuine internal market. This involves clarification of the social and economic goals of Europe and the member states and exploration of the meaning of the Treaties. The relevant treaty articles are listed in Box 9.2.

BOX 9.2

Treaty Provisions on Services of General Economic Interest

PART ONE: PRINCIPLES

Article 16 (ex Article 7d)

Without prejudice to Articles 73, 86 and 87, and given the place occupied by services of general economic interest in the shared values of the Union as well as their role in promoting social and territorial cohesion, the Community and the Member States, each within their respective powers and within the scope of application of this Treaty, shall take care that such services operate on the basis of principles and conditions which enable them to fulfil their missions.

TITLE V: TRANSPORT

Article 73 (ex Article 77)

Aids shall be compatible with this Treaty if they meet the needs of coordination of transport or if they represent reimbursement for the discharge of certain obligations inherent in the concept of a public service.

TITLE VI (ex Title V): COMMON RULES ON COMPETITION, TAXATION AND APPROXIMATION OF LAWS

Chapter 1: Rules on Competition

Section 1: Rules Applying to Undertakings

Article 86 (ex Article 90)

1. In the case of public undertakings to which Member States grant special or exclusive rights, Member States shall neither

enact nor maintain in force any measure contrary to the rules contained in this Treaty, in particular to those rules provided for in Article 12 and Articles 81 to 89.

2. Undertakings entrusted with the operation of services of general economic interest or having the character of a revenue-producing monopoly shall be subject to the rules contained in this Treaty, in particular to the rules on competition, insofar as the application of such rules does not obstruct the performance, in law or in fact, of the particular tasks assigned to them. The development of trade must not be affected to such an extent as would be contrary to the interests of the Community.

3. The Commission shall ensure the application of the provisions of this Article and shall, where necessary address appropriate directives or decisions to Member States.

Section 2: Aids granted by States

Article 87

2. The following shall be compatible with the common market:

(a) aid having a social character, granted to individual consumers, provided that such aid is granted without discrimination related to the origin of the products concerned;

3. The following may be considered to be compatible with the common market:

(a) aid to promote the economic development of areas where the standard of living is abnormally low or where there is serious underemployment;

(b) aid to promote the execution of an important project of common European interest or to remedy a serious disturbance in the economy of a Member State;

(c) aid to facilitate the development of certain economic activities or of certain economic areas, where such aid does not adversely affect trading conditions to an extent contrary to the common interest;

(d) aid to promote culture and heritage conservation where such aid does not affect trading conditions and competition in the Community to an extent that is contrary to the common interest;

(e) such other categories of aid as may be specified by decision of the Council acting by a qualified majority on a proposal from the Commission.

The Commission has led the way in seeking to clarify these issues in two formal communications on SGIs, one in 1996 and another in 2000, and a Report to the European Council at Laeken in 2001. Not surprisingly, the scope of SGIs and the nature of state aid given to support them, has also been shaped by decisions of the ECJ[3].

In its 1996 Communication, the Commission stated that 'Europeans have come to expect high quality services at affordable prices. Many of them even view general interest services as social rights that make an important contribution to economic and social cohesion'[4]. It stated that universal service is characterised by 'the obligation to provide a certain service throughout the territory at affordable tariff and on similar quality conditions irrespective of the profitability of individual operations'[5]. The Commission has observed that public funding of infrastructure should not be considered as state aid, provided that the infrastructure is open to all firms in the relevant area without discrimination. The Commission recognises the difficulty of balancing services of general economic interest with the desire to achieve both competition and a single European market in such services. As noted above, the task of

3. An important decision on the protection of services of general economic interest materialised in the Corbeau case, where the European Court of Justice ruled that services could be opened to competition only if they did not compromise the 'economic equilibrium of the service of general economic interest performed by the holder of the exclusive right' (Case C-320/01 *Procureur du Roi v. Paul Corbeau*, 1993, ECR I-2533).

4. 'Services of General Interest in Europe', 96/C/281/03, OJ 281, 26 September 1996: cited in Bergman *et al*. (1998).

5. COM (2000), 580 final, "Services of General Interest in Europe.

upholding public and universal service obligations is often complex and sector-specific. This task is even more complex where we seek to facilitate competition and trade across the member states.

In its report to the Laeken European Council in 2001, the Commission re-iterated the importance of SGIs in maintaining the European model of society and the competitiveness of European industry. In order to increase the legal certainty and transparency surrounding application of the rules concerning SGIs, the Commission proposed a number of actions. These included:

- Undertaking regular assessment of such services through the Cardiff process;
- Inclusion of a section on SGIs in the annual Competition Report;
- Implementation of a two phased approach, consisting of: consultations with member states to produce a framework for state aid granted to SGIs and, depending on the experience in applying this framework, adoption of a block exemption regulation covering services of general economic interest;
- Sectoral and horizontal monitoring of services of general interest;
- Qualitative assessment of the importance citizens attach to such services and their view of the liberalisation process;
- Assessment of the appropriateness of a horizontal Directive;
- Exploring the scope for introduction of a new subparagraph into Article 3 of the Treaty at the next IGC; and
- Steps by member states to guarantee the financial stability of services of general interest.

Given the importance of SGIs to both economic and social life in Ireland and the rest of the EU, the Council views these as significant steps. In the meantime, Irish policy for networked sectors, public utilities and infrastructure must be formulated within the current state of EU policy and law.

9.5 ENERGY

9.5.1 Recent Developments and Current Issues

The provision of energy through networked industries such as electricity and gas has undergone fundamental transformation in recent times with the establishment of the Commission for Electricity Regulation in 1999. It has subsequently taken on responsibility for gas and became the Commission for Energy Regulation in April 2002. As noted above, much of this process has been driven by the European internal market programme and legislation. However, the fact that Ireland opened its energy market faster than prescribed under EU directives underlines Ireland's belief in the benefits this regulatory approach can deliver.

Both electricity and gas supply are subject to substantial economies of scale. These industries contain elements that are naturally monopolistic and elements that can, in certain circumstances, be opened to competition. Economies of scale derive from the high fixed cost regardless of throughput. This means that normal pricing methods, based upon the cost of providing additional units of output, will not cover average costs. There is, therefore, a conflict in the provision of these important services between the need for affordable access on the one hand, and their provision at a price that covers costs. The general issue of payment and cost recovery for infrastructure is discussed further below.

A major programme of infrastructural investment is currently being undertaken in both electricity and gas networks. This investment will see gas brought to much of the country for the first time. It involves the construction of the gas ring main from Dublin to Galway and Limerick and the announcement of further pipelines from Gormanstown, to connect with the Northern Ireland gas system and further potential developments in the North West. Meanwhile, security of gas supply will be further assured with the construction of a second interconnector with Scotland and the potential to bring ashore indigenous gas supplies from Corrib off Co. Mayo and Seven Heads off Co. Cork.

The programme in electricity will see the construction of lines to relieve congestion on the east coast, in the Greater Dublin Area in particular, as well as improvements in power delivery to the North-West and reinforcement of the level of interconnection with Northern Ireland. These developments should help to overcome some of the deficiency in transmission infrastructure and possible constraints on industrial location. The Council recognises that one of the greatest impediments to the delivery of the necessary transmission infrastructure has been the need for planning permission and associated requirements, and that the streamlining of the process for major infrastructural projects of national importance, and the criteria by which they are assessed, must be re-visited. The Council returns to the issue of planning for infrastructure below.

The year 2002 marked the introduction of a new era in electricity supply in Ireland, with the first connection to Great Britain, albeit indirectly through the Moyle interconnector between Scotland and Northern Ireland. This opens much greater supply opportunities in an industry where, as noted above, economies of scale are of great importance. Studies are being undertaken to look at integration of the market in the Republic of Ireland with Northern Ireland and at the possibility of connecting Ireland's system to that of Wales. The Council encourages the exploration of these possibilities and welcomes the fact that European funding has been made available under the Trans European Networks (TENs) programme to take account of Ireland's peripheral position in the Single European Electricity Market.

In addition to these investments at the macro level, there is a €1.5bn programme of work underway on the electricity distribution network. This includes the ongoing programme of rural network renewal and the conversion from 10kV to 20kV. A significant incentive mechanism has been introduced by the regulator to reduce the number of Customer Minutes Lost through interruptions to supply. This is planned to deliver a targeted reduction of almost 40 per cent from (2000 levels) by 2005 and a focus on the quality of supply for the customers most prone to interruption.

Transparency has also been improved with the requirement under the

Electricity Regulation Act, 1999, for EirGrid[6] to publish an annual seven year forecast statement. Under statute, the new independent Transmission System Operator (TSO), EirGrid, must also take into account national and regional governmental objectives when submitting its 5 year Development Plan for approval.

The Government is fully committed to liberalising the electricity market. As was noted above, the initial market opening target set down in the EU Electricity Directive has been surpassed by Ireland. Since February 2002, approximately 40 per cent of the market, or some 1,600 customers, is open to competition under the regulatory oversight of the CER. Both the markets for "green" energy and for combined heat and power (CHP) have already been fully liberalised since February 2000 and April 2001 respectively. Many of those customers eligible to switch supplier have done so, and approximately 16,000 customers have switched to green suppliers. There has also been significant international trading. The Government has recently decided to lower the threshold of "eligibility" in the electricity market to 0.1 GWh per annum, thereby increasing the level of electricity market opening to 56 per cent, with effect from 19 February 2004. This will mean that approximately 12,000 additional industrial and commercial customers become eligible to source their electricity from independent licensed suppliers. This represents a seven-fold increase in the target customer base for independent players in the market. However it falls someway short of market opening for all non-residential customers. In arriving at its decision, the Government had to be mindful of the substantial once-off system costs which would have been involved in supporting a greater level of interim market opening and the need to focus resources on achieving full market opening by 19 February 2005 to which the Government is committed

The liberalisation process in the energy market has, however, not been without its difficulties and its critics. Electricity prices have

6. It is NESC's understanding that the requirement for EirGrid to produce system forecasts is in accordance with SI No. 445 (2000). However, the TSO licence developed under the same Statutory Instrument is still in abeyance pending formal completion of the Infrastructure Agreement and transfer scheme which will allow EirGrid to become fully operational.

increased substantially, in many cases in excess of 20 per cent. Competition has been limited to a few large players and it is not clear whether this oligopolistic structure has yet delivered many benefits to consumers. Meanwhile, some 99 per cent of consumers are currently unable to choose electricity supplier except to choose to be supplied by currently more costly, but more environmentally friendly, forms of energy generated from renewable or alternative sources, or from combined heat and power (CHP). In addition, the independent TSO established under statute in 2000 has yet to take on its statutory responsibilities and has only recently emerged from lengthy legal proceedings with the regulator.

The increase in electricity tariffs has come at a time of inflationary pressure and follows only two increases in the previous 15 years. However, the tariffs as previously structured were unsustainable. Indeed, the pressure to rein in cost increases, and to finance any necessary investment off balance sheet while prices remained static in the past, has given rise to much of the infrastructural deficit inherited at the time of market opening and subsequent increase in prices.

The regulator must ensure that the incumbent firm earns only what may be described as a ‘reasonable rate of return’ on investments, that it must not seek to abuse its dominant market position, and that its capital and operating costs be benchmarked over time and space to ensure that they fall in line with prudent and efficient utility practice. The regulator must also ensure that fair and transparent open access is granted to the regulated network infrastructure.

In addition to an evaluation of the necessary network infrastructure, the regulator is one of a number of entities charged to have regard to the need to promote the continuity, security and quality of electricity supply. Given that electricity cannot be effectively stored, with the limited means of pumped storage at Turlough Hill providing the only such facility in Ireland, it is necessary to be able to maintain supply and demand balance at all times, including the incidence of peak demand which may imply electricity generating plant running for only a few hours per year or not at all. Given the obvious costs of operating such plant, and the absence of comprehensive mechanisms for real-time pricing for consumers reflecting the costliness of their decision to consume, it is difficult to see how it can be left to the market to provide the necessary plant margin. The regulator has endeavoured to overcome this difficulty through the introduction of payments for unused capacity on the system to cover reasonable fixed costs and the creation of the appropriate market conditions to encourage investment.

However, it is noticeable that there are no firm proposals for new large scale generation in times of rising demand. Given the long lead times and difficulty of acquiring planning permission, this puts Ireland's economic and social development at risk. The recently published Generation Adequacy report by the Transmission System Operator identifies potential generation shortfall by 2005. The Council recognises that initiatives are currently being undertaken by the CER, but urges all relevant agencies to move quickly to ensure that Ireland's electricity demands are met.

The Council welcomes the process recently commenced by the CER to give further consideration to the issue of security of supply in the context of an overall market review for electricity trading and the announcement in December 2002 that it was to proceed with the procurement of a new power station which would have the certainty of a long term contract with the ESB in its role as Public Electricity Supplier. While this approach differs from the market driven investment which was envisaged at the time of market liberalisation, and further reinforces ESB's share in the supply market, the Council believes that the approach is both measured and proportionate, and is likely to protect the consumer from the asymmetric costs of supply shortages at minimum cost given the process of competitive tendering. The Council notes that even with these measures the CER anticipates the possibility of an "interim" deficit prior to the commissioning of the new plant, and which it intends to deal with under a separate project.

Given the importance of such infrastructure for Ireland's development, the Council does not believe its provision can be left entirely to the market. Therefore, the Council welcomes the provision in the Gas (Regulation) Act for the CER to "secure that there is sufficient capacity in the natural gas system to enable reasonable expectations of demand to be met" and "to secure the continuity, security and quality of supplies of natural gas" (S.8 (g) and (h).) In this vein the Council also welcomes the means to fulfil this obligation as provided for in the Gas (Interim) (Regulation) Act, 2002 whereby the CER at its own behest, or at the request of the Minister, may conduct a competitive process for construction of a pipeline. Indeed, there may be wider institutional implications for ensuring infrastructure delivery in key sectors, which are discussed below.

9.5.2 Locational Charging and Energy

It is a fair and reasonable first principle that people should pay the costs which they impose upon society, whether that be in terms of congestion, loss of environmental amenity or the incremental cost of providing infrastructure. However, access to high quality and affordable basic services, where appropriate on a universal basis, is also a key objective not only of social policy but also in supporting spatial balance. In that sense, the Council supports the provision of Public Service or Universal Service Obligations upon all producers of essential services. There are, of course, differences between the supply of electricity and postal charges, which are subject to universality, and the supply of piped gas by Bord Gáis Éireann, which is subject to a purely commercial mandate given the more ready availability of substitutes. Despite the need to support these objectives, the Council supports the introduction of locational charging for those actors whose locational decisions may be affected by exposure to appropriate prices.

In the case of electricity generators, it could therefore be argued that the move from the charging of all connection assets, which was cost reflective, to purely local ones, only partially cost reflective, is retrograde in nature, but that an on-going locational charging system[7] can contribute to the development of only the necessary level of transmission infrastructure in Ireland, paid for by those who utilise it. This location-based charging for producers, while

7. This system is nodal in nature and premised on the reverse MW mile principle. For further details see www.eirgrid.com

maintaining a uniform postalised charge for consumers, encourages more efficient use of the infrastructure while protecting consumer welfare.

An element of locational pricing combined with uniform charging for final customers is also consistent with the approach adopted by the Government (on the recommendation of the Brattle Group) that gas transmission charges should also be assessed on a locational basis for entry to the system, thus ensuring shippers contributed towards the cost of the off-shore assets they were employing but on a postalised, or non-locational, basis for final customers.

It is worth emphasising that in both these cases it is the producer of the product that faces the locational element of the charge. Indeed, it is the producer who has the greatest influence on the need to construct additional infrastructure, while the charge for individual consumers is levied on a uniform basis. This combines the Council's preference for user-based charges for those whose decisions have major impacts upon costs of infrastructure provision, with policies that protect universal access at an affordable level for the consumer.

While universal service, where applicable, is often combined with uniform charging for the delivery of such services to customers, this does not prevent some form of discrimination between customer classes, as indeed is already the case for electricity connections which are levied on a cost reflective basis. Nor does it prevent variations in on-going charges, as is the case of the differential between the urban and rural domestic standing charge for electricity customers.

9.5.3 Sustainable Energy

In recent times there has been an increased focus on the supply of energy from sustainable sources. It is Government policy as set out in the Green Paper on Sustainable Energy to put in place measures to help deliver 500 Megawatts (MWs) of additional renewable energy based electricity generating plant by 2005 and to meet the EU target to generate 13 per cent of energy from renewable sources by 2010 (Department of Public Enterprise, 1999; European Commission, 2001). It is clear that there is potential to dovetail these targets with some new approaches to waste management infrastructure detailed below, given the possibility of producing alternative forms of energy through incineration or from landfill gas.

The government has included concessions to sustainable and energy efficient forms of energy in the opening up of the electricity market, facilitating supply to all customers from renewable or alternative forms of energy and CHP in addition to providing direct support to the production of energy from alternative sources through the administration of the Alternative Energy Requirement (AER) schemes funded by Public Service Obligation (PSO). It is also a duty of the CER to promote energy from renewable or alternative sources and there are a number of concessions to such producers in the trading and grid access regimes established by the regulator. However, technological progress is continuing to make renewable sources of energy ever more cost competitive in their own right.

By 2001, approximately 379 MWs of capacity had been connected producing 4 per cent of Ireland's energy supply (TSO, 2002). A further 362 MWs approximately has been offered power purchasing agreements under the AERV competition administered by Government in 2001. Several large off-shore wind farms totalling in excess of 1,000 MWs, have obtained foreshore leases from the Department of Communications, Marine and Natural Resources or are at various stages in the process. The Government has recently announced the forthcoming AER VI competition, and the Council supports an appropriate level of ongoing direct support for the promotion of renewable energy.

Sustainable Energy Ireland (SEI) has been created out of the Irish Energy Centre under the Sustainable Energy Act, 2002. SEI is charged with implementing the Sustainable Energy Priority Measure of the Economic and Social Infrastructure Programme (ESIOP) which has a budget of €223 million from 2000-2006. SEI has a remit to promote alternative energy sources and to develop and implement an intensified energy efficiency programme. The work of SEI will include a programme of Research, Development and Demonstration. A further priority for the main players in the sustainable energy sector, including SEI, EirGrid and CER, will be to aid the implementation of network upgrading in areas most suitable to the connection of renewable generating capacity.

To date, a substantial focus on the delivery of renewable energy, and its contribution to climate change, has focused on energy derived from wind power, of which Ireland has a natural abundance. However, it is recognised that the delivery of wind-power brings with it other problems in the form of reduced power quality, enhanced plant margin and the costs of ever-ready operating reserve. In this regard, the Council welcomes the recently published work carried out by the regulator in conjunction with his counterpart in Northern Ireland, and the TSOs north and south of the border, which conducted a thorough assessment of the likely ability of Ireland's electricity infrastructure to absorb large levels of increased wind power. It is clear that the development of sustainable energy is not simply an issue of infrastructure provision but includes overall environmental sustainability and climate change policy.

9.6 COMMUNICATIONS INFRASTRUCTURE

9.6.1 Recent Development and Current Issues in Telecommunications

Given the role of information technology in Ireland's economy, communications infrastructure is a most important requirement for future prosperity. Indeed, business opportunities based on the knowledge economy—for example, software development, web hosting, digital media content development, call centres, data processing and storage, on-line working opportunities and design functions—are playing an increasingly important role in the Irish economy. A modern high-speed, low cost communications and broadband network is an essential enabler of economic activity and social inclusion in this sector and in a range of other arenas. In addition, access to telecommunications is an essential dimension of social development and social inclusion in the modern world.

In considering a sector such as telecommunications there are a hierarchy of requirements and decisions. These include the following:

- Ireland's connections with the wider world (often called 'external connectivity');
- The core connections within Ireland ('internal connectivity');
- Connections within each Irish region ('regional connectivity');
- The regimes governing the price and content of messages on these systems; and
- Technological options at each of these levels (such as the choice between fibre and satellite communication).

To an extent, the policy issues at each of these levels can be separated from one another. But is clear that there are some interactions between them. As noted in Section 9.1, policy in this area must address a range of questions.

Ireland's approach to telecommunications is shaped in a number of ways by the evolution of the European internal market. This involves rules on state aid to industry, procedures for public procurement and, most importantly, a specific set of Directives and regulations governing the telecommunications sector. This is a particular version of the EU approach to the regulation of service sectors, as described in Section 9.4 above.

Ireland has made significant progress in meeting the hierarchy of requirements and decisions listed above. External connectivity is largely in place, and positions Ireland as a low cost bridge between the USA and Europe and to which access is at relatively low cost. Internal high-speed links between the main cities and towns generally follow the road and rail networks radiating from Dublin and are being improved under the National Development Plan. These measures will engage many actors in the sector, including the local and regional authorities and communities.

Within the context of the EU internal market, the telecommunications market in Ireland has been significantly liberalised and re-regulated over the past five years. This has involved privatisation of the major company, Eircom, the encouragement of competition in the fixed line and mobile markets and passing regulation from a government department to an independent regulator, the Commission for Communications Regulation or ComReg (formerly the ODTR).

The degree of market penetration and market developments are well documented in the commentaries produced by ComReg on a quarterly basis. These commentaries show that the level of mobile penetration is now reaching saturation, with nearly 80 per cent of the population in possession of some form of mobile telephony. They also show that while fixed line access is fully open to competition, and there are in excess of 20 companies competing in this marketplace, some 80 per cent of all customers are currently served by the incumbent operator. Despite the level of customer inertia a combination of competitive pressure, regulatory initiatives and technological advances mean that customers have experienced significant reductions in prices in real terms for fixed line services.

