5 Transcending Limitations: how Ireland's Economy Emerged

Amanda DELAMER
Solid-IT, Austria

5.1 Abstract

Emerging from the struggle that marked its birth as a small independent state a century ago, Ireland prospered to become one of Europe's economic success stories as the new millennium dawned. Benefitting from membership of the European Union over almost five decades until now and having attracted billions of euro in foreign direct investment, the country has been transformed from a largely agricultural society into a modern, high-technology economy thriving on a diversified world-wide export market. This paper highlights the determining factors that played a role in Ireland’s overcoming various drawbacks, to thus become the flourishing and more resilient small open economy it is today. Having embraced digitalization and innovation as a foundation for its evolution, the country faces further inherent challenges to sustain its economic model, both with regard to domestic issues and in a more global setting. A closer look is taken at what the significant needs and priorities are that the Irish economy must now continue to address.

Keywords: Ireland, economy, EU, innovation, Celtic Tiger

5.2 Introduction

Ireland’s geography and history have played important roles in defining the nation that was reborn a century ago. It is Europe’s third largest island and is separated from Great Britain to the east by the narrow Irish Sea and from America to the west by the Atlantic Ocean. Often referred to as the Emerald Isle because of its lush green landscapes, it owes these to abundant moist air and a relatively temperate climate resulting from the warming currents of the Gulf Stream. The origins of Ireland’s own culture and language are predominantly Celtic with later strong influences including the coming of Christianity, Viking invasions, Norman colonisation and English suppression.

Following centuries of British rule and struggles for independence, a political division and partitioning of the island of Ireland was formally implemented in 1922. The larger part of it is now officially referred to as the country *Ireland* (also called Éire or the Republic of Ireland), as shown in Fig.1. The remainder is *Northern Ireland*, which is a part of the UK (United Kingdom of Great Britain and Northern Ireland).

Expanding its largely agricultural economy to modernise and embrace new industries was a slow process for newly independent Ireland, due to various circumstances. Still one of the poorest countries in Western Europe at the start of the 1990s, with high levels of unemployment, inflation and emigration, the country then prospered to enjoy a period of rapid economic growth fuelled by foreign direct investment. The boom was curbed in 2007 with the bursting of an untenable property bubble, which led to severe economic recession and major fallout as the global financial crisis took hold. After benefitting from a substantial bailout deal, the Irish economy recovered by 2014 to resume growth at a robust pace that has been sustained. This paper outlines the development phases of the Irish economy, focussing on the major causes and effects that determined how in recent years it soared, to crash and then recover to thrive again.

IRELAND

- Population: 4 921 500
- Area: 70 273 km²
- Languages: English, Irish

Figure 1: *Aerial view of the island of Ireland*
(Source: satellite image from https://visibleearth.nasa.gov/)

5.3 A Timeline of the Modern Irish Economy

5.3.1 Early Years

When Ireland gained independence in the 1920s the economy was predominantly based on traditional agriculture with small farms that were often cost-ineffective. The financial situation was further weakened in the early turbulent years of the state, until greater political stability was achieved. In the 1930s, the new government embarked on a protectionist policy in economic dealings, introducing tariffs on a wide range of imported goods, primarily from the UK, the country's main trading partner. However, instead of nurturing native industries, this tactic led to economic isolation, stifling trade and prolonging widespread emigration. The constricting policy was reversed from 1960 and Ireland slowly embraced the industrial world, to progressively become an open economy [1].

To help stimulate the economy, the Industrial Development Authority (IDA) Ireland was established as a national agency responsible for the attraction and retention of vital inward foreign direct investment (FDI). It sought out innovative modern industries and promoted Ireland as a location to investors from abroad. These stood to benefit from the attractions of both the availability of plentiful English-speaking labour at a relatively low-cost as well as full exemption, at that time, from corporation tax on all profits from exports. The IDA concentrated on companies that represented the future, displaying high technology, high output and high skills. Main targets included the computer industry, pharmaceuticals and medical technology followed by international services. In the decades that followed, the proposals on offer proved to be of greatest interest to multinationals from the US. Pfizer, which established its first plant in 1969, was one of over 350 overseas companies that had set up in Ireland by 1970. Today, it still is the country's leading investor and employer in the pharmaceutical sector [2].

