



Ireland's rollercoaster economy

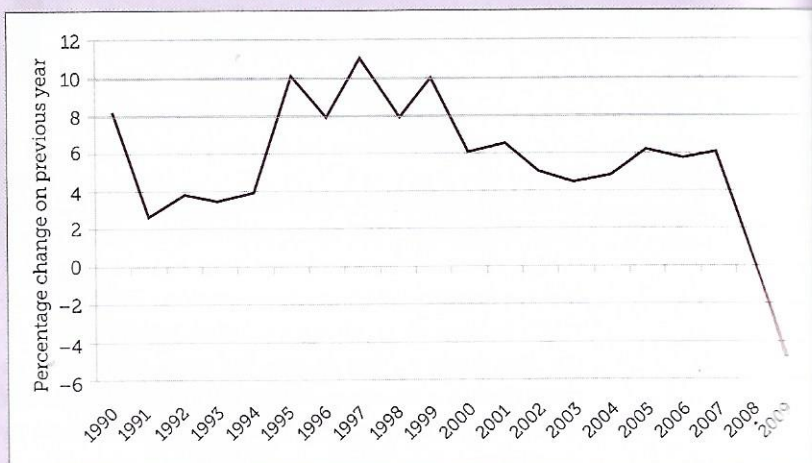
Ireland became one of the world's most remarkable success stories for globalization's benefits. From an economy based mainly on low-cost production in the 1980s, it transformed itself into a global player.

Ireland's so-called 'miracle' growth took place between 1986 and 2001. It attracted FDI in high value-added sectors such as pharmaceuticals. American companies led the rush to Ireland, with its educated, English-speaking workers, low costs and low taxes. Computer companies such as Dell built factories. Numerous American pharmaceutical companies piled into the country in the early 2000s, establishing multiple sites: Pfizer (5 sites), Abbott (7 sites) and Schering Plough (4 sites). State grants and access to the EU single market were additional attractions. Called the 'Celtic Tiger', Ireland enjoyed buoyant growth, which seemed to be sustainable (see figure). The country gained rapidly in global competitiveness, reaching a rank of third, behind only Hong Kong and Singapore (Krugman, 2009). How the Irish boom turned to bust offers lessons to other small, open economies exposed to global forces in all their manifestations.

A construction boom went hand in hand with economic growth, resulting in a huge expansion in numbers of houses, office blocks and retailing outlets. Builders and developers, along with home buyers, enjoyed easy access to credit from banks which in turn were able to borrow easily in global markets. By 2007, construction accounted for 20% of Ireland's GDP (IMF, 2009). Ireland's growing financial sector benefited from global financial flows. Its major domestic banks flourished, as did numerous foreign banks which set up in the country, attracted by the openness of the economy and low interest rates that prevailed, thanks to Ireland's membership of the

eurozone. Exposure to global financial forces, however, made the country vulnerable to global shocks (IMF, 2009).

Ireland had long prided itself on a 'social partnership' between business, workers, trade unions and the government, in which there was a consensus on moderate wage growth. However, wages escalated during the boom, both in the private and the public sectors. Lax fiscal policy on the part of the government contributed to soaring public spending. A cut in income tax, while welcomed by taxpayers, left government finances in a perilous position. When the property bubble burst and financial crisis struck in 2008, the economy went into reverse. Construction companies were left with unsold properties, leading to widespread insolvency in the sector. Banks were left with bad loans connected with the domestic



Ireland's GDP

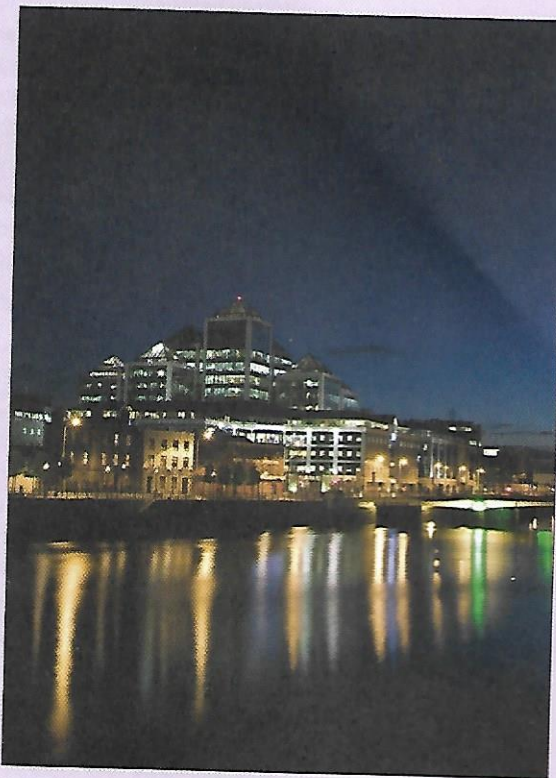
Source: *The Economist*, 21 March 2009

construction industry, as well as their expansion into unregulated global financial markets. In September 2008, in order to avert a bank run, the Irish government offered to guarantee most bank deposits and debts, which would have amounted to two to three times the country's GDP. A number of the banks involved were foreign owned, leading many to question the policies that allowed the country to descend into this disastrous situation (Krugman, 2009).

► More online ... The Irish government's website is www.gov.ie and has links to a number of sites, including government departments. GlaxoSmithKline's website is www.gsk.com

Government finances went dramatically into the red as revenues from taxes dried up but commitments on public spending continued to rise, including welfare payments for the mounting numbers of unemployed people. The Irish government had little prospect of borrowing its way out of difficulties, as potential bond investors had lost confidence in its bonds, especially in light of its bank guarantee policy. From a slight budget surplus in 2001, it plunged into a budget deficit of nearly 12% of GDP in 2009. The government was compelled to bring in drastic austerity measures, effectively cutting public-sector pay and reducing welfare payments. By 2010, the painful measures of wage freezes and reduced public spending appeared to be working, and the economy was forecast to be slowly recovering. However, unemployment, especially severe in the construction sector, was still expected to reach 14% of the workforce. Foreign investors such as pharmaceutical companies were expected to stay, but with slimmed-down workforces. Dell closed down its Irish factory and moved to Poland. Ireland was not expected to restore its budget deficit to the 3% set by the EU stability pact until 2014. Late in 2010, a bailout package of 85 billion euros was put in place by the EU, in support of the Irish economy, but austerity measures remained core to Ireland's economic recovery.

Sources: IMF (2009) *Report on Ireland* (Washington, DC: IMF); Krugman, P. (2009) 'The lessons of Ireland', *The Guardian*, 21 April; Brown, J. (2010) 'Ireland finds tough measures paying off', *Financial Times*, 3 February; *The Economist* (2009) 'The party is definitely over', 21 March; Brown, J. (2009) 'Ireland meets economic crisis head on', *Financial Times*, 24 December



Ireland became one of globalization's success stories, reflected in the gleaming new buildings lighting up Dublin's skyline, but the image dimmed as financial crisis gripped the Irish economy

Source: Istock

Questions for discussion

- ◆ How did globalization promote Ireland's stunning growth?
- ◆ What were the causes of Ireland's shattered economy?
- ◆ What lessons can other economies learn from the Irish example?