Substantial progress has been made in market development and there is pressure to deliver full 'local loop unbundling'. The degree of competition is reaching the point where the regulator can consider weakening the price or revenue cap on Eircom's retail operation. Nevertheless, there are still many issues to be addressed, such as the cost of interconnection access, full mobile number portability and others.

In this report, the Council is most concerned with the development of the infrastructure necessary to support broadband services and with some issues that are common to broadband development and other forms of infrastructure.

9.6.2 Broadband Development

Broadband is a high speed connection which allows communications at speeds higher than can be achieved through standard public telephone networks. It is widely believed that broadband services will be an essential aspect of future telecommunications and all the business and social activities that use information technology. In its action plan on the Information Society, *New Connections* (Department of the Taoiseach, 2002b), the Government sets out the objective for Ireland to be in the top decile of OECD countries for broadband connectivity within three years. This aspiration was modified and further reinforced in the Programme for Government, 2002, to take account of the possible use of fiscal instruments and to ensure adequate rural access. At present Ireland falls far short of these goals.

In developing a national strategy for broadband investment and services there a number of complexities that must be taken into account:

- Communications infrastructure differs from most other types of infrastructure in that while it may have the physical capacity to last many years, the speed of technological advancement may render some communication technologies obsolete much more rapidly than in other sectors. Thus, it seems necessary to recover the cost of investment more quickly and to consider carefully various ways in which infrastructure might be delivered;
- Supply of broadband infrastructure can stimulate demand for broadband services. Consequently, the policy problem can not be adequately thought of as balancing supply and demand. Demand and supply can be in balance at either a high or low level. It is possible to become trapped in a low-demand, high-cost, equilibrium.
- A given level of broadband connectivity can be achieved by a wide variety of technological approaches, a combination of which may be suitable given the state of the existing backbone network and the population density characteristics of Ireland.

Not surprisingly, the resultant public policy will also be a complex mix. Policy must ensure sufficient investment to guarantee that Ireland has a leading role global information economy, determine the respective roles of the public and private sectors, set prices that stimulate widespread use of communications technology but also recoup investment adequately, shape the choice between technological options, determine the nature and extent of public service and universal service obligations, conform with EU internal market rules and operate within public finance constraints. A further complexity is that the outcome is shaped not only by government policy, but also by the action of independent regulators, private enterprises and, on occasion, the European Commission and the ECJ.

Recent Developments and Current Issues in Broadband

As regards investment in the core broadband infrastructure, there is now a very significant amount of fibre optic cable installed in Ireland by a variety of enterprises. Much of this fibre has been laid along multi-utility corridors, in association with ESB, BGE or CIE, as noted by Forfás in its 2002 review of *Broadband Investment in Ireland* (Forfás, 2002). Forfás proposed that greater linkages and interconnection between the telecoms networks of semi-state bodies should be reviewed and actively supported. The Council supports this assessment and discusses multi-utilities below.

The Government has allocated some €200 million to support regional broadband investment in the National Development Plan 2000-2006. This has enabled the Government to co-fund or pump prime a number of projects including the development of fibre networks in conjunction with other operators. As regards investment in regional connectivity, the Government has initiated tenders to build 19 Pathfinder projects consisting of metropolitan fibre and ducting networks which will hook up to the multi-utility corridors, on an open-access basis and cover approximately 13 per cent of the population at an estimated exchequer cost of €60 million. Any further developments in this area will be contingent on the outcome of the Pathfinder projects.

Towards the end of 2002 the Office of the Director for Telecommunications Regulation (ODTR; now ComReg) launched a consultation process which sets out options in *Future Delivery of Broadband in Ireland* (ODTR, 2002). The paper lists a number of the possible technological approaches to meet the objective of a high level of connectivity and the potential costs of achieving a certain level of population penetration at a certain level of bandwidth. In their work for the ODTR, consultants Ovum estimated that the cost of providing 2Mbit/s access to 65 per cent of the population would be in the region of €560 million, rising to €2,000 million if that access were to be extended to 85 per cent of the population (Ovum, 2002). Depending upon the level of take-up for the service, the cost could approach €5,000 per user and more at higher speeds. However, such costings are only preliminary in nature, and other market commentators believe that they may be on the high side.

It is clear that for many internet users, particularly domestic users, a reliable connection at a lower level of bandwidth may be sufficient. However, connectivity is increasingly seen as a key element of business competitiveness and Ireland's ranking is low in this regard. An important means of significantly improving Ireland's ranking is through widespread provision of DSL services using existing copper wires. In marketing broadband services to the domestic users, packages incorporating the combination of a flat rate 'always-on' broadband service, combined with flat rate voice telephony and access to high quality broadcasting packages, will have to be developed. The Council notes the recent draft policy direction by the Minister for Communications, Marine and Natural Resources to ComReg in this regard.

As regards stimulation of demand, the Government document *New Connections* noted that increased eGovernment services have a role to play.

The policy approach underlying these developments can be identified as follows. Government believes that the state's role in the core telecommunications infrastructure, beyond providing the appropriate regulatory environment, 'is confined to provision of seed capital' (p.7). In general, competition is the best way to ensure the diffusion of new technologies. In addition to seed capital, Government may have role in ensuring that local areas have access to the backbone infrastructure. This can involve stimulation from Government support the upgrade of networks and to encourage the delivery of services to end users.

The Council broadly supports this policy approach. However, it believes that government bears ultimate responsibility for ensuring that Ireland has sufficient broadband services to be at the leading edge of both economic and social development in the 21st century. In the first instance, this responsibility consists of monitoring whether the action of a range of public and private players are leading Ireland in that direction. These actions include the government's own its involvement in programmes of focused investment to leverage private sector investment in the deployment of advanced broadband technologies and services in the regions. If existing steps are not sufficient, the behaviour of the various actors may have to be tweaked to ensure more coherent outcomes. In the final instance, government will be considered, by both citizens and enterprises, to bear ultimate responsibility for ensuring that our telecommunications facilitate economic and social development.

9.7 WASTE MANAGEMENT

The Council has chosen to include a number of indicators reflecting its commitment to environmental sustainability in its recent report on *National Progress Indicators* (NESC, 2002a). These include the level of household and commercial waste expressed on a tonnage per capita basis and the disposal and recovery of household and commercial waste as expressed through the comparative composition of disposal methods.

The European Community has adopted a waste hierarchy, stemming from reduction in waste at its pinnacle, to disposal through landfill at the base and encompassing reuse, recycle and heat recovery, or incineration as the intervening strata.

The Environmental Protection Agency (EPA) estimates that almost 600kg of waste is generated by each person in the State every year and landfill remains the primary form of disposal, accounting for 87.8 per cent of the household and commercial waste stream in 2000 (EPA, 2002). With only 12 per cent recycled, this remains a considerable distance from the Government's stated target of a

35 per cent recycling rate. The recent 15c levy on plastic bags, introduced in 2002 following the Waste Management (Amendment) Act, 2001, will reduce considerably the 1.26 billion plastic bags consumed in Ireland each year, with a corresponding improvement in landfill requirements and associated litter problems. The Act also led to the introduction of a levy on landfill at an initial rate of not more than €19 per tonne. However, the EPA believes that there is still considerable scope for further application of the "polluter pays principle" in tackling waste management.

Ireland's waste management programme is partly governed through the EU Directive on Packaging and Packaging Waste (94/62/EC), adopted in December 1994. The measures under the packaging directive were transposed into national legislation with the Waste Management Act, 1996. The packaging directive requires each member state to achieve a certain level of packaging waste recovery. The targets for Ireland are 25 per cent by 2001 and 50 per cent by 2005, with further sub-targets for the recycling of materials.

In 2001, there were a number of scandals in Ireland concerning the illegal dumping of waste, including hospital waste, into landfill. This has reinforced the need for effective monitoring of waste disposal, improved waste management systems and the need for tough penalties for those who operate outside the designated waste management framework. Local authorities have been required to produce waste management plans since the enactment of the Waste Management Act, 1996, a requirement that has been further refined in subsequent legislation. With 2.28 million tonnes of waste placed in landfill in 2000, and an estimated 10.38 million tonnes of landfill capacity available for municipal waste disposal, it is estimated by the EPA that Ireland has only four and a half years landfill capacity remaining on a national basis, with less than four years' capacity in the South East, Mid West and Dublin (EPA, 2002). Meanwhile, local objections have so far forestalled the introduction of Ireland's first incineration facility.

Ultimately, the strongest driver for packaging minimisation is cost, although this must be weighed against the consumer's preference for ever more elaborate and eye-catching packaging. While a concerted waste management strategy must focus not only on downstream incentives but also upstream producer responsibility and prevention, the reality is that much of Ireland's packaging is imported from abroad. Ireland has no sizeable producer of steel can packaging, aluminium cans and, with the recent closure of Irish Glass, no significant glass producer. This makes it the more difficult to create a cost effective recycling industry. Meanwhile, consumer preferences for long life and high-value-added packaging brings with it significant difficulties for recycling markets through the technologies employed. This is combined with an immaturity in the overall demand for recycled products, particularly for composite materials. At the same time, several significant producers within Ireland export much of their material which is exempted from the packaging regulations and may therefore discourage upstream initiatives.

In its recent policy statement on waste, *Delivering Change*, the government has committed itself to a number of actions concerning waste prevention and minimisation (Department of the Environment and Local Government, 2002c). These include the 'seed' funding to facilitate the immediate establishment of a National Waste Prevention Programme (including assistance to industry, research and education) and a Core Prevention Team to prioritise and coordinate this Programme which will contribute significant financial investment and technical assistance to achieve a "win-win" situation for both industry and the environment. The statement also outlines a number of measures in the area of re-use, recycling, the biological treatment of organic waste and the public service waste management programme.

In June 2002, Peter Bacon and Associates carried out a *Strategic Review & Outlook for Waste Management Capacity and the Impact on the Irish Economy* for Celtic Waste (Bacon *et al.*, 2002). They found that the projections of likely waste output included in the local waste strategies were likely to be too low. Therefore, even if the recycling targets were to be met, and thermal capacity developed as proposed, there would remain a critical deficit of capacity to handle the waste that requires disposal. The study also concluded that Ireland's target to recycle some 45 per cent of total waste was ambitious by EU standards and unlikely to be achieved. Given this, it is clear that effective waste management will require not only strategic development but a series of initiatives—whether fiscal incentives, the introduction of cost reflective customer charging or simply increased consumer awareness—to manage disposal in the context of Ireland's existing landfill capacity.

In the European Commission's White Paper *Growth, Competitiveness and Employment,* it was stressed that environmental regulations were not expected to lead to additional cost, but to promote growth through the introduction of green products, green industries and a greater competitiveness induced by technological innovation, investment and the encouragement of the new manufacturing standards, such as lean production, which are considered to be more environmentally friendly (European Commission, 1993).

Claims such as these have been tested in a number of sectoral studies which Ireland benchmarked to European counterparts (Hitchens *et al*., 1997, 1998). They investigated the claims made by Porter and van der Linde (1995) that innovation takes place in response to increasing regulation which may lower costs, and that greater regulation may give rise to a first mover advantage, if similar regulations are adopted by trading partners and international comparators. The work by Hitchens *et al*. found no clear evidence to support the hypothesis that environmental policy had either an adverse or beneficial effect on firm competitiveness. They concluded that evidence to support the hypothesis of "innovation offsets" and "first mover" hypotheses tends to be based on case studies and lacks systematic statistical evidence.

It is clear that not only the economic benefit, but also the environmental responsibility of engaging in extensive re-use and recycling is greatest in areas of high density population and packaging usage. Thus, while industry has generally abandoned the return of bottles by individual consumers, in favour of less material and alternative technologies, such schemes still generally survive in the catering and licensing trade given their higher volumes. In the same vein, "collection" systems for segregated waste are only likely to be viable in high density areas with significant levels of participation, while "bring" systems (whereby consumers return their waste to a specified point for recycling) may only be beneficial if combined with a journey for another purpose. On the other hand there are other areas, such as the introduction of the plastic bag levy, whereby direct reuse by the consumer himself (as opposed to reuse by the upstream producer) can deliver significant environmental improvement.

The issues of sound planning, forward thinking, local opposition and user charges, which are common to other forms of infrastructure, also apply to environmental infrastructure such as waste management and, to some extent, fresh water and sanitation services.

These issues are starting to be tackled through the production of waste strategies at the local authority level, and also at regional and national levels. Under Part II of the 1996 Waste Management Act, local authorities are required to make waste management plans in respect of their functional areas, and the EPA is required to make a national hazardous waste management plan. Progress is being made in getting users to take into account some of the costs that their actions impose through waste disposal charges and moves to levy these on a per kilogram basis. Significant progress has also been made at the local level in terms of segregated waste collection streams.

Further to the 1996 Act, local authorities were encouraged to adopt a regional approach to this planning process, with a view to the more efficient provision of services and infrastructure. The Waste Management (Amendment) Act 2001 provided a legal mechanism to address the refusal of three out of fifteen local authorities (across three regional groups) to adopt the proposed plan, and the conditional or qualified adoption of other regional plans. For regional plans to be valid, they must now be adopted by all of the local authorities involved.

This has resulted in the adoption of 10 separate regional waste management plans, covering the following regional areas:

- Connaught region – covering Galway, Leitrim, Mayo, Roscommon and Sligo County Councils and Galway City Council;
- Cork region – covering Cork Corporation and Cork County Council;
- Dublin region – covering Dublin City Council, Fingal County Council, South Dublin County Council and Dun Laoghaire-Rathdown County Council;
- Midlands region – covering Laois, Longford, Offaly, Tipperary (NR) and Westmeath County Councils;
- Mid-west region – covering Clare, Kerry, Limerick County Councils, and Limerick City Council;
- North-east region – covering Meath, Cavan, Monaghan and Louth County Councils;
- South-east region – covering Carlow, Kilkenny, South Tipperary, Waterford, Wexford County Council and Waterford City Council; and
- Donegal[8], Kildare and Wicklow County Councils, who have adopted stand-alone plans.

In particular, these plans make provision for the development of an integrated waste management infrastructure, including:

- Kerbside collection of recyclable materials in urban areas;
- Bring facilities for recyclable materials in rural areas;
- Biological treatment of ‘green’ and organic household waste;
- Materials recovery facilities;
- Recycling capacity for construction and demolition waste;
- Thermal treatment facilities; and
- Residual landfill requirements.

8. It is fair to note that Donegal has adopted a regional waste management strategy with a number of Local Authorities in Northern Ireland.

On reviewing individual regional plans, the Council notes the provision for joint funding for shared posts in the area of waste management, and the provision of certain facilities on a regional basis, although the latter would appear to be the exception rather than the norm.

The Council has noted above that it is increasingly recognised that through mutually beneficial co-operation, an "added value" can be realised for regions over and above what would happen if individual places go separate ways in their promotion and development" and that this interdependency within regions also extends to the disposal of waste for large settlements, just as these settlements help support the hinterland through job creation an access to social infrastructure.

This requires a concerted planning framework for energy recovery units whether upstream (via incineration) or downstream (through the increased production of electricity from landfill gas). In addition, while targets for recycling and reuse of packaging in Ireland are set out by EU Directive, the Government should give consideration to the feasibility, and desirability of continued pursuit of its more ambitious domestic targets. Given immature markets for products manufactured from recycled material, particularly the limited markets for recycled materials, (especially from composite materials) and changing circumstances, such as the closure of indigenous capacity processing recyclable material, such as Irish Glass, these targets may not be the most appropriate ones.

The Council believes that the effective management of the waste problem is one of the highest priorities in Ireland for the next three years and every aspect of the waste hierarchy must be addressed to tackle it. The effective management of waste will need to incorporate both regulatory and spatial institutions. At present, the problem seems to be passed from one agent to another:

- Overly optimistic recycling targets may mask the need for a more concerted incineration and landfill policy;
- Increased producer responsibility is limited by the fact that much of the resulting waste stream is imported from abroad; and

- There is a tension between an enhanced civic culture, in which citizens would take more responsibility, and an incentive to free-ride.

The drive to tackle waste management ought to encompass all of civil society and incorporate not only waste management companies and local authorities but also enhanced producer and consumer responsibility. It will have to be premised upon a set of institutions with sufficient power of delivery to ensure a satisfactory outcome. In this context, the Council welcomes the Government's intention is to establish a National Waste Management Board and urges immediate action on this.

9.8 TRANSPORT

The problem of serious traffic congestion and deficiencies in transport infrastructure and services has become of growing concern in recent years. To some extent, these problems are a result of the dramatic growth in the economy; vehicle numbers, for example, are almost perfectly correlated with the growth of GDP (Clinch *et al.*, 2002). However, the problems are also the result of under investment in earlier periods as well as policy and institutional weaknesses. This section outlines the current position on transport and congestion, and the policies that are being implemented.

A recent IBEC survey has illustrated the extent to which traffic congestion is now a very significant issue. The survey covered 580 companies across the country, 50 per cent of which were located in Dublin. The survey found that for 85 per cent of companies (91 per cent in Dublin) traffic congestion was having an adverse affect on their business. While congestion is an issue for business nationally, the effects are most severe in Dublin. This is most notable in relation to the impact on staffing, which is closely associated with the quality of life dimension of traffic congestion. The survey found that for 94 per cent of companies in Dublin, traffic congestion had an effect on staff punctuality. Traffic congestion also had a particularly adverse impact on Dublin companies in relation to labour costs, (83 per cent), recruitment (72 per cent), staff turnover (69 per cent) and absenteeism (62 per cent).

The survey also asked companies about their favoured strategies to address traffic congestion. The most favoured response to traffic congestion was the introduction of more flexible work arrangements (77 per cent). Other options proposed by companies were encouraging public transport (40 per cent) and contracting-out distribution (40 per cent). In Dublin, a substantial proportion (38 per cent) favoured relocation as a response to congestion (20 per cent for the rest of the country).

There are many costs associated with traffic congestion. It is a major source of air pollution. The emissions from traffic in congested conditions can be up to 250 per cent higher than from free flowing traffic. Traffic is a major source of growth in greenhouse gas emissions and also a source of local air and noise pollution, with associated health problems. The number of accidents is influenced by traffic levels and the efficiency of fuel consumption is reduced by traffic congestion. The delays caused by traffic congestion also have significant time costs (Clinch *et al*., 2002). Overall, the problems of traffic congestion are a significant influence on the quality of life.

A report by Goodbody Economic Consultants (2000) for the NSS has predicted that the number of cars in the country will grow to 2.1 million by 2016, compared to the level of just over 1.3 million in the year 2000. This is based on continuing growth in the adult population, along with movement towards the assumed saturation level of car ownership of 80 to 90 cars per 100 adults, although some believe this projected level of saturation to be particularly high. In 1999, the number of cars per 1000 population (total population) in Ireland was 346, considerably below the EU average of 460 passenger cars per 1,000 population. Continuing growth in car numbers points to continuing pressure on transport infrastructure.

However, the implications of rising car numbers are very much influenced by the *use* of cars as well as levels of ownership. Transport policy needs to take account of the growth in car numbers, but the focus of policy should be on catering for transport needs in a way that is socially and environmentally sustainable, including demand management measures and more efficient use of existing infrastructure, rather than a simple expansion of infrastructure in line with numbers of cars and other vehicles. In this way, access to personal car transport can be combined with more responsible usage, as is the case in many other European countries.

9.8.1 Investment in Transport

An ambitious programme of investment in transport infrastructure is set out in the National Development Plan (NDP) for the period 2000 to 2006. The NDP allocates €8.8 billion to transport investment, representing just over 21 per cent of total NDP investment and 39 per cent of infrastructure spending. Investment in the upgrading of national roads is the largest planned element of infrastructure investment, accounting for 68 per cent of NDP transport investment (€5.9 billion). Public transport in the Greater Dublin Area accounts for 23 per cent of transport investment (€2 billion), while the remaining 9 per cent of transport expenditure is for regional public transport (€825 million).

The NDP investment in roads is based on a policy of providing a high quality service on the national primary network. The investment aims to achieve a minimum level of service on the five inter-urban routes that will enable an average inter-urban speed of 94 kilometres per hour on a dual carriageway (and 105 kilometres per hour on a motorway) to be achieved from completion of construction through to 2020. In relation to the rest of the national primary network, it is estimated that the investment planned will result in a minimum level of service to enable an average inter-urban speed of 80 kilometres per hour on 90 per cent of the routes involved. The NDP also provides for substantial investment in selected national secondary roads. The Council recommends that the implementation of the road building programme should strongly reflect the priorities identified in the National Development Plan and in particular the proposals for strategic linking and strategic radial routes proposed in the NSS.

There is a strong focus in the NDP on investment in public transport in the Greater Dublin Area (GDA)[9]. The investment is designed to address projected growth in traffic through a combination of investment in infrastructure and demand management measures to reduce the relative attraction of commuting by car, thereby reducing traffic congestion. Investment and other measures to address traffic congestion in the GDA are discussed further below.