5.3.2 EU Membership

Adjusting to becoming a more open market took time but better prepared Ireland for a major milestone in 1973, namely joining the European Economic Community, now known as the European Union (EU). Becoming part of the EU's Single Market made it easier for Irish businesses to trade on both European and international markets, reducing an excessive commercial reliance on the UK and a dependence on it as a gateway to the continent of Europe. At that time Ireland's economy was still highly dependent on agriculture with almost a quarter (24%) of the working population employed in the sector [3]. Support received from the Common Agricultural Policy (CAP), the Structural Funds and the Cohesion Fund benefitted Ireland, both in social and in economic terms. These shared EU funds aim to help reduce regional disparities in income, wealth and opportunities among Member States. While emerging as an economy and before the state transitioned to becoming a net contributor, Ireland's total net gain from EU budgets from 1976 on was €44.6 bn [4, 5]. Investments helped to strengthen the sustainability of agriculture, to modernise agri-food industries, support major road and railway infrastructure projects, improve education standards and tackle chronic youth unemployment [6].

5.3.3 The Celtic Tiger and its Origins

Despite considerable boosts, underlying economic problems in Ireland of the 1970s persisted into the next decade. This coincided with a severe global economic recession in the early 1980s as well as a prolongation of the shadow cast over Ireland by ongoing violence in neighbouring Northern Ireland. Ensuing economic decline brought the return of high unemployment, a renewed rise in emigration and steady worsening of the public finances until the government ultimately succeeded in restructuring state bodies and tax regimes to resolve the budgetary crises. While cutting back on spending, the government took steps to promote business investment. A notable example was the adoption of a proposal to create the International Financial Services Centre (IFSC) in the old Docklands area of Dublin. The successful development of the IFSC and its on-going expansion are evidence of the strength of the well-established co-operation between business interests and all parts of the Irish state system [7]. The EU granted a temporary waiver of State-aid rules, which ensure fair trading and competition among the EU-28, to allow Ireland a reduced rate of 10% taxation in this special economic zone until the agreement was phased out between 1996 and 1998. Ireland subsequently reduced its standard corporate-tax rate from 40% to 12.5%, making it one of the lowest in the EU [8]. With the added advantages of being the only English-speaking nation in the euro area and offering the availability of a young, highly-educated workforce, Ireland's transformation to become a knowledge-based economy was accelerated.

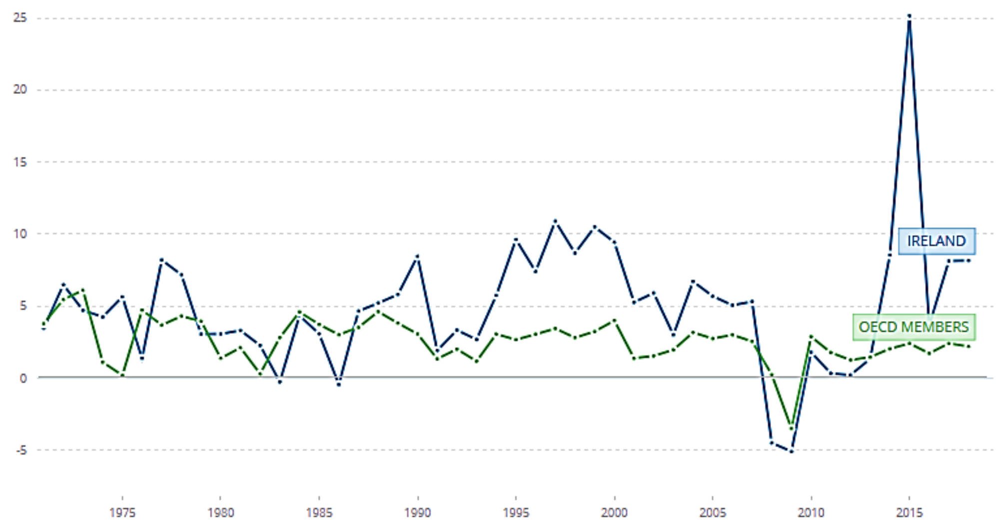

Figure 2: *GDP growth (annual %) Ireland and OECD-average*
(Source: https://data.worldbank.org/indicator/NY.GDP.MKTP.KD.ZG?locations=IE-OE)