Investment in mainline rail is by far the largest element of the regional public transport strategy and incorporates both a rail safety programme and rail renewal and upgrading. The level of investment has increased substantially since the publication of the NDP and now stands at over €1.05 billion on rail safety and €396 million for upgrading. While expenditure is on target with regard to rail safety, only 43 per cent of the money allocated for upgrading in 2000/2001 has been spent (NDP/CSF Evaluation Unit, 2002a). The review established to examine the future of Iarnród Éireann made recommendations on changing governance, rolling stock, fares structure and policies for handling peak traffic. The review recognised that the core business of Iarnród Éireann was passenger transport and that the purpose of most of the Government's investment and expansion in renewal and expansion of rail services was to improve passenger transport. The Council believes that ongoing development of mainline rail can make an important contribution to the delivery of a viable system of public transport on both inter-city and suburban routes. A high-quality rail system can greatly enhance national well-being and is an indispensable factor in an advanced economy and society. Consequently, the Council welcome the decision to undertake a Strategic Rail Review and looks forward to its conclusions.

The NDP also includes investment in public transport in the main cities (€63 million). This focuses on the upgrading of bus services in Limerick, Galway and Waterford, while in Cork the commuter rail service is also being upgraded. The NDP also provides for investment in regional bus services outside the five main cities and the renewal and expansion of the Bus Éireann fleet.

A detailed report on progress on NDP infrastructure projects is

9. The GDA covers Dublin City and County as well as Meath, Kildare and Wicklow.

included in the *Eighth Progress Report of the PPF* (April 2002). Following a commitment in the NDP to develop a new pilot rural transport scheme, the Rural Transport Initiative (RTI), was launched in July 2001 to promote and support the development of innovative, community-based transport projects in rural areas. It is being managed by Area Development Management (ADM). Following a competitive selection process, ADM selected thirty-three community transport groups for funding and eight of these groups are expected shortly to commence transport operations in their areas.

Reports have now been completed evaluating the progress under the National Development Plan for both the public transport and road development programmes. The recently published evaluation of the roads programme by the NDP/CSF Evaluation Unit makes clear that while considerable progress has been made in the delivery of the national roads programme under the NDP, the programme is now estimated to cost substantially more than initially anticipated. (NDP/CSF, 2002b) This is not to make light of the significant achievements that have been made in so short a time under the NDP across all sectors. While it appears that cost control at the individual project level is adequate, a combination of external factors—such as the high cost of land acquisition, inflation in the construction sector, changes in project scope and initial under-estimation of the likely cost of the project delivery—have led to cost over-run. A key component of construction price inflation is the shortage of skilled labour in the construction sector. This is seen as a fundamental constraint on overall construction capacity, recognised in the Government's recent review of the construction industry (Department of Environment and Local Government, 2001).

The report argues that there are a number of improvements in programme management that could be implemented, including increased use of formal appraisal techniques *ex ante*. The report argues that benefit could be derived from looking at road projects from a network perspective, as opposed to individual project perspective, and adaptation of the road development priorities in the context of the NSS. The Council concurs with this point.

The NDP/CSF Evaluation Unit report, carried out by Indecon economic consultants, undertakes a detailed analysis of the various public transportation initiatives that are currently being undertaken. In addition to specific recommendations on individual projects a number of recommendations are made in relation to the project selection and management issues. In particular, it is suggested that a clearer information and reporting system would greatly assist the monitoring of projects. It is also suggested that lessons could be learnt with respect to the planning process that would overcome some of the incrementalism involved in the design of the current plan.

In Section 9.10 which examines improved project delivery, the Council highlights its belief that only through the effective monitoring of projects and initiatives is it possible to achieve further improvements in policy planning, management and implementation. The Council welcomes evaluation exercises of national programmes which can contribute not only to our understanding of current developments but aid us in our planning for future initiatives.

9.8.2 The Dublin Transportation Office (DTO) Strategy

The most severe traffic congestion problems exist in the GDA. In 2001, the Dublin Transportation Office (DTO) published a long-term strategy to address the transport needs of the GDA, *Strategy 2000-2016: A Platform for Change*. The baseline adopted for the DTO strategy was the existing infrastructure and all investment schemes to which there were commitments in 1997. The DTO calls this the ‘do minimum’ strategy, although it involves substantial investment. The investments in ‘do minimum’ strategy include: the Luas lines from Tallaght to Connolly and from Sandyford to St. Stephen’s Green; the completed M50 motorway; the Dublin Port tunnel, 11 quality bus corridors; the extension of the DART to Malahide and Greystones; the upgrading of the Maynooth line from Clonsilla to Connolly and lengthening of platforms and additional DART and other rail-cars. Estimates of the future transport demand were developed: it was estimated that the number of person trips in the morning peak hour would increase from 250,000 in 1997 to 488,000 in 2016. The implications of these projections were examined using a model, assuming the "do minimum" strategy was pursued. In all of the strategies considered it was assumed that the Strategic Planning Guidelines[10] were implemented. The investment in public transport means there will be a substantial increase in public transport trips in the morning peak period and, in fact, some increase in the public transport share of total trips from 27.8 per cent in 1997 to 35.2 per cent in 2016. However, a major increase of 135,000 in the number of car trips is projected which would lead to severe road congestion. The model estimated that the average speed of the radial routes into the city in the morning peak would fall to 8 kilometres per hour, a little above fast walking pace.

The DTO explored a number of strategies to achieve an improvement on this outcome. The strategy recommended by the DTO involves substantial additional investment in public transport as well as traffic management measures. Following the investment proposed by the DTO, the transport network in the GDA would comprise the following elements:

- an improved DART/Suburban rail network, including improved passenger carrying capacity in the existing network and the development of more tracks on existing alignment, an interconnector (underground) between Heuston Station and East Wall and other new rail lines;
- an extension of the on-street lightrail network (Luas);
- the development of a higher capacity segregated lightrail network (Metro);
- a much expanded bus network, comprising an integrated mesh of radial and orbital services and a substantial increase in passenger carrying capacity;

10. The Strategic Planning Guidelines were prepared for the local and regional authorities in the GDA and the Department of the Environment and Local Government by a consortium of consultants to provide a strategic planning framework for this region's development.

- strategic but limited improvements to the road networks; and
- a package of measures designed to improve the integration and attractiveness of the public transport network, including park and ride facilities, integrated fares and ticketing, quality interchange facilities and improved passenger information.

Some elements of the DTO investment strategy are part of the NDP. However, the DTO strategy has a longer time period and involves substantial additional investment to the NDP. Significant elements of the DTO investment strategy that go beyond the NDP include the Metro system and additional Luas lines. The Government has agreed to the development of a Metro for Dublin. It is assumed this would be substantially funded on a PPP basis.

If the DTO strategy were implemented, the DTO predicts that there would be a very substantial change in the modal share by 2016. It is projected that most of the increased number of trips by 2016 would be by rail so that rail would account for 49 per cent of total trips in the morning peak hour. There would also be an increase in the number of bus trips although the bus travel share declines. The total number of car trips is assumed to stay constant with a substantial decline in its share, falling from 73 per cent in 1997 to 37 per cent in 2016. The strategy is designed to reduce the level of congestion on the road network to its 1991 level. Average journey times would fall dramatically: compared to the alternative of not implementing the strategy, average journey times by bus and rail are projected to be 37 per cent and 53 per cent less than if the strategy were not implemented. The average journey time reduction for cars is projected to be 39 per cent.

Preliminary results of more recent surveying carried out by the DTO in 2001/2002 have recently become available. These show a very substantial increase in the number of morning peak hour journeys made, up almost 70 per cent over 1997 levels to 422,000. The modal split is c. 302,000 or 72 per cent by car, 92,000 or 22 percent by bus and 28,000 or 7 per cent by rail. According to the DTO this is the first time ‘in living memory’ that bus has managed to maintain or increase its share of such journeys.

TABLE 9.2
Mode Split in the Morning Peak Hour (Person Trips)

	1991		1997		2016	
Bus	44,000	26%	47,000	19%	69,000	14%
Rail	18,000	10%	21,000	8%	239,000	49%
Car	110,000	64%	181,000	73%	180,000	37%
Total	172,000	100%	249,000	100%	488,000	100%

Source: DTO, Strategy 2000-2016, A Platform for Change.

The overall number of journeys has increased by an average 7 per cent per annum since 1994 so even modest projections of growth, such as 2 per cent per annum to 2016, would see the previously forecast number of journeys exceeded, with approximately 580,000 morning peak journeys being undertaken. However, if this ‘slack’, of around 100,000 journeys in excess of target were to be taken up by car use, the situation would still be better than it is today. The DTO figures encompass the entire Greater Dublin Area and therefore show some variation within this area. More anecdotal evidence would suggest that for workers in the city centre the proportion travelling by public transport is in the region 60-70 per cent whereas in out of town office or retail parks this number falls to less than 10 per cent.

A cost benefit analysis of the proposed strategy is included in DTO’s report *A Platform for Change*. The costs and benefits are those that are additional to the ‘do minimum’ strategy. Costs and benefits were measured over the 30 year period from 2000 to 2030. The costs of the proposed investment, including both capital and operating costs, are estimated to be €11.3 billion out of a total cost for the implementation of the *Strategy* in excess of €21 billion. The primary benefits are the time savings, but there are also the benefits of a reduction in accidents and lower air and noise pollution. The DTO estimates that the benefits are almost 2.8 times higher than the costs, including both capital and operating costs. The annual rate of return for the strategy is estimated at 14.7 per cent.

The DTO strategy emphasises that investment in infrastructure alone will not be sufficient to address traffic congestion. Investment in infrastructure must be accompanied by measures to manage the growth of traffic so that the infrastructure is used efficiently, including the development of traffic management schemes and the promotion of public transport, including, for example, bus priority measures.

9.8.3 Land Use and Transport

There is significant interaction between land use and transport. The spatial distribution of housing, workplaces, shopping, educational establishments and other services has a major impact on the infrastructure required to provide transport. Below minimum thresholds of population density, it becomes financially difficult to serve the population with public transport.

The spatial dimension of transport in the GDA has been examined by Williams and Shiels (2000). He points out that there has been a major increase in development activity in this region of Ireland over recent years. This region experienced employment growth of 39 per cent between 1994 and 1999, compared to 29 per cent growth for the rest of the State. The GDA accounted for 50 per cent of the growth of population over 15 years of age, 49 per cent of the national increase in the numbers at work, and 46.3 per cent of all new private cars registered over the 1994 to 1999 period. This disproportionate share in economic activity was well in excess of the region's 1996 population share of 38.8 per cent. However, in relation to housing there was a critical under performance and this region accounted for less than 37 per cent of total house completions over the period 1994 to 1999. This imbalance between the location of employment and housing has meant a spilling out of housing development and population growth to the outer Leinster region and the emergence of long distance commuting. Williams and Sheils estimate that the commuting region has expanded from the general area of 15 kilometres in the 1980s up to a current level of 100 kilometres from the core area. While some of this growth involves consolidation of development in large towns, it also has involved much housing growth in small villages lacking infrastructure.

A number of issues therefore arise in relation to the implications of the Strategic Planning Guidelines for transport. First, the transport infrastructure investment being undertaken in the NDP, or the additional investment proposed by the DTO, will be less effective if the guidelines are not implemented. A key purpose of the guidelines is to limit development outside either the metropolitan area or development centres to growth that meets strictly local needs. If ‘local needs’ is interpreted too widely, there could be a continuation of development in small centres and this would make it more difficult to achieve the desired modal shift to public transport.

A second issue is that the Strategic Planning Guidelines did not consider the issue of development outside the GDA. As highlighted by Williams and Sheils, the commuter area for Dublin has extended beyond the area used in both the Strategic Planning Guidelines and the DTO strategy. The Strategic Planning Guidelines are in need of review following the recent publication of the NSS. With the planned major investment in upgrading transport in the GDA, it is desirable to consolidate more of the development within population centres in this region.

A third issue that arises is whether the land use strategy proposed in the Strategic Planning Guidelines is optimal in view of the major public transport investment proposed by the DTO. While the Guidelines envisage some consolidation of development, the strategy implicit in them can still be considered as a fairly dispersed one. As McCarthy (cited in McDonald, 2000) has pointed out, the area covered by Dublin City Council will see a decline in its share of the GDA population under the Guidelines, from 32.9 per cent of the GDA in 2001 to 30.4 per cent in 2011. Of the total increase in population of 159,000, projected for the GDA up to 2011, the guidelines envisage that only 11,000 of this increase will be in the Dublin City area. However, it is this area that will be most intensively served by the proposed new investment. The Guidelines note that there are significant areas of land relatively under-occupied in the inner and middle suburbs of Dublin, due to an ageing population and recommend that measures be taken to increase occupancy in these areas. However, their population projections would seem to envisage only limited success with such measures. The Guidelines project an increase in population in the metropolitan area outside Dublin city of 75,000, while the population in the hinterland area increases by 73,000 by 2011. There is a significant increase in the hinterland share of the GDA population from 22.1 per cent in 2001 to a projected level of 24.3 per cent in 2011.

In recognition of the interaction between land use and an effective transport system, a consultation paper, *New Institutional Arrangements for Land Use and Transport in the Greater Dublin Area*, published by the Government in March 2001, proposed the establishment of a statutory strategic land use and transportation body for the GDA. The functions of this body would include the preparation and regular review of an integrated long-term land use and transportation strategy for the region and the adoption of a medium-term (5-7 years) transportation implementation programme and short-term (2-3 years) action plans. In addition to strategic land use and transport planning, the paper proposes that the new body would be the public transport regulator for the GDA. This would involve the setting of detailed service requirements and standards on all modes of passenger transport on an integrated basis, having regard to Government policy on an appropriate level of public transport provision and on revenue support. As regulator, it would be the body that would procure the provision of transport services principally through tender competitions for franchises and also through public service contracts.

The paper proposes that local authorities will continue to be responsible for roads, traffic and physical planning, but will have to act in a way that is consistent with the overall land use and transportation strategy and subject to the oversight of the strategic body. It will have significant enforcement powers, including the power to issue binding directions and advisory guidelines. The consultation paper proposes that the new strategic body would consist of a council comprising local authority elected representatives and managers, social partners and Government nominees. In addition, there would be a small executive board responsible for the execution of policy, including regulation of the transport market.

The Council considers the pattern of uncoordinated peripheral expansion in the eastern part of the country and elsewhere to be one of the most important issues confronting Irish society. The Council welcomes the proposals for a new strategic body and urges that legislation be quickly introduced to set it in place. However, the Council does not consider that the establishment of this new body will be sufficient to achieve a coherent and desirable pattern of land use settlement and that its remit should extend beyond land use and planning. It suggests that high priority be given to devising institutional arrangements that can make this body effective in both planning and delivering a more sustainable pattern of settlement and land use.

9.9 FUNDING INFRASTRUCTURAL DEVELOPMENT

Given the limits on public borrowing and taxation noted in Chapter 5, alternative methods of financing infrastructure and recovering costs must be considered. These include:

- Public Private Partnerships (PPPs)
- Public recovery of some of the increased land values that arise from development; and
- User Charges

The funding of infrastructure development can broadly be divided into two categories: firstly the *ex ante* financing decision and, secondly, the cost recovery following completion of the project. This section considers both in turn.

9.9.1 Financing the Project – ex ante

Public Private Partnerships

In its 1999 *Strategy* report, the Council discussed the financing of infrastructure and in particular in the role for Public Private Partnerships (PPPs). The Council recognised that PPPs were in their infancy and that wider use of PPPs could not be seen as a panacea for infrastructural development in Ireland. However, the Council was generally supportive of PPPs and, in particular, viewed the potential attainment of private sector efficiency gains as a principal benefit. The Council emphasised that PPPs must respect overall budgetary parameters having regard, inter alia, to any budgetary costs that they may generate over the long term (NESC, 1999).

In 2001 the Institute for Public Policy Research in London reviewed a lengthy public debate on the merits of PPPs with the following overall assessment:

> Being open minded about the contribution that partnerships could make to public services means challenging two intransigent perspectives on public private relations. On the one hand we totally reject the *privatisers* vision of public services: their aim is always and everywhere to increase the role of the private sector in the provision and funding of public services. Their desired outcome is smaller government and residualised public services. On the other, we distance ourselves from a public monopoly perspective which holds that as a matter of principle public services should always and everywhere be provided by the public sector (IPPR, 2001).

The IPPR believes that both approaches view PPPs as privatisation by stealth. This contrasts with the IPPR's own view that PPPs open up a wider potential pool of service providers and permit public services to capture the skills, creativity and expertise that reside in a wide range of private and voluntary organisations.

It is clear that the decision about how to fund a public service is distinct from the decision on how to deliver the service, which is itself separate from the question of financing the investment. For example, on-going funding is primarily related to cost recovery and could be in the form of general taxation or user charges, whereas financing relates to how the capital needed for the investment is raised (OFMDFM, 2002).

The cost of private financing is obviously higher than that of public sector borrowing However, if it is expected that subsequent efficiencies can be achieved by private sector involvement, then this potential deficiency in the use of PPPs can be overcome. It must be recognised that simply because a project is to be undertaken by a private body, as opposed to a public sector entity, does not necessarily imply it will be carried out in a more efficient manner. PPPs may also entail a transfer, or sharing, of the risks, in particular demand risks associated with the project, which may be appropriate where a project and its associated risk may not be deemed to be entirely in the public interest.

The Government has recently published its own framework on Public Private Partnership (Department of Finance, 2001). In its framework the Government has emphasised the need for PPPs to yield value for money for the exchequer, including the allocation of risks to the party best able to control and manage them; and it stressed the importance of maximising the benefits of private sector efficiency, expertise, flexibility and innovation. The Council supports this assessment. This may imply that the applicability of PPPs is somewhat more limited than was previously thought to be appropriate, or than is current government policy, although some of the potential contribution of PPPs could be addressed by undertaking an evaluation of the current barriers to employing PPPs and some of the deficiencies in the design process. In particular, the Council re-asserts its previous position that PPPs should be seen more as a way of procuring private sector efficiency and expertise or for adding to supply capacity, rather than as a pure financing mechanism for funding infrastructure. The Council also notes the recently published bill on the National Development Finance Agency (NDFA) and its remit to seek a wide variety of financing mechanisms for the delivery of new infrastructure.

Funding through increased land value

Society, through government, must establish clear priorities among infrastructure projects. The Government is currently running a current account surplus implying capital investment is to a large degree being funded out of current revenue. In principle, every project that has undergone thorough evaluation, and been shown to provide net benefits to society, should be undertaken. However, as noted in Chapter 5, limits on public borrowing may not permit that to happen. There is something of a dichotomy between the ability of semi-state bodies to finance infrastructure provision through borrowing and the limited ability of central government to do so for infrastructure provision financed through general taxation. To the extent that government borrowing is not possible, or deemed undesirable, alternative means to finance the necessary infrastructure provision must be considered. Indeed, the Government has already introduced such a measure in the form of the 'affordable housing' provisions discussed above. In this instance, a portion of the benefit that is conveyed to the landowner in the form of planning permission for development is captured in a form of taxation.

Notwithstanding the difficulties of the affordable housing scheme, and the Council's commitment to undertake a thorough analysis of land and housing policy, there is no *a priori* reason why this concept cannot also be extended to other infrastructure projects such as roads or sanitation. Indeed, such an approach has been advocated by Glaister and Travers (1994). They propose an 'infrastructure fund' whereby a proportion of the increased capital value of the land in the region of an infrastructural development could be used to contribute towards its financing. This is the means available under Section 49 of the Planning and Development Act, 2000, for new infrastructure and which is supported by the Council in Chapter 7. It is recognised that changes in capital value are not easily captured as the increased value is only crystalised when the asset is sold. However, the Council believes that mechanisms of this nature should be further explored.

9.9.2 Paying for Infrastructure – Funding the Project

Allied to the issue of financing the infrastructure project is the issue of cost recovery once completed. It is not an unreasonable first principle that a person who utilises a good should pay for it. This is the case with most 'normal' goods in society. However, the incremental cost of making use of infrastructure may be very low, particularly outside of times of peak demand. Moreover, the infrastructure may itself seek to correct for other external costs present, but not accounted for, (such as congestion) or to serve a social objective and may therefore require a pricing mechanism that captures these important effects. Hence, cost recovery for infrastructure often differs substantially from normal goods. In its 1999 *Strategy*, the Council welcomed greater use of pricing mechanisms in the management of infrastructure services and their ability to lead to improved efficiency of provision and the promotion of sustainable development (NESC, 1999). Some such mechanisms are discussed below.

In carrying out infrastructure planning one must generally plan for peak demand but accept a less than 100 per cent level of utilisation. The greater the utilisation of a fixed level of infrastructure the lower the average cost of serving each individual customer. This difference between the average cost and the marginal, or incremental, cost of service delivery represents a smoothing out of the fixed costs of construction and operation over a large number of units. It is the presence of these economies of scale in infrastructure provision that account for two of the phenomena we often see in their provision: two-part pricing or more complex tariff arrangements, and time-of-day pricing.

Under two-part pricing arrangements the customer commonly pays a fixed standing charge regardless of use combined with a marginal throughput charge. Sometimes this fixed charge is based on a customer headcount, whereas in other cases it is based upon the customer's peak usage of the infrastructure concerned[11]. In many cases the fixed component of the tariff can justifiably comprise a

11. Or indeed in some cases peak usage at system or global peak coinciding with other users peak usage of the system.

significant component of the charge as is the case with gas network charges, where 90 per cent of the fee is levied based on the individuals peak day demand.[12]

Under time-of-day pricing users take account of the costs of their usage in congesting the network. Yet time-of-day prices are rarely levied when it comes to the use of infrastructure. One example where they do apply is in the incentive given to electricity users to reduce demand during peak winter hours, although this is only implementable for large users. Some elements of infrastructure—such as the West and East Link Toll bridges, or the use of public transport such as bus networks—are subject to a flat pricing structure leading to congestion at peak times. Admittedly, the user of this infrastructure at this time is facing a higher cost as he/she must bear not only the cost of the toll but also the costs of congestion, higher fuel consumption etc.

Similarly, for some services we accept an implicit cross-subsidy from one class of customers to another, such as the universal postage charge across the state. In other cases we do not, and levy a more cost-reflective incremental charge, as in the case of distance-based tariffs for public transport. Sometimes this subsidy is from one class of customer to another, but within one industry, as in the case of urban to rural customers for the supply of electricity. In other cases it is a direct subsidy from general taxation such as the Public Service Obligations for the provision of regional airline services.

The Council recognises the importance of many of the services provided by national infrastructure for the quality of life and for economic development and hence, often, the universal nature of their provision. It was for this reason that many of these services evolved under state planning and ownership. The Council believes that this universality of service, where applicable, is compatible with a new regime characterised by the introduction of controlled competition, independent sectoral regulation and the possibility of

12. This is the case for gas transmission charges although the proportion of fixed charge has recently been amended to 80 per cent of the tariff on the gas distribution network.

the operation of national infrastructure in the public good by private owners. However, as noted in Section 9.4 above, achieving this compatability and balance is a complex task, to be addressed at both national and EU level. It recognises that this compatibility requires high quality regulation and institutional arrangements that ensure accountability (see below).

No one principle of pricing is superior in all cases and a case-by-case analysis is required. However, the Council cautions against the introduction of purely cost-reflective pricing, without consideration of the other important objectives to be fulfilled through the provision of infrastructure. Where models of cross-subsidy are employed to meet such objectives, consideration should be given to the possible distributional and efficiency effects.

9.10 INFRASTRUCTURAL DELIVERY

9.10.1 Ensuring Necessary Infrastructural Investment

The Council advocates above the delivery of all infrastructure projects that can be shown, under thorough evaluation, to deliver a net benefit to society. However, an important step precedes evaluation, namely planning for infrastructure and the process by which options are put forward for evaluation. There are at least three possible means by which the decision to invest can be arrived at: through the market, through decisions made by government or through the decision of an independent arbitrator such as the independent regulatory bodies. In most cases, it should be the pressure from citizens and customers through increased demand that gives rise to the need in the first place, although with long lead times in infrastructural delivery, and given the overall national spatial objectives, forward planning is essential. While there may be a role for all three types of agent, the Council does not support an approach which leaves entirely to the market the decision to invest in vital infrastructure, and has expressed this concern above with regard to the provision of future electricity generation plant and broadband services.

9.10.2 Infrastructural Evaluation – A Complex Task

By its very nature infrastructural investment entails large-scale capital projects expected to have a lifetime of many years, if not decades, and hence involve a trade-off between consumption today and future benefits. It is therefore vital, given the myriad of infrastructural demands, that a thorough evaluation of the likely benefits of any project should be undertaken before it should proceed.

Development that may appear uneconomic today may in due course come to be accepted as a societal norm. This was the case for rural electrification. In other areas technology may move on, as in the case of canal development in the 19th century, and society may be encumbered with an uneconomic project that will never yield a reasonable return on its capital investment. However, in some cases it is only by the establishment of a critical mass of users, such as voice telephony, that supply will bring with it its own demand for use of the infrastructure. Therefore, in some cases, development to deliver universality of service may be appropriate, whereas in other cases a more location-specific economic test may be preferred. Whatever the approach, it is incumbent upon the *proposer* to recognise that raising money through taxation is not without its costs, that citizens' preference between consumption today and consumption tomorrow may vary across time and space, and that infrastructural development today may materially affect economic and regional development into the future.

Canning and Bennathan (2001) estimate the social returns on infrastructure investments and, in particular, electricity generation and paved roads across countries. They find that infrastructure is highly complimentary with human and physical capital, but has rapidly diminishing returns if increased in isolation. In developing countries, this produces an optimal mix of capital inputs and makes it very easy to have too much or too little infrastructure. They find that rich countries have rates of return just as high as those in the poorest countries, though the highest returns to capital are found in the class of middle income countries.

It is clear that that economic infrastructure brings with it social opportunity and improvement, and that social and community infrastructure can bring with it economic dividend (NESC, 1999). It is important, therefore, to take into account all potential costs and benefits, including any environmental improvement or burden, prior to carrying out infrastructural investment. While there is uncertainty over the potential demand for services in future, and this should be taken into account, the long lead times necessary to put in place infrastructural investment mean that appraisal should not be short-sighted.

The current system of policy evaluation is somewhat fragmented and ad hoc in nature and is generally not transparent. This ad hoc in-house evaluation has been supplemented by additional procedures in the form of poverty proofing, equality proofing and rural proofing. The government is currently preparing a national policy statement on regulation that will encompass not only sectoral regulation but also policy evaluation and regulatory effectiveness. The introduction of a system of Regulatory Impact Assessment was one of the key recommendations of the OECD review of regulatory reform in Ireland.

A case can be made for a more holistic assessment of regulation and policy, increased transparency in the policy making process and a development from traditional cost benefit and cost effectiveness type analysis to a situation more characterised by multi-criteria decision making analysis. Multi-Criteria Analysis (MCA) establishes preferences between options by reference to an explicit set of objectives that the decision making body has identified, and for which it has established measurable criteria to assess the extent to which the objectives have been achieved. MCA then assesses the relative importance weights for the criteria that allow an overall weighted average sum of the performance levels on different criteria to be managed. MCA recognises some of the limitations of traditional cost-benefit analysis and the difficulties involved in deriving a meaningful monetary value for every possible contingency or outcome. MCA also recognises that decision making may by its very nature be multi-dimensional and allows for policy makers to consider trade-offs beyond those that can be assessed purely in the financial sphere. Multi Criteria Analysis has been applied in the Irish context by the DTO in its assessment of the relative merits of the various proposals in its *Strategy 2000-2016*. Consideration might be given to wider use of this approach.

In carrying out infrastructural evaluation it is important to recognise that demand may vary over time due to technological change or change in consumer preferences. In addition there is the possibility of a 'dual equilibrium' as suggested in the Forfás Report on Broadband Investment in Ireland (Forfás, 2002). This may arise where economies of scale, created by high levels of fixed cost, are not realised and a low-demand high-price equilibrium may be reached. Further investment or subsidy may facilitate the move to a high-demand low-price equilibrium where the fixed costs are shared among many more users. It is for this reason that Bord Gáis Éireann offered residential customers in excess of €500 to connect to the network, although this payment, and its capitalisation over some 15 years, has recently been retracted following regulatory review.

The Council's discussion now turns to the preferred method of infrastructural delivery, the role of market liberalisation, the creation of regulatory agencies and the necessary support to ensure delivery of a quality service in a cost effective manner.

9.10.3 Infrastructural Delivery

The Planning System

The planning system in Ireland, and planning for infrastructure of national importance in particular, is subject to a balance between local democracy and the property rights of the individual, on the one hand, and the advancement of the overall developmental objectives of society as a whole.

The Council believes that the primary consideration in planning should be the common good. The Council calls for a more structured set of guidelines setting out national planning policy on sustainable settlement patterns, settlement density, rural dwellings and renewable energy projects, which would inform planning at the local authority level and help ensure that the overall objectives in the NSS are met. In addition, the Council re-iterates its previously expressed desire to see the development of fast-track planning procedures for projects of particular strategic importance (NESC, 1999:482).

Under Section 143 of the Planning and Development Act, 2000, Bord Pleanala shall, “in performing its functions, have regard to the policies and objectives for the time being of the Government, a State Authority, the Minister … whose functions have, or may have, a bearing on the proper planning and sustainable development of cities, towns or other areas, whether urban or rural.” The Council believes this constitutes an acceptance of the need for some projects that are in the ‘common good’ but that may legitimately be subject to local opposition. However, if necessary, the need to allow for the provision of infrastructure of national importance could be made more explicit. The Council recommends that government undertake whatever measures are necessary to ensure that national objectives are taken into account. The Council has expressed its concerns in this regard above with respect to the delivery of electricity network infrastructure.

Land Acquisition

One important reason for the substantial increase in costs in the programme of national infrastructure delivery has been the higher than anticipated cost of land acquisition. While it is necessary for those whose land is acquired to be reasonably compensated for the value of such land, and some reasonable cost for the inconvenience and attachment which such acquisition brings, the overall developmental objectives of society must be taken into account. As set out in Article 43 of the Constitution, individuals have the right to own private property which, like other rights, must “be regulated by the principles of social justice”, and which can only be de-limited by the State “with a view to reconciling their exercise with the exigencies of the common good.” The role of land in national development will be addressed in the Council’s proposed study on housing and land policy.

Monitoring Projects

A key element of project delivery is the ability to keep the project on track, in time, space and financially. The Council recognises that the necessary project management resources to deliver large-scale infrastructure projects are limited. One approach has been to let private contractors take both the risk and responsibility for project management and delivery. There may be increased scope for this. A second approach would be for the public sector to build a core competency in project management capability, which would be non sector specific and could be employed throughout the wide remit of public sector infrastructure delivery. There is a role for each approach.

The Council believes that monitoring and ex-post evaluation of the cost effectiveness of projects can lead to a virtuous cycle of improved project planning, evaluation, delivery and monitoring. The Council believes that Ireland must develop the capacity to better achieve the planning and implementation of national infrastructure programmes in a co-ordinated manner.

9.11 INSTITUTIONAL ARRANGEMENTS

The Council has identified increased competition, managed in a socially sustainable manner, as one of the key policies for the combating of inflation in the Irish economy. The programme of market liberalisation and re-regulation of traditionally state owned network industries has seen the establishment of three independent sectoral regulators for utilities in Ireland to date: the Office of the Director for Telecommunications Regulation (recently amended to become the Commission for Communications Regulation), the Commission for Energy Regulation and the Commission for Aviation Regulation. These offices have been accompanied by the creation of a large number of semi-autonomous state bodies with the responsibility for the delivery of change in specific sectors. Examples of these would include the national Pensions Board, Comhar, the Competition Authority and the Health Boards. Each of these is subject to a different form of governance.

Meanwhile, debate is ongoing as to the means by which public transport can best be regulated and the Department of Transport has recently published a consultation paper on the regulation of bus services outside the Greater Dublin Area. Combined with this has been reform to improve service delivery in a number of other areas such as taxis, pharmacies, the Commission on Liquor Licencing and other studies of professions as identified in the OECD review of Regulatory Reform and undertaken by the Competition Authority.

The Council has emphasised above the important strategic role that public institutions must play in ensuring the delivery of sufficient infrastructure, and that it is not always possible or desirable to leave such decisions to the market. In deriving an infrastructural programme, it is important that independent decision makers, be they regulators or state-owned enterprises, take into account overall social and governmental objectives. As discussed in Section 9.1 above, any new institutional arrangements for the regulation of utilities must meet a number of goals: customer needs, real or virtual competition, social obligations, long-term investment and accountability.

Running in parallel with the debate on the role and effectiveness of independent sectoral regulation is the issue of the appropriate balance between local, regional and national decision makers in infrastructural and spatial planning and provision. While the Council is in favour of more devolution to the local level in many policy areas, infrastructure and spatial planning is a national issue and therefore requires national co-ordination. A major challenge is to devise institutional arrangements which combine national strategy with regional co-ordination and local devolution.

9.11.1 Institutional Reform: The Spatial Dimension

Ireland has a fragmented set of institutions in the spatial dimension combined with a set of unclear and underdeveloped linkages between them. In addition to national policy set by central government, there are regional assemblies, regional authorities, County Development Boards, local authorities as well as specific agencies that transcend local authority boundaries such as Údáras na Gaeltachta, the Western Development Commission and Shannon Development. An increasingly strategic role is necessary for planning and in particular planning for major infrastructural projects. However, it is clear that this needs to be informed by local communities and by those at local government level. This is necessary to ensure that we achieve communities which are inclusive, deliver social cohesiveness and contribute to overall economic and social objectives in an environmentally sustainable manner. The Council believes that the County Development Boards have an important role to play in this regard. However, there is a need to clarify the relationship between local and regional actors, such as the CDBs and the GDA, and that of national government.

In particular, the Council calls for a much more structured set of guidelines setting out national planning policy in relation to sustainable settlement patterns, settlement density, rural dwellings, set in the context of NSS. Meanwhile, infrastructure and other developments of national importance should be decided upon at a national level while preserving a degree of local accountability.

9.11.2 Institutions for Utility Regulation

In a world of perfect competition the behaviour of firms competing in the marketplace would deliver market outcomes which use resources efficiently. In a world of perfect information, public policy and regulation could be administered by a system of complete contracts which would cover every possible contingency. However, given incomplete contracting and imperfect competition, policy for network utilities must address three key questions (Newbery, 1999). Firstly, how do we ensure that large amounts of specific sunk capital are financed, and specifically, how are property rights in this capital to be defined, allocated and protected? Secondly, we must address the appropriate industry structure, both horizontally and vertically, if network utilities are to be liberalised in the long run consumer interest. These questions are concerned with issues of forward looking or dynamic adjustment and efficiency, and are often set out in the legislative framework that governs regulation and are, therefore, subject to infrequent updating or adaptation. The third key question is more concerned with static efficiency and relates to the best use of the existing network. This question has tended to be the focus of public utility regulation and pricing and the associated institutional design on an incremental basis.

Modern analysis of the relationship between regulators (principals) and firms (agents) emphasises informational asymmetries. Such informational asymmetry exists between the regulator and the firm whether that regulator is an arm of the state or an independent statutory body. Given such informational asymmetry, the regulator (or principal), acting in the public interest, faces a trade-off between her attempt to extract efficiency improvement from the firm (or agent) and her desire to extract the maximum amount of economic rent. "Price cap regulation", as is commonly practiced in Ireland, and in much of Europe, is *ex ante* regulation which gives the firm an incentive to make cost savings which can ultimately be passed onto the customer. 'Cost-plus regulation', or cost–of-service regulation as is commonly practiced in the United States suffers from the incentive to over-invest. However, it ensures that the firm with market power is unable to retain any of its economic rent and thus make super-normal profit. The cost-plus approach focuses on the guarantee of reasonable return on capital, although in many cases subject to a "used and useful" test, whereas the price-cap approach concentrates on encouraging dynamic organisational change at the firm level.

Accountability in the Regulatory Process

In 1999/2000 the Minister for Public Enterprise carried out consultation on *Governance and Accountability in the Regulatory Process* (Department of Public Enterprise, 2000a). In particular, the consultation addressed the responsibility of regulators to look after the customers' interests and the relationship between regulators and Ministers, the Oireachtas, the Courts and the general public. The establishment of independent regulatory bodies, and the separation of regulatory powers from the other functions of Government, enables us to reduce some potential conflicts of interest whether these be between the State (in its role as both regulator and shareholder) or between political interests and overall efficient development of network industries. However, it is clear that the interests of society and economy in a democracy demand that such delegation of responsibility be accompanied by clear and defined accountability mechanisms.

There are a number of means by which the recently established independent regulatory bodies are currently held accountable by the State. The first is through their openness to public scrutiny. All such independent regulators currently come under the umbrella of the Freedom of Information Act, 1997, which requires them to keep records for public scrutiny. In addition, the production of well-designed and implemented consultation programmes and strategy statements in which they are required to engage can not only increase transparency but can "contribute to higher quality regulations, identification of more effective alternatives, lower costs to the consumer and businesses, and better compliance and faster regulatory responses to changing conditions" (Department of the Taoiseach, 2002a). The independent regulatory bodies are also subject to *ex post* budgetary scrutiny by the Comptroller and Auditor General and by the Oireachtas through the requirement to present an annual report of work completed and a work programme for the coming year to the Minister, which must be laid before the Oireachtas within six months of the end of the year.

The independent regulators are also subject to the relevant sectoral committee of the Oireachtas. However, in its review of *Regulatory Reform in Ireland,* the OECD noted that the Oireachtas and its committees lacked capacity for effective oversight and recommended that Ireland should consider a strategy to improve Oireachtas accountability procedures, including appropriate resources (OECD, 2001d). In particular, it was suggested that attention should be paid to managing information to permit the committees to focus on strategic policy decisions.

The independent regulatory bodies are also accountable to the judiciary through statutory provision for judicial review of decisions made by regulators. This can examine the manner in which such decisions were made and the procedures followed by the regulator in the process. Proposals are also being put in place at a European level for an oversight or appeals panel to be put in place to review regulatory decisions and progress is being made in this regard in the area of telecommunications.

Finally, and perhaps most importantly, a strategic role is reserved for the Minister with responsibility in the particular sector. In many cases it is the Minister who can decide upon the level of market liberalisation, it is the Minister who, with the agreement of the European Commission in Brussels, can put in place Public Service Obligations to deliver societal objectives and it is the Minister who has the power to review certain cases. An example is the Commission for Energy Regulation, where the decision to grant or to refuse licences to market operators is subject to Ministerial appeal. It is the view of the Council that this strategic role may increasingly be extended in the interests of ensuring infrastructural development, as is the case in the catalytic priming of broadband investment, in line with overall national and regional objectives, while continuing to permit day to day autonomy for regulatory decision making.

It was proposed in *Governance and Accountability* that the Minister would undertake a periodic formal evaluation of regulatory developments within the utilities area. The Council believes that such a review should be carried out in the next few years given the ongoing changes in regulation of new sectors such as post, aviation and gas, combined with the increased uncertainty in infrastructure provision and the need for a co-ordinated and strategic government role in ensuring Ireland's overall developmental objectives are met. Such a review should also give consideration to the ongoing development of a multi-utility approach.

A Multi-Utility Multi-Institutional Perspective

It is increasingly possible and common for an individual firm to provide a number of utilities—such as gas, electricity or telephone—to a consumer. This is often referred to as a multi-utility approach. This approach is relatively under-developed in Ireland. It may encompass not only the physical delivery, but also the marketing of a portfolio of products allowing the exploitation of economies of scale and scope. This allows a company that was once engaged in only one business to diversify and exploit its brand loyalty across a number of different sectors. This can extend beyond the sale of utility products to include the marketing of financial products or insurance, allowing these firms to exploit their information advantages over their competitors, such as their prior knowledge of customers' household characteristics and attributes. This vision is not so new since utility providers, such as the ESB, have traditionally branched into retail operations which were financed through ongoing utility bills.

We are now seeing the development of multi-utility corridors, whereby telecommunications fibre is being laid alongside other forms of infrastructure such as gas pipeline, or railroads or on top of the electricity pylons. In addition, Bord Gáis is now active in the market for the supply of electricity, as is the ESB in gas supply (ESB being Ireland's largest consumer of gas), and National Toll Road's (NTR's) subsidiaries Airtricity and Celtic Waste are important players in the markets for renewable energy and waste management.

There are substantial opportunities for spatial co-ordination and increased efficiency, combined with the potential for reduction in environmental impact from such an approach. However, the multi-utility approach brings with it new challenges.

The first challenge is at a purely organisational level and concerns the role and responsibility of the various sectoral regulators in ensuring the appropriate level of service delivery and investment. For example, in the case of fibre wrapped on electricity transmission lines: What rental should be paid to the owner of these lines? What should be the policy regarding maintenance? Who should have priority in the case of outages and who should pay for them? A second challenge concerns the increasing dominance in the utilities market of a few firms and the implications this might have for competition and customer welfare. However, the opportunities for spatial co-ordination and increased efficiency, combined with the potential for reduction in environmental impact, are likely to outweigh any problems identified above and the Council welcomes ongoing development of the multi-utility approach.

This raises the question of the appropriate institutions to regulate and co-ordinate wide-ranging developments. The paper *Governance and Accountability* considered the possibility of a single regulatory authority to cover all sectors, but concluded that a sectoral approach was more appropriate. The sectors and regulators are defined broadly, so as to exploit linkages, such as between gas and electricity or post and telecommunications. Given this approach, and bearing in mind not only the linkages between sectors but the benefits of shared regulatory experience among the limited pool of human capital, the Council emphasises the importance of cross sectoral co-operation between regulatory bodies and also with those organisations who may have potential demand for the infrastructure which is provided (e.g. IDA Ireland). The Council welcomes ongoing development of the multi-utility approach, whether through formal integration and amalgamation of firms and regulatory bodies or through greater co-ordination between sectors.

The Council also broadly welcomes the enactment of the Competition Act 2002, and the increased powers granted to the Competition Authority along with a more co-ordinated remit in conjunction with the sectoral regulators. It is clear that while competition powers are key to the delivery of effective competition, the Act also recognises that competition in its purest sense may not always result in the best form of service delivery and recognises the role controlled competition and regulation has to play.

Virtual Competition

A key component of competitive pressure in small and highly concentrated markets can come through the operation of "virtual" competition, as seen in the regulatory contract between the principal (regulator) and the agent (regulated firm). Often such an approach, which is really one of re-regulation as opposed to de-regulation or liberalisation, can deliver greater benefits to consumers in both the short and long term than one where the market is artificially tilted to ensure competition develops.

Sometimes, this virtual competition is administered by the regulator, as is the case with the Virtual Independent Power Producer (VIPP) auctions introduced in the case of electricity supply. However, more often the competitive pressure is exemplified through the benchmarking of company performance with similar companies competing in home or foreign markets. In carrying out benchmarking exercises, similar to those conducted by firms, the regulator can identify a level of costs, and in many cases organisational traits that represent "prudent and efficient utility practice". The regulator can then set a level of charges based upon a transition to this more efficient level of performance. This form of competition, also known as yardstick competition, can provide a very useful tool for simulating competitive pressures on firms when the introduction of full-scale competition would impose costs that are not necessarily in the consumers' interest.