Real national income per capita rose from less than 65% of the EU average to achieve rough parity by the end of the 1990s. Unemployment tumbled at a rate without precedent in Irish history from a high of 17% in 1987 to less than 4% in the early years of the new millennium. Numbers at work expanded by more than 50%. The peace dividend of the Good Friday

Agreement signed in 1998 in Northern Ireland began to pay off, encouraging new synergy in various sectors between both parts of the island. [9]

Fig. 2 indicates the period of rapid economic expansion in the mid-1990s to the mid-2000s, which earned Ireland's economy of the time the name of the Celtic Tiger[9], and compares it to the OECD[10] average. From 1995 to 2000, Gross Domestic Product (GDP) growth rate was a record almost 10% annually; it then slowed to about half of that from 2001 to 2007 [10]. During this growth period, the Irish GDP per capita rose dramatically to equal, then eventually surpass, that of all but one state in Western Europe. The exceptional GDP-growth spike of 2015 in Ireland is discussed in more detail in the section 'Recovery since 2014' below.

Over time more than a thousand FDI giants, mostly American global companies, made Ireland the hub of their European operations, including names such as Google, HP, Apple, IBM, Facebook, PayPal, Microsoft, Yahoo, eBay, AOL, Twitter and Intel. Benefitting from the presence of a high concentration of these multinational corporations relative to the size of its domestic market, Ireland ultimately became the world leading exporter of ICT[11] services providing up to 14% of services worldwide in recent years [11].

The growing success of the economy, fuelled by FDI, encouraged entrepreneurship countrywide, allowing people to embrace change and try things differently. An innate openness enhanced a certain ease of doing business and a readiness to engage when opportunities did arise, to release the potential of the Irish economy. Whether in smaller undertakings or with a new business model for an existing industry, innovation was nurtured at all levels. Success stories emerged, like Ryanair pioneering no-frills, cut-price air travel within Europe to carry 800 000 passengers annually 25 years ago and over 140 million now. [12]

5.3.4 Collapse and Bailout

By 2001, the benefits of new jobs created by intensive foreign investment had begun to slow. Still focussed on high growth, Ireland's political leadership and its banking sector turned to the mortgage and construction industries to maintain momentum, causing housing prices to double from 2000 to 2006. Prices continued to soar as tax incentives and laissez-faire lending regulations allowed a massive property bubble to form. The boom ran out of steam in 2007, the building industry collapsed and the country fell into a recession in the wake of the global financial crisis of 2008. The Irish government fatefully guaranteed the liabilities of the country's six major banks for two years until September 2010 and pumped massive sums into the failing sector. As the financial crisis took hold, there was the human toll of a surge in emigration, unemployment that soared to 15% by 2012 and crippling mortgages on negative equity [13].

In late 2010, an international bailout loan of €67.5 bn was negotiated with the EU and the International Monetary Fund (IMF). Ireland's own resources contributed a further €17.5 bn to the Programme through the treasury cash buffer and investments from the national pension reserve funds. This financing, coupled with very strict austerity measures and restructuring, rescued Ireland and allowed the economy to recover at a remarkable pace. The GDP growth rate had rebounded to 4.8% by 2014, by which time the bailout scheme had been exited [14].

5.3.5 Recovery since 2014

The strong recovery of the economy continued and confidence in it grew again. The construction industry began to expand once more and the banks benefitted from a robust, more fit-for-purpose, regulatory framework. A new tax relief in 2015 led to a rush of multinationals transferring Intellectual Property (IP) assets to Ireland. To capitalise on a minimal tax rate, Apple adjusted its accounting procedures to run all European sales through its Irish

[9] UK economist Kevin Gardiner, head of global equity strategy at the investment banking unit of global bank HSBC, coined the term Celtic Tiger in 1994, comparing Ireland's economic take-off to the Asian tiger economies.