Having determined a level of permissible prices, a key challenge remains the catalyst within the utility or other regulated entity to initiate change to operate as if in a competitive market, and the effectiveness of the advice contained within the regulatory contract. In other words, what can be done to maximise the impact of the regulator's report and ruling on business practice? The Council believes that this calls for the initiation of not only strategic management and a management culture driven by results, but in addition a well developed human resource policy and partnership system focused on both performance and work conditions. This may require external assistance through public audit or the NCPP. The Council believes that consideration should be given to finding arrangements that can assist organisational change and performance in providers.

9.11.3 Institutional Reform : Conclusions

A joint study by the Centre for Economic Policy Research (CEPR) and Swedish Centre for Business and Policy Studies (SNS) identified ten conflicting priorities in designing regulatory policy to govern the network industries (Bergman *et al*., 1998).

BOX 9.3

Ten Conflicting Priorities in Designing Regulatory Policy

1. Short term versus longer-term objectives.
2. Efficiency versus equity objectives.
3. Competition versus monopoly
4. Slow versus fast liberalisation.
5. Public versus private ownership.
6. Sector specific regulation versus general competition rules.
7. Rules versus discretion.
8. Permanent versus temporary regulation.
9. Centralised versus de-centralised regulation.
10. Light-handed versus heavy handed regulation.

Source: Bergman *et al* 1998.

Conflicting priorities 1-2 relate to society's preferences, 3-5 relate to market structures and 6-10 relate to regulatory structure or institutions. In many regards a subset of these, and in particular 1,2,7,9 &10, are also apt in respect of regulation more generally and in the spatial dimension in particular.

Institutions include not only public bodies but also established law, custom and practice. They are supported by a complex web of rules, norms, expectations and sanctions and correspondingly have great inertia and evolve in an incremental and path dependent way. Williamson (1985) argues that transaction cost economics is the appropriate framework to explain why different institutions evolve to handle different kinds of transaction. He views three ingredients as being key. The first is 'bounded rationality', or the cost of acquiring and processing information. The second is the role for opportunism, also known as moral hazard. The third is 'asset specificity', or the extent to which the original value of assets is difficult to realise once they have been committed to a particular purpose. Newbery expounds this approach in the following manner:

> The relative importance of these three features in any transaction will determine the appropriate institution for mediating these transactions. Thus if there is bounded rationality and opportunism but not asset specificity competitive outcomes are efficient. If there was no problem with bounded rationality, both opportunism and asset specificity could be handled by sophisticated contracts or plans, with every contingency carefully anticipated and dealt with. If there were no opportunism, transactions could be handled by simple contracts in which agents would do as they said they would without further monitoring or enforcement. But if all three features are present, then governance structures are required which specify tasks in advance, together with mechanisms to monitor and enforce outcomes *ex post*. (Newbery, 1999: 54)

All three features are present in both spatial development and network industry regulation. In the terminology of the ten conflicting priorities, it is clear that mechanisms must be in place to ensure that whatever the institutional design it takes account of society's preferences for the present over the future and for equity versus efficiency. These dynamic elements are related to the key questions identified by Newbery, being dynamic or forward looking in nature. There is clearly a role for society, through its democratic mandate to be able to set and revise these priorities. Similarly, there is a role for society to ensure that the sectoral approach be co-ordinated with more overarching national economic and social objectives. While those firms which are in possession of the greatest information are those best placed to make many decisions, unfortunately it is often the very same firms, when in a position of market power, that have the least incentive to operate in the overall public good. It is for this very reason that institutions are complex in nature and should be subject to a wide variety of checks and balances. It is widely recognised in developed economies that well designed institutions lead to improved efficiency and better decision making. Progress along this path is by its very nature incremental and, while Ireland has progressed substantially in many respects, it also has some way to go in others.

9.12. CONCLUSIONS

As argued in Chapter 5, given the pressing need for infrastructure, the Council believes that it may be appropriate to ease the overall fiscal position to maintain public investment for both economic and social purposes. There is something of a dichotomy between the financing of some forms of state-owned infrastructure—such as electricity and gas networks and airport infrastructure through the issuing of debt by commercial semi-state enterprises—and the difficulty of borrowing for other capital programmes which will deliver benefits in the future, such as roads, hospitals or schools. Of course, no programme or project should proceed without rigorous scrutiny or evaluation.

The Council believes that to the extent that government borrowing is not possible, or deemed undesirable, alternative means to finance the necessary infrastructure provision must be considered. These include approaches that capture some of the increased land value created by the delivery of infrastructure and ongoing contributions by those who use infrastructure through charges, keeping in mind the possible distributional and efficiency effects.

The Council draws the following conclusions and recommendations from this chapter:

- Physical infrastructural development should be considered in the context of the appropriate spatial balance and, in this context, the Council welcomes the publication of the NSS;
- Spatial balance is itself an evolving concept, premised on society's economic and social trajectories and evolves with the provision of infrastructure through a mutual dependency;
- Policy always confronts trade-offs between the short-run focus and a long-term economic and social development;

- Infrastructural development is a key requirement to sustain growth and is assumed in projections of long term growth and productivity improvement;
- There is a need to achieve a more cross-sectoral and cross-cutting approach to policy making while recognising that there is no set of institutions that will optimise all possible policy decisions;
- There are, however, issues common to the delivery of all forms of infrastructure, such as the need to secure investment, ensure the delivery of a high quality service and deal with issues of institutional and organisational change;
- The co-ordination between land use planning and providers of infrastructural development is crucial to ensure co-ordinated and sustainable development, as is the need for interaction between the central and local and regional levels;
- The co-ordination of a number of key agents will be required to ensure that programmes are implemented in line with the NSS in a timely and effective manner;
- There may be a role for strategic intervention to ensure sufficient infrastructure is delivered given the long lead times, and given that supply of some infrastructure has the ability to generate its own demand;
- Several key areas of infrastructure are particularly pressing, such as the need for more affordable housing, increased waste management capacity, an improved transportation network, enhanced communications connectivity and adequate margins of electricity generation capacity.
- The Council welcomes the provision of affordable housing through the planning system but sees the need for further work on land and housing markets;
- The ability of PPPs to finance infrastructure has not yet been fully evaluated and there may be other ways to capture the benefits that private sector involvement can deliver;

- Alternative means for the financing of infrastructure should be investigated, including using the enhanced land values created by infrastructural improvements;
- Infrastructure should be paid for by those who make use of it provided that overall societal objectives, such as universality and equity, are met. Current payment for the use of infrastructure is based upon a set of conventions and we should be open minded to changes in our approach;
- With careful policy and planning the delivery of social objectives can be combined with the introduction of controlled competition and independent regulation in sectors that were once dominated by monopoly enterprises.
- There is an important role for virtual competition tools, such as benchmarking, in markets which are not conducive to competition. The Council believes that consideration should be given to the necessary and appropriate institutions to deliver this organisational change at the enterprise level;
- Amendment to the planning system and better control of land acquisition may be required to ensure projects are delivered on time and in a cost-effective manner;
- Institutions are complex in nature and should be subject to a variety of checks and balances. It is widely recognised in developed economies that well designed institutions lead to improved efficiency and better decision making; and
- It is a major challenge is to devise institutional arrangements which combine national strategy with regional co-ordination and local devolution.

APPENDIX 9.1

INSTITUTIONAL ARRANGEMENTS FOR TRANSPORT

At a time when there is a major programme of investment underway to revitalise public transport, it is useful to consider the institutional and regulatory environment in which public transport operates. In the last couple of years there have been a number of papers on institutional issues published by the Government and the Public Transport Partnership Forum (established under the PPF). This appendix reviews the key issues in these papers.

A9.1 A New Institutional and Regulatory Framework for Public Transport

In August 2000, the Government published a consultation paper, *A New Institutional and Regulatory Framework for Public Transport* (Department of Public Enterprise, 2000b). This paper defined the overall objectives for public transport as follows:

- to ensure the provision of a well-functioning, integrated public transport system which enhances competitiveness, sustains progress and contributes to social cohesion;
- to ensure the provision of a defined standard of public transport, at reasonable cost to the customer and the taxpayers;
- to ensure the timely and cost effective delivery of the accelerated investment in the infrastructure facilities necessary to ensure improved public transport provision.

The paper proposed changes in the role of the state in relation to public transport. Up to now the state has not specifically defined what standards of public service it wishes to have delivered. The paper proposed that the state, through the Minister for Transport, will broadly define what standard of public transport services that it wishes to see provided. The paper proposed that public financial support for public transport would be provided on a contractual basis, specifying the payments made for a defined quantity and quality of service. It proposed that such contracts would as far as possible, be awarded by tender, thereby exposing them to market forces. This would ensure greater transparency in the allocation of resources.

The paper proposed the following broad outline of new institutional arrangements:

- Bus Átha Cliath and Bus Éireann will be established as separate independent companies and the existing geographical restrictions of their areas of operation will be removed;
- The state will divest itself of ownership of at least one of the bus companies;
- Iarnród Éireann will be divided into two independent companies—one responsible for railway infrastructure and the other responsible for the operation of railway services;
- The infrastructure will remain in state ownership while consideration will be given at a later stage to transferring ownership of the company responsible for the operation of rail services to the private sector or to the franchising of some or all railway services;
- Public Private Partnerships will be used to procure the design, construction, maintenance, operation and financing of major new public finance infrastructures, including the Dublin light rail network and any new suburban rail lines;
- The procurement of major infrastructural projects on a public partnership basis will be established as a separate function, independent of the public transport companies;
- An independent public transport regulatory function will be established.

A9.2 Regulatory Framework for the Bus Market in the Greater Dublin Area

The paper outlined a new regulatory framework for the bus market in the GDA. The approach adopted to regulation of bus services in the GDA was informed by an earlier paper prepared by the Department of Public Enterprise on the experience of regulation in the UK, Sweden and Finland. That earlier paper considered three models: the status quo in Dublin, full deregulation and limited competition or route franchising. The paper argued that the status quo, a regulated monopoly in Dublin, was not likely to optimise efficiency (Department of Public Enterprise, 2000c).

A model of full deregulation of bus services has been applied in only two developed countries, the UK (outside London) and New Zealand. As implemented in the UK, full deregulation allowed free entry of operators and allowed operators to choose routes, timetables and fares. Where a bus service was not being provided commercially, the relevant local authority could choose to subsidise the route by putting it out to tender. Positive results from deregulation included a reduction in operating costs and an increase in bus miles run and a decline in subsidies. However, negative effects were a decline in bus passenger numbers and increase in fares.

The franchising model involves limited competition, in which the public authorities define the public transport service to be delivered and invite tenders for its provision. Franchising means that there is competition *for* the market rather than competition *in* the market. In the UK, franchising was adopted in the London area, in contrast to the deregulation that applied outside London. A key difference between the experience of London and large metropolitan areas outside London is that over the period 1985 to 1997, bus passenger journeys increased by 8 per cent in London, while they fell by 40 per cent in other large metropolitan areas. In both cases, there was an increase in fares, (not surprising in the context of falling subsidies), but the increase in real bus fares was 37 per cent in London compared to an increase of 57 per cent in the other metropolitan areas. The subsidy per passenger journey in London fell by 79 per cent over this period, while it fell by 34 per cent in other metropolitan areas.

The Department's paper on bus regulation also reviewed the experience of competitive tendering in Sweden and Helsinki. The paper concluded that the benefits of competitive tendering in terms of lower costs and improved quality outweighed any of the costs associated with the problems encountered.

The Government's consultation paper proposed that the franchise model be adopted for regulation of the bus market in the GDA. The State will define the public service to be provided and tender for its provision. The companies who secure franchises will have exclusive rights to provide services on a particular route for a defined period of time. The company winning the tender will either make a payment to the state or receive a subvention, depending on the potential profitability of the route in question.

Under this franchising model, the role of the Government will be to define policy, set overall targets (in terms of modal split and passenger numbers) and set the overall level of financial support. An independent regulator, (to be established), will then ensure the provision of a defined level and quality of bus service. It will organise tender competitions and design an integrated bus network as part of a wider integrated public transport network.

A9.3 Public Transport Partnership Forum Response

The Public Transport Partnership Forum has recently responded to the Government's proposals for regulatory change. The Forum supported the position of the Government's paper that state support for public transport should be clearly linked to the quantity and quality of the service provided. The Forum supported effective mechanisms for the enforcement of performance and, where appropriate, incentives for operators to exceed minimum standards. It also recommended that public transport operators be made subject to a statutorily-based public service obligation in respect of non-commercial services. It recommended that payments for public service obligations should be linked to meeting specific and challenging performance requirements and that work should commence immediately on developing these.

In relation to the regulation of the bus market in the GDA, the Forum suggested the following way forward:

- An independent public transport regulatory authority should be established for the GDA;
- Bus Átha Cliatha should be established by statute as an independent commercial state company with a strong commercially focused board; this does not preclude the development of an alternative corporate structure in the future;
- Bus Átha Cliatha should retain its existing network for a period of years;
- All new services should be put out to competitive tender by the proposed regulator and revenue support should be provided where the services are not commercial. The contracts should link payments to specific and challenging performance requirements.

Thus, the Forum provided support for initial steps to be taken towards a new regulatory model for the bus market in the GDA. To the extent that the franchise model works well for new services, it would seem reasonable that over time it would be extended to existing services.

The Forum also welcomed the publication in July 2001 of *Iarnród Éireann: The Way Forward*, the report of the review group established by the Minister for Public Enterprise, and strongly urged all interested parties to proceed with the implementation of all its key recommendations. One of the key recommendations of this report was the establishment of Iarnród Éireann as a separate company with its own board. The report recommended that the shareholder should set out the specific objectives to be achieved by the company. These objectives would include both operational targets as well as key milestones for the further development of the company. Having defined the targets, the role of the shareholder would be to monitor and benchmark developments on a quarterly basis through the use of key performance indicators. The report emphasised that the shareholder should not become involved in the day-to-day operations of Iarnród Éireann.

The Forum also welcomed the decision of the Minister for Public Enterprise to commission a Strategic Rail Review to provide a blueprint for the development of the railways in Ireland over the next twenty years.

CHAPTER 10

COMPETITIVENESS, CONTINUOUS IMPROVEMENT AND LEARNING[1]

10.1 INTRODUCTION

Continued success in enterprise development depends upon a combination of an appropriately skilled workforce, a drive to higher value-added products, processes and services, access to international markets and on-going change within the organisation, in addition to the general economic environment.

This chapter discusses these components of competitiveness in the context of Ireland's enterprise policy and deals with trends in industry, enterprise policy, and key elements of competitiveness, including the provision of a skilled workforce, research and development, organisational performance and international access. In addition, it reviews important sectors of our economy that require more sector specific policies to address their on-going growth and development, principally agriculture and tourism

10.2 THE ROLE OF PUBLIC POLICY IN ECONOMIC DEVELOPMENT AND COMPETITIVENESS

10.2.1 The Rationale for Industrial Policy

The Council's Evolving Perspective

The Council's approach to the role of public policy in economic development is based on an analysis formulated in a range of reports since the early 1980s. As noted in Chapter 1, the Council has formulated its advice on the basis of a number of empirical observations and analytical principles concerning the development of the Irish economy. These reflect a particular view of Ireland's

1. This Chapter draws in part on material on enterprise policy provided by the Department of Enterprise, Trade and Employment and Forfás.

long-term position in the international system, the challenge of developing a small peripheral agricultural country, the dynamics of international trade and regional development and the role of the EU in creating an international system of governance. A similar perspective has been neatly encapsulated by Krugman in the idea of Ireland as a regional economy (Krugman, 1997). This perspective is expressed in a set of propositions outlined in Chapter 1, among which are:

- The importance of specialisation in high-value, high-growth, sectors in maximising the gains from trade and integration;
- The damaging long-run effect of net emigration and the importance of increasing population and employment in Ireland;
- That technological development can make it possible for certain countries or regions to rapidly improve their position in the international economic system;
- The importance of competitiveness in a small open economy;
- The role of European integration in facilitating the development of a small peripheral region;
- The inter-dependence between the traded and non-traded sectors, and the importance of an efficient non-traded sector;
- The importance of regional networking in strengthening competitive advantage; and
- The importance of organisational capability and learning in modern business competition and public policy.

As outlined in Chapter 1, this perspective can yield a useful interpretation of Ireland's economic failure through much of the 19th and 20th centuries and much greater economic advance in recent decades.

In Chapter 1, it was pointed out that this interpretation differs from two others that have been advanced recently. One is that Ireland's economic development is fatally contradictory and, the second, that Ireland's progress is nothing remarkable, best seen as an inevitable convergence that happened to be delayed. While each of these interpretations bears some similarity to the Council's, they would seem to have distinctly different policy implications. The view that Ireland's development is fatally contradictory would seem to reject the policy of attracting inward investment. The view that Ireland's recent growth is a delayed, but inevitable, convergence, tends to reject active industrial policy and suggest that financial prudence and market liberalisation are now sufficient to secure Ireland's economic prosperity and ranking in the international economy.

Irish policy would seem, for several decades, to reflect a view more like that of the Council, summarised above. But we should not make too much of this somewhat high-level conceptual framework. For several reasons, the policy implications of that perspective have never been easy to identify adequately. A policy approach reflecting that perspective has evolved significantly over recent decades. This is so because of the difficulty of re-orienting indigenous business in the 1960s and 1970s, the evolving EU internal market, the emergence of new technologies and changes in corporate strategy and organisation. This demonstrates that identification of a goal of economic development, and adoption of a broad perspective on the nature of the development challenge, are only the first steps in formulation of a strategy and policy. Such a strategy and policy has to be reformulated and implemented in response to experience in changing circumstances. That reformulation and implementation is the heart of the development policy challenge. Indeed, as argued in Chapter 3, the reformulation and implementation of industrial policy can itself alter our understanding of the goal of economic development, because it can shift our image of what successful business development would look like in the Irish context. This is evident in the changing understanding of Porter's work, and the role of 'clusters', in discussion of Irish industrial policy (see NESC, 1998).

Reflecting this, there has been an ongoing debate on the rationale, feasibility and best method of state action to promote economic development in Ireland—debates in which the Council has been very active.

Debate on the Concept of National Competitiveness

An important theme in the Council's work over several decades has been the challenge of Irish economic development. Within that, the concept of national competitiveness and national competitive advantage has played a significant role. Indeed, as noted in Chapter 1 and above, the importance of competitiveness in a small open, or regional, is economy is one of the key empirical observations and analytical principles that underpin much of the Council's advice and the interpretation of Ireland's economic development. The meaning, measurement and determinants of national competitiveness has, not surprisingly, been the subject of much research and debate among economists, business analysts and social partners. In re-stating its belief in the importance of competitiveness to the Irish economy and society, the Council should clarify some aspects of its view.

Most of those who debate the measurement and determinants of national competitiveness share the view that competitiveness is a critical factor in determining national economic performance, including employment. They differ over the relative importance of cost and non-cost dimensions of competitiveness, and on the impact of various policies (such as exchange rate policy and industrial policy) and structural characteristics (such as size, geographic location and institutional arrangements) on the cost and non-cost elements of competitiveness. The Council's position on these debates has evolved through undertaking numerous reports on Irish economic development. It is one that recognises the importance of both cost and non-cost dimensions, attaches significance to some structural factors, especially EU membership, supports active industrial policy to build capacity, enhance capability and achieve a position in high-tech sectors and is sceptical of the ability of exchange rate policy to sustain competitiveness and of fiscal policy to compensate for a poor export performance.

A quite different debate concerns the validity of the very idea of national competitiveness or national competitive advantage. This has long been questioned by some economists, and this scepticism has been revived by the adoption of this position by the influential American economist Paul Krugman (1996). This has led a number of other economists and business analysts to discard the concept of national competitiveness and to criticise the focus of governments and public agencies on studying and building competitiveness (Turner, 2001).

BOX 10.1

The concept of competitiveness

National Competitiveness
A number of writers have argued that the concept of competitiveness has limited meaning when applied to countries (Turner, 2001; Krugman, 1996). This argument has been developed most fully by Krugman who emphasises that a country as an economic entity is fundamentally different to a company so that analogies drawn between countries and companies can be misleading. To say that a company is uncompetitive is to say that its position is unsustainable; if it does not improve its position it will cease to exist. There is no equivalent for a country of an overall profit or loss. This scepticism about national competitiveness is contentious. Many would still contend that national competitive advantage is a meaningful concept and a critical goal of public policy (see Dunning, 1995). In any case, the relevance of Krugman's scepticism depends on the size of the economy, as explained below.

Comparative Advantage
The perspective on trade as mutually advantageous exchange rather than a zero-sum is based on the economic theory of comparative advantage. According to this theory, market forces will lead countries to specialise in those areas in which they have a comparative advantage. This applies to trade between two countries, even if one country has higher productivity in everything. The less productive country will specialise in those areas in which its productivity disadvantage is lowest; i.e., where it has a *comparative* advantage. Provided wages reflect the difference in productivity between the two countries, one would not expect either country to have a competitiveness problem.

The question arises as to what determines the pattern of comparative advantage. If comparative advantage is based on a country's natural endowment of factors of production, then one can take comparative advantage as given. However, much trade among advanced countries, particularly in sophisticated products, does not reflect inherent comparative advantage but is due to created advantages. If an industry becomes established in some country, this initial success may reinforce itself through a process of cumulative causation and external economies may become significant (Krugman, 1996). The possibility that comparative advantage is created rather than exogenously given raises the issue that some patterns of specialisation may be more favourable than others. Industries with high levels of innovation, product differentiation, income elasticity of demand or economies of scale can yield higher returns than others. In contrast to the text book idea of comparative advantage, - in which it makes no difference whether a country specialises in agriculture, industry or mineral extraction – it matters what industries a country specialises in. Achieving competitive advantage in desireable sectors can then become a focus of national economic debate and policy.

Competitiveness in Small Economies

The significance of this factor for living standards is related to the size of the economy. Krugman (1996) argues that US success or failure in international competition for desirable sectors will have only a modest impact on US living standards. However, in a smaller economy the external sector will be much larger relative to the size of the economy and the impact of developing specialisation in desirable sectors will be larger. Indeed, Turner who supports Krugman's scepticism about the concept of competitiveness in general, cites Ireland as an example of an economy in which the composition of the traded sector can make an appreciable difference to prosperity.

In addition to a compositional effect, there is another mechanism through which competitiveness has significant implications in a regional economy. As outlined in Chapter 1, a characteristic of a regional economy is that factors of production flow much more easily into and out of a regional economy. The export base and external competitiveness of a region can have a significant effect on the level of employment in the economy. If the economy becomes more competitive in some rapidly growing export activity, workers will be attracted to the region, both to work in the export sector and in local services whose expansion is induced by the export boom. Conversely, a significant contraction of the export sector may lead to a contraction in the economy and emigration of some of the labour force. Deficiencies of demand in a regional economy due to the decline in the export sector cannot generally be offset by macroeconomic policy measures.

Thus, the implications of, for example, a high-tech boom in a regional economy are greater than in a large economy such as the US, for two reasons: (i) the external sector is a larger part of the total economy, so that the expansion of a sector paying above average wages has more impact on average living standards; (ii) expansion of an export sector in a regional economy can expand the level of total employment in the economy, given labour mobility. By contrast in a larger economy such as the US a high-tech boom may not have any effect on the level of employment. In the US, "the growth of employment is not determined by the ability of the US to sell goods on world markets or to compete with imports but by the Federal Reserve's judgement of what will not set off inflation" (Krugman, 1996: 29).

Foreign Direct Investment

The most direct form of competition that exists between regions and some countries is in the attraction of foreign direct investment (FDI). Ireland's success in attracting FDI during the 1990s made a critical contribution to the rapid economic growth that was achieved, as described in Chapter 1. FDI contributed directly to employment growth and also facilitated employment in domestic services. Productivity levels in the FDI sector are above average, so FDI contributed to faster productivity and wage growth than would otherwise have been sustainable.

10.2.2 Identifying the Challenge for Irish Industrial Policy

The debate on industrial policy is ongoing, and now confronts some critical issues. These include:

- The nature and role of activist industrial policy after the IT slowdown and the slowing of the international economy;
- The relation of industrial policy to wider policies of market regulation;
- The role of pay determination and organisational performance in economic development; and
- The relation of the developmental arm of public policy to welfare and social policies.

It has been argued in Chapter 1, that an understanding of Irish development can be assisted by Ó Riain's idea of the 'flexible developmental state' (Ó Riain, 2000). This idea has been developed to characterise the role of the state in Ireland's economic development, especially in an era of global information technology. Ó Riain contrasts the 'bureacratic developmental state', found in several of the rapidly-industrialising Asian countries, with Ireland's 'flexible developmental state' (FDS). The latter is viewed as capable of nurturing development through its ability to attract international investment, embed it into the economy, develop local enterprise and embed this globally. The state may be 'autonomous' in its policies but is also 'embedded' in its approach as it works closely with individual firms both in Ireland and internationally. Ó Riain emphasises both the importance of growth driven by foreign direct investment and the embedding of foreign firms into the local economy and the development of local networks of indigenous firms in the global marketplace. 'This ability is sustained by the multiple embeddedness of the state in professionally led networks of innovation and in international capital, and by the state's flexible organisational structure that enables the effective management of this multiplicity' (Ó Riain, 2000: 158).

If the concept of the FDS provides a valuable general account of

Irish development in the recent decades, we have still to identify the nature of Ireland's current developmental challenge. Ó Riain's analysis fits well with Porter's three stage model of advancing national development: factor-driven, investment-driven and innovation-driven. To summarise, the factor-driven stage involves competition based on simple factors, such as commodity agricultural produce, and the exploitation of indigenous factor resources such as minerals. The investment-driven stage involves greater depth of industrial production, frequently driven by 'national champion' industries. The innovation-driven stage involves the development of industries involved in significant R & D and the emergence of indigenous firms capable of competing internationally and developing their own overseas presence.

Both Business Environment and Activist Industrial Policy

It is important to note some implications of the Council's evolving perspective and the new ideas noted above. They imply that we reject any strong distinction between activist industrial policy, on the one hand, and policy to secure the business environment, on the other. *Both* are required to achieve the development of a small peripheral regional economy. They also imply that we reject any strong distinction between 'cost' and 'quality' as the aspects of competitive advantage. Recent Irish and international experience, discussed further below, shows that even firms that rely primarily on technical or organisational innovation must be conscious of costs; and, even more radical, even firms in cost-based sectors must adapt their product and adopt new organisational disciplines.

After decades in which the focus of analysis was on the structural weakness of the Irish economy and the structural weakness of Irish enterprises (because of small size, peripheral location and barriers to entry), attention is now turning to organisational capability and performance (see section 10.4.4 below). This has potentially important implications for how we think about indigenous development and the role of public policy in supporting it.

In its 1999 *Strategy*, the Council argued that in the context of a tighter labour market enterprise policy needed to place greater emphasis on productivity and job quality than on employment creation alone. Elsewhere, the Council has argued that enterprise policy must be grounded on a stable macroeconomic policy and the establishment of the necessary factor pre-conditions for enterprise (NESC, 1996a, 1996b, 1998). The Council welcomes the reorientation of enterprise policy over the last three years to sustaining productivity growth, balanced regional development, promotion of knowledge-intensive sectors and to provision of an integrated package of support to client firms, and substantial investment in publicly funded strategic research.

The Council believes that Ireland has the potential to advance to the innovation-driven stage of development and that to do so enterprise policy must focus on competitiveness, continuous improvement and learning. Improvements across these areas and in the conditions which promote them have the potential to grow quality employment and productivity in both industry and services. The Council believes that support should be provided to enterprises only where it is required to address a market failure (NESC, 1986). Among the likely market failures are positive externalities and spillovers, including those that derive from transnational corporations located in Ireland. Furthermore, the Council emphasises that value for money is as important in industrial and development policy as in any other area of public expenditure. Consequently, expenditure on industrial policy, including tax concessions, must be subject to rigorous evaluation.

Achieving this development will depend on the broad competitiveness environment in areas such as regulation, market access and fiscal policy. To manage the transition process successfully, Ireland needs to preserve as far as possible the strengths that underpinned the progress made during the 1990s. These include maintaining a disciplined approach to wage determination, preserving appropriate rates of corporation and capital gains tax, and fully participating in the evolution of both a more economically integrated European Union and of a Social Europe. These and other core elements of enterprise policy still have a key part to play, while we work to develop new sources of strength in areas such as research and development and a wider national system of innovation. However, in the context of the development model described by the Council in Chapter 1, activist enterprise policy also has a significant role to play.

Activist enterprise policy represents one important area where policy makers should seek to embed the framework of the *National Spatial Strategy* (NSS). Economic activity, and especially investment and job-creation, represents one of the most significant influences on spatial patterns. Accordingly, the location, concentration and distribution of economic activity will have a crucial bearing on the ability of the NSS to achieve balanced spatial development.

There are clear patterns not only between urban and rural areas but also sectorally, with indigenous enterprises being more highly dispersed than foreign firms. Enterprise policy, and in particular the active encouragement of foreign direct investment and indigenous start-ups, should seek to contribute to the overall framework set out in the NSS. However, for this to occur it will need to be facilitated by:

- A critical mass of innovative, high value-added business enterprises distributed across a range of sectors;
- Designated centres for investment will need to have a high quality environment with access to the appropriate physical infrastructure, and be well developed and effectively networked;
- Ease of access to domestic and overseas markets; and
- Access to a diversified pool of labour

It is partly for this reason that many of these elements received attention in Chapter 9.

Another important empirical and conceptual issue—concerning the differences between foreign owned and indigenous enterprises—is discussed at the end of Section 10.3

10.3 TRENDS IN MANUFACTURING AND INTERNATIONALLY TRADABLE SERVICES

The performance by the manufacturing and internationally traded services sectors has been outstanding over the last decade. This performance was driven by strong inward investment, rapid export growth by foreign firms located in Ireland and a greatly improved performance by Irish-owned enterprise in both industry and services. This section identifies the main trends in manufacturing and internationally traded services.

10.3.1 Foreign-owned Enterprise

Employment

Over the period 1990 to 2000, employment in foreign-owned enterprises grew by over 70 per cent, before a fall of 2.8 per cent in 2001. Over the past two decades, the composition of the foreign-owned sector has changed markedly as the chemicals/pharmaceuticals, ICT, and international services sectors have grown in prominence. The combined share of the chemicals, metals and engineering, and international services sectors rose from 44 per cent of employment in 1980, to 55 per cent in 1990, and to 78 per cent in 2000.

Wages are significantly higher in foreign-owned than in Irish-owned firms. In 1999, average wage and salary payments in foreign-owned manufacturing firms (€26,161) were one-quarter higher than in Irish firms (€20,850).

Research and Development

Expenditure on research and development among foreign-owned firms in Ireland in 1999 was 0.8 per cent of output, well below both the OECD average (2.4 per cent) and the highest level in OECD countries (3.7 per cent). Rapid output growth has been associated with a fall in the share of expenditure on research and development (R&D). However, among foreign owned firms expenditure as a share of sales and output is prone to distortion by the very high recorded output and sales of these enterprises. A better measure may be R&D expenditure per employee. Ó Riain presents data on this measure by sector for Irish and foreign-owned enterprises. There are noticeable differences between sectors in the level of R&D expenditure per employee. In two of the 'high-tech' sectors, R&D expenditure per employee in foreign-owned enterprises is distinctly low (€1794 per employee in software and €1406 per employee in instruments). These data are well below the corresponding figures for Irish-owned firms in these sectors (€5521 for software and €4343 for instruments). However, in other 'high-tech' sectors the data show R&D expenditure per employee in foreign-owned firms that is similar to the corresponding figures for Irish-owned firms. Ó Riain characterises this pattern as the 'boom within the bubble' of foreign investment.

Linkages

Expenditure by foreign-owned enterprises on good and services in the Irish economy has shown rapid growth. In 1999, foreign owned enterprises spent over €10 billion on good and services in the Irish economy, more than double the level of real expenditure in 1994. By 1999, the level of expenditure by foreign-owned enterprises in manufacturing and tradable services was 30 per cent higher than the corresponding figure for Irish-owned firms, although relative to sales, spending by Irish-owned enterprises was higher.

Recent Trends

While there is an ongoing process of job losses from the existing stock of FDI, 2001 was the first time in 15 years that job loses exceeded job gains among IDA-Ireland companies. There were 17,535 job loses in IDA companies in 2001, while there were job gains of 13,100. The net decline in employment was approximately 4,000 or 2.8 per cent. Job loses were concentrated in the electronics/engineering sector, reflecting the global ICT downturn. Recently announced figures by the IDA for 2002, show a further net decline of approximately 3,000, or 2.2 per cent. There were 11,713 jobs created by IDA supported companies in 2002 and 14,754 job losses.[2] There are currently 133,084 persons employed by 1,098

2. It should be noted that these figures, taken from the Forfás employment survey are preliminary in nature.

IDA supported companies, which in 2002 received grants of €116 million. Pharmaceuticals and healthcare and Miscellaneous Industries were the only two industry sectors which recorded overall growth in 2002. Combined with Electronics and Engineering and International and Financial Services, pharmaceuticals and healthcare provide the best opportunities for sustained growth in the short to medium term.

10.3.2 Irish-owned Enterprise

The past decade has seen a marked improvement in the performance of Irish-owned enterprise. Between 1993 and 2000, employment in indigenous enterprise grew by almost 30 per cent and indigenous firms accounted for around 35 per cent of the net expansion in employment of the manufacturing and internationally trading sector. Up to 2001, the expansion of employment and output took place in a range of sectors. Within manufacturing, the strongest growth was in the high-tech sectors. While most of the employment in these sectors is in overseas firms, there was also strong growth by indigenous firms, although the total number employed remains modest. Total employment in indigenous firms in the combined sectors of pharmaceuticals, office machinery, radio, television and communications and medical, precision and medical and optical equipment, increased from 3,553 in 1991 to 7,844 in 1999, an increase of 122 per cent.

Employment growth in internationally traded services was faster. Employment in Irish-owned international services companies increased more than fourfold, from 4,158 in 1990 to 19,049 in 2000. The outstanding success of indigenous international services is the software sector. Between 1991 and 1999, employment in indigenous software firms more than trebled to 11,000. This sector has, however, been very much affected by the global downturn in the ICT sector.

The first half of the 1990s saw strong growth in expenditure on research and development in the indigenous manufacturing sector. The proportion of total output devoted to R&D almost doubled, from 0.5 per cent in 1991 to 0.9 per cent in 1995. Though expenditure on R&D by Irish-owned manufacturing firms continued to rise after 1995, it increased at around the same rate as output. Between 1995 and 1999, the share of output accounted for by R&D remained at 0.9 per cent. This contrasts with an OECD average for manufacturing of 2.4 per cent.

Although this suggests a relatively low level of research intensity in indigenous industry, the average figure for Ireland is affected by the dominant position of the food industry—a relatively low research sector internationally—within the Irish-owned enterprise sector. In eight of the fourteen sub-sectors for which data are available, the proportion of output devoted to R&D by indigenous firms was above the OECD average.

One weakness of the recovery of indigenous enterprise was modest progress in increasing manufacturing exports in the 1990s. Manufacturing exports by indigenous firms grew at an annual average rate of 2.5 per cent between 1991 and 1999, and the share of output exported fell from 34.8 per cent in 1991 to 31.3 per cent in 1999. There was a larger indirect contribution to export growth in the form of sub-supply to multinationals. The strength of domestic demand during these years is one factor explaining the slow growth of indigenous exports.

Productivity data compiled by Enterprise Ireland show that the productivity of Irish-owned manufacturing was fairly low compared to a number of other European countries. Value-added per employee in Irish-owned manufacturing was €48,300 in 1998. This was at the same level as manufacturing in France and above that registered in Italy. However, productivity in Britain, Denmark, Germany and Finland was on average 20 per cent higher.

Recent Trends

Irish-owned manufacturing has been less adversely affected by the downturn in the global economy and the problems affecting the ICT sector. Irish-owned industry sells most of its output on the domestic and British market and so has been less affected by the global economic downturn than some of the FDI-dominated sectors. There has been a sharp decline in employment in textiles in the year to June 2002 down 1,500 or 16.3 per cent), but the sector accounting for the bulk of job loses was the optical and electrical equipment sector down by 7,400 or 11 per cent).

The macro data show the growing importance of the services sector and construction in accounting for overall employment generation. However, given Ireland's position as an small open economy and its dependence on trade, the performance and prospects of the manufacturing and international services sectors continues to deserve particular attention. The traded sector is important as a driver of the overall value chain as well as a generator of employment in itself. This is true for both foreign and indigenous firms.

10.3.3 Indigenous and Foreign Owned Enterprise: Differences or Duality?

The continuing differences between indigenous and foreign owned enterprises, noted above, raises a question that is important in framing Irish economic strategy and industrial policy. Does Ireland still have a 'dual' economy of the kind that was identified in much research in the 1970s and 1980s? That research identified big differences between indigenous and foreign firms in almost all aspects of business process and performance: technology, production systems, management, training, finance, marketing, export-orientation, logistics, as well as profitability and employment creation. It is clear from the trends summarised below that significant differences remain. Does this imply that the Irish economy is in the same fundamental position now as it was in the 1960s and 1970s? Has industrial policy simply attracted more inward investment without overcoming the duality between Foreign and Irish-owned enterprises? While the evidence reviewed in this report is not sufficient to answer this question, the Council is not inclined to believe that Ireland's economy and business is characterised by 'duality' of the kind identified in earlier research. Firstly, it is important to think carefully about comparisons between the aggregate performance of foreign-owned and indigenous firms. The foreign-owned firms in Ireland are a select group, with characteristics that differ from indigenous firms in their own countries of origin. Simple comparison of the overall export performance of indigenous and foreign firms in Ireland would not be a valid means of assessing the degree of progress in Irish business. Secondly, it is possible that the different performance of the two groups of business reflect the fact that many foreign firms own valuable rent-yielding assets and are much larger than indigenous firms. While these differences are important, they do not imply that other business practices and capabilities are very different in foreign-owned and Irish enterprises. While there is a need for much greater research to test these hypotheses, it might be unwise to base industrial policy, and wider economic strategy, on an assumption of duality.

10.4 KEY ELEMENTS OF DEVELOPMENT AND COMPETITIVENESS POLICY

Given the conceptual approach outlined in Section 10.2 and the trends reported in Section 10.3, this section discusses the main elements of development and competitiveness policy. These are:

- Enterprise support policy;
- Science, technology and innovation;
- A skilled workforce and quality employment;
- Organisational performance; and
- Sectoral policies.

10.4.1 Enterprise Support Policy

Enterprise support policy has shown itself to be adaptable over time. That process of adaptation needs to continue given the changing circumstances outlined in this report and the challenges now facing the economy and society. The Council recommends that policy should continue to move towards measures that promote growth in innovation and productivity leading to sustainable competitive advantage, rather than widespread financial support to firms.

In seeking to adapt to a higher cost economy, a focus on organisational change is also important. To be successful in a higher cost environment requires that organisations engage in continuous learning to achieve continuous improvement. An emphasis on problem solving capabilities and sharing of gains are key characteristics of this approach.

Foreign Direct Investment

It is appropriate to continue seeking new inward investment in sectors where Ireland is competitive and has the potential to grow further, to replace jobs lost in sectors where Ireland is no longer competitive, to achieve a shift in the structure of the traded sectors of the economy towards higher-productivity sectors which can sustain higher income levels, and to develop Ireland's position in new high-growth, knowledge-intensive sectors This can best be achieved by reinforcing niches in which Ireland is currently successful and can develop a world-ranking position. Within these niches, leading companies should see Ireland as an essential place in which to have strategic operations. Appropriate investments in infrastructure, skills and R&D can help support the development of these niches (see below). The concentration of elements of these supports in particular locations can help promote regional development and cluster dynamics, to the benefit of both foreign and indigenous firms. As a first step towards this goal, IDA Ireland has formulated proposals for the development of Strategic Business Areas (SBAs). The focus of the SBA initiative is on promoting cluster dynamics rather than simply helping individual companies to grow.

Enterprise policy can also help to support existing FDI enterprises in upgrading the nature of activity undertaken in the 'Irish subsidiaries'. IDA Ireland is working with client companies to assist them in developing strategic, value-adding functions. This is a difficult challenge and the methodology and techniques involved need to be further developed. The Council welcomes the fundamental review of the project evaluation system used by the industrial development agencies, taking full account of the national economic and regional development objectives and the fundamentally changed environment including lower levels of unemployment and increasing immigration. This review will be published soon (Forfás, 2002).

Indigenous Enterprise

The Council is strongly committed to the policies which promote the development of an indigenous enterprise sector capable of meeting world class standards and competing on an international basis. As Ireland moves into the innovation-driven stage of development, such enterprises would be expected to become more significant in the economy's development. Enterprise Ireland is focused on helping new indigenous companies to emerge and flourish globally in high growth sectors and in assisting locally-controlled companies to compete and grow in world markets.

The Council notes that Enterprise Ireland's current business plan focuses on helping client companies to increase exports, productivity and employment and to promote the emergence of increased numbers of high-potential start-ups. This focus is appropriate in helping indigenous enterprises upgrade their competitiveness and embedding in the economy an ongoing culture of entrepreneurship. Enterprise Ireland maintains a strong focus on sectors with growth potential. Its international services strategy sets targets for the development of informatics, digital media, eBusiness, and health sciences, while the agency has also adopted a detailed strategy for the biotechnology industry. Efforts to build up strong niches and clusters in high-tech sectors, particularly in the regions, all require close links and co-operation between the enterprise agencies and enterprise and higher education sectors. In existing sectors, such as food and engineering, companies are facing increasing domestic cost inflation and competition from low cost countries. In this context increasing competitiveness is vital. Enterprise Ireland places particular emphasis on increasing competitiveness and growing exports through investment in technology, new product development and developing organisation and management capabilities.

10.4.2 Science, Technology and Innovation

In a world without market failure the production of knowledge through R&D would be left to the market. However, information, whether it be on new product development or process improvement, has the characteristic of being a public good and can therefore be easily acquired by potential imitators if not protected. Left to the market innovative activity would therefore be under provided. It is for this reason that countries both guarantee individual intellectual property rights through copyrights and patents and provide various kinds of public support for R&D.

The strategic importance of research and innovation to Ireland's future development is now recognised by Government. This is reflected in the increase in public sector funding for research and innovation, rising from €196m in 1998 to €342m in 2001. The National Development Plan (NDP) allocated almost €2.5 billion for research, technological development & innovation (RTDI) in recognition of "the evolution of the knowledge based economy where intellect and innovation will determine competitive advantage." The importance of business investment in R&D has also been recognised by the Council, and is included as an indicator in its recent report on *National Progress Indicators*. The Council recognised that in a global economy increasingly driven by technology and technological changes, simply following the lead set by other countries will ultimately limit productivity (NESC, 2002a).