[10] The Organisation for Economic Co-operation and Development (OECD) has 35 member states worldwide

[11] ICT services include information, computer and telecommunications

office. This distorted the country's official statistics to produce an annual increase in GDP of 26% (cf. Fig.2). Following State-aid investigations by the European Commission (EC) concerning the tax-ruling practices of Member States, Apple was ordered in this case to pay €13 bn in arrears [15]. Appeals are still pending but the tax loophole was duly closed. The Central Bank of Ireland has since recommended the use of modified Gross National Income (GNI*)[12], which is adjusted and excludes the profits that foreign firms remit back to their own countries, as an arguably more meaningful instrument for economic surveillance in Ireland. In 2018, Ireland's real GDP grew by 6.7% to reach an annual total of €312 bn. A breakdown of the percentage per sector for the economy is detailed in Fig. 3. GNI* in 2018 was estimated at €197.5 bn [16].

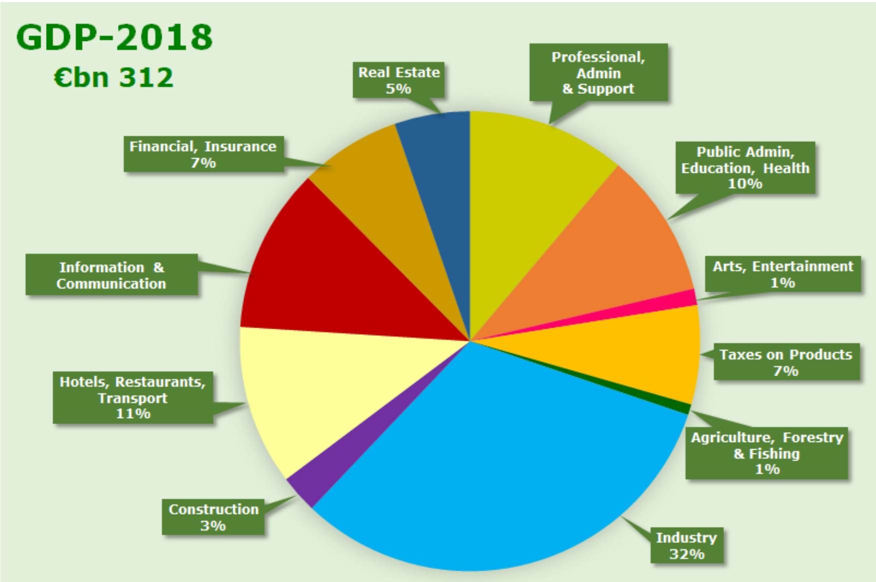

Figure 3: *Breakdown of Ireland's GDP in 2018*
(Source: data from Central Statistics Office, https://www.cso.ie/)

5.4 Prosperity and Population Correlation

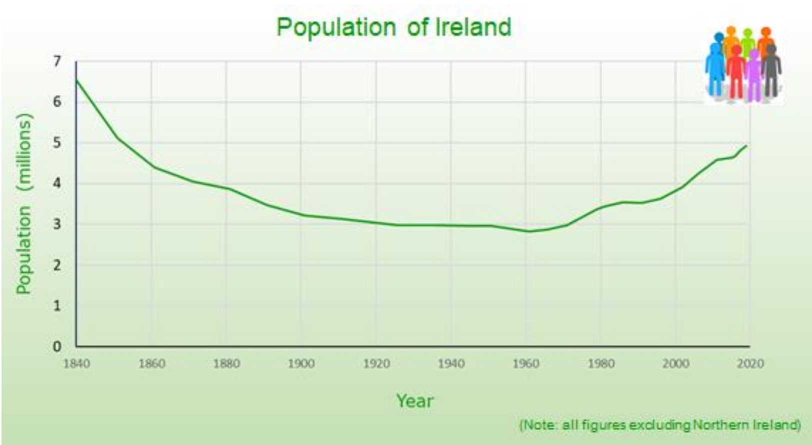

Figure 4: *Progression of the population of Ireland*
(Source: Central Statistics Office data, https://www.cso.ie/en/census/censusthroughhistory/)

[12] Modified GNI (GNI*) is an indicator that was recommended by the Economic Statistics Review Group in 2016. It is designed to exclude globalisation effects, which are disproportionally impacting the measurement of the size of the Irish economy without being considered relevant in explaining the resources available to the domestic population.