The Government's RTDI strategy, as outlined in the NDP, includes strengthening research capability in third level institutions, increasing linkages between institutions and companies, providing public investment in niche technologies and embedding the culture of R&D in small and medium enterprises (SMEs). The trends in expenditure in R&D are outlined below.

Trends In Expenditure On R&D

Ireland's gross expenditure on research and development increased significantly in the period 1991 to 1999. However, the base from which Ireland has grown is low by international standards. During this period, Ireland's ranking amongst 26 OECD countries, as measured by the proportion of GDP devoted to R&D, improved. But, at 18th position, it remains low. With 1.2 per cent of GDP invested in R&D, Ireland is significantly behind the EU average and well short of the EU target of 3 per cent by 2010. Ireland's spend is below the OECD average (2.21 per cent) and significantly below best performing countries, such as Sweden (3.8 per cent), Finland (3.2 per cent), the US (2.65 per cent) and Japan (2.9 per cent).

TABLE 10.1

R&D EXPENDITURE
Gross expenditure on R&D as a % of GDP and GNP 1991 to 1999

	1991	1993	1995	1997	1999
Gross Expenditure on Research and Development €M	345.4	501.8	667.4	856.2	1,075.6
GERD as a % GNP	1.07	1.30	1.43	1.45	1.42
GERD as a % GDP	0.92	1.16	1.27	1.28	1.21
Ireland's Rank (out of 26 countries) for GERD/GNP ratio	19	17	17	17	17
Ireland's Rank (out of 26 countries) for GERD/GDP ratio	21	18	17	17	18
EU Average (GERD as % GDP)	1.98	1.92	1.81	1.80	1.86
OECD Average					
(GERD as % GDP)	2.32	2.25	2.11	2.16	2.21

Source: *Annual Competitiveness Report* (various), Forfás; *Main Science and Technology Indicators*, OECD (2002b) (Nearest year used where data is not available for a particular year).

Ireland's Business Expenditure on R&D (BERD), at around 0.9 per cent of GDP, is well below the OECD average of 1.5 per cent and has remained static since the mid-1990s. The EU 2001 Enterprise Policy Scoreboard ranked Ireland below 75 per cent of the EU average on BERD as a percentage of GDP and also on the number of high-tech patents.

The process of competitiveness upgrading in both indigenous and FDI firms will be critically dependent on a positive environment for science, technology and innovation and the ability of firms to harness that environment to achieve competitiveness gains.

Spatial Distribution of R&D

Recent work by Andreosso-O'Callaghan *et al*. has looked at the spatial distribution of knowledge creation capability in Ireland (Andreosso-O'Callaghan *et al*., 2002). Knowledge creation capability was defined on the basis of R&D intensity and of knowledge transfer flows. The analysis was carried out on a NUTS II basis on multi-national enterprises. It showed that—despite regional differences in prosperity, and a distinct difference in productivity—being located in the South and East (as opposed to the Border Midlands and West) made no difference to the propensity to engage in R&D or knowledge transfer. Roper analysed the importance of locational factors on firms' innovative activity throughout Ireland and also found no evidence that agglomeration economies represented any specific environment to firms in terms of their probability to innovate (Roper, 2001).

Development of the STI Environment

The Council is concerned at Ireland's low overall level of expenditure on R&D and its poor performance in respect of business R&D. However, it notes that the research environment has been significantly altered by the Government' decision in the NDP to allocate almost €2.5bn to the RTDI priority across all departments and agencies. This reflects its recognition of the emergence of "the knowledge-based economy where intellect and innovation will determine competitive advantage". There is also a role for government in relation to BERD through the application of an appropriate fiscal regime.

Key investments aimed at building Ireland's research capability are now underway through Science Foundation Ireland (SFI), the Programme of Research in Third Level Institutions and through increased support aimed at building R&D capability and capacity in industry, including collaboration between industry and the third level sector.

The Irish Council for Science, Technology and Innovation (ICSTI) is currently engaged in developing a framework for an overarching national policy for research and technological development. Commenting on the need for a new framework Dr Walsh, Chairman of ICSTI noted:

> Given the dramatic increase in research activity that is now taking place, with the establishment of new research entities and the launch of a wide variety of new programmes it is not surprising that there are tensions in the system and an absence of the kind of coherence one might like to expect … There is a clear need for an appropriate overarching framework that will sustain and give coherence to Ireland's combined research effort. There is a need to underpin innovation for economic and social development in Ireland through the improvement of structures and mechanisms for the formulation and implementation of national policy (ICSTI, 26.09.02)

SFI has been established to administer the Technology Foresight Fund, set up to support world-class research in specific areas, initially in ICT and biotechnology. Grants from SFI are made on the basis of competitive calls for funding. Funding support is based solely on performance and merit and researchers supported by SFI enjoy a degree of freedom and autonomy. The Council believes it is vital that SFI not only builds partnerships between researchers and industry but also works in partnership with the other agents of enterprise policy.

Commercialisation of R&D

The NDP included €698m to develop the R&D physical infrastructure of third level institutions in line with national strategic priorities. A further €267m was allocated to the promotion of collaboration networks between the supply side, including colleges, research organisations, agencies and industry. While investment in R&D performance and facilities will create technology, ensuring its commercialisation requires a different set of skills and resources. A recent survey conducted on behalf of Inter-Trade Ireland found that in 21 institutions—including universities, institutes of technology and research institutes—only 16.21 full time equivalents were involved in commercialisation (Ryan and Forde, 2002). Only six organisations in the entire island had a specific staff member to fulfil the function of Intellectual Property (IP) management.

A further important role in commercialisation is carried out by the Programmes in Advanced technologies (PATs) managed by Enterprise Ireland. Several of these provide assistance to college researchers in technology commercialisation. For example, BioResearch Ireland has at least one staff member in five colleges plus a full time patents and licensing manager.

The InterTrade survey identified four perceived barriers to increased commercialisation:

- Funding for patents and associated activities;
- Availability of staff with expertise in IP management;
- Awareness of institutional researchers of IP issues; and
- Commitment within the institution.

Among these, the commitment of the institution was seen as the most significant barrier. Overall, the study found that the commercialisation function across the island was seriously under-resourced in relation to the current investment in R&D, and the expectation of technology generation. The number of FTEs engaged in commercialisation is less than can be found within a single R&D institution in other countries. However, it is clear that, with increasing spend on R&D institutions are actively involved in improving this position.

The Irish Council for Science, Technology and Innovation published a statement on the commercialisation of publicly funded research in 2001. In particular, it recommended the following actions:

- Government departments should ensure that agencies have adequate procedures in place and should commit sufficient resources to the commercialisation of research;
- Funding agencies should encourage commercialisation of the research they sponsor;
- Universities, institutes of technology and research institutes should encourage commercialisation as an option for all researchers;
- The resources available to industrial liaison officers in third level institutes are quite inadequate and resources for technology transfer / commercialisation be increased substantially; and
- There is a particular need for Enterprise Ireland to review and strengthen its role in the provision of early or seed venture capital.

The Council supports increased programmes for commercialisation of research to maximise the return to public investment in R&D and its contribution to Ireland as a knowledge based society.

Business Models and R&D

Individual businesses which engage in research and development face many questions. These include the appropriate balance between basic and applied research, the degree to which research activities should be vertically integrated with manufacturing, the choice between centralisation and de-centralisation and the decision whether to go it alone or set up joint ventures. There is a role for Government in encouraging private sector R&D, firstly through the provision of a skilled workforce, discussed below, but also through the application of an appropriate fiscal regime. A recent report by IBEC suggested a number of possible fiscal measures in this regard. Despite having a sizeable proportion of businesses in technologically advanced industries, business R&D in Ireland remains low by international standards (1.03 per cent of GDP expended by businesses on R&D in 1999, 12th out of 17 countries surveyed). However, the study also showed that a greater percentage of SMEs were engaged in innovation in Ireland than in any other European country (IBEC, 2002).

For maximum value-added to accrue from investment in R&D, coordinated action is required from all players in the national system of innovation. These include business enterprises, the higher education sector, research institutions, enterprise development agencies and the relevant government departments. It will require continued rapid development of R&D capacity and capability in the higher education sector, achievement of world-class research excellence, particularly in strategic areas allied to the needs of industry, and attraction to Ireland of significant R&D activity. Building the R&D capability of industry, and its absorptive capacity to utilise the human and technological outputs of the investment underway, will be key priorities. Research collaboration between industry and the third level sector must become fully embedded. A modern framework for commercialisation of the outputs of publicly funded research must also be developed. Expenditure on R&D policy should be subject to evaluation to ensure value for money. The Council welcomes the establishment of the high level Commission under the auspices of the Irish Council for Science, Technology and Innovation, which is to bring forward proposals for an effectiveness oversight and review mechanism for the national research and innovation systems.

10.4.3 A Skilled Workforce and Quality Employment

The substantial increase in the supply of labour in the 1990s resulted from the combination of demographic factors, increased participation rates and a reversal of many years of net outward migration. The Expert Group on Future Skills Needs predicts that these three factors, which have contributed to extensive growth are likely to decline over the coming years. It forecast labour supply growth to average around 2 per cent (Expert Working group on Future Skills Needs, 2002).

Nevertheless, it is noted that the labour force is likely to increase by 200,000 people by 2007. The ESRI forecasts of employment growth predict the largest increases to be in services sectors, with non-market services employment forecast to rise by 23 per cent and market services by 18 per cent. Within the overall growth forecast, occupational forecasts by FÁS/ESRI to 2005 suggest that the greatest proportional increases will be in managerial, professional and sales positions. These forecasts are indicative of the dominance of the services sector and the increasing demand for knowledge workers.

The National Competitiveness Council's *Annual Competitiveness Report* 2002 shows an 18 per cent increase in enrolment in third-level education in Ireland between 1995 and 1999. It estimates that 22 per cent of 25 to 64 year olds participate in continuing education and training. Meanwhile, Ireland has the highest proportion of university graduates in science in the OECD, with 2,879 per 100,000 persons in the labour force aged between 25 and 34 (National Competitiveness Council, 2002). The position was further improved by 2001, when Ireland has 48 per cent of the population aged 25-34 with some form of third-level education, the second highest in the OECD (OECD, 2002a). Ireland will need to sustain a high proportion of high calibre science graduates if it is to continue to deliver the high value added research and development strategy outlined above and to build a knowledge-based society. Indeed, there is evidence of a decline in numbers opting for science at second level. In addition Ireland will need to develop language skills among its workforce, although progress in this field may be best advanced early in the education process. There is concern among employers that the recent slowdown and maturation in the ICT sector may have prompted some drop in the number of quality applicants opting for IT in courses. It is argued that given the high non-completion rate in computer science additional efforts should be made in this area (see below).

Third Level Education

One key component of a highly skilled and well-qualified workforce is participation in third level education. While the data reviewed above would seem to indicate that Ireland currently fares pretty well in third level participation this masks a number of important issues.

A report jointly commissioned by the Higher Education Authority (HEA) and Conference of Heads of Irish Universities (CHIU) in 2001, undertaken by Malcolm Skilbeck, reviewed international trends and issues in the university sector with particular reference to Ireland (Skilbeck, 2001). The report notes the continuing growth in demand by society for ever higher levels of educational attainment combined with declining numbers of potential new entrants to third level from the traditional pool of school leavers. It notes that universities need to improve their institutional capability, through improved governance and through building and strengthening partnership with other sectors. This partnership should include not only industry and the local community, but also other universities and the Institutes of Technology. The Council also considers it important that Ireland has an integrated system of third level education and believes that the harmonisation of quality standards and a mutual recognition of accreditation, as provided by the Natioanl Qualifications Authority of Ireland, have an important role to play.

One significant issue in the public policy debate has been the non-completion of third level courses. Of the total population of first time entrants to Ireland's seven universities in 1992/93, 67.9 per cent graduated on time, 15.3 per cent graduated late and 16.8 per cent did not complete the course (Morgan *et al*., 2001). Major differences across courses are identified. In law and medicine, which have high entry requirements, the drop out rate was in the region of 7 per cent; in computer science over a quarter (26.9 per cent) did not complete their course. In general, non-completion rates are higher for courses with lower entry requirements. Is should be noted that studies of retention rates are, by their very nature, subject to long lags between the time of college entry and the reporting of data, given that some students may take longer than the initially allocated course time to complete. A separate study of non-completion in three Institutes of Technology (Carlow, Dundalk, Tralee) indicated a non-completion rate of 37 per cent among first year students (Healy *et al*. 1999). Cross country comparisons carried out by the OECD show that Ireland has a significantly above average completion rate for third level students (OECD, 2002a). A significant step is the forthcoming establishment of the Irish Universities Quality Board, which will oversee the procedures for quality assurance and improvement in each university and to verify that they meet best international practice.

An important issue is equality of access to third level education. It is well recognised that there is a positive relationship between parental income or socio-economic group and participation in third-level education. The cost of third-level education is clearly a factor. This includes not only direct costs but also the opportunity cost of earnings foregone. Where the issue is mainly one of cost the abolition of fees, means tested grants and loans for students may go someway to overcoming inequality of access. However, where the issue is one of ingrained inequality in earlier education—including as a result of housing segmentation, schooling quality etc.—or cultural factors, other means have to be employed to encourage wider participation in higher education.

Under the PPF,—an Action Group on Third level Access was established to advise the Minister for Education and Science on the development of Education and Science of a co-ordinated framework to promote access by mature and disadvantaged students and students with disabilities to third level education (Government of Ireland, 2001). The report of that Working Group examined issues relating to access for students from socio-economically disadvantaged backgrounds, students with disabilities, mature students and those from disadvantaged communities. The Working Group made some 78 recommendations to improve access. While the Council has not yet discussed these recommendations in detail, it believes that access to third level education must remain a core priority of government policy to enhance both economic development and a socially inclusive society.

Lifelong Learning

A well qualified workforce will contribute to Ireland's productivity growth and competitiveness. Lifelong learning can contribute not only to improved employment opportunities but also to personal fulfilment and enhanced societal well-being and increasing social inclusion. Lifelong learning is important for Ireland's economic development for at least two reasons. Firstly, given demographic trends it is necessary to encourage older workers to remain in workforce. But many of them have low levels of formal educational attainment. Secondly, there is an increasing need for all employees to up-skill over the course of their career, given the pace of technical change and the need for flexibility within enterprise and between jobs.

The Expert Working Group on Future Skills Needs published a study on Labour Market Participation of the Over 55s in Ireland 2002. It should be noted that most governments and many employers in EU and OECD countries are reversing the support, which they gave in the 1970s and 1980s, to promote early exit from the labour force and are formulating and pursuing policies to encourage greater labour force participation by people over 55. While the long term problem of an ageing workforce is less pressing in Ireland than in other developed countries, increased participation of the over 55s will be a key feature in meeting the demand for labour when, as has been projected, Ireland returns to a tight labour market situation in the medium term. The National Economic and Social Forum will shortly publish work on the issues facing workers aged over 45 in the Irish context.

The European Commission produced a memorandum on Lifelong Learning in December 2000 (European Commission, 2000b). The memorandum emphasised the need to build an inclusive society which offers equal opportunities for access to quality learning throughout life to all people, and in which education and training provision is based first and foremost on the needs and demands of individuals. A consensus was established around four broad and mutually supporting objectives: personal fulfilment, active citizenship, social inclusion and employability/adaptability.

The *Report of the Taskforce on Lifelong Learning* was recently published. It addresses a range of key issues such as the national qualifications framework, guidance and information, access and flexible provision, learning leave and training in employment which are required to upgrade skills and qualifications across the workforce (Government of Ireland, 2002). The Taskforce focused primarily on adult learners. The framework established by the Taskforce has the following essential elements:

- Developing and implementing the National Framework of Qualifications;
- Ensuring basic skills for all;
- Providing comprehensive guidance and information;
- Addressing delivery, access and funding issuers; and
- Better learning opportunities in the workplace and for workers.

The Taskforce concluded that work remained to be done on, among other things the modularisation and accreditation of courses, open and distance learning, learning leave and the removal or reduction of some of the barriers to the funding of part time education for mature students. A report by the European Foundation for the Improvement of Living and Working Conditions noted that Ireland lags many of its European counterparts in the promotion of life-long learning in the context of collective bargaining (European Foundation, 2002c). The Council believes that meeting the challenge of lifelong learning is critical if Ireland is to combine productivity and individual well being. To do so will require innovation on the part of the training and education institutions, employers, the social partners and individuals.

A recent FÁS study on company training found that 79 per cent of Irish companies carried out some form of training. Companies spent €364 million on training in 1999, representing 2.4 per cent of their labour costs. Average expenditure was €600 per employee, or €1450 per person trained. However, employees of larger firms were twice as likely to receive training as employees of small firms. Foreign companies were also more likely to train than indigenous companies, even taking into account the size and sector in which they operated. FÁS recognises that because companies tend to provide training to the better qualified, measures will be needed to encourage training of less well qualified employees. The Council believes that training should be available to all regardless of age, gender or ability and that substantial productivity enhancement can be achieved through even basic training of less skilled people.

It is clear that the overall level of human capital available in Ireland needs to be raised, through programmes of training and education that will facilitate workforce flexibility. In addition its development should be focused on these areas where Ireland is exhibiting skill shortages and which offer the greatest gain for national competitive advantage. The absence of an appropriately qualified workforce could be a significant constraint on the success of the enterprise strategy outlined above. In addition, increasing the opportunity for all to participate in programmes of education and skill upgrading is an important element in a strategy to tackle social exclusion.

10.4. 4 Organisational Performance

After decades in which the focus of analysis centred on the structural weakness of the Irish economy and the structural weakness of Irish enterprises (because of small size, peripheral location and barriers to entry), attention is now turning to organisational capability and performance (NESC, 1998; O'Connell, 2001). This has potentially important implications for how we think about indigenous development and the role of public policy in supporting it.

The practice of business improvement—which can and should deliver mutual gains —rotates around processes of inquiry designed to highlight the reasons why processes do not work as they should and how they might be improved. It is this process of continuous investigation and learning that characterises many of the most successful organisations. The environment in which firms operate now demands that companies successfully engage in this competitive benchmarking of their processes and performance.

Cost competitiveness and improved efficiencies within these kinds of companies are a function of management capability, staff competency, innovation and a general commitment to problem-solving. In these companies the continuous pursuit of corporate survival and improvement means that no stone is left unturned in the search for new ways to approach a problem.

The firm, in this view, is increasingly seen as a problem-solving entity. There are few restrictions placed on the boundaries of this activity; issues of hierarchy, corporate governance and geography are superseded (in the ideal case) by issues of problem-solving capability (ideas such as reputation and skill). The challenge for the organisation is to create the conditions in which to allow the most effective mix of skills to come together to solve a particular problem, while also meeting overall requirements for corporate survival and improvement. Principles like control and trust remain important but the emphasis shifts to problem-solving.

In this setting, there are no simple industrial policy solutions. The solution is complex and specific to each company. Each company examines in detail, and on an ongoing basis, its relative performance across a range of indicators—cost, innovation, quality, customer service, and technology. There is no single model or road to development. However, there is a defining mode of analysis and learning based upon a customised mix of innovative organisational arrangements.

There is wider evidence that this type of organisational change and focus on learning is receiving increasing prominence in the competitiveness agenda of Irish firms (O'Connell, 2000). The Council believes that enterprise policy needs to immerse itself in the process of business improvement. It must continue its evolution to becoming an effective and functional part of local, regional, national and international networks of activities.

This approach to industrial development suggests that cost, quality, high technology, or core and peripheral locations no longer define the limits or possibilities for industrial development. A driving feature underpinning international industrial development is the set of organisational characteristics that enable any given firm to blend cost, quality, technology and location in a manner that will maximise competitive performance.

The tendency to consider policy routes for competitiveness as either low cost or high quality is increasingly superseded by a focus on organisational characteristics. In concrete terms, evidence is now emerging that, with a customised mix of innovative organisational arrangements, it is possible to develop new routes for competitive survival. In broad terms, these routes transcend the dualisms of old: cost versus quality; scale versus innovation; and national versus global.

10.4.5 International Market Access

Given the small size of our domestic market, Ireland is highly export dependent. Consequently, public policies that influence physical access to other countries and continents should be viewed as primary elements of industrial and business development policy. While aviation policy and maritime policy must seek the development of their respective industries, they must also focus on how these sectors can facilitate or inhibit the development of the wider economy. In addition, the proactive promotion of trade opportunities and market access for indigenous industry, especially SMEs, remains vital in continuing to promote export-oriented industry.

While physical access to international markets is obviously vital, the Council believes that virtual access through the reduction and abolition of barriers to trade is equally important. The Council has argued that access to Europe through the Single European Market programme has been a vital contributor to Ireland's economic development, both directly and indirectly through the attraction of FDI. The Council welcomes the enhanced opportunities for the free movement of goods and services that arise from EU enlargement. The Council also wishes to see a satisfactory outcome to ongoing discussions at the World Trade Organisation.

10.4.6 Sectoral Development Policies: Agriculture and Rural Development[3]

Irish agricultural policy is significantly influenced by our membership of the EU and by international agreements, such as those entered into under the auspices of the WTO, negiotiated by the Union on our behalf. Notwithstanding this, it is important that Ireland has its own clear and strategic approach to EU agriculture policy, world trade liberalisation and the role of agriculture in the Irish economy and society.