A correlation between economic progress and population levels in the longer term in Ireland is clearly shown in Fig.4. In the wake of a devastating famine in the mid-19th century the population of 6.5 million people[13] fell dramatically. It continued to decrease for over a century as many were forced to emigrate in search of employment prospects elsewhere, most typically in the UK or the US. Despite high birth rates, a population low of close to 2.8 million was reached in 1961 [17]. Thereafter, as the economy improved, numbers had by 1986 increased again by 25%. The depressed conditions in the 1980s reversed the growth trend once more, due to a gross emigration in that decade of some 450 000 people from a total population of approximately 3.5 million [18]. This was a disheartening drain of human capital.

During the prosperous Celtic Tiger years, the population rose again steadily. To meet labour demands, a phenomenon new to Ireland developed: significant immigration, comprising both returning Irish and an inflow of non-nationals. Today's population of 4.9 million includes over 12% non-Irish residents, mainly from the UK and other EU countries. Studies show Ireland to be the EU-28's most youthful country and to have the largest proportion of children aged 0-14 years. In 2016, some 39.5% of the population was aged 0-29 years, the EU average being 33%. The workforce currently available in Ireland is well-educated with more than half of those aged 24-34 years having third-level qualifications. [19,20]

5.5 Challenges to the Economy

Notable challenges to the economy remain. Government efforts are concentrated in: transitioning to a low-carbon economy, augmenting productivity, increasing labour-force participation, enhancing skills and improving both the health services and the supply of housing [21]. Despite progress, the homelessness rate since the recession continues to rise with some households experiencing poverty and social exclusion. The paralysis of the construction industry over several years, while the population continued to increase, gave rise to excess demand for accommodation in large cities and a resulting housing crisis, especially in Dublin. Among major European cities, average rents there are second only to London [22].

Brexit looming on the horizon leaves Ireland deeply concerned, especially for the agri-food export industry, where additional tariffs or certificates may become necessary to continue trading with the UK. A hard EU border to Northern Ireland would damage mutual trade benefits across many sectors and could compromise the peace agreement implemented there. The threatened no-deal scenario would be highly disruptive, although the Irish government's extensive preparedness and contingency efforts should help mitigate negative effects [23]. Recent observations and studies suggest that the Irish economy, while continuing to grow strongly, has already absorbed some of Brexit's adverse impact over the last three years [24]. Furthermore, a significant overhang of public debt remains since the crash and bailout years. A prudent approach to managing the public finances will continue to be required, to reduce public indebtedness to lower and safer levels, particularly given the degree of integration into the globalized economy and susceptibility to fluctuations there.

5.6 Conclusions

In embracing technological and other transformational change, the economy of Ireland has demonstrated itself to be resilient, innovative, and globally connected. It has thus emerged to find its own unique position within the greater union of Europe, as a small but open and export-oriented economy. These same assets also make for vulnerability, due to a dependency on FDI, international trade and influences of global markets. After some hard lessons learned, the appropriate fiscal policies implemented over recent years have placed Ireland in a stronger position to better weather current challenges and to continue to reduce the significant debt burden acquired during the financial crisis of a decade ago. Prospects for the Irish economy

[13] Figure does not include the population of today's Northern Ireland

are good today, although clouded with some uncertainty, particularly concerning Brexit. Paradoxically, risks associated with that schism may also represent opportunities in the future for a country that has proven adept at transcending limitations and expectations.

5.7 References

[1] Bradley, John. "The history of economic development in Ireland, North and South." Proceedings-British Academy, vol. 98, pp. 35-68. Oxford University Press Inc., 1999. https://www.thebritishacademy.ac.uk/sites/default/files/98p035.pdf, accessed 29th August 2019

[2] Industrial Development Authority (IDA) Ireland, https://www.idaireland.com/about-ida/history, accessed 29th Aug 2019

[3] European Commission, https://ec.europa.eu/ireland/about-us/impact-of-EU-membership-on-Ireland_en, accessed 29th August 2019

[4] European Commission, Impact of EU membership on Ireland, https://ec.europa.eu/ireland/about-us/impact-of-EU-membership-on-Ireland_en, accessed 29th August 2019

[5] Enterprise Ireland, Horizon 2020, http://www.horizon2020.ie/ireland-still-a-net-contribution-to-eu-funds/ accessed 29th August 2019

[6] European Commission, Common Agricultural Policy – Ireland, https://ec.europa.eu/info/sites/info/files/food- farming-fisheries/by_country/documents/cap-in-your-country-ie_en.pdf accessed 29th August 2019

[7] Dorgan, Sean. "How Ireland became the Celtic tiger." Heritage Foundation, Issues, June 23 (2006).

[8] Walsh, Aidan, and Chris Sanger. "The historical development and international context of the Irish corporate tax system." A report commissioned by the Irish Department of Finance, EY (2014).

[9] Berry, Frank. "Irish economic development over three decades of EU membership." Czech Journal of Economics and Finance (Finance a uver) 53.9-10 (2003): 394-412

[10] International Monetary Fund, https://www.imf.org/en/Countries/IRL, accessed 29th August 2019

[11] OECD (2017), OECD Digital Economy Outlook 2017: 127-8. (OECD Publishing, Paris). http://dx.doi.org/10.1787/9789264276284-en, accessed 29th August 2019

[12] McWilliams, David. “Renaissance Nation: How the Pope’s Children Rewrote the Rules for Ireland.” Gill & Macmillan Ltd (2018).

[13] International Monetary Fund, https://www.imf.org/en/Countries/IRL/ireland-lending-case-study, accessed 29th August 2019

[14] European Commission, Ireland’s Economic Future: an EU perspective (2016) https://ec.europa.eu/ireland/sites/ireland/files/irelands_economic_future_-_an_eu_perspective_final_for_web.pdf, accessed 29th August 2019

[15] https://ec.europa.eu/ireland/news/é-cinneadh-aontais-eorpaigh-nach-mór-do-apple-€13-billiún-aisíoc-le-héirinn_en, accessed 29th August 2019

[16] https://www.cso.ie/en/releasesandpublications/ep/p-nie/nie2018/mgni/, accessed 29th Aug. 2019

[17] Central Statistics Office, Census through History, https://www.cso.ie/en/census/censusthroughhistory/, accessed 29th August 2019

[18] Hayes, Treasa, and Ruth BT Mattimoe. "A Historical Profile of the Irish Economy and Irish Government Economic Policies with regard to the Enterprise Sector." (2002): 79-108.

[19] European Commission, https://ec.europa.eu/eurostat/statistics-explained/index.php/Being_young_in_Europe_today_-hdemographic_trends#Past.2C_present_and_future_demographic_developments_of_children_and_young_people, accessed 29th August 2019

[20] Central Statistics Office, Population and Migration Estimates. https://www.cso.ie/en/statistics/ population/populationandmigrationestimates/, accessed 26th April 2019

[21] https://dbei.gov.ie/en/What-We-Do/Business-Sectoral-Initiatives/Future-Jobs/#, accessed 29th August 2019

[22] https://ec.europa.eu/eurostat/documents/6939681/7243182/Booklet_2019_rents_2018_e_ DRAFT.pdf/1321ca38-8039-4f95-aade-434e9550462e, accessed 29th August 2019

[23] https://www.dfa.ie/brexit/getting-ireland-brexit-ready/governmentcontingencyactionplan/ Brexit Contingency Action Plan, Publication of Brexit Contingency Action Plan Update, 29th Aug. 2019

[24] McQuinn, K., O’Toole, C., Matthew Allen-Coghlan and Economides, P., 2019. Quarterly Economic Commentary, Summer 2019. ESRI Forecasting Series.