The State of Irish Agriculture

As outlined in Chapter 1, employment in agriculture has been in long term decline for several decades. In 2002, employment in agriculture, forestry and fisheries stood at approximately 115,000, with some 40,000 additional workers employed in the food sector. However, total labour input on farm work is substantially higher, at over 155,000 (2000 figures on an AWU basis[4]) and almost 250,000 persons are engaged on working on farms either full-or part-time. With total employment in the economy in the region of 1.7 million in 2002, agriculture and related food production still comprise a significant employment base, some 9.7 per cent of the total workforce, and are particularly important in rural areas where agriculture and related activities underpin the rural economy. Consolidation in farm production was enhanced in the 1990s by the overall strength of the economy, which increased the opportunity for agricultural workers to take other employment, often part time employment combined with their agricultural activity.

The structure of Irish agriculture is such that averages mask significant disparities, across regions and between different types of land use. The Census of Agriculture, conducted in 2000, has recently been published by the CSO (CSO, 2002a). Of the 141,527 farms identified, 87,754 were under 30 hectares in size. Some

3. This section draws on a position paper prepared for the Council by Professor Gerry Boyle of NUI Maynooth.

4. The Annual Work Unit (AWU) basis is used to assess the input of farm labour and corresponds to 1,800 hours of work input in any given year.

92,000 family farm holders were over 45 years of age, with 28,000, or almost 20 per cent of the total, being over 65 years of age. Comparing these results with the previous survey (carried out in 1991) shows that in a period of less than a decade there has been relatively rapid consolidation in farming practice in Ireland. This continues the long run trend of a decreasing number of agricultural units with an increasing average size. Average size rose over the period from 26.0 hectares to 31.4 hectares, or in excess of 20 per cent, and there was a 17 per cent decrease in the number of farms from 170,578 to 141,524.

Currently some 39 per cent of family farm holders are over 55 years of age. This represents only a modest improvement over the position in 1975, when 51 per cent of family farm holders were over 55 years of age, in spite of a variety of policies to encourage inter-generational transfer of holdings to younger family members. In a recent survey by Teagasc, only 11 per cent of farmers eligible for the Department of Agriculture Early Retirement Scheme, aged between 55 and 66 years of age, stated that they planned to avail of the scheme. In relation to transfer of the family farm, all farmers, regardless of whether they were eligible for the scheme or not, were asked if they had a successor. Some 50 per cent had a successor, while 16 per cent did not. Other respondents were either too young or were unsure/didn't know. A key structural weakness of Irish agriculture remains the large number of non-viable holdings, often controlled by older farmers. The Council believes that to encourage a healthy and sustainable agriculture sector, keeping younger farmers on the land and structural measures to achieve viable holdings must remain a key area of government policy and support.

TABLE 10.2

A Comparison of Farming based upon the Agricultural Censuses of 1991 and 2002

	1991	2000
Number of Farms	170,578	141,342
Number of Farmers[1]	124,746	78,723
Average Farm Size (ha)	26.0	31.4
Average ESU	11.6	20.7
Farms engaged in Organic Production	574	1,558
Farms engaged in non-agricultural activity	1,917	6,996

Source: Central Statistics Office: Census of Agriculture (1994, 2003).
Note: 1. Based upon those who have farming as their sole occupation. It should be noted that while the decline of those in sole occupation was some 46,000 there was a corresponding increase in those who acknowledged farming as their main occupation of 10,000 to 19,643. A further 42,976 were listed as having farming as a subsidiary occupation.

An assessment of farm income is not straightforward but rather can be open to a number of differing interpretations. Farm income must reward farmers not solely for their labour input, but also provide a return based upon capital employed in the business, including the opportunity cost of land utilisation. An EU-wide system known as the '*Community Farm Typology'* is used to classify farms based on the type of farming activity involved, and also to derive a measure of the economic size of farms. This is done by applying standard economic coefficients per unit area of crops or per head of livestock, known as Standard Gross Margin (SGM) coefficients. The SGM takes account of specific variable costs and is a proxy for the potential gross value added per unit of area or per head of livestock. The total SGM is a value which determines the economic size of the farm. It is expressed in terms of an EU unit of measure, the European Size Unit (ESU). The ESU used in the 2000 Census corresponds to a value of €1,200 calculated using the 1996 SGMs. Further details on the calculation of the ESU are given in the Census of Agriculture.

When assessing farm income on the basis of the 2000 Household Budget Survey (that is on a household basis), almost 60 per cent of household income now comes from off-farm sources. Farm households had a weekly disposable income of €160 per household member, compared with €149 for non-farm rural households and €195 for urban households. The NFS estimates that average farm income (excluding off-farm income) was €15,840 in 2001, although there are large variations depending upon the size of farm and the system of farming. Full-time farms, as defined by Teagasc, had an average income of €30,959 and part-time farms €5,948. The National Farm Survey carried out by Teagasc estimates that in the case of 45 per cent of farms either the holder and/or the spouse had an off farm job; and in the case of 64 per cent of farms either the holder or the spouse had some form of off-farm income. However, the same survey shows that two thirds of farmers are full time farmers in terms of not having an off-farm job; their average farm income was €19,200 in 2001, while the average farm income of part-time farmers was about €9,000. The securing of off-farm employment by farmers is now a well-established pattern of adjustment in Irish agriculture.

The European Model of Agriculture

The 'European Model' of agriculture enshrines what may be regarded as the principle of 'conditional competitiveness'. This principle implies that European agriculture and food production must be globally competitive, but this must be achieved within the constraints of animal welfare standards, production practices (such as the non-use of artificial growth promoters), environmental standards and food traceability that are broadly acceptable to European taxpayers and consumers. While it may be reasonable to expect that in the long run the market will return a premium for food products that are produced according to these standards, it is clear that in the short to medium run European producers will be at a severe competitive disadvantage if corrective subsides (in the form of Common Agricultural Policy direct payments) are not permitted.

A formal statement on the European Model appeared in the text of *Agenda 2000*. The model comprises three interrelated pillars:

- Competitive production and sale of quality and safe products in the international marketplace;
- An agricultural system which is environmentally sustainable; and
- A menu of policies to ensure the diversity of agriculture, underpinning vibrant and active rural communities.

It is clear, therefore, that while the primary role of agriculture in the EU is the production of high-quality food, it fulfils other important roles also and encompasses rural and environmental custodianship. The regional economy dimension has many aspects but the goal is clear—to maintain and foster vibrant rural areas that can stand on their own feet economically without a drip feed of subsidies. Agriculture performs this role mainly as a supplier of output for a thriving processing sector and as a major purchaser of inputs. As agricultural households diversify into areas such as agri-tourism and off-farm activities, the need for such employment opportunities and their supply will form a key requirement of the future.

Europe's high population density implies the need for Europeans to be more vigilant about farming practices which could damage the environment. This vigilance provides a rationale on public good grounds for strictures on agricultural activity that then impinge on international competitiveness. It also provides a rationale for the subsidisation of environmentally-friendly farming practices. Small family-farm structures confer a pattern on the European landscape that is valued by the non-farming population of Europe. However, if small scale producers are to be retained in sufficient numbers to maintain the fabric of rural communities then very significant changes in rural development policies will have to be considered which are outside the remit of traditional agricultural policies.

European producers, who would be expected to deliver on the competitive goal in the 'European Model', are not of sufficient scale to cushion the impact of the profit squeeze to the same degree as competitor countries. In addition, with small scale producers benefiting from direct payments and rural development measures, this implies that land prices will remain higher than otherwise may have been the case. This will close off one of the avenues that commercial producers wishing to enter the market or to expand operations might otherwise have had open to them to cushion the profit squeeze through falling land prices.

The real tension in the model, however, is the commitment to this 'conditional competitiveness', namely competitive production which internalises concerns about food safety, quality etc. Either EU producers are rewarded for their adherence to these standards through direct payments or other measures or the market (i.e. the European consumer) must be prepared to pay adequate compensation.

Agricultural Policy Reforms

Based upon the European model, the Fischler proposals in the 2002 Mid-Term Review of the CAP announced that future direct payments would be effectively 'decoupled' from production (i.e. direct payments would be independent of current production levels). This differs from the traditional forms of intervention through price support for produce and restrictions in the market place such as quotas. The implications of decoupling would probably be to reduce the levels of agricultural production and this may in turn impact negatively on output, employment and profitability levels in the food-processing sector.

The Fischler proposals seek to enhance the competitiveness of EU agriculture, to promote a more market oriented, sustainable agriculture and to provide a better balance of support and strengthen rural development. The European Commission believes that the introduction of de-coupling will allow the EU to maximise its negotiating capital in order to achieve its WTO objectives.

In the Fischler proposals, the basis for direct payments would be to compensate farmers for the provision of environmental goods and services and custodianship. Payments would be area-based in nature but would protect farm incomes, or at least provide for a smooth and prolonged transition, as they would be determined upon the land tilled and payments received by individual farmers in specified 'reference years'. The proposals include the 'modulation' of payments, whereby direct support is reduced on a phased basis from 2006–2013. The payments will reward those farmers who have been most productive and are likely to be able to be transferred with or without the land.

A significant consequence of the Fischler proposals is that a clear distinction will become apparent between policies that address the economic well-being of commercial farming activity and policies which are targeted towards environmental, equity and social concerns. The Fischler proposals on decoupling of direct payments from production include proposals for an environmental audit of farms.

The European Commission believes that the proposed adjustments in CAP policy measures will permit maximum flexibility in production decisions, will greatly simplify the means by which support is provided to farmers while guaranteeing their income stability and will promote sustainable farming practices (European Commission, 2003). The European Commission has carried out an impact assessment of the proposals. While the effect of the proposals varies depending upon individual circumstances, the Commission believes that, taking into account the effects of rural development, farm income would be 0.3 per cent higher than under the Agenda 2000 policies.

The Minister for Agriculture has proposed that the EU Commission should undertake a comprehensive impact analysis of the decoupling element of the Fischler proposals. He also recommended, as part of this analysis, that a full review of the farm income situation within the EU be undertaken. The Council supports this proposal but wishes to see it extended to encompass the food and agribusiness sectors. It also recommends that a similar analysis be carried out on the Irish agricultural and food sector to inform the strategy that should be pursued by Ireland.

Rural Development

In its 1999 Strategy the Council welcomed the broad approach to rural development adopted in the rural development White Paper published in the same year. The challenges facing rural areas are clearly set out in the White Paper. They range from the necessity for increasing numbers of farm families to supplement their farming income with off farm sources to the on-going issue of rural de-population. Rural areas can also be afflicted by social problems relating to access to services to older persons, women and teenagers.

Rural development must be seen in the context of the NSS which envisages an urban-rural relationship hierarchy whereby urban development can help support the rural hinterland and vice versa. The NSS also emphasises the importance of a hierarchy of access to services and social infrastructure including those services which should be available to all households, villages and small towns. The NSS recognises that "policies designed to consolidate the small town or village, with the support for example of small housing developments and local enterprise units, would assist in sustaining them and their store of social and other services into the future." In this sense much of what might be classified as rural development policy might also come under the category of public infrastructure provision. The NSS recognises that there are issues of access to services in more remote rural areas which are outside the scope of its remit and must be addressed by the relevant sectoral policy providers.

Clearly the issue of rural housing and rural settlement patterns is key to the ongoing development of sustainable rural communities. In Chapter 9, the Council commented briefly on the dispersed village pattern of development that characterises Ireland's rural community and the need for the planning system, in as far as is possible, to accommodate rural generated housing needs. The issue of rural settlement will be further explored in the Council's forthcoming study on housing and land.

In addition there are specific measures targeted at certain specific rural problems. The Council supports on-going development in those areas most subject to rural de-population through the CLÁR programme and other measures addressed to tackle the issue of rural poverty, area based partnerships and the LEADER programme. The

Council reconfirms its belief expressed in its 1999 *Strategy* that policy should be balanced and equitable in terms of the treatment of urban and rural areas.

Much of what has been categorised as rural development in fact takes the form of an agricultural based payment such as the Rural Environmental Protection Scheme or payments for forestry. The key to ongoing rural development lies in diversification of activity away from traditional agricultural activity. Such activities include the growing market for rural based tourism discussed below while others include diversification into energy production, organic production or specialist food production such as farmhouse cheese or high quality preserves. However, many of these are inherently niche sectors with small markets and the key to sustainable rural development will lie more in the ability to foster small scale industrial development through targeted supports and the deployment of the necessary infrastructure.

Agriculture – Conclusions

The Council supports the need to develop a profitable and competitively viable agriculture and food sector. The Council believes that there is substantial capacity in the twin policy pillars of 'price and market' and 'structural' policies to deliver ongoing development of the sector. In particular the Council supports ongoing Government intervention through research and advisory services, including programmes of agricultural training, to further improve competitiveness and measures to support increased diversity in rural and agricultural development combined with enhanced environmental sustainability.

10.4.7 Sectoral Development Policies: Tourism

Given the climatic conditions and its relatively peripheral position, Ireland has traditionally 'punched above its weight' in the tourism industry. Tourism is a significant employer in Ireland, sustaining close to 140,000 jobs, up from 82,000 in 1990, and it is estimated that the hotels and guesthouses sector alone contributes 2.2 per cent of GNP (Department of Tourism, 2002; Irish Hotels Federation, 2001). The total number of visits to Ireland has risen from 5.1 million in 1997 to 6.1 million in 2001, an increase of almost 20 per cent and the estimates of the associated overseas expenditure (excluding international fares) have risen from €2 million to €2.9 million, a 45 per cent increase (CSO, 2002b). This equates to an increase in revenue per visitor from €384 in 1997 to €482 in 2001, a 26 per cent increase over the period. In addition, a further €222 million was earned from cross-border tourism and domestic tourism contributed earnings of over €1.2 billion (Bord Fáilte, 2002; Department of Tourism, 2002; CSO, 2002b).

In 2001, the tourist industry was subject to two unforeseeable negative shocks: visitor restrictions due to the Foot and Mouth Disease and the terrorism attacks in the United States. The overall number of overseas visitors to Ireland fell by some 5 per cent in 2001 over 2000 levels. The effects of the second came to light in 2002 with a 17% fall in visitor numbers from the USA and Canada in the first quarter of 2002. Visitors from North America represent one of the most lucrative segments of the tourism industry with an average spend of €781 per visitor in 2001.

The most recent figures available relate to the numbers of visitors for the third quarter of 2002 which encouragingly show an overall increase of 1 per cent on the previous year despite the traumatic events in 2001. Meanwhile earnings from visitors for the quarter rose by 6 per cent from 2001, and 19 percent from 2000 levels, which by many in the tourism industry was considered a bumper year. Interestingly, however, the third quarter of 2002 was the first quarter ever to see expenditure by Irish residents abroad exceed earnings from visitors to Ireland.

Tourism is an internationally traded service, and subject to the wide-ranging pressures associated with the provision of goods in the traded sector. The cost competitiveness of Irish tourism will therefore depend upon input costs, and in particular wages and currency fluctuations. Productivity growth is necessarily more limited in the service sector where opportunities for technological progress are fewer and therefore the tourism industry cannot compensate for high levels of wage increases with associated productivity improvement. The tourism industry consumes a relatively high proportion of low-skilled labour which has been subject to significant wage inflation in recent years itself, associated with labour market tightness. However, this particular cost pressure has eased somewhat in recent times and wage levels in Accommodation and Catering, a significant proportion of the employment engaged in tourism, were virtually static from Q1 2001 to Q1 2002 (CSO, 2002).

Tourism will also have benefited from the relative weakness of the euro to the extent that tourists were sourced outside of the euro area and the statistics for 2001 show that only 28 per cent of tourist revenue was sourced from other European countries. However, combined with the relative recent weakness in the US dollar which accounted for another 24 per cent of tourism revenue in 2001 over 50 per cent of tourism revenue is immune to recent euro weakness. Combined with the fact that the euro is beginning to show signs of modest appreciation against Sterling it would appear that the tourism industry has suffered and is suffering a potential decline in overall cost competitiveness.

The Irish Tourist Industry Confederation launched *A Recovery Programme for Tourism* in February 2002 following the events of 2001. In particular it focused on the need to return Irish tourism to the growth targets set out in the NDP, to place a greater focus on sustainable tourism growth by attracting those who stay longer and spend more, and the need for a year round marketing presence in Britain, continued investment in North America and a reappraisal of Ireland's positioning and market effectiveness in key European markets. To achieve these goals they put forward programmes in marketing, access and business relief measures such as tax breaks.

Like other goods the market in tourism is governed by the supply and demand balance, and the lags in adjustment. One significant component of supply is changes in the number of beds available and their occupancy rates. A further proxy for this is the level of construction activity in the tourism sector. The *Construction Industry Review 2001* notes that the volume of construction output in the tourism sector is forecast to fall by 21.9 per cent in 2002 following decreases of 19.9 per cent and 47.9 per cent in 2000 and 2001 respectively. However, given the substantial increases in the preceding years the level of output is still 8 per cent above the level in 1997 and the number of hotel rooms has grown by some 53 per cent since 1995 while guesthouse capacity has grown by 43 per cent (Department of the Environment and Local Government, 2002d; Irish Hotels Federation, 2001). To translate these changes into numbers, it is estimated that 5,500 hotel rooms were added to the stock in 1999, 1,700 in 2000, around 2,000 in 2001 and only 140 in 2002. This should facilitate some overall improvement in the occupancy level assuming the growth in visitor numbers experienced in the first quarter can be maintained.

The recently published consultancy report for the Irish Tourism Industry Confederation addresses the need for a future strategy for tourism. It shows a ‘deep deterioration’ in price competitiveness in the Irish tourism industry (Irish Tourism Industry Confederation, 2002). The report recommends the completion of a tourism development strategy which would focus on price competitiveness, access transport, enterprise development and quality of service. In addition, the viability of developing new tourism regions should be examined.

In the early chapters of this report, the Council has noted that rapid extensive growth can bring certain problems, given the vulnerabilities of Ireland’s economic situation. This is particularly the case in tourism where much of what is marketed as the Irish tourist experience is our natural landscape, culture and Irish hospitality. Rapid growth in tourist numbers alone may inhibit the delivery of this ‘core’ product, with the possibility of saturation, particularly in centres of rural tourism, such as Westport, Killarney, the Burren or Cashel. In addition, the quality of the product (landscape, culture and hospitality) might be diluted as a result of rapid growth of the number of operators and the need to fill job vacancies rapidly.

The previous chapter examined the important role of trans-national infrastructure. One of the most important elements of a successful tourism policy is international access. A new market in airline access has been established with the advent of the low cost carrier. This provides not only increased access for foreign nationals to visit Ireland but also opportunities for Irish residents to travel overseas. The number of air passengers arriving in Ireland has risen from 5.39 million in 1996 to 8.24 million in 2000. The vast majority of these air passengers arrive at Dublin airport. Access to regional locations will have to be improved if there is to be an increased spread of tourism beyond the concentration emerging in Dublin.

It is apparent that the regional distribution of tourism has been skewed by the superior performance of Dublin compared with other regions. For example Dublin attracted just 22 per cent of overseas tourism revenue in 1986 but this had risen to over 35 per cent by 2001 (Deegan and Dineen, 2000: updated by NESC secretariat). Attendance at visitor attractions collated by Bord Fáilte also indicate that four out of the top five are located in Dublin. Yet, it is not so much that these are visitor attractions that attract people to Dublin in the first place but rather sites they visit once they are in situ. A report by Fitzpatrick Associates took up the challenge of not only extending the spatial spread of tourism but also extending the season during which visitors travelled to Ireland (Fitzpatrick Associates, 2001). Their report recommended a three-track approach to the spatial balance of tourism. Firstly, all areas should be developed to their natural tourism potential reflecting genuine market needs. This includes sustaining rather than reducing the role of existing major centres. The study noted that our existing top tourist areas are Ireland's key tourist assets, not tourism 'problems' and we would 'downgrade them at our peril'. Secondly, there should be the designation of a small number of new tourism centres with focus on the BMW region. Thirdly, policies should be embraced which maximise the spread of benefits out from centres via ancillary attractions such as day trips, pilot projects etc. If these proposals were adopted they would contribute to the achievement of the goals of the NSS.

With regard to the seasonal spread about 25 per cent of tourism revenue is earned in the peak season of July-August, 30 per cent in the 'shoulder season' and 43 per cent off-peak. However, this masks the fact that the revenue numbers include trips to visit friends and relatives and for business, in addition to those engaged in tourism activities per se. It is clear, however, that the increasing short or weekend breaks, both in the domestic market and aided by easy and affordable air access may increase the seasonal spread of tourism but exacerbate its concentration in Dublin.

Tourism makes a vital contribution to the local economy, particularly in rural areas. However, it is important that tourism dovetails with the local economy, both from the perspective of the local residents and for full enjoyment of the tourist experience. The Council believes that Ireland should continue a strategy that focuses less on visitor numbers and more on the revenue to be derived from visitors, particularly in rural areas.

Marketing is all about product placement. Where tourism is concerned, however, the product being marketed is Ireland itself and if such marketing were left to individual agents would result not only in a duplication of costs but also an incentive to free ride on others' actions. Moreover visitors are likely to base their decision to travel to Ireland on a wide variety of criteria including cost, quality of service, entertainment on offer, places to see and overall ambience. It is therefore important that Ireland has a prominent overall marketing agency.

The training of personnel in key customer service attributes, and the reduction of staff turnover in the hospitality trade remains one of the key challenges for the tourism industry if it is to deliver on the high value-added strategy the Council envisages.